###### State Comptroller

Preparations for sale

Bank stocks in the arrangement



State Comptroller

Preparations for the sale of bank shares in the settlement

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Introduction

The manipulative regulation of bank stocks during the 1970s and early 1980s, until the crisis in October 1983, created a multibillion-dollar gap between the artificial market value of the shares and their economic value. In the long run, the regulation was futile. And when it ended in crisis, the stock of shares held by the banks for the purpose of regulating was equal to 162%of their financial capital, orto 44% of their own[[1]](#footnote-1)fortunes.

The bank stock crisis was the biggest and worst financial crisis in the country's history.

In the wake of the crisis, the government was rescued from collapse and even[[2]](#footnote-2)to maintain most of the artificial market value of the shares held by the[[3]](#footnote-3) public.[[4]](#footnote-4)

The financial dimensions of the expenditure on the stock arrangement were enormous. From October 1983 to the end of October 1991, the government spent an amount of NIS equal to approximately $9.1 billion (including the cost of financing attributable to this expenditure until that date - see below; the cost of financing continues to add up even after that date).

The direct financial loss to the state is the difference between the expenditure on the "redemption" of the shares (including the financing cost of this expenditure) and the proceeds the state receives when you sell the shares. This loss is reflected in a considerable addition to the state's debts, the largest in Lao.

As for the other outcomes of the arrangement, see the State Comptroller's Report on the Bank Stock Crisis, Chapter 8, the economic and public implications of the arrangement to ensure the value of bank stocks" (p. 65).

### Decisions regarding the right to "cash in" the shares of banks

1. Given the responsibility of the controlling shareholders of the banks and their executives for the throes crisis, the government has refrained from granting those defined as "stakeholders" (see below) the right to "redeem" their shares under the arrangement. In contrast, in order to prevent fatal harm to the steaddness of the banks, the government granted the banks the right to "redeem" the shares of nostro, the sharespurchased by bank corporations for the purpose of regulating. The arrangement stipulates that nostro shares will be "lost" at the end of five years (October 1988),and will not be traded until then except with the prior consent of the Ministry[[5]](#footnote-5)of Finance and the Bank of Israel (see below).

The right given by the government to banks to "redeem" Nostro's shares was also a very considerable benefit to the controlling shareholders.

2. During the discussions on the formulation of the arrangement, a definition of "stakeholders" was established, who would not be entitled to "redeem" their shares under the arrangement. This definition was based primarily on the definition in the Securities Law,1968 below – the Securities Law), but certain changes, intended, according to the Treasury's explanations, to grant the right of "redemption" under the arrangement to economic entities related to banks, which held bank shares as part of their policies or as a long-term investment, and whowere not interested in the sense of the banks' policymakers or participants in their management. In addition, it was decided to exclude from the list of stakeholders prepared by the Bank of Israel according to the same definition, bodies or individuals agreed upon by the committee whose members will be representatives of the Ministry of Finance, the Bank of Israel and the banks. The Deputy Prime Minister has been empowered to decide on disagreements, if there are any.[[6]](#footnote-6)

3. In discussions held with the Deputy Prime Minister in October 1983, it was decided to transfer shares on a substantial scale from the list of stakeholder shares prepared by the Bank of Israel according to the definition set forth in the classification of "Nostroshares" - whose owners would beentitled to "redeem them" - and mainly:

(A) Shares of Bank Hapoalim Ltd. (hereinafter – Bank Hapoalim) amounting to 5.6% of the issued capital, whose market price on the eve of the crisis was $121 million, which was in the hands of serenity controlled by the employees' company.

(B) Shares of IDB Holdings totaling 7.8% of the issued capital, whose market price on the eve of the crisis was $85.2 million, which were held by El-Am Anyaim Ltd. (hereinafter - El-Im), a company controlled by the controlling shareholders of IDB Holdings Ltd. (hereinafter - IDB Holdings); El-Yim was a stakeholder in IDB Holdings.[[7]](#footnote-7)

In February 1993, the Bank of Israel explained to the State Comptroller's Office:

"Discount Bank representatives have asked the Deputy Prime Minister to characterize this shareholding in the "Public" category. The supervision of the banks sought to characterize these shares in the "stakeholders" group, and the compromise made by the Deputy Prime Minister was to characterize these holdingsas Nostro.

In April 1993, the deputy prime minister announced at the time of the settlement to the State Comptroller's Office that the discussion was being done in a broad forum that included other ministers, the Governor of the Bank of Israel, the Director General of the Treasury and the Attorney General; And that the continuation and summary of the discussion was handed over to the finance minister, who was appointed in the meantime, who headed the team instead of the deputy prime minister.

4. After the settlement was made, at an unknown time, it was decided that the shares of Discount Bank Ltd. (hereinafter – Discount Bank) totaling $52.3 million, according to the price in the market on the eve of the crisis - which the bank intended to issue to another group of banks, as part of the proceeds for the purchase of shares in that group - would also be entitled to "redemption" under the arrangement (as "public" shares). This decision found no reference or reasoning.

In December 1991, the Ministry of Finance informed the State Comptroller's Office that the person who was the Treasury's legal advisor at the time of the crisis informed him that it was the then finance minister who made this decision, contrary to his opinion.

5. According to other decisions, the classification of "stakeholders" was transferred to the classification of "public" shares of some of the stakeholders in the banks, especially expat directors.

6. In some cases, permits were granted to sell Nostro shares prior to October 1988:

(A) In 1986, the Minister of Finance and the Governor of the Bank of Israel allowed the employee company to sell $45 million in Nostro shares to help Solel Boneh.[[8]](#footnote-8)

(B) In July 1987, the Governor of the Bank of Israel agreed, on the recommendation of the Minister of Finance, that the company of employees sell to the Ministry of Finance shares of Bank Hapoalim that it had, and were classified in their time as "Nostro" shares, for anamount not to exceed $15 million. The sale is intended to provide the employees' company with a source of funding for the investment in the equity of "Hasna"; The agreement was given that the company of employees would invest in increasing the capital of the "hesna" the same amount from its means.

(C) In April 1987, the Ministry of Finance and the Bank of Israel permitted the Bank of Israel to sell M.I. Assets (see below) Nostro shares to finance increasing the bank's wealth; the permit was conditioned on the bank's controlling shareholders investing in an increase in the bank's capital.

### Interim period of bank stock arrangement

1. According to the conditions set forth in the Bank Stock Arrangement, the government will refrain from the interim period, which is scheduled to last until the end of October 1993, from taking ownership of the shares that Padionen was funded from the state budget. In order to settle the holding of shares in the interim period, the controlling shareholders established, in each bank included in the arrangement, a safe company; the government signed with each such company an agreement under which the amounts[[9]](#footnote-9)that the government would hand over to the company would be deemed to be for the purpose of financing the "redemption" of the shares as a loan. If at the end of the period it becomes clear - as was reasonable to expect, given the large gap between the actual value of the shares and the redemption values promised to shareholders - that the value of the shares will not be sufficient to cover the repayment of the loan, including the interest accumulated, the Safe Company will transfer the shares to the government, and this will be considered a full repayment of the loan and interest fund.

 The government may at any time instruct the Safe Company to sell them, in whole or in part, on conditions determined by the government, and to transfer the proceeds to the government as a partial repayment of the loan, according to the proportional portion of the shares sold.

2. In light of almost certain predictions that the safe companies would not be able to repay the loans to the government at the end of October 1993, but by transferring the shares of the banks they would have, the Bank of Israel and the Ministry of Finance began to examine the possibility of selling the shares of the banks in the hands of the safe companies within the interim, rather than waiting until the end of October 1993. In early 1987, the Ministry of Finance prepared proposals on this matter, and held discussions with the Bank of Israel. Since then, the Ministry of Finance has been working to realize this possibility.

3. From May 1990 to November 1992, intermittently, the State Comptroller's Office examined the preparations for the sale of bank shares in the arrangement. The examination was carried out at the Ministry of Finance and M.I. Property Company[[10]](#footnote-10)Ltd. (hereinafter - assets).[[11]](#footnote-11)

### The fundamental problems of preparing to sell bank stocks

1. Besides the large financial loss resulting from the difference between the amounts spent by the government on the "redemption" of the shares and their actual value (see table below), the stock arrangement involves two fundamental problems regarding control of the banks:

(A) The voting rights bought by the shares of the banks in the hands of the public (as well as the shares of Nostro) - and which was expected to be handed over tothe government in 1993 - were inferior, At a sailing rate, from the voting rights bought by the controlling shareholders of the banks, as detailed in Table 2 below.

(B) In the interim, control of each of the banks remained in the hands of the body that controlled it until the crisis; The same body chose the bank's board of directors, and the board appointed the bank's management. The government preferred to refrain from taking control of the banks in the arrangement, and even from involvement in managing them, even as a group

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**With you forgiveness**

Table **2: Distribution of banks' capital** in settlement (in percentage)(1) to 13.10.91 but before voting rights are compared)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Union Bank** | **Mizrahi Bank(3)** | **IDB(2)** | **Bank Leumi** | **Bank Hapoalim** |  |
| **On the ballot** | **In the hon** | **On the ballot** | **In the hon** | **On the ballot** | **In the hon** | **On the ballot** | **In the hon** | **On the ballot** | **In the hon** |  |
| 99.89 | 49.94 | 98.04 | 24.51 | 93.85 | 73.15 | 99.97 | 49.98 | 58.00 | 14.50 | Shares that are "cashed in" by the safe companies Funded by the government  |
| 0.11 | 50.06 | 1.96 | 75.49 | 6.15 | 26.85 | 0.03 | 50.02 | 24.00 | 85.50 | Stakeholder Shares |

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

(1) The source: M.I. Assets Company (B) In the table, the distribution of the holding in the share capital is presented at the end of the "redemption" of the shares of the banks in the arrangement on 13.10.91 in fact, voting rights were compared to IDB and the Eastern Bank prior to that date, while in the rest of the banks - after it. The distribution of voting rights in all banks is presented here according to the prevailing situation prior to the comparison of the rights. Prior to 13.10.91 ((c) the data relating to the General Bank and the Bank of Finance and Trade are not presented in this table.

(2) E.D.B., Banking Holdings Ltd. held approximately 66% of Discount Bank Ltd.'s shares,which gave itapproximately 60% of the bank's voting rights; and about47% of the share capital and voting rights of IDB Development Ltd. as part of the arrangement, the government also funded the acquisition of Discount Bank shares at a rate of 8.33% of the capital and 7.9% of the shares.

(B) In August 1991, the government signed an agreement with the previous controlling shareholders under which it sold them a portion of IDB's shares held by the Safe Company.

(3a) The shares of those defined as stakeholders were not included in the bank stock arrangement.

(B) The controlling shareholders of Bank Hapoalim (the employees' company) and Mizrahi Bank (Mizrahi Holdings Association) had fundamental shares that gave them 5% of all voting rights. The decision of the Special Ministerial Committee on Economic Affairs from October 1983 stipulated that IDB would be entitled to change the voting rights of the controlling shareholders similar to the situation of the controlling shareholders of the large banks.

For this reason, as noted, the safe companies of the banks, which hold shares that have[[12]](#footnote-12)been "cashed", have been established.[[13]](#footnote-13)

According to the Treasury Department' explanations, the main considerations for this were these: to prevent the negative reaction that could have been in overseas banks and bodies

 others abroad take over the banks in the arrangement, or even the government's involvement in managing them, if only for appearances; prevent political appointments and the introduction of political considerations in the management of banks; and prevent harm to policies of reducing government involvement in the economy.

In December 1991, the Ministry of Finance explained to the State Comptroller's Office:

"Exercising control of banks would have resulted in deep and unwanted involvement, both in the management of banks and in all areas and industries in which banks and IDB have subsidiaries or related companies."

According to the terms set forth in the arrangement, according to these considerations, those who controlled the banks[[14]](#footnote-14) remained in the hands of those who controlled the banks at the time of the stock regulation "the control and full powers of the banks, as they were before the settlement."

2. Due to the stock crisis and subsequent settlement, it was created, according to the aforementioned government considerations, An anomalous situation in which the controlling shareholders of the banks (who have nothing but a small minority of the share capital) were allowed to continue to control them, at the same time it was the government that paid for the "redemption" of the vast majority of the shares,[[15]](#footnote-15)according to the inflated prices that prevailed on the eve of the crisis as a result of the manipulative regulation that the banks initiated and operated. In fact, the government was the stakeholder in the functioning of the banks, as the benefit of its damages depended on their business results.

3. In the opinion of the State Comptroller, he was asked to defend the interest of the state – which is charged with the interest of the entire public – in each of the following ways:

(A) Comparing the voting rights of bank shares, i.e., eliminating the inferiority of the rights of the large majority of the shares, which the Government funded by the Government, as opposed to those of the special shares of the controlling shareholders, was a prerequisite for obtaining a return for the shares that would minimize the large loss resulting from the share arrangement (regarding additional considerations for the purpose of comparing the rights, see below p00).

As part of the bank stock arrangement - an arrangement formulated by the government and banks in circumstances of intense pressure, given the danger of the collapse of the banking system - the government received nothing from the controlling shareholders in exchange for its pledge to spend a huge sum to prevent the collapse, which would have caused severe damage to many investors (including the controlling shareholders themselves) and the economy as a whole.

Due to the above considerations, the government did not require that the controlling shareholders and banks commit, under the arrangement, to compare the voting rights that banks' shares give. However, since it was expected, as noted, that the safe companies could not repay the government the loans they received from it, there was no escape, morally and publicly, from a demand to compare voting rights without delay, and there was no justification for the government to make substantive and fundamental concessions to the controlling shareholders in exchange for their agreement to compare the voting rights.

(B) It has been requested that the government guarantee itself full laitry in determining at its sole discretion the sales processes of the shares whose purchase it funded is from state budget funds.

In order to achieve optimal results, the government needed flexibility in determining the methods, conditions, quantities and timing of sales, and had to focus on creating sales processes that would enable and encourage as much lively competition as possible.

(C) He was asked to drink the sales processes of the settlement shares on the principle of providing equal opportunities for candidates to acquire control of the banks, and to determine that no candidate would be given preference over other bidders. [[16]](#footnote-16)

Moreover, there was a determination, as a condition of not passing, that no preference would be given to those who controlled the banks during the thyst crisis.

When a business body (or other) fails diligently, it is natural that its collapse will cause the property of the controlling shareholders to go down the drain, in whole or in part, and that they will lose control of the failing body in favor of an able-bodied party to acquire it, or be entrusted with operating or dismantling it. However, especially when it comes to a large body, the government is sometimes called upon to intervene and save the body from collapse, in order to preventor minimize the expected harm to itsemployees, customers, customers and suppliers; In the exceptional event of the bank stock crisis, the government decided to provide very large amounts of financial assistance to minimize the financial damage that was expected to the public investing in bank stocks.

You won't let them collapse. Such a danger (known as "moralhazard"- moral hazard) exists in the bankingsector, especially in connection with large banks.

In accordance with this rule, the bank stock arrangement states that those who were interested in banks at the time of the crisis will not be entitled to "redeem" their shares (for some exceptions to this restriction - some of them in considerable amounts - see above). However, the stakeholders in the banks enjoyed, as noted, indirectly but at a considerable rate (according to their share of the banks' share capital), the right given by the government to the banks themselves to "redeem" their Nostro shares.

Furthermore, due to the government's concern about preventing damage to the status of banks as independent bodies, the controlling shareholders enjoyed the right to continue controlling them for the long interim period set forth in the arrangement; And under its original terms (without comparing the rights), they were supposed to continue to control them even after the end of the interim period, indefinitely.

When the Treasury concluded that it had to act to compare the voting rights that bank shares give, so that the sale of bank shares that would be "processed" would involve the sale of control of the banks, the Treasury department was tasked with not setting conditions in the sale processes that would make it difficult for other potential buyers to compete for the acquisition of a controlling core in the bank, increase the chances of the controlling shareholders winning it or allow them to purchase.

(D) It was necessary to ensure the full cooperation of the banks in the sales processes of their shares, especially in regards to the delivery of information for the purpose of evaluating the banks' valuations and preparing prospectuses for the sale of the shares (subject to the reservations determined by the supervisor of the banks, in order to maintain the rules of banking confidentiality).

(E) It was necessary to set conditions that would allow, as much as possible, to prevent, during the interim period, the action of a bank that could undermine the economic value of its shares, such as making a transaction with a body associated with the controlling shareholders of the bank under conditions that are not in the bank's best interests.

(F) Given the great centralization of the banking system in Israel and the great economic strength of the three largest banking groups, it was necessary to examine the issue of the fragmentation of the banking groups in the arrangement, i.e., to examine mainly the following questions: (1) whether the centralization of the banking system, and the great power of the banking groups per se, are weighing on the proper and efficient functioning of the national economy; (2) whether the fragmentation of the bank groups in the arrangement contributes to improving the functioning of the economy; (3) whether a split may facilitate the sale of bank shares, and whether it may contribute to increasing the total monetary value the government receives from the sale of the shares; (4)

 What are the disadvantages of splitting up bank groups, and whether the economy's wages from such a split are not likely to go out at a loss.

It was appropriate for the Ministry of Finance and the Bank of Israel to examine this issue in depth ahead of time, i.e., before the practical preparations for the sale of bank shares, and however, before a commitment to the controlling shareholders of the banks, or to other purchasers of shares in the banks, would be extinguished by the execution of a split or prevented it altogether. The moral right to decide the issue of fragmentation and determine the capital structure of the bank groups was in the hands of the government. She had full justification to stand that she would also have the legal authority to decide on a split undisturbed.

(G) During the years of preparations for the sale of bank shares, the Ministry of Finance implemented the capital market reform, a major aspect of which is a very large increase in the involvement of provident funds in this market. Since the banks control the vast majority of provident funds, as well as mutual funds, It was necessary (even regardless of the sale of bank shares) to establish rules and arrangements that would prevent as much as possible the abuse of conflicts between the interests of banks as[[17]](#footnote-17)lenders, as securities underwriters, investment advisors,and more, and their interests as provident fund managers and mutual[[18]](#footnote-18)funds.

4. Naturally, it was expected that the banks and controlling shareholders would oppose the leadership of each and every one of the state's interest protection measures listed above.

5. At the end of 1988, the Ministry of Finance issued a memorandum of law comparing the voting rights of bank shares (see below); In January 1990, the government placed a bill on the Knesset table to compare voting rights, including, among other things, provisions that would force banks to have the leadership of the measures that were necessary, as noted, to protect the interest of the state.

However, the government and the Bank of Israel continued to prefer that these safeguards be moved, if only possible, with the consent of the banks and their controlling shareholders. To energize controlling shareholders to compare voting rights by consent, the Finance Minister informed them that a bank whose shares' voting rights would be compared by consent

And without the need for legislation, its controlling shareholders will be given shares of 2%-3% of the bank's share; It would also be possible to remove such a bank from the law's ability to compare the rights.

6. In the opinion of the State Comptroller, the Ministry of Finance did well, trying to persuade the controlling shareholders to compare the voting rights of bank shares by way of consent, without the need for legislation. It was reasonable to discuss with the controlling shareholders of the banks and their executives - for a limited and predefined period of time - to hear their opinions on matters such as: determining reservations to prevent government involvement in the management of banks in the interim; preventing harm to bank secrecy when preparing valuations; upsizing the banking system; and determining effective ways to sell the shares. There was, however, no room to give up the measures necessary to protect the country's interest. Mole was to stand that the Treasury Department's reluctance to imitate and coerce - due to weighty considerations, primarily because of its concern for the status and independence of the banks - would not be exploited as leverage against it, in order to gain advantages for the controlling shareholders, or to prevent, reject or weaken these measures. In discussions with the controlling shareholders of the banks, it was forbidden to cross "red lines," and the state interest protection measures, listed above, were, in the opinion of the State Comptroller, worthy of being "red lines," for this matter.

It was appropriate to establish a sharp distinction between the takeover of the banks or government involvement in their ongoing management and business considerations - from which it was decided to abstain, in practice and even for appearances - and the measures necessary to enable the government: (a) to sell the shares on reasonable and proper terms; (B) determine - if you deem it appropriate to do so - what changes will be made to the structures of the bank groups before offering their shares for sale; (c) prevent damage to the economic value of the shares of the banks in which the government was interested.

It was necessary to make it clear to the controlling shareholders of the banks that the government would not be able to give up the leadership of these measures to protect the interests of the state and the public, and if on that basis the controlling shareholders agreed to compare the voting rights, I will be happy; However, if not, the government will not refrain from taking, without choice, the alternative path, namely promoting the legislative procedures of the Voting Rights Comparison Act, in which all such measures will be enshrined.

7. Da'Aqa, that's not how it happened. The preference to reach agreement with the banks and their controlling shareholders prompted the Ministry of Finance as a representative of the government to reach far-reaching compromises in terms of safeguarding the interests of the state as detailed below.

8. In December 1991, the Ministry of Finance explained to the State Comptroller's Office that its desire to refrain, if only possible, from legislation regarding the aforementioned was due to the fear that it would be because of the nationality of the banks, in practice or for appearances.

9. This reason is not convincing.

10. In addition to the Treasury Department's desire and assets to avoid legislation in this matter as much as possible, they tended to refrain as much as possible from getting into conflict with the banks and controlling shareholders, if this could involve legal proceedings, and refrained several times from insisting that the banks and their controlling shareholders fulfill their obligations to the[[19]](#footnote-19)state.

11. These are the results of the treasury's methods of action and assets, based, as noted, on the strong preference to refrain from legislation in question and even from taking steps to exercise the rights of the government against the wishes of the banks and their controlling shareholders:

(a) The voting rights that bank shares are actually being compared at a fairly late stage of the interim period: BDB and United Eastern Bank Ltd. (hereinafter - Mizrahi Bank) in May and September 1990, respectively; and Bank Hapoalim, Bank Leumi Israel Ltd. (hereinafter - Balal) and Bank Igud Ltd. (hereinafter - Union Bank) - only in the last quarter of 1991, That is, eight years after the throes crisis, more than five years after the Baysky Commission voted on the need to remedy the inferiority of rights, and three years into negotiations (hereinafter - the negotiations) with the controlling shareholders of the banks.[[20]](#footnote-20)

Until the end of the audit, November 1992, the Ministry of Finance and Assets did not sell bank shares, except for a minority of General Bank Ltd. shares (hereinafter – General Bank), which was in the hands of the Safe Company; In August 1992, they sold IDB shares (including indirectly, discount bank shares at a very small rate), in a deal that was tied up in unmatched negotiations (which, for the likelihood of its terms, see below, p00) in August 1992.

The great delay of the sale processes was primarily due to the continued negotiations with the controlling shareholders and the banks, which only eventually, as noted, were the voting rights of the shares compared. However, the conditions set forth in the memos and agreements regarding the comparison of voting rights exceed, in the opinion of the State Comptroller, the "red lines" mentioned above. It should be noted that negotiations continued even because the Ministry of Finance and Assets opposed unity from the demands of the controlling shareholders. However, as noted above, there was no room for bargaining with the controlling shareholders, and the continued bargaining of the measures necessary to protect the state's interest, including comparing voting rights; the right of the government to determine at its discretion the sales processes and structures of the bank groups that would be sold; and to prevent any preference of the controlling shareholders in dealing with the control nuclei.

(B) During negotiations with the controlling shareholders regarding the comparison of voting rights, the Ministry of Finance responded to their request to negotiate it also determines the terms of the sale processes of the bank's shares. Indeed, in the agreements formed in the negotiations ("Memorandums of Principles" - see below) the sale processes under which the government must act have been established in great detail, including many conditions in which to limit the government's freedom of action and discretion in the sale of bank shares.

Some of the conditions set out - especially in the Principles Memorandance and the detailed agreement with the controlling shareholders of IDB - was also to give the controlling shareholders a definite priority over other candidates in the run-up to the purchase of bank shares.

(C) In an agreement signed with the controlling shareholders of IDB in May 1990, rules were established to provide information that would harm the chances of any applicant, other than the controlling shareholders, acquiring the company on reasonable terms. Although agreements signed with the banks (including Discount Bank) and their controlling shareholders at a later stage – from March to December 1991 – established plausible rules for the banks' cooperation in the sales processes, during preparations to sell the banks' shares, difficulties arose in the implementation of these rules.

(D) The protection against harm to the economic value of the shares of the settlement was not actually used – except for certain measures used by the Bank of Israel's supervision of banks – but at a fairly late stage in the interim period, as part of the agreements signed with the three largest banks and their controlling shareholders from August to December 1991. In an agreement signed with the controlling shareholders of Mizrahi Bank in August 1990, no rather limited safeguards were signed, apparently based on the assumption that its control would be sold shortly (in fact the sale process lingered longer than expected, and the contracted sale transaction was eventually cancelled).

(E) The Ministry of Finance and the Bank of Israel have not yet examined two of the main aspects of the bank group split issue: the possibilities of separating and selling separately (1) banking subsidiaries, (2) non-bank subsidiaries. The Memorandum of Principles signed in late 1989 with the controlling shareholders of IDB stipulated - as the controlling shareholders demanded - that it be sold as a single piece. As part of a deal to sell IDB shares to its controlling shareholders in August 1991, the Group was split partially, but this split served the interests of the controlling shareholders. A memo signed with the controlling shareholders of each of the two largest bank groups states that, in agreement, between the government and the controlling shareholders of each, the list of banks sold separately (except a union bank controlled by Bank Leumi). But in fact no such lists have been determined; And in agreements signed with those bank groups and their controlling shareholders in 1991, it was not determined that the government could decide on splitting them or making changes to their structures.

(F) The handling of the issue of centralized control of banks in most provident funds and mutual funds and the conflicts of interest involved has been delayed for years. The Ministry of Finance and the Bank of Israel are naïve about the need to take

Real steps to resolve this issue, but the steps they took, until the end of the review, were relatively limited, and were not - in both opinion - to resolve the issue.

(G) It turns out that in some of the above topics there are considerable differences between the terms set forth in agreements with the controlling shareholders of the various banks. In various matters, special benefits were given to the controlling shareholders of one bank or another: the controlling shareholders of IDB were given significant advantages in dealing with a controlling core, while some of the measures to protect against harm to the economic value of the shares, which were included in the agreements signed by the Ministry of Finance and assets in 1991 with some banks and their controlling shareholders, were not included in the agreements signed that year with other banks and their controlling shareholders. Apparently, these differences arise, among other things, from a different bargaining capacity with the various banks and their controlling shareholders.

(H) The government paid the controlling shareholders of the four bank groups 3% of the share capital, as it was obligated to do according to the principles memorandums.

12. In the opinion of the State Comptroller, it would be possible to prevent the deficiencies listed above, if the Treasury and assets were to reassure their leadership without delay of the measures to protect the rights of the state and to allow the government to sell the shares on reasonable terms, listed above. The Treasury and assets had to make the choice to accept these terms and anchor them in the agreements (as noted, the Finance Minister offered them a financial tribute if they agreed to it), or to refuse it.

The leadership of these terms was not - and even in their enclose of legislation - because it seriously impaired the considerations of the government mentioned above. These measures had to be designed and implemented, by the way, setting a sharp distinction between government involvement in the ongoing management of banks and their business considerations - which it was decided to avoid - and the measures needed to allow the government to sell the shares on reasonable and appropriate terms, to prevent damage to their economic value, and to determine - if it deemed necessary to do so - what changes would be made to the structure of the banking system before offering the banking shares for sale.

### Protection against impairment of the economic value of stocks

Following the agreements signed under the Bank Stock Arrangement in October 1983, each of the banks, in a letter to the Finance Minister, pledged that it would do "nothing in the act or cease, which infringes the rights of the state arising from the agreement." However, no ways for practical protection of state rights were established under the arrangement in those agreements.

In March 1984, the Governor of the Bank of Israel (hereinafter – the Governor) proposed to the Minister of Finance, and the Minister agreed that the Bank of Israel, through the supervision of the banks, would stand up for the country's rights. In July 1987, the Supervisor of Banks informed the State Comptroller's Office that the implementation of this task was reflected, inter alia, in providing instructions to banks and conducting checks regarding transactions with entities that have an affiliation with the controlling shareholders of those banks; and establishing rules for financial reporting and regarding the status of the board, accountants and internal auditors in banks. However, the Supervisor of Banks made it clear to the State Comptroller's Office in April 1991 that since the supervisor of the banks - and in his opinion he also did not want to have any powers in managing the banks

(e.t., pre-approval of transactions or determination of pay policies), it cannot be held liable for any decisions and actions of the banks, in terms of its suitability to the interest of the state as the actual stakeholder in the shares. Absolute safeguarding of the interests of the state would have necessitated participation in the management of banks through representatives in the boards of directors of the banks; in his opinion, the shortcomings of such oversight are very numerous, and it is good that he was not taken.

The Ministry of Finance explained to the State Comptroller's Office that the General Law establishes control mechanisms to reduce the risk that bank management will act in a manner that could harm the bank's economic value. In the opinion of the State Comptroller, there was no place to assume that the supervision mechanisms employed under normal circumstances would be able to provide the state with a plausible defense even in the exceptional circumstances created as stated in the interim period. Indeed, in 1991, after long negotiations and in return for significant concessions by the government on various issues, the Ministry of Finance and Assets obtained the consent of banks and their controlling shareholders to take measures to protect the country's interests.

### Invoking the voting rights that safe companies buy

##### Exercising the rights under the loan agreements with the safe companies

1. The safe companies are under the control of the controlling shareholders of the banks in the arrangement. Under the agreements signed between the government and the safe companies regarding the terms of the loans it gave them in 1985-1991 to fund the "redemption" of the shares, each safe company undertook to "exercise the rights granted to it by virtue of its ownership in the enslaved securities ... Including participation in general meetings, voting, selection or appointment of directors ... In a way that will be agreed between the government and the company before exercising any such right."

2. In April 1991, the Legal Advisor of the Ministry of Finance explained to the State Comptroller's Office that this meant that even after comparing the voting rights of the shares (see below), the government was not entitled to make decisions in the aforementioned matters until the end of the interim period, except with the consent of the controlling shareholders (a situation called "mutual veto").

3. On the other hand, in a legal opinion received by assets in May 1991 from one of its external legal advisors, it is stated that the provision of the loan agreements does not mean a mutual veto, but as follows:

"The government has a positive right to initiate the exercise of voting power, subject to the limitations of fairness and reasonableness. In the absence of any business reasons, the Safety Company is not entitled to oppose the government's legitimate demand."

The Treasury's legal advisor adopted this opinion in one opinion with the external asset legal advisors. In December 1991, the Ministry of Finance explained to the State Comptroller's Office that the idea raised in the legal opinion "was not raised before, and certainly was not raised regarding the exercise of voting power in circumstances that are not extreme in terms of sales capability, we were not in connection with ongoing management and not in connection with the situation in which there is also a possible alternative of action by way of consent."

It should be noted that the Ministry of Finance and Assets refrained from putting to the test the government's ability to exercise voting rights in the said way, even under the same circumstances as the advisor wrote the[[21]](#footnote-21)opinion.

##### Invoking the rights to avoid damaging the value of the shares

1. The agreement signed by the government with Discount Bank and its controlling shareholders in August 1991 states:

(A) If there is concern of real infringement of the government's rights in connection with the shares held by the Safe Company, or the ability to sell them, the Safe Company will act, at the request of assets, to convene a general meeting of the Bank, and exercise the voting rights of the shares it holds as it requests assets.

(b) the assets have the right to order at any time that all bank shares held by the Safety Company (or those to determine assets) be transferred to it; When the shares are transferred, there will be assets entitled to exercise the voting rights that buy those shares.

2. An agreement signed in December 1991 with the controlling shareholders of the L.A.L.A. stipulates that the Safety Company and the controlling shareholders vote in general meetings of the Bank in accordance with the provisions of the government, to the extent necessary to prevent infringement of government rights or shares, or their value.

3. In an October 1991 agreement with the controlling shareholders of Bank Hapoalim, it is determined that if a controlling core of the bank is sold to the controlling shareholders, the government may instruct the Safe Company on how to exercise voting rights, if the government believes, in its sole discretion, that a decision that is up for a vote could infringe on the rights of the government or shares or the ability to sell them.

4. In the opinion of the State Comptroller, it was essential to include in all agreements the right of the government to instruct the safe companies how to exercise the voting rights granted by the shares in their possession, if, in its sole discretion, it is necessary to prevent a decision that violates the value of the shares or the rights of the government therein. As noted, even after comparing voting rights, the government will not have such a right to bank hapoalim, as long as no core control of the bank is sold. There's no justification for that either.

Had the same agreements included proper safeguarding mechanisms for the country's interests - and in a situation at the time it would not have been easier than that - the Treasury would not have had difficulties protecting the country's interests. It was the owner of the "hundred" who should have had the "opinion".

### Appointment of external directors

1. In agreements signed in the second half of 1991 between the government and the controlling shareholders of Discount Bank, Bank Hapoalim, B'BL and IGU Bank, provisions regarding the appointment of external directors by an independent public committee were established. In these agreements, the appointment of external directors has been linked to "the government's intention to continue its policy of non-interference in ongoing management... While expressing the public interest regarding [the bank's] shares." Agreements signed with Mizrahi Bank and its controlling shareholders did not stipulate that external directors be appointed at the bank.

Under these agreements, an independent public committee of the government - headed by a retired judge, along with a member appointed by the Governor of the Bank of Israel and a member to appoint the president of the Bureau of Accountants (hereinafter - the public committee) - will determine on the list the candidates for external directors at each of the four banks. The controlling shareholders of each will cause three of the listed names to be added to the bank's board of directors (in addition to the directors from the incumbent public by virtue of the membership ordinance). The controlling shareholders of each bank will be entitled to express "reasonable reservations about the matching of personalities on the list for office." If there is such reservation, the public committee will add other personalities to the list of candidates until three persons are found to have no reservations. In an agreement with Bank Hapoalim and the controlling shareholders, it is also determined that before formulating the list, the Committee will hear the position of chairman of the Bank's board of directors regarding the suitability of the proposed personality for the term, given the need to maintain teamwork on the board.

The appointment of external directors under these agreements will continue until a controlling core of John Doe Bank is sold, or until 31.10.93, according to the earliest of them.

In agreements with three of the banks in which external directors will be appointed - with the exception of Discount Bank - it is determined that a bank will not make a material business change[[22]](#footnote-22)

 But with the consent of a majority of external directors and directors from the public.

2. In the interim, the board of directors of each of the banks in the arrangement – as in a normal public company – was left with the power to determine the pay of its members and the wages of senior executives.

The Treasury Department's response to the State Comptroller's Office, from December 1991, stated that "good pay may attract good management powers to banks, and the benefits produced to the bank exceed the pay differences it would have added," had it reduced the pay of the directors and directors and the most senior executives.

However, it should be noted that the high pay conditions also apply to managers who were responsible in their time for regulating the shares and the crisis that followed.

In the opinion of the State Comptroller, it is difficult to see justification for the fact that throughout the interim, the board members of each bank have the right to determine their pay and the wages of the most senior executives. This issue should have been included in the list of the above issues - that decision-making by the board in which the consent of a majority of directors from the public and external directors is charged. A pity for the external directors, who are in the public interest of banks in a broad sense, who would not have ignored the need to pay adequate wages to attract good management powers.

### Bieskey Committee Report

1. Following the State Comptroller's report on the bank stock crisis, the Knesset's State Audit Committee decided, in January 1985, to establish a commission of inquiry to investigate the regulation of bank stocks and the crisis that followed. In the same month, the President of the Supreme Court appointed the Commission of Inquiry into the regulation of bank stocks (hereinafter – the Baysky Committee) in April1986, and the Committee submitted a report to the government and the Knesset's State Audit Committee. They were the only factor that resulted in the regulation of the shares." The committee also determined findings that raised suspicions that the banks and their managers had committed criminal offenses.

2. The Bisky Committee recommended that those who were the directors of the banks who regulated their shares no longer take management positions at the bank.

3. Some of the committee's findings and recommendations have something to do with the preparations for the sale of bank shares in the arrangement. Among other things, the committee pointed to the need to compare the voting rights of bank stocks and recommended that ways to reduce banks' control of the capital market (see below, p. 00 and 00).

Comparing the voting rights that banks' shares buy

and determining the processes for selling them

### Preliminary planning of the sale of bank shares

1. In January 1985, the Governor appointed the Supervisor of Banks to head a team (whose members included representatives of the three largest banks in the arrangement) to examine the main problems of the banking system, including the voting rights of banking stocks and the separation of businesses under the[[23]](#footnote-23) Banking (Licensing) Act, 5741 (hereinafter – the Banking Law).

In a preliminary report submitted by the governor in January 1986, it was proposed - given the large gap between the redemption value on which the government pledged and the value of the shares - to improve the shares by changing the capital structure of the banks, including changing the state of voting rights, and a streamlining plan to improve bank profitability.

The team also recommended reducing centralization in the banking system to increase competition there, primarily by separating medium-sized financial institutions from the large groups of banks that control them. He also recommended that banks limit their control of provident funds, engaging as brokers in the securities market, and advising on investment matters – areas where conflicts of interest may[[24]](#footnote-24)arise.

2. In June 1987, a joint team of the Ministry of Finance and the Bank of Israel submitted to the Minister of Finance and the Minister of Finance a summary of the discussions they held beginning in February 1987. The team recommended that legislation be used to compare the voting rights of the banks' shares in the settlement, and to sell to large investors and the public the shares that would be cashed in under the arrangement. The team also recommended that the settlement with the safe companies be revoked, and that the state directly hold all bank shares that Padionen would fund from state budget funds. It has been suggested that in the interim period, from the end of October 1988 until the government sells the shares it holds, the government will control the banks through directors appointed by the Minister of Finance and the Minister, while the previous controlling shareholders will be granted the rights of a special minority, until the end of the sale of the shares. The legislation will determine that the provisions of the laws regarding membership

Governments will not apply to banks during the transition period. The team recommended that a steering committee be established, whose members will be representatives of the Treasury and the Bank of Israel and public representatives, and this will establish a policy regarding the definition of the business units that will be sold (i.e.,

If the structure of the bank groups, such as by splitting them, and if so , should be changed, and in the case of the methods, pace and timing of the sale of the shares.

3. In May 1988, the Finance Minister appointed his deputy chairman of a joint steering committee, whose members are representatives of the Ministry of Finance and the Bank of Israel, and tasked her with preparing the infrastructure under which the rules for selling bank shares would be established.

The committee discussed several proposals made by the Ministry of Finance and the Bank of Israel in 1987-1988, particularly the proposal prepared by the Governor's Advisor in March 1988 and the achievements of this proposal written by the Deputy Finance Minister in April of that year.

In July 1988, the Committee submitted a document to the minister entitled "Lines for Negotiating Ownership of[[25]](#footnote-25)Banks".

(A) The Committee recommended that the objectives be set:

(1) Minimize the loss to the government as a result of the bank stock arrangement (i.e. achieve as high a price as possible in favor of the shares, given the other objectives as well).

(2) Act that control of each bank will be based on investment in the bank's capital.

(3) Keep banks stable by concentrating a sufficient number of shares in the hands of one party that will have a stable controlling core in each bank.

(4) Avoid government control of long-term banks as much as possible.

(B) These are the rules proposed by the Steering Committee for negotiations with the controlling shareholders of the banks: legislation must be prepared to compare voting rights, along with negotiating with the controlling shareholders in order to obtain the voluntary comparison of rights. A deal must also be negotiated with them in which the government will sell control of each of the banks a controlling core (such as 25%) and a controlling interest in each of the banks ." From the shares held by the safe company associated with that bank. In exchange for comparing the rights (apparently referring to voluntary comparison, without the need for legislation) the controlling shareholders must be given a discount in the share price at a very low rate (it is unclear whether the discount was intended only if the controlling core was sold to the controlling shareholders).

 from invoking the voting rights that the shares that will remain in its hands\*; These rights will only be expressed when the government sells the shares. If agreement is not reached with the controlling shareholders regarding the comparison of voting rights, the government will work to compare the rights by way of legislation. If by October 1988 no agreement is reached with the controlling shareholders of one of the banks, according to which they will acquire a core of shares, they will not have control of the bank, but the government will have to worry that control over the shares it holds will be operated in a business and professional way, in as short a transition period as possible, until a controlling core is sold to another body. Whether a controlling core would be sold to previous controlling shareholders or sold to another body, there was room, in the committee's opinion, to determine that any decisions on certain issues, which have a potential impact on the value of the remaining shares by the government and its ability[[26]](#footnote-26) to sell them, would be charged with the government's consent.

(C) The steering committee's recommendations imply a preference for selling controlling nuclear to existing controlling shareholders (if a reasonable price is agreed).

According to the findings of the Biski Committee report (published two years before the steering committee's recommendations were written), bank managers brought about an undermining of the stability of the banks, and the committee's report presented findings that raised alleged suspicions that the regulation involved criminal offenses.

The controlling shareholders of the banks appointed the board members of the banks, who appointed the directors of the banks responsible for regulating the shares, and those boards of directors had the responsibility to oversee the operations of the managements. The committee noted (p. 367) that even after the crisis, the controlling shareholders of the banks allowed the managements responsible for regulating to continue their positions, Despite their failure, thecommittee also voted that some controlling shareholders - who had influence or control over the operation of regulation and access to insider information about the thy owning - had a financial interest in regulating the shares; and that some bought and sold shares of considerable scale at various times during the thylosing period (pp. 80-82).[[27]](#footnote-27)

Against the backdrop of these findings by the Baysky Commission,the steering committee's preference for selling control nuclei to existing controlling shareholders is puzzling.

(D) The document implies that the committee believes that a controlling interest should be attempted and sold to another body only if no such agreement is reached with the controlling shareholders. Although one paragraph mentions the possibility of selling shares to other entities, including foreign investors, it implies that it is a share sale of the scope

Less than the planned scope of a minimum control core (25%); Among other things, to help the government set a scale for the price worthy of requiring the controlling shareholders for the shares offered by the government.

During steering committee discussions in 1988, a world-famous banker informed the finance minister and acting prime minister that he wanted to acquire a controlling core at one of the banks in the arrangement. The Finance Minister replied that the government intended to sell the banks' shares by way of competition, which he would also be able to participate in.

In January 1989, the Chairman of Assets informed the Finance Minister and the heads of the banks in the arrangement that "the previous Finance Minister has concluded that the proper way is to cope, with the existing controlling shareholders allowed to participate in it."

Since the role of selling bank shares was imposed on it, assets have worked to realize the principles set out by the Finance Minister and the Legal Advisors of Assets. It offered for sale in nuclear dealing control of three of the banks in the arrangement; The proposals were made in public appeals to those interested in the force. However, assets have encountered many difficulties in implementing these principles, mainly because of the objections of the controlling shareholders of the banks (see below). The ongoing confrontation over this principled problem, in its various aspects, is probably one of the main reasons for the great delay in preparing for the sale and sale of bank shares. By the end of the review, only one controlling core had been sold (IDB Holdings shares, in August 1991); Despite the efforts of the Ministry of Finance and assets to sell the controlling core in a competition process, They finally complied with the demand of the controlling shareholders to sell them in a negotiation process, without competition, as part of a deal that was also determined by the requirements of the controlling shareholders (see below, p. 00; regarding the competition processes operated by the Ministry of Finance and assets for the sale of controlling cores of the Eastern Bank and the sale of a minority of general bank shares, see below, p. 00 and 00).

(E) In the Treasury Department's files and property files, no document was found indicating that an appropriate party in the firm had approved or adopted the recommendations of the Steering Committee. However, a letter written by the Chairman of Assets to the Finance Minister in May 1989 indicates that the previous Finance Minister approved the committee's recommendations.

(F) The steering committee document also states that representatives of the Bank of Israel raised three issues requiring preparation for negotiations with the controlling shareholders, and they recommended:

(1) Schedule the negotiation stages in advance and to trigger the choice of legislation.

(2) Determine the government's patterns of involvement in controlling banks, if agreement is not reached within a reasonable time in negotiations with the controlling shareholders. To ensure

 Professional management of banks without foreign considerations, it was suggested to consider establishing public trusts or appointing directors by a professional and non-political body.

(3) To examine the fragmentation of the banking groups, each to several business units – banking and non-banking – in order to increase competition in the financial and capital markets, and to improve the chances of selling a controlling core in each bank (regarding the issue of the splitting of the bank groups, see below, p. 00).

The steering committee did not adopt these recommendations of representatives of the Bank of Israel.

### M.I. Property Company

1. M.I. Properties Ltd., is a wholly owned company of the government. It was founded in 1969 according to the government's decision, in which it was determined that the company's goal would be "management and ownership of assets that were granted to the state for various reasons and that the state intends to transfer them in due course into other hands."

2. In November 1988, the former Deputy Finance Minister became chairman of the Board of Assets, and the Finance Minister tasked the company with advising him on matters related to the banks' shares and sale, and to handle various aspects of the sale proceedings. In January 1989, the government and Assets signed an agreement establishing the functions of assets - to provide consulting services and to perform the tasks agreed upon.

3. At the beginning of the company's handling of the sale of bank shares, in November 1988, two public representatives (including the chairman) and four senior Treasury officials called on its board.

In January 1989, three other public representatives were added to the board, so the number of members was nine, of whom five were public representatives. In November 1991, a male exchange was made on the Property Board. Among other things, three public representatives were appointed, including chairman and general manager. In November 1992, two public representatives and four senior Treasury officials called on the board. In addition, he serves on the board of directors, as with any government company, a representative of the Government Companies Authority, who does not have the right to vote.

4. The company employs a general manager and deputy general manager (until October 1991 the company did not employ a general manager). At one time, an employee was employed under a special part-time contract, and he concentrated the handling of the sale of two of the bank groups.

5. The Legal Advisor of the Ministry of Finance is a member of the Board of Assets and also the company's legal advisor. In order to perform its tasks, assets are occasionally assisted by external legal advisors and other professional services.

### Comparing the voting rights of bank stocks

At the opening of negotiations on this issue in 1988, each of the controlling shareholders of the banks in the arrangement argued that comparing the voting rights of the shares held by the safe companies - which are expected to be handed over to the government - with the rights of the controlling shares in his hands, was nothing more than an expropriation of his own rights, and in violation of the original arrangement signed between the government and the safe companies, in which nothing was said about changing voting rights.

The controlling shareholders opposed comparing voting rights by way of legislation. However, they agreed, at various stages of the negotiations, to discuss comparing the rights, to try and reach an agreed solution, without legislation.

In September 1988, the Treasury's legal advisor submitted an opinion on this matter, In it, she recommended that the finance minister and his deputy take action to compare the voting rights of bank stocks.

The opinion, "They are certainly not entitled to any prize in the form of granting compensation for disennchising them." She also noted that it is expected that the government will sell the shares that Padionen will fund. In order to achieve as good a price as possible, thereby reducing the loss it will incur because of the arrangement, it is necessary for government-held shares to have full voting rights.

It should be noted that there was another reason that justified a demand to compare voting rights without compensation to the controlling shareholders: many of the shares that give inferior rights, which the government funded "padionen," including the sharesof Nostro, ordered and their birth in the sin of regulation. pp. 328-329), due to the inferior rights granted by ordinary shares, banks at the time, during the period of stock regulation, were able to issue them in bulk without prejudice to the full control of the controlling shareholders; whereas it was the manipulative regulation that enabled them to issue to the public the same shares "thanks to" the artificial returns that the banks' shares generated during the thyme, which caused the public to ignore, among other things, their inferiority.

### Negotiations on comparing voting rights with controlling shareholders from March 1988 to January 1989

In March 1988, a team headed by the Deputy Finance Minister, appointed finance minister, began negotiating with the controlling shareholders of IDB; At the time, they were the only ones among the controlling shareholders who expressed willingness to discuss comparing voting rights, along with the sale of shares held by the safe company to the controlling shareholders.

During the negotiations, the controlling shareholders demanded compensation of 9% of the company's value for comparing the rights, and determining a sales process in the format they proposed,

 That would have allowed them to acquire a controlling core in the IDB without much competition. The negotiations did not yield an agreement.

In December 1988, the Ministry of Finance issued a memorandum comparing voting rights in the shares of banking corporations,5748 -1988. The shares cashed and the shares that will be cashed, according to the arrangement, with state budget funds, will be transferred to the state's ownership (and will not be held in the interim by the safe companies established by the banks), or to the ownership of a holding company appointed by the government for this purpose.

In January 1989, the controlling shareholders of the banks made several suggestions before the new finance minister that the government would sell, unmatchedly, a controlling core of each of the banks to the existing controlling shareholders (some of them - in conjunction with investors they would choose). At the same time, the controlling shareholders of some of the banks expressed willingness to slightly increase the voting rights of the shares held by the government, but only at the time of the sale of the controlling core as stated.

In February 1989, the Minister of Finance directed the assets as follows:

(A) Act quickly to compare rights and sell the shares, because losing time is a loss of money.

(B) Comparing consensual rights is preferable to legislation, although the minister does not rule out legislation.

(C) The sale of the shares must be negotiated not only with the controlling shareholders, but also with other interested parties, who will compete with them.

(D) Try to sell Union Bank and IDB first. For this purpose, negotiations with the controlling shareholders of these banks must begin immediately.

In February and March 1989, the controlling shareholders of most banks expressed agreement to fully compare rights, but demanded, among other things, that they be given full compensation for the value of their preferred voting rights. Because it is a gesture in favor of cooperation that will prevent the need for legislation and save time, not compensation for the economic value of voting rights.

During the negotiations, which held assets with the controlling shareholders of each of the banks in 1989, it rejected all the demands of the controlling shareholders to sell the shares to them without competition and give them compensation at the rate they demanded. However, from the course of negotiations and memorandums of principles signed between assets and the various controlling shareholders in late 1989 and early 1990, it can be learned that later in the negotiations, the Ministry of Finance and assets were actually complied with by the controlling shareholders' demand to include substantive matters related to the process of selling bank shares.

In March 1991, a chairman of assets explained to the State Comptroller's Office that Assets had agreed to some requirements of the controlling shareholders - not the controlling shareholders of IDB not to split this group - given the Treasury Secretary's approach that the rights should be compared by way of consent, rather than through legislation.

In March 1989, the Knesset received a prefabricated reading, with the consent of the Deputy Finance Minister, four private bills comparing voting rights in the banking corporations, and were passed to the Finance Committee for discussion. The proposals are mostly similar to the bill memorandmon prepared by the Treasury Department in December 1988.

In May of that year, the Director General of the Ministry of Finance submitted to the Finance Minister a document regarding the handling of the shares of the banks in the arrangement, which he said was formed in discussions between representatives of the Bank of Israel, headed by the Governor, and representatives of the Treasury, without the participation of a chairman of assets. In this document, it was proposed, among other things, to give the controlling shareholders the first right of refusal in the sale proceedings of the controlling nuclear[[28]](#footnote-28) banks. The Bank of Israel informed the State Comptroller's Office in April 1991 that the Governor had not been complicit in the preparation of the document, and that the proposal to give the first right of refusal was solely on the opinion of the Director General of the Treasury.

In response to this document, the Chairman of Properties protested in a may 1989 letter to the minister that the document had been formulated in discussions that took place without his participation and without his knowledge. The Chairman of Assets also noted that the proposal in the document to give the first right of refusal to the controlling shareholders is contrary to the minister's decision in a discussion he held with the CEO and chairman of properties a few days earlier. According to a report by the Chairman of Assets to the Board of Directors, the Minister decided that the document submitted by the CEO would not be considered as a document acceptable to all as the basis for discussion, and that the controlling shareholders would not be given the right of first refusal.

In the same month (May 1989), the Governor of the Bank of Israel, the Legal Advisor of the Ministry of Finance and Chairman of Assets to the Minister of Finance, recommended that the legislative process be promoted to compare rights, even as a means of negotiation.

During the months of May - September of that year, the Ministry of Finance made two attempts, which did not go well, to reach agreement with the Treasury of Settlement

 The Jews, regarding the comparison of voting rights and the sale of controlling nuclear, regarding bank leumi shares, and with Bank Leumi - regarding the shares of a union bank.

In June and July 1989, the Chairman of Assets and its Board of Directors recommended that the Minister of Finance set a short period of time after which the government would initiate rights comparison legislation in those banks, for which assets would not reach agreement with controlling shareholders regarding equal rights.

In July of that year, the Finance Minister informed the controlling shareholders of Bank Iguod (Bank Leumi) that if they did not announce a comparison of rights within a week, he would submit a proposal to the government for legislation on this issue.

In early September of that year, the General Assembly of a union bank convened and decided on a partial and suspended equal rights, which is fundamentally different from that demanded by the minister; According to the decision, the rights will be compared by a national bank refraining from using its basic shares. The decision will take effect only after the government sells all the shares it has.

An external property legal advisor recommended that you not be satisfied with comparing rights in this format because recognizing these terms would be considerably inferior to a sale after a full and immediate comparison of rights.

In November 1989, along with the government's discussions of the bill, assets, according to the Finance Minister's directives, negotiated with B'L.L. regarding the proposal of the Chairman of the Board of Directors of L.A.L. to compare consensual rights in the bank.

Binding only, and determining an agreed and joint process for selling the bank's shares. In December 1989, this negotiation ended in disagreement.

Since negotiations between assets and controlling shareholders in each of the banks in the arrangement were at an impasse, in October 1989, the Ministry of Finance prepared a draft law comparing voting rights (banking corporations),5749 -1989, which is primarily similar to the December 1988 memorandum of law.

At a meeting of the Knesset Finance Committee dated 10 March 1990, in which the committee approved the memos signed with the controlling shareholders of IDB and Bank Hapoalim, the committee recommended that controlling shareholders who do not sign until 31.1.90 receive no compensation for comparing the rights.

### Bill to compare voting rights

On 23 January 1990, the government placed on the Knesset table the bill for comparing voting rights in banking corporations (order of the hour), the 5770 - hereinafter - the bill).[[29]](#footnote-29)

1. The principles of the bill are similar to those in the draft law from October 1989, and these are the main objectives of the law, as set out in the proposal:

(a) to impart equal voting rights to shares, in order to reduce the cost of the arrangement and create a match between voting rights and investments in companies' capital, so that effective oversight of their managements is guaranteed.

(B) Allow the government to sell the shares purchased by the safe companies in accordance with the arrangement, on the best terms and as soon as possible.

(C) To regulate the ways of selecting directors during the transition period in a way that ensures the stability of the banks and their professional and proper management.

(D) Allow structural changes to be made to the banking system to increase competition there.

2. The bill stipulates that during the sale period of Bank Doe, the General Assembly is entitled to take away from the Board of Directors the power to decide on the sale of shares owned by that bank. This section of the bill is intended to enable the government to pass decisions at the General Meetings of banks that will see it as necessary to change the structure of the banking system and to recognize the banking groups in the best way for the government.

3. The explanatory notes to the bill stated: "It is proposed that the banks continue to operate as private business entities for everything."

4. In practice, the government did not seek to bring up the bill for the first reading in the Knesset. The Treasury Department explained to the State Comptroller's Office in December 1991 that it considered the bill "only a last resort of disagreement," because the proposal "included transferring control of banks to the government," with all the negative consequences that might have been, as explained above.

5. In obtaining this answer from the Ministry of Finance, the State Comptroller's Office remarked that the bill submitted to the Knesset did not involve government control of the banks or government involvement in their management.

In the opinion of the State Comptroller, it was appropriate that a clear distinction be made between the government's involvement in bank management and the creation of a semblance of nationalization - which the Treasury decided to avoid, according to the above considerations - and the government's ability to maintain the country's interests in stocks and their sale in a proper and optimal way, at its sole discretion (including in the matter of fragmentation). While it is possible to understand the approach that is swayed by avoiding legislation, it is not at all costs. There are red lines that should not be crossed and in the absence of agreement from the banks the government had to turn to legislation.

### Detailed memorandums of principles and agreements to compare voting rights by consent

In mid-December 1989, towards the end of the Ministerial Committee for Legislative Affairs' handling of the Draft Voting Rights Comparison Act, the controlling shareholders of IDB and Bank Hapoalim, each separately, informed the Finance Minister that they were ready to negotiations to compare rights without the first refusal right.

##### IDB Holdings

**Memorandum of** Principles: At the end of December 1989, a memorandum of principles was signed between assets and the Ministry of Finance, and the controlling shareholders of IDB subject to the approval of the Minister of Finance, the Knesset Finance Committee and the Board of Assets.

According to the memo, the controlling shareholders pledged that the voting rights of all types of IDB shares would be fully changed within 45 days of the memo's approval. In return, the controlling shareholders will receive 3% of the company's shares.

Here are the highlights of the memo:

1. A controlling core will be sold at a rate between 25%and 51%- within 30 days of the memo's approval.

Limiting the controlling core soldto 51%- there was a compromise between therequirement of the controllingshareholders to limit it to -26% and the desire of assets to avoid any restrictions.

2. The purchaser of the controlling core will be able to sell to the public and IDB employees some of his shares within six months of the date of purchase, provided he continues to hold at least 26% of IDB's share capital. At the same time, assets will be prevented from selling IDB shares (avoiding this should make it easier for the controlling core purchaser to sell some of his shares in the market at a relatively high price).

3. If the controlling shareholders do not win the contest, they will be entitled to sell the government their share of the IDB, in whole or in part (depending on the size of the nucleus sold).

4. The group will be "sold as it is today." This section means that IDB Holdings - which mainly includes Discount Bank and investment firm IDB Development - will be sold without splitting (see below, p00).

5. If there is a single candidate for the acquisition of the Group, assets will be signed in good faith in order to reach an agreement to sell the controlling core.

6. The kernel of control will be offered in a public appeal to those interested.

7. Assets will examine the competency of each applicant according to established agreed standards, and these are the main principles:

(a) knowledge and experience in the business sectors in which IDB is invested; (B) The candidate's contribution to the group's business stability, among other things, his ability to manage the entire group in a proper and stable manner; and its ability to maintain a normal working relationship with employees; (C) The non-existence of conflicts of interest between IDB's business and the applicant's other businesses. If necessary, you will receive assets from the applicant with appropriate liabilities and collateral to avoid conflicts of interest.

Assets will give IDB the option to make its comments on this matter, but the assets will have the final authority to decide on the question of the competency of the applicants, subject to their approval by the Bank of Israel.

8. The sale of the controlling core will end at the end of five months from the approval of the memo (the memo has an estimated timetable attached).

9. Upon approval of the memo, IDB will result from the list of companies to be included in the voting rights comparison bill if such a proposal is submitted for approval by the Knesset. However, if the controlling shareholders violate a major clause in the memo, IDB will be included in the bill unless the violation is not corrected, after giving notice and an adequate opportunity for regulation within a reasonable period of time.

10. IDB will provide any information and cooperate with the entities that assets authorize to evaluate the Company and prepare a brochure and prospectus, subject to the Bank of Israel's confidentiality guidelines and the provisions of the Securities Law,1968.

At the board of assets meeting, which took place three days after the memo was signed with the controlling shareholders of IDB, reservations were raised about the pledge to sell IDB in one piece. One member of the team negotiating with the controlling shareholders explained to the board that the pledge to sell IDB in one piece was given only to the controlling shareholders of IDB, and that this memo would not serve as an example to the other banks. The board approved the memo unanimously, after which the Finance Minister and the Knesset Finance Committee also approved it.

From January to May 1990, negotiations took place between assets and controlling shareholders to formulate the memorandum of principles for a detailed agreement. During the negotiations, assets did not meet that the controlling shareholders would fulfill their obligation to compare the voting rights of the company's shares at the date set forth in the memo, and in practice they did so only after the signing of the detailed agreement.

In March 1990, Property received an opinion from an external legal advisor regarding the draft agreement with the controlling shareholders of IDB. The advisor noted, among other things, that in the draft agreement, clauses that give the controlling shareholders an advantage or a preferred starting position over other bidders. He also noted that the failure to charge the controlling shareholders to allow candidates to do an in-depth examination (known as " due diligence" thatwas promoted

") of the group's business situation - contrary to accepted practices in this special market - gives the controlling shareholders a significant advantage in the tender; they purchase a property in certainty conditions, while the other bidders purchase it under uncertainty conditions, and must deduct from the sum of their offer the risk premium they undertake by the way of the bank's acquisition.

In summing up his remarks, the advisor noted:

"From every angle of view we will look at the draft agreement, the position of the contestants in differential starting positions creates a shameful situation... I would recommend in every tongue of recommendation to make every possible effort to remove this failure and put the tender procedures on equitable, simple and publicly hygienic stripes. In another language, the principles upon which the draft is based deserve a rethink, and in my opinion a thorough overhaul."

However, the final agreement signed by assets is very similar to the draft mentioned above, and none of the deficiencies voted on by the advisor have been corrected.

It should be noted that in an August 1991 agreement under which the government sold control of IDB to the previous controlling shareholders, it was determined that anyone with assets would confirm that they[[30]](#footnote-30)were a serious candidate to acquire control of Discount Bank, And that the Governor of the Bank of Israel has confirmed that he is fit to purchase control of the bank, he will be entitled to appoint an evaluater to perform a "due diligence" examinationon his behalf regarding the bank's business situation, subject to certainrestrictions.

**May 1990 Agreement: In May 1990, an agreement was signed between the Government of Israel and Assets and Israel Financial Holdings Ltd. (which is the controlling shareholder** of IDB), IDB Safe (1983) Ltd., and IDB (hereinafter - the Agreement from May 1990).

An examination of the terms set forth in the May 1990 Agreement compared to those set forth in the Principles Memorandance indicates that in some matters, assets agreed to the terms in which they could add benefits to the controlling shareholders. However, add in the Article 16 Agreement, which states:

"If it becomes apparent to the assets at the time of the sale or before it or during the sale process that the share package cannot be sold at that time under conditions that it believes are reasonable and appropriate by the government, assets may determine that the sale will be postponed to another date and will be carried out in a process that is as similar as possible to the sale process in the agreement, in those changes that will be required as a result of the accumulated experience and the change of circumstances, and on equal terms regarding all applicants, as determined by all applicants, as determined by the applicants.

after consultation with the controlling shareholders; Or that the shares or options for purchasing them will be offered to the public according to a prospectus on time and conditions that you determine assets."

Among other things, the agreement states that:

1. In addition to E.D.B. being sold without splitting (as agreed in the Principles Memorandum), no priority will be given to those who offer to split it after purchase.

2. The right of the controlling shareholders of IDB (set forth in the Memorandum of Principles) to sell their shares to the government at a price per share, under which the controlling core will be sold, if they do not win the contest, will be taken into account when comparing their offer to any other offer made by a John Doe bidder.

It should be noted that the option granted to the controlling shareholders according to the memo was a considerable benefit because it was expected that the price per share to be determined at the time of the sale of a controlling core would include a "control premium" (the additional price - above the price of the relative portion of the company's shares - which can be expected when selling control of the company); Therefore, the price the government would have to pay the controlling shareholders if they exercised their right was expected to be higher than the price at which the government could sell the same shares in the capital markets.

It was expected that assets would have to consider the proposals, among other things, by the scale of the net proceeds the government would receive in favor of a controlling core of a certain size. According to the condition added, as stated in the agreement, assets will be required to take into account in this consideration that if another candidate wins, the government may be required to use the proportional portion of the proceeds from the sale of the shares to finance the purchase of the shares from the controlling shareholders (as noted, at the same price per share at which the shares were sold to the purchaser of the controlling[[31]](#footnote-31)core).

Because of these conditions, a situation could arise that the controlling shareholders' offer would be accepted even when another candidate offered to purchase a controlling core of the same size (in percentage of the share capital) at a price slightly higher than that offered by the controlling shareholders. This is because assets will have to be taken into account that if you accept the other candidate's offer, and if the controlling shareholders sell her their shares at the price at which the shares were sold to the purchaser of the controlling core, she will have to sell those shares in the capital markets, and will likely get a price in Aden below the price she paid the controlling shareholders. Consequently, the total proceeds from the sale of the shares will be lower than that received from the sale of the controlling core to the controlling shareholders at the price they offered.

It should also be noted that since every offer, including the controlling shareholders, was allowed to bid for a purchase of up to 51% , the controlling shareholders of ID were allowed to purchase

Bea, who already held 9%, willoffer to purchase over 42% in order to have a share and be the largest nuclear acquisition offer; this is given that if the company is sold to the other bidder, the previous controllingshareholders will be entitled to sell their shares to the government.

3. Only existing controlling shareholders, if they win a contest to acquire a controllingcore, [[32]](#footnote-32) grants the agreement the right to benefit from "market clearance".

This condition could have made it easier for controlling shareholders (but not another candidate) to offer to purchase a higher proportion of the shares, knowing that they would then be able - due to exploitation of the "market clearance" - to sell some on relatively favorable terms.

4. IDB will prepare a document that will be similar in shape and scope to the prospectus, and it will be delivered to applicants approved by assets and the Bank of Israel. Applicants will also be able to request information beyond the prospectus.

5. IDB will transfer to property evaluator the material they need to assess the bank's value and subject to confidentiality arrangements as determined by the Supervisor of Banks. Such information will be confidential by the evaluator, while the assets will only be evaluated, if requested; The data confidentiality will be valid even if they are the only challenger to the IDB. Assets' relationships with the evaluator should have actually been reduced to discussing the assessment methods taken. It emerges, therefore, that assets tied itself to an assessment as is without being given the opportunity to study in depth and criticize the work[[33]](#footnote-33)of the evaluaters. Especially since it applies even if the contest ends in negotiations between assets and the previous controlling shareholder in IDB as a single bidder, equipped with maximum information about the company and the bank.

In the opinion of the State Comptroller, the conditions set forth in the memo and the agreement, as detailed and explained above, were to give the controlling shareholders of IDB benefits of considerable economic value, in addition to the 3% of the company's shares, which the controlling shareholders received in exchange for their consent to compare voting rights. In all these benefits, it was to give the controlling shareholders of IDB priority in the run-up to the acquisition of the controlling core, and this may even have been to discourage candidates by force from participating in it.

The memorandums of principles signed by the Ministry of Finance and assets with the controlling shareholders of the other banks in the arrangement in January - February 1990 - as well as the detailed agreements they signed between 1990 and 1991 are markedly similar to the memorandum and agreement signed with the controlling shareholders of IDB, Somewhat, however, the conditions set forth in the memos and agreements with the controlling shareholders of the other banks were because of an improvement, in terms of the state's interest, relative to what was set forth in the December 1989 memo and the May 1990 agreement with the controlling shareholders of IDB. In an agreement to sell a controlling core in IDB to previous controlling shareholders in the same company, signed in August 1991, provisions were set out to protect the state's interest in Discount Bank shares, and similar provisions - in some differences - were included in agreements subsequently signed with the controlling shareholders of the two largest banks and a union bank. However, in all memos and agreements, the influence of the controlling shareholders on the design of the sale processes is evident, reflected in the imposing restrictions on the government's freedom of action and discretion in the sale of the[[34]](#footnote-34)shares.

In the opinion of the State Comptroller, there was no room to include in the memos and agreements any condition that would allow the controlling shareholders to participate in shaping the sale process or to shred the government's discretion and freedom of action in selling the shares whose purchase was fully funded from the state budget.

##### Parties signing the Memorandums of Principles

In each of the memos signed with the controlling shareholders of the banking corporations, there are also obligations imposed on the corporation itself, as opposed to its controlling shareholders - such as a commitment to provide information, or a commitment by the corporation to agree to a split.

In June 1990, Assets informed the State Comptroller's Office that the liabilities of the banking corporations would be enshrined in detailed agreements between them and assets. In fact, however, the anchoring of these obligations in detailed agreements involved quite further and protracted negotiations: regarding three of the banks in the arrangement - until the last quarter of 1991.

In December 1991, the Ministry of Finance explained to the State Comptroller's Office that it had seen room to engage in negotiations first with the controlling shareholders, on the issues under their responsibility (especially comparing voting rights), and then - with the banks, on the issues under their responsibility (especially cooperation in the process of selling and providing information).

In the two-step negotiation format, It was determined in each of the principles memos that the memo would not include the same bank in the legislation, if any, to compare voting rights.

### Compare the actual rights

The memorandums of principle signed with the controlling shareholders of IDB and Bank Hapoalim took effect on 10 March 1990, those signed with the controlling shareholders of the B'Al and the Eastern Bank – on 13 March 1990. In practice, the voting rights that the shares buy late were compared: on IDB on 29 September 1990, over three months late; At Mizrahi Bank – on 24 September 1990, about five months late; Bank Hapoalim – on 1 November 1991, over 20 months late; And B'Al and The Union Bank (included in the Bala'l memo) – on 15 December 1991, more than 19 months late.

Sale of control of IDB Holdings

### Agreeing to sell the company as a single piece

IDB Holdings is the parent company of Discount Bank and investment firm IDB Development. She held about 66% of Discount Bank's shares and74% of IDB Development's shares.

Had the government had the authority to split the IDB Group and sell its various parts separately, at its discretion, the two sister companies could be sold separately. Other bank-controlled financial and banking companies are all trending towards achieving optimal results for the government.

A separate sale of IDB Development could have increased the number of bidders for its acquisition and improved the government's chances of receiving a higher return from the sale. Acquiring control of the Bank requires compliance with the Bank of Israel's strict conditions for permits, and this reduces the number of applicants, partly because some applicants by force to purchase the non-bank corporations cannot meet the same conditions or do not want to be exposed to the careful scrutiny of the supervisor of banks. , reduce the number of investors who could or would like to compete for the acquisition of a controlling core in the entire group compared to the number of potential candidates to purchase parts of it.

It should be noted that a separate sale of the two sister companies should not have prevented the previous controlling shareholders from acquiring a controlling core in each, and kept the entire group in their entirety.

In a discussion with properties in March 1989, the controlling shareholders announced that they wanted to acquire control of the group in its entirety, without splitting.

In the Treasury Department's files and property portfolios, there is no document indicating that the need to examine, with the help of the Bank of Israel or other bodies, the importance of splitting the group, and determine whether the split should be met, contrary to the stated wishes of the controlling shareholders. An examination of this issue was necessary, among other things, to present to the Finance Minister the implications of the choice between relinquishing control of this issue and needing legislation to achieve the comparison of rights.

When the controlling shareholders announced in December 1989 that they would refuse to sign the equal rights agreement if it was not guaranteed that the group would be sold as a single piece, Assets informed them that it had no position on this matter, subject to guidelines issued by the Bank of Israel and the Knesset Finance Committee.

In the opinion of the State Comptroller, it was appropriate that decisions on this issue, which had material effects and results financially and in principle, would be made after properly orderly and documented consultation.

In the Memorandum of Principles, signed on 31 December 1989, it was agreed that the group would be "sold as it is today," i.e. without splitting. In the absence of a defined position of its own or that of the Treasury department in this matter moving to the signing of the memo, Assets decided to comply with the demand of the controlling shareholders.

However, on the same day, prior to the signing of the memo, the Chairman of Assets held a telephone consultation on this matter with the Governor of the Bank of Israel and the Supervisor of Banks. After this consultation, Properties signed the memo with the controlling shareholders. After the fact, disagreements were discovered between the Bank of Israel and assets regarding the positions presented by the Governor and the Supervisor in the telephone conversations: on 7 March 1990, the Governor announced in a letter to the Finance Minister that, in the aforementioned consultation, the Bank of Israel objected to the sale of IDB in one piece. On the other hand, the Chairman of Assets claimed, in a letter to the Finance Minister on 25 January 1990, that he had explained to the Governor and the Supervisor that the negotiations would end in disagreement if he was not included in the non-splitting memorandum, and they did not advise him to refuse to sign the memo under the circumstances.

An assets chairman explained to the State Comptroller's Office in March 1991 that the advice of the governor and supervisor, as he understood it, matched their position according to the document presented by the Director General of the Ministry of Finance to the Finance Minister in May 1989 (see above); And that the chairman of the negotiating team on behalf of properties asked the supervisor, in a hearing before the memo was signed, if he opposed the sale of IDB without even splitting even at the cost of "blowing up" the negotiations, and his answer was that negotiations should not be "blown up."

At a hearing held at the Knesset Finance Committee in January 1990 to approve the memorandum of principles with the controlling shareholders of IDB, the Supervisor of Banks explained the Bank of Israel's position that in the process of selling the banks it was also advisable to increase competition in israel's banking system, so the Bank of Israel disapproves of the sale of IDB in one piece. However, the supervisor of banks did not recommend that the committee not approve the memo.

In the memo and agreement with the controlling shareholders of IDB, as noted, I will die.

A measure to examine the competency of candidates to purchase the group, among them - knowledge and experience in the business sectors in which IDB is invested, both in the real and banking sectors.

In response to comments made by the State Comptroller's Office regarding the possible consequences of agreeing not to split IDB, the Chairman of Assets to the State Comptroller's Office announced in March 1991 that Assets expected a "quantitative return" in favor of agreeing to sell IDB in one piece.

It is unclear what the Chairman of Properties relied on in this expectation (see also below, p. 00).

### Unmatched negotiating sale

1. Following the May 1990 agreement, a special meeting of shareholders of IDB Holdings decided, at the end of that month, to compare the voting rights that the company's shares give. Discount Bank also decided to compare the voting rights of the bank's shares. As a result, the process of selling a controlling core in IDB began. The agreement includes, among other things, a timetable that determines each stage of the coping process for a short and binding period of time. According to the agreement, no assets were entitled to change the schedule except with the consent of the controlling shareholders, and those interested in participating in mole dealings had to announce their desire for the assets, within 75 days of the publication of the application of assets to interested parties, and to deposit $10 million with the General Accountant; the interested party was also required to fill out a detailed questionnaire on its business data.

2. At a property board meeting in September 1990, eight days before the deadline to apply to participate in the contest, a director on behalf of the public proposed postponing the deadline due to the situation in the Persian Gulf in those days and the uncertainty that prevailed in the global economy; But his offer was not accepted.

The first company to apply for the assets, and even deposited as required, was Al-Am Financial Holdings (Migdal) Ltd., established in June 1990 to acquire a controlling core in IDB as a single target; the company (hereinafter - the controlling shareholder company) established El-Am Anyaim Ltd., and other companies controlled by the previous controlling shareholders in IDB, and other shareholders in these companies (see this matter).

Two days before the deadline, the chairman of the properties knew of three interested parties, in addition to the controlling shareholder company, who announced their desire to participate in the contest. In about 24 hours, however, they all announced one by one that they were recanting their intention to participate, and that the reasons were the situation in the Persian Gulf in those days and the failure to split IDB.

The day before the deadline, the Investment Bank - which it rented assets to help it with some issues related to the sale process - recommended that the deadline be postponed.

In light of the situation created by the avoidance of those interested in participating in the contest, the Chairman of Properties requested an opinion from an external legal advisor. According to the legal opinion she received, the assets had no grounds to postpone the date, since - in light of the Supreme Court's verse halacha - tensions in the Persian Gulf are not, in his opinion, "thwarted."

In February 1993, in response to an appeal by the State Comptroller's Office, the Ministry of Finance announced that, in consultation with several members of the Board of Directors of Assets with the External Legal Advisor, the advisor noted that since the terms of the agreement had been considered that the number of bidders would be small, or that there would be only one (controlling shareholder company), it was difficult to stop the process of dealing based on Article 16 of the agreement, which allows the assets and the government to stop the sale process, if they see that they cannot. , and resume the process in a similar format, with the changes that will be required in light of the accumulated experience. Therefore, the process must also be conducted with one challenger. Only if negotiations become apparent that the core of control cannot be sold on good terms will there be room to consider using Article 16.

3. At the deadline for applying, a group of overseas investors (who were not among the three said interested party) announced that it would participate in the contest, depositing $10 million in the General Accountant. The Group (hereinafter – the Overseas Investors Group) informed the Chairman of Assets that its partners in acquiring the controlling core are large investment banks in the U.S. and Canada.

In October 1990, the Property Board approved the controlling shareholder company and the group of overseas investors as candidates in the contest, referring the group of overseas investors to the Bank of Israel in order to obtain a permit to acquire control of a banking corporation under the Banking (Licensing) Law, 5741 (hereinafter - the Banking (Licensing) Act).

In November 1990, during discussions at the Bank of Israel requesting a permit from a group of overseas investors, the Group informed the assets that it was struggling to recruit investors, and therefore requested a three-month extension to allow it to recruit more investors. In December of that year, Assets rejected the request, and the overseas investor group decided to withdraw its application.

In March 1990, the Supervisor of Banks informed the Chairman of the Board of Directors of Discount Bank, based on the opinion of the Bank of Israel's legal advisor, that the holders of the permit would not need a new permit if they purchased shares held in the safe company from the government.

In May 1990, a ruling was issued in the High Court of Justice, which ruled, among other things, that the Attorney General's decision not to prosecute the banks and bankers because of the lack of a "public interest" was void, and that the matter would be returned to the Attorney General, in order to decide whether there was alleged evidence of the prosecution of the banks[[35]](#footnote-35)and bankers.

 The state indicted the banks that at the time regulated their shares and against the executives responsible for regulating, including the chairman of the board of directors of the controlling shareholder company IDB. The indictment attributes to him, in his past role as chairman of Discount Bank, criminal offenses in the banking and securities sector.

That same month, the Chairman of Assets contacted the Governor of the Bank of Israel and asked him to determine whether to continue to see the controlling shareholders in IDB as having a permit even after the indictment of the chairman of the board of directors of the controlling shareholder company.

In January 1991, the Governor of the Bank of Israel recommended that the Minister of Finance, given the severity of the indictment against the chairman of the controlling shareholder company, refrain at this time from selling the controlling interest to the company.

In February 1991, following the Governor's letter, the Finance Minister asked the Chairman of Assets to pause the sale process for a while. That same month, the Ministerial Committee for Economic Affairs decided, at the suggestion of the Finance Minister, that the government was obligated, under the May 1990 agreement, to negotiate with the controlling shareholder company. At the same time, the committee asked the Attorney General for an opinion on this issue.

In April 1991, while property was negotiating with the controlling shareholder company, the Attorney General ruled that under Section 34 of the Banking (Licensing) Act, a controlling shareholder also needed a permit from the Governor of the Bank of Israel to add and buy controls from a different or additional range of controls.

In light of the indictments filed and the nature of the offenses attributed to the intended purchasers, the legal advisor noted that the proper judgment is to refrain from granting the permit. He also noted that the opinion applies only to the acquisition of means of control of a banking corporation and a banking holding corporation, and that it does not apply to the acquisition of controls or the acquisition of control of the non-banking sectors of the holding company.

4. Following the Attorney General's decision, the Finance Minister asked assets to submit to him her recommendations for continuing the sale process of the banks. A property chairman has asked three external property legal advisors for an opinion on the options of action before assets.

In May 1991, the Minister of Finance submitted a summary of the opinions of the Treasury's legal advisor and external assets legal advisors. Among other things, it said, following the attorney general's opinion, negotiations with the controlling shareholders regarding the non-banking part could not continue. The continuation of the negotiations will undermine the principle of equality and create an improper preference, since as part of the September 1990 contest, interested persons were not given the option to submit proposals regarding part of the group, but only regarding IDB as a whole. In their opinion, supported, among other things, by an expansive interpretation of Article 16 of the Agreement, assets are entitled to determine that the group should be split. It is advisable and proper to continue to work in cooperation with the controlling shareholders in order to reach an agreement, within a short period of time, with regard to the continuation of the sale, even if it involves providing a certain consideration to the controlling shareholders, who will meet the test of reasonableness, fairness and business aspects.

And the public requires that a split sales procedure be carried out, while holding a contest between several candidates.

The opinion also noted that unless agreement is reached with the controlling shareholders, the course of the split and sale can be carried out unilaterally, and that the government has the means to achieve its objectives even though these may involve difficulties and yield results after a longer period of time, especially if the previous controlling shareholders attempt to impede or delay them by appealing to courts or by other means.

5. In May 1991, the Finance Minister informed the Chairman of Assets that he would approve the moves proposed by assets to split IDB, provided that assets determined that the two main parts of the IDB would be sold separately, in order to enable the controlling shareholder company to participate in an immediate contest for the acquisition of IDB Development, and also to deal with the acquisition of the bank by an agreed stay for a timeout of its placement.

6. In the same month, the Chairman of Assets informed the State Comptroller's Office that the controlling shareholders had informed the assets that it was requiring it to continue negotiations with it, from the stage at which it was terminated in accordance with the Attorney General's decision, subject to limitations created by the decision. According to the controlling shareholders' company's interpretation of these limitations, assets must sell IDB Holdings to it in this negotiation, after the majority of Discount Bank's shares are separated from it, in such a way that the controlling shareholder company will continue to hold the share rate that the Bank of Israel permits (see below).

That same month, the controlling shareholders' company announced that unless this requirement was met, it would file a lawsuit against the government and assets for violating the May 1990 agreement.

7. In June 1991, the Board of Assets decided to adopt, as a basis for negotiations, a proposal raised by the Treasury's legal advisor and an external assets legal advisor to sell the controlling shareholders to[[36]](#footnote-36)IDB Holdings after it separated the vast majority of discount bank shares it held.

The Chairman of Assets informed the State Comptroller's Office, even before the decision was made, that necessary conditions for the transaction were the attorney general's opinion that the state could protect the transaction if a petition was filed with the High Court of Justice against assets or the government in connection with this transaction, and confirmation by the Governor that no permit was required under the Banking (Licensing) Act to carry out the transaction.

Concern over a petition to the High Court of Justice expressed one of the external legal advisors of assets in a june 1991 letter to the Chairman of Properties, with this tongue:

"After the smoke clears, it will turn out that the Recanati Group purchased according to the existing tender the real part of IDB while separating it from the banking part. In my opinion, a petitioner who appeals to the High Court will have no difficulty removing its thin, transparent veil above the deal. Once the veil is removed, it will become apparent that a fundamental condition of the tender has been violated, and is the sale of the group as a whole. Therefore, the High Court will rule, in my opinion, to cancel the transaction."

The proposal adopted as stated above stated that it constituted the implementation of the May 1990 agreement, in which the government and assets pledged to engage in good faith negotiations with a single candidate (if there is no competition between several candidates), and that it came towards the controlling shareholder company if possible, "Given the attorney general's opinion, and ensuring the framework of the May 1990 Agreement is maintained, it was also noted there that the offer may ensure the full cooperation of the previous controlling shareholders in the actions necessary to continue the sale process, such as performing a (partial) split of the Group and preparing a prospectus for the sale of the remaining shares held by the Safe[[37]](#footnote-37)Company.

The proposal also states:

"The sale of IDB development to the previous controlling shareholders is done without tender, although the state is not obligated, in our opinion, to do so. Purchasers must compensate the state for this waiver."

In a consultation on this matter in July 1991, the Attorney General concluded his position as follows:

"Under the circumstances, according to which there is some obligation to [the previous controlling shareholders] following the negotiations that were conducted with them even before the 12th opinion was issued on the question of the permit, with the trend to negotiate in good faith and out of a trend towards its predecessor, and in light of the position of the General Accountant and the Chairman of the Board of Directors of Assets M.I. and others, that the public[[38]](#footnote-38) register will be hired, a legal position can be defended whereby the tender will not be reopened."

8. In the opinion of the State Comptroller, there was no justification for the Treasury Department's response and assets to the controlling shareholders' demand to sell it control of IDB Holdings (in fact, control of IDB Development) without competition:

(A) It was highly likely that the process taken under the May 1990 agreement would not have ended in negotiations with a single candidate, had the same process given interested partyers the option of contending for control of IDB Development. However, as noted above, this was avoided at the time due to a condition set forth in the memo and agreement on the ultimate demand of the controlling shareholders.

The deal formulated in the negotiations, unmatched, is essentially an indirect sale of control of IDB Development. Its format is set to allow the controlling shareholders to acquire control of that company (and a significant portion of its capital) through the acquisition of IDB Holdings shares, after its capital structure is changed, so that IDB Holdings holds discount bank shares at the maximum rate permitted to the controlling shareholder company, as long as the criminal charge with which it is barred from acquiring IDB Holdings in its original format is pending.

(B) The position of the General Accountant and the Chairman of the Board of Assets and others that the "public register shall be hired" from making an unbeatable transaction is unacceptable to the State Comptroller: anyone who strongly demands to allow him to purchase an addictive property in unparited negotiations, a peddle on him whose demand stems from his desire to avoid the risk of a choice between two undesirable options for him that competition may put him before (1) to purchase the addict, But at a higher price than in an unbeatable negotiating deal;(2) to refrain from acquiring the addictive, if the high bid in the competition was too [[39]](#footnote-39) high for him.

9. The Treasury and Assets files do not contain a document establishing the assumption that the "public register will be hired" from complying with the controlling shareholders' demand.

10. The sale of IDB development in the process of competition would have necessary to use one of the possible courses of action raised by the legal advisors of assets in May 1991, but there was concern that in such a case the controlling shareholder company would take legal action, based on claims that the government had violated the May 1990 agreement.

In deciding whether to follow the legal opinions they received in May 1991, or to comply with the controlling shareholders' demand, the Treasury and Assets had to examine, based on a thorough examination, the risk that the controlling shareholders would win legal action against the government, as opposed to the prospect of the government winning the law, and the risk that the legal proceedings would continue for a long time, including the financial aspect

On hold. It was appropriate to consider the financial aspect, among other things, to the prospect that the rate of increase in the value of IDB Holdings would exceed the interest rate on bonds issued by the government as a temporary replacement for the proceeds from the sale of the shares, if the sale was postponed due to litigation. There was also room to assess the prospect of the controlling shareholders avoiding postponing the sale, given in part that it was expected that if a deal was not tyed up by October 1991, The controlling shareholders will have no choice between losing the possibility of "redeeming" IDB shares ata rate of approximately 4.2% of the company's capital and taking the risk that if they are submitted to "redemption," the holding rate allowed by discount bank will be reduced, as long as criminal law is pending against them (see this matter below, p. 00).

It was also appropriate to consider the risk that repeatedly complying with the demands of the controlling shareholders of IDB (as well as the other banks), because of the treasury's recoil and assets from legal challenges, could encourage the controlling shareholders to harden their positions - which could create a negative vicious cycle.

The Treasury and assets preferred to avoid the risk of legal proceedings, perhaps prolonged, rather than standing up for the government's right to obtain maximum value for shares.

### Sales transaction

1. As noted, at the end of August 1991, an agreement was signed between the government and assets and IDB Holdings, IDB Safe and the Controlling Shareholders Company. Under the agreement, 25.1% of IDB Holdings' capital was sold to the controlling shareholders for $229.7 million. The portion of the company's property sold to the controlling shareholders was the small proportion for the sale of a controlling core under the agreement set forth in May 1990.

Prior to the transaction, the controlling shareholders had approximately13% of the share capital of IDB Holdings. As long as criminal law is pending against them, the remaining shares of IDB Holdings were in the hands of the Safe Company or were supposed to be "redeemed" by it, under the stock arrangement, on 31 October 1991.

2. At the time of sale, IDB held holdings in the following assets:approximately 74% of IDBDevelopment's shares;approximately 66% of discount bank's shares; and other assets valued at $15 million.

To prevent the controlling shareholders from controlling Discount Bank by purchasing the shares in IDB Holdings, the following actions were done: A.E.D.B.

Holdings transferred 53% of the bank's capital to The Safe Company; b. In return for this, shares of IDB Holdings, which are owned by the Safe Company, were cancelled, so that its capital was reduced by the amount supposed to be equal to the value of the Discount Bank shares transferred to the Safe Company.

The sale and the totality of the actions that followed it were based on negotiations between the parties, under which it was determined, for the purpose of the transaction, that the total value of IDB Holdings in its original format was approximately $915 million; The total value of IDB Development – approximately $594 million, and the total value of Discount Bank – is approximately $700 million.

Due to the reduction of its capital and the transfer of most of the bank's shares it had to the Safe Company, the composition of IDB Holdings' assets changed as follows:

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In September 1991, the Knesset Finance Committee approved the transaction, and its implementation was completed at the end of December 1991.

With the implementation of the transaction and its accompanying actions, the controlling shareholders' holdingsamounted to 57.2% of IDBHoldings' capital reduced; out of this the controlling shareholders sold to an American investor on the day of the transactionIDB Holdings shares of 4.8% of the company's capital after its reduction (see below).

3. The controlling shareholders' companypurchased approximately 25% of the shares of IDB Holdings priorto the reduction of its capital, and these wereadded to 9% of the shares it had prior to the transaction (excluding the settlement shares that were supposed to be "redeemed").

Given their previous holding in IDB Holdings, and indirectly in its assets, the bulk of their acquisition at IDB Development was reflected in the following panel:

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The board indicates that as part of the transaction, the controlling shareholders added 35.5% of IDB Development's shares to their ownership andonly about 1.6% of Discount Bank's shares.

4. In addition to the shares purchased by the controlling shareholders, under the agreement, two more options, unrelated to each other.

(a) IDB has been given an option to purchase 18% of the bank's shares (if the controlling shareholders receive a permit from the Governor); However, it was given that those who acquire a controlling core in the bank will have the right to prevent the sale of shares of the bank to the previous controlling shareholders ata rate of more than 11.7%- (i.e., A third body that acquires a controllingcore in the bank will be able to prevent the previous controlling shareholders from increasing their holding in the bank to(25%-it is determined that the option will take effect after30 months, or after a controlling core is sold to a third party - according to the earliest of them; and it will expire at the end of five years.

It is determined that if the option is exercised, the higher of these two redemptions will be: (1) the price of Discount Bank shares on the Stock Exchange on the last trading day prior to the delivery of the notice of redemption;(2) the average price in the 35 trading days prior to delivery of the notice of redemption and in the 35 trading days following the delivery of the notice.

Ultimately, at the request of the U.S. banking regulatory authorities, the controlling shareholder company[[40]](#footnote-40)had, among other things, to waive this option.

(B) It is determined that up to ten days before the determining date, the controlling shareholder company will be able to[[41]](#footnote-41) notify the assets that it wants to purchase more shares of IDB Holdings, up to 5% of its capital, according to the price per share set for the main transaction in the agreement.

The controlling shareholder company has not exercised this right.

5. The agreement also referred to the matter of "redemption" of buyers' settlement shares. The controlling shareholders of IDB Holdings held, among otherthings, 4.22% of the share capital of that company, Such shareholders could "redeem" them at the end of October 1991, at a price that wasapproximately 51% higher than the price at which the government sold IDB Holdings sharesto the controllingshareholders under the agreement.

It was expected that if the transaction was not completed by the time of the "redemption," the controlling shareholders would face the following choice: to give up the "redemption" of the settlement's shares and lose the difference in prices, of approximately $20 million; Or "redeem" the shares and risk that after holding them in IDB Holdings' capital would be reduced to about 9%-if only temporarily, they would again be unable to increase to13%- [[42]](#footnote-42) the indirect holding rate at Discount Bank. However, in the Attorney General's opinion, in April 1991, the possibility of retaining the existing holding rate of controlling shareholders at Discount Bank was not ruled out.

The agreement between the government and the controlling shareholders dismissed them from the dilemma. The agreement guaranteed the controlling shareholders that if the transaction was not completed by the "redemption" day of the settlement shares, they could purchase in it on the day, at the price per share set forth in the agreement regarding the controlling core, the same amount of shares that were "redeemed" under the bank stock arrangement. This promise will be fulfilled even if the entire transaction is cancelled, but then the government will be entitled to purchase the shares back for six months, on the conditions set forth.

On 31 September 1991, the controlling shareholders exercised their right under the section in question.

In this matter, the State Comptroller's Office asked the Supervisor of Banks in December 1991 if the Governor would have allowed the controlling shareholders to increase their holdings in the bank again (viaIDB) from9% to 13% (which temporary depreciation rate

Holding to-9% as a result of the "redemption" of the shares prior to completion of the transaction). In January 1992, the deputy supervisor of banks responded as follows:

"The question was not up for discussion, so it is difficult to answer completely. However, it must be assumed that after the indictment was filed, the Recanati Group was not given a permit to increase its holdings in The New YorkTimes.

The State Comptroller's Office asked the Ministry of Finance why the agreement included a promise of this bill, and whether its value was taken into account in determining the price of the transaction.

In February 1993, the Ministry of Finance explained to the State Comptroller's Office that the promise seemed reasonable and fair to him, and was one of the conditions set forth in negotiations between the parties, which should not be determined what its monetary value was. The Ministry of Finance noted that the planned date under the agreement to complete the transaction was 31.10.91, And that if the controlling shareholders were able to complete the process of obtaining the permits and permits necessary to complete it in a timely manner, the aforementioned dilemma would not have been created.

The Treasury also explained that in its opinion there is no fundamental difference between holding 9% of the bank's controls and holding 13% of them.

In the opinion of the State Comptroller, the said promise was included in the agreement of a real benefit to the controlling shareholders, which was appropriate for the government to receive a return for it under that agreement. The fact that the agreement was signed prior to the "redemption" date allowed the controlling shareholders to reverse the 13% holding rate, including shares that were to be "redeemed," to the fixed holding rate of IDB Holdings at Discount Bank. Even if the Ministry of Finance did not see a material difference between 9% and13%, it is presumed that the controlling shareholders saw it as a fundamental difference.

##### Price achieved vs. valuations

1. The share price sold to the controlling shareholders is determined in negotiations.

In order to consolidate the transaction, IDB Holdings' valuations were ordered from Exponent A (one of the largest investment bank in the U.S.) and Exponent B (an Israeli economic consulting firm). At the request of assets, they submitted valuations of IDB Holdings, and a breakdown of those estimates according to the relative portions of IDB Holdings holdings in Discount Bank and IDB Development; and extensive sub-detail. Exponent B submitted valuations according to two methods: one method - the value of corporations according to the method of capitalization of expected future profits; And method two - corporate value if

Their holdings in their subsidiaries will be realized.

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The agreement stipulates that the price of approximately $227.9 million will be paid for 25.1% of IDB Holdings' shares, and that the total value of IDB Holdings is, for the purpose of the transaction, approximately $915 million.

In an October 1991 letter to the State Comptroller's Office, the Chairman of Properties noted that the price agreed upon was higher than the two said valuations, close to one-third, and not far from the fourth.

2. The chairman of the assets was referred to the price of the transaction based on the total valuation ofIDB Holdings.

The value attributed in the deal to IDB Development was $594 million; At this value, the bank's shares were also transferred from IDB to the safety company.

And the capital of IDB Holdings has been reduced. Therefore, the price set for the main component of the transaction was about5% higher than the lowest valuation ($594 million vs. $565 million), but about 6%-5% lower than the other two lower estimates, and by 15%-2% from the three higher estimates.

In his explanations of the valuations he submitted, Reckoning A, which estimated IDB Development's value at $630-700 million, explained that the low end of the valuation range represents valuations without a "control premium"; Estimates B, which valued IDB Development at $565-672 million, the control premium ratio is less than estimates A.

3. It should be noted that the market value of IDB Development, according to its stock price on the stock exchange on the day the agreement was signed, was approximately $776 million - i.e. a valuation approximately31% higher than the estimate set in negotiations as the basis for the transaction price. The market capitalization was higher than $667[[43]](#footnote-43)million.[[44]](#footnote-44) , at the discretion of the Treasury and assets, due to the prevailing conditions in the market.

4. As noted above, the price of the transaction is determined in negotiations in which government representatives made an effort to obtain maximum value in favor of the shares sold.

In assessing the likelihood of the price set forth in the transaction by the way of comparing it to the valuations and the price of IDB development shares on the stock exchange, it must be taken into account that the main component of the transaction was the price of controlling IDB Development.

In addition, the reasonableness of the price should be examined given the expectations the assets had, to receive monetary consideration in favor of its concessions to the controlling shareholders in the sales orders:

(A) In December 1989, when the Ministry of Finance and Assets decided to comply with the demand of the previous controlling shareholders to offer IDB Holdings in one piece for sale, instead of split and offer the sale of its two main subsidiaries separately, there was concern that the state would be lost because of the phenomenon of "conglomerate cost": the realization value of a group of companies could, for various reasons (including tax considerations) be lower than the total realization values of the group components. This concern was very real about IDB Holdings (whose great-In March 1991, in response to comments made by the State Comptroller's Office on this matter, the Chairman of Assets explained that since assets had complied with the said demand of the previous controlling shareholders to sell the group in one piece, it would expect assets that the controlling shareholders company would offer as part of the negotiations a price close to the total value of the group's components.

(B) Internal memos submitted by the General Counsel of Assets in May and June 1991 state that if the government waives the sale of the shares in the process of competition, the controlling shareholders should be expected to compensate the state for this waiver.

It is impossible to determine objectively whether the price set in the negotiations was in order to realize these expectations. However, comparing the price set with the valuations prepared by the evaluator and with the value of IDB development according to the tase prices, and considering the additional benefits to the controlling shareholders included in the agreement does not support the hypothesis that the expectations of assets have been realized.

5. When assets were called to the demand of the previous controlling shareholders to sell them control of IDB Holdings reduced in unbeatable negotiations, assets could not rely on the valuations it had ordered and the price of IDB development shares on the stock exchange. These are the only two standards at which the likelyness of the price set in the transaction can be assessed retrospectively.

6. As noted above, it was unlikely from the outset to assume that the "public register would come out hired" from giving up competition.

The Ministry of Finance informed the State Comptroller's Office in February 1993 that it thought there were many benefits, both economic and public, in that the sale of the shares - both the controlling core and the shares sold to the public - was prevented from being postponed - both the controlling core and the shares sold to the public in 1992.

The fear of postponing the sale of the shares due to prolonged litigation and the lack of cooperation by the company and its controlling shareholders in the sale process, if they did not comply with their demands, therefore caused the assets to take an inadequate sales process, the result of which was not optimal from a business standpoint.

IDB's sale process, in all its stages, demonstrates the damage that would have involved allowing the controlling shareholders of the banks to participate in determining the sale process, and in this way condition the comparison of voting rights in determining acceptable conditions, rather than standing for the government to have sole discretion in determining the sale processes of bank shares.

### Financing the transaction

1. The agreement included the statement of the controlling shareholder company (in this section - "the buyer") as follows:

"3.5 That a chart that includes a complete description of the buyer's ownership and control structure, including any right, agreement or understanding, whether written or oral, that exists regarding the ownership, management and control of the buyer, has been provided to the assets and that there is no obligation to allocate shares in the buyer or securities that can be converted or redeemed into the buyer's shares or any such right, agreement or understanding unless included in that chart.

3.6 That the buyer is able to perform and perform its obligations under this agreement from her equity which, alone from its original sum of NIS 2 million, will result from the investment of El-Im Equity Ltd. in the buyer's equity, out of the self-equity of El-Im Anyot Ltd. and/or from the financing sources available to it from banking institutions, which are not affiliated with the IDB Group.

The aforementioned sources of financing shall not be directly or indirectly embossed from the IDB Group, or from any Israeli banking corporation, including its branches and offshoots abroad, and will not be guaranteed, in any way, by other companies in the IDB Group, or subsidiaries or affiliates of other companies in the IDB Group, or by the assets of all of these."

2. According to a footnote to the chart, the control structure of IDB Holdings was included in the prospectus of the sale of IDB Holdings shares from[[45]](#footnote-45) November 1992 (Section 10.1.2).

"Discount Investments and P.I.C., which are subsidiaries of IDB Development, together hold 24.41% in capital and voting in El-Yam Anyot Ltd.and 24.41- on the ballotand about 0.05%- in capital in the tower company."

It also said there (Section 7.13.3) that El-Yim acquired all of the company's debut shares in the last quarter of 1991 for approximately $204 million, and that theygranted it approximately 99.8% ofthe company's value and did notgrant it voting rights.

3. This holding of subsidiaries of IDB Development in El-Yam shares was not expressed at all in the "Control of El Yam Financial Holdings (Tower) Ltd." chart as of 28 August 1991, Submitted by the Controlling Shareholders' Company to the Assets on 29 August 1991 under Section 3.5 of the Agreement (this chart was not attached to the Agreement but delivered to the Assets separately), not in the charts and documents attached as appendixes to the Agreement (nor in the documents submitted to the Antitrust Commissioner for approval of the transaction). It should be noted that the list of controlling shareholders of the assets did not present the planned situation (and which was indeed created during the execution of the transaction), according to which El-Yam will invest 99.8% of the controlling shareholders' total money; However, the situation that existed at the time the agreement was signed, when the controlling shareholders' fortune amounted to NIS 2 million, from that 50% el-Yum investedand 50% invested in El-Yum shareholders (including the two subsidiaries of IDB Development). On 5 September 1991, after the agreement was signed, the controlling shareholders' company handed over confidential annexes to the bank supervisor regarding the holdings of the company's shareholders, reflecting El-Yum's planned investmentin 99.8% of the controlling shareholders' share capital.

4. Given the partial holdings of IDB Holdings in its subsidiaries and granddaughters, its indirect holding rate in El-Am's capital wasapproximately 12% on the eve of the transaction, And given the safety company's partial holding in IDB Holdings, the safety company's indirect holding rate in El-Yim's capitalon the eve of the transaction was more than10% in chaining.

5. The phrase "aforementioned sources of financing" at the beginning of the second paragraph of Section 3.6 should probably apply to "the sources of financing available to it from banking institutions, which are not affiliated with the IDB Group," but not to El-Am's self-equity, although this is also a source of funding in the usual sense. The holding of IDB Holdings (through its granddaughters' companies) in a portion of the company's capital invested in the equity of the alleged controlling shareholder company was therefore not contrary to the language of the controlling shareholders' statement. However, the non-mention of this holding in its views is puzzling; what is also the wording of its statement, as shown above, can create the impression that the sources of the controlling shareholders' funding for the acquisition of IDB shares will not be directly or indirectly derived from the IDB Group, whereas in fact, almost all of the controlling shareholders' equity from the investment of El-Im Anyot, which two companies belonging to the Group hold.

This means that, in financing the buying of shares in IDB Holdings in order to acquire control of it for the controlling shareholders through the controlling shareholders, El-Im Onyot - a company close to a quarter of its capital belongs to the Group

IDB (as defined in the Agreement) - invest the equity in the equity of the controlling shareholder[[46]](#footnote-46) company, or raise external funding sources for this purpose.

6. The State Comptroller's Office raised the following questions before the Ministry of Finance, Assets and the Bank of Israel:

(A) Whether el-ym's investment in the controlling shareholders company actually resulted from El-Yum's equity or external financing sources, or both - and, if so, in those amounts.

(B) Whether the Ministry of Finance and Assets, at the time of the transaction or at another time, examined the sources of financing, to ensure that the controlling shareholder company held its statement.

(C) Why it is determined that the self-de facto fortune of the controlling shareholder company will result from El-Im - a mixed company of the controlling shareholders and IDB - rather than a definite company of the controlling shareholders.

(D) Whether the Ministry of Finance, Assets and the Bank of Israel have established rules regarding the sharing of a company whose significant portion of its capital belongs, if not indirectly, to the company that the state (through a safe company) offers for sale its shares, in financing the purchase of these shares; therefore, what are the rules, and how the findings presented above are settled with these rules.

(E) Have they conducted an analysis of the significance of the financing methods of this transaction:

(1) regarding possible impact on the acquired company, financially, accounting or[[47]](#footnote-47)otherwise.

(2) Regarding the relief of this to the controlling shareholders in financing the acquisition. Therefore, what is the monetary value attributed to this relief, and how this was taken into account in determining the price of the transaction.

(F) Was it planned in the 1990 challenge stage to enable the controlling shareholder company to raise the capital necessary to acquire control of IDB primarily

By issuing shares to El-Yim. If so, was this brought to the attention of the other interested parties; If not, why was this benefit granted to the controlling shareholder company after a single candidate remained.

7. The Ministry of Finance and those who were chairman of assets at the time of the agreement responded in February 1993 to some of these questions as follows:

(A) Since the vast majority of El-Yum's capital was in the hands of the controlling shareholders of IDB and only slightly morethan 10%- El-Yum Capital indirectly belonged to the Safe Company, The Ministry of Finance and Assets did not see a place to prevent the use of El-Yum's means to finance the acquisition. A place to prevent those with whom the government indirectly shares a particular society, and that full control body in society, from exploiting its rights therein."

(B) The value of the relative portion of IDB Holdings' capital security company invested through El-Yum in the controlling shareholders company was included in the value of IDB Holdings at the time its shares were sold to the public in November 1992, and the government received the proceeds from their sale.

(C) The holding of the IDB Group in El-Yim was presented in the information booklet that distributed assets in June 1990 to those interested in acquiring a controlling core in IDB Holdings. In the opinion of the then chairman of properties, El-Yum's investment in the controlling shareholders was not the interest of other interested parties in acquiring a controlling core in IDB Holdings in the process of coping in 1990.

It should be noted, however, that the holding of the IDB Group in El-Yam was included in the information booklet without any embossing as one of the items on its holding list.

(D) According to a reply given by the controlling shareholders' company to the Ministry of Finance, El-Yim's investment in the controlling shareholder company was made out of the liquid measures it had as detailed in Article 3.6 of the Agreement.

It should be noted that this answer does not clarify whether these liquid measures resulted from El-Yam's self-de facto fortunes or external funding sources.

8. In March 1993, the Bank of Israel notified the State Comptroller's Office as follows:

(A) The Bank of Israel has not established rules regarding the participation of a company whose capital belongs partly, indirectly, to the bank or bank to bank holdings, in financing the acquisition of controls at the bank or holding company; in his opinion, this is a private case that should be examined on the meritsof the matter, and not through predefined rules.

(B) As far back as December 1990, the bank supervision worker expressed, in a letter to the supervisor, reservations about the planned use of El-Yum's means to acquire a controlling core in IDB Holdings, in part because it gives an advantage to the controlling shareholders of El-Yum over a candidate of other force. However, since it was decided to transfer to the safe company most of the shares of Discount Bank that IDB Holdings had, and to limit the holding rate of IDB Holdings in the Bank to a rate of 13% of the rate held by the controlling shareholders on the eve of the transaction, the Bank of Israel did not see[[48]](#footnote-48)this transaction as a transaction to acquire control of the bank, And the Supervisor of Banks stopped handling the matter.

9. In the opinion of the State Comptroller, it is appropriate for the Ministry of Finance, the Bank of Israel and assets to examine this issue in all its interests, and consider whether there is room to establish rules under which a limit will be placed on a candidate'sability to purchase bank shares (or shares of another company) that the state offers for sale, To use financial means that belong partly, if indirectly, to the proposed body for sale.

Whether or not such rules are established, it is appropriate, however, to determine that if a candidate is authorized to use means belonging to the acquired company, this fact should not be ingested - as is done in the IDB transaction - but must be disclosed in appropriate detail and prominently in the coping documents, the purchase agreement, and any other documents belonging to the matter, such as a prospectus for a public offering.

##### Selling some of the shares to another investor

The controlling shareholder company's equity (the equivalent of $204 million plus NIS 2 million) was not equal to the full price set in the transaction (close to $230 million). The November 1992 prospectus states (in Section 3.5.4 that, at the same time as the acquisition agreement was executed, the controlling shareholder company sold to an American investor shares of IDB Holdings that provide approximately 4.8% of the company's capital of origin (after its capital reduction).

This sale was permitted under a clause in the August 1991 agreement under which, under a "limitation period" of up to 30 months from the execution of the transaction, in which the government would be given priority in the sale of IDB shares, the controlling shareholder company may, under certain conditions, sell IDB shares, up to 5% of IDB's estate.

### Control of Discount Bank

In order to eliminate the need to obtain approval from U.S. bank supervisory authorities to carry out the August 1991 agreement - which could have run into difficulties in light of the pending criminal trial against IDB Holdings and the heads of the controlling shareholder company - changes were made in December 1991 to the control structure of Discount Bank and IDB Group and the August 1991 agreement, following which IDB Holdings ceased, in effect, to be considered a banking holding company. :

(A) The Safe Company (a company that the controlling shareholders of IDB Holdings founded, and they control) transferred all the shares of Discount Bank that it held, at a rate of 86.78% of the bank's capital, to two personalities, who hold shares in trust for the government. The terms of holding the bank's shares in escrow are primarily similar to the conditions set forth in the first place for holding them by the Safe Company under the August 1991 Agreement (see above, p. 00), the terms intended to enable the government to protect state rights in the Bank's shares and the provisions regarding the appointment of external directors.

(B) In the matter of appointing directors at the bank, it is determined that the holders of the bank's shares in the trust will choose the directors – apart from the directors from the public under the orders of the companies and external directors – whoever the outgoing board of directors of the bank proposes.

### Commitments to sell shares of other banks

1. When the Bank of Israel granted a permit to the controlling shareholders to acquire control of IDB, IDB pledged to the Bank of[[49]](#footnote-49)Israel:

(A) If IDB Holdings acquires control of Discount Bank, it will act to sell the bank's holdings in the First International Bank, within a reasonable time agreed with the Bank of Israel.

(B) If it acts to sell its sharesin Isrup, which controls General Bank, within 24 months of completing the implementation of the Acquisition Agreement fromAugust 1991: If no suitable buyer is found despite reasonable efforts, IDB will contact the Bank of Israel requesting an extension of the period.

2. Discount Bank has informed the Bank of Israel that its management has long wanted to sell the shares of The Israel Industrial Development Bank Ltd. (Lennen - Balat) in its hands,and that thebank is ready to sell at an appropriate price.

### Sale of the remaining shares of IDB Holdings on the Stock Exchange

In November 1992, The Safe Company offered the remaining shares of IDB Holdings, which were held by the Safe Company, amounting to 42.56% of the company's capital. The units offered for sale included shares and options for buying shares during the periods and conditions set forth in the prospectus. At the maximum price set by assets, over-underwriting is recorded at a very high rate. The immediate gross proceeds to the government were NIS 510 million; assuming all options are exercised, an additional value of NIS 435 million is expected, in a linkage to the October 1992 index (some until May 1993 and some by October 1993).

The State Comptroller's Office has not yet looked into this sales proposal.

The issue of splitting bank groups

1. The country's largest bank groups include, apart from the four main banks in the arrangement, many other corporations, especially the following types:

(a) medium and small commercial banks, controlled by the main banks (mainly: a union bank controlled by B.L.A.; Barclays Discount Bank controlled by Discount Bank - until recently, jointly with a bank from abroad; and an American-Israeli bank and a Continental Bank controlled by Bank Hapoalim).

Discount Bank also holds a substantial minority (and does not control) the shares of the holding company that controls First International Bank. IDB Development holds a substantial minority (and does not control) the shares of Isrup, which controls a general bank.

(b) Branch banks, especially mortgage banks.

(C) Banks that serve, primarily or exclusively, certain groups of employees (Treasury soldier, Yahav and Mesad held by Bank Hapoalim).

(d) Banking subsidiaries abroad.

(E) Companies in the non-bank financial field, especially some of the largest insurance groups in Israel and lease companies.

(F) Companies in non-financial fields (hereinafter - real corporations) mainly in the industrial, real estate and fuel sectors - many of them by investment companies controlled by bank groups. Among other things, "Clal Israel" (hereinafter – clal), the largest group of investment companies in Israel, is controlled by Bank Hapoalim and IDB Holdings (through IDB Development, which is one of the largest investment companies in Israel).

2. Banks also control most provident funds and mutual investment funds (hereinafter – mutual funds) in the country, whose total volume is very[[50]](#footnote-50)large.

The Histadrut pension funds are controlled by the employees' company; The employee company and Bank Hapoalim control "Reward", which manages the investments of pension funds and many other provident funds; And senior managers of "Reward" serve as members of the investment committees of the pension funds, as well as the provident funds controlled by Bank Hapoalim, Bank Yahav and Bank Masad.

3. For years, representatives of the banks had a majority on the Board of Directors of the Tel Aviv Stock Exchange; As of 1977, their relative share declined, and despite this their position on the stock exchange continued to be dominant during the period of stock regulation. Since Section 45A of the Securities Law was added,1989, five representatives of the banks have served on the TASE Board of[[51]](#footnote-51) Directors, and are one-third of the board members.

4. The three largest banks hold 8.3% of the share capital of The Tel Aviv, whichgrants70%of the voting rights; to the government, which holds41.7% of the share capital of the Balat, only25% of the voting rights.

In November 1991, the Bank of Israel notified the State Comptroller's Office:

"The Bank of Israel's position is that the government and the three banks holding control of the Industrial Development Bank must sell their share of the bank simultaneously. The Bank of Israel's position found, among other things, an expression that, as a condition of approving the transaction between the government and M.I. Assets and the RecontiGroup, approval of the transaction was conditioned on the commitment of Discount Bank to sell its shares in the Industrial Development Bank."

The Ministry of Finance informed the State Comptroller's Office in December of that year that it was working to transfer shares in the Tel Aviv held by Bank Hapoalim to a trustee, and then to sell them.

### The need for reform of the banking system

1. Following the October 1983 stock arrangement, a number of committees and teams worked on ways to sell the banks' shares in due course. The same committees also discussed the centralized structure of Israel's banking system and its control over a large portion of investment and savings institutions and real corporations.

The Bisky Committee has addressed these issues extensively.

A team appointed by the Governor of the Bank of Israel in January 1985, who had representatives of the three largest banks included in the arrangement, recommended reducing centralization in the banking system to increase competition and limit banks' control over provident funds, the securities market and investor advice. The review of this team and the other committees dealing with the matter focused on the following three issues:

(a) Centralization in banking: The three largest banking groups concentrate a crucial part of all banking activity; They hold about86% of the total assets of all banks.

(B) The banks' control of real corporations, one of the largest in the country, has increased their involvement in industries such as insurance, construction, fuel, industry and commerce. This activity puts the banks in a conflict of interest situation.

(C) The control of banks over most mutual funds and provident funds, i.e. the institutions that centrally manage much of the savings of Israeli households, It also puts the banks in a conflict of interest situation.

2. The strong criticism of the centralization of banking and capital markets was also reflected in the Finance Minister's letter to the Governor of the Bank of Israel, dated 31 May 1992, a letter discussing the business results of the banking groups in 1991.

The minister attributed the increase in the financial range of the banks to "the fact that the banks operate under the conditions of lack of competitiveness".

"The capital market reform is intended to bring about the proper allocation of funds and better business use of the sources of the economy, among other things - by transferring some of the savings from investing in government bonds that guarantee a high yield at any point in time, regardless of the economy's fitness, to stocks that are supposed to reflect the economy's capacity.

Fellow provident funds and mutual funds that are entrusted and managed to acquire a takeover of the various sectors of the economy. The centralization will increase and the edict of entrepreneurs, issuers and credit seekers in banks will increase. There is also concern about the possibility that depositors' money will be used directly and indirectly to purchase the shares of the banks themselves, thus perpetuing the 'rule of directors'."

3. During the preparations for the sale of bank shares in the arrangement, various options were discussed to split the bank groups. The main suggestions can be categorized as follows:

(a) Increase competition between banks by separating certain banking corporations from the groups of banks that control them.

(B) The sale of shares, in all or some of them, of real corporations owned by the major banks.

(C) Transferring control of provident funds and mutual funds from banks, or, at least, limiting their involvement in managing them, and especially managing their investments.

The proposals to tie the sale of bank shares in a settlement with changes in the structure of the banking system were due to considerations from all farms, rather than the desire to increase the proceeds to the state from the sale of the shares.

Some thought that splitting up the banking groups, and selling separately the shares of the real corporations owned by the banks, and especially on the IDB, would increase the number of competitors for the purchase of those assets and , as a result, the proceeds to the state, and some thought otherwise. However, it wasn't, and shouldn't have been, the only consideration. When the government sells the shares of the banks in the arrangement, it wants to achieve maximum monetary return from the sale, minimizing the loss from the stock arrangement.

### Reducing centralization in the banking system

1. The team appointed by the Governor of the Bank of Israel in January 1985 and the joint staff of the Ministry of Finance and the Bank of Israel, which concluded its discussions in June 1987, saw increased competition in the banking system as a destination. The first team recommended that the centralization of the banking system be reduced and increased competition in which they would be the target of the sale of bank shares in the arrangement. The other team recommended that the units be sold be defined, i.e. whether it is advisable to split a banking group or merge small units, according to the consideration of the desired banking structure.

2. In May 1988, a steering committee was appointed. Representatives of the Bank of Israel in the Steering Committee recommended that the increased competition in the banking system be determined as one of the objectives of the sale process, and to examine the possibility of spliting the groups

banks for several business units - banking and others; To this end, they recommended that a joint team be established to prepare a detailed working paper on this matter as soon as possible.

The steering committee did not determine that increasing competition was a target, but rather a consideration in negotiations with the controlling shareholders. No team has been set up to examine the possibility of split the banking groups.

Representatives of the Bank of Israel on the Steering Committee addressed in August of that year a letter to the Deputy Finance Minister requesting that the government be informed of the Bank of Israel's position. In their opinion, increasing competition in the banking industry is a very important macroeconomic target for the growth and well-being of the economy. It's a goal the government needs to work towards achieving. The letter also said:

"The concentration in the Israeli finance and capital markets is relatively large and a broad spectrum of areas of activity. As a result, competition in the banking industry, the efficiency of the finance and capital markets, the functioning of business firms and the welfare of individuals are impaired. For example, the lack of competition in the banking industry causes too high an interest rate and therefore harms investments and growth of the business sector.

In September 1988, the Deputy Minister of Finance appealed to the Governor of the Bank of Israel to make up the preparatory and research work that underpinned the recommendations of the Bank of Israel's representatives on the steering committee regarding the possibility and importance of splitting the banking groups, despite the legal and economic difficulties involved. The Deputy Finance Minister suggested that this option be examined in preparation for negotiations with the controlling shareholders, and emphasized the special weight the governor's detailed position on this issue would have.

The Governor of the Bank of Israel responded in October of that year that the Bank had examined on the principled level the structural changes that could be achieved during the sale process; When the Deputy Finance Minister and the committee members rejected the recommendation made by the bank's representatives on the steering committee, the Governor found no place to invest efforts in preparing a practical plan for this matter. Unless it is decided in principle that encouraging competition in the banking industry is indeed a central objective.

That same month, the Deputy Finance Minister asked the Governor that the Bank of Israel prepare a practical and detailed plan to increase competition in the banking system by splitting the banking groups in the arrangement. He sought to point to how the desired change in the banking system had been made and solutions to the legal and economic problems such a change could cause. The deputy minister noted that the steering committee did not reject the Bank of Israel's principled approach on this matter, and asked that the Bank of Israel participate in a joint committee of the Ministry of Finance and the Bank of Israel, which will discuss, among other things, the plan the Bank will prepare.

The Bank of Israel did not comply with a request to draw up a plan to split the banking groups.

The Bank of Israel notified the State Comptroller's Office in August 1990 that its research department had not prepared research papers on corporate segregation options

 Bankers and real corporations from the banking groups, their expected results and solutions to the difficulties involved, because representatives of the Treasury Department on the steering committee and property company opposed the compensation of the bank groups.

3. In August 1989, during the negotiations held by the Ministry of Finance and assets with B'Alal for comparing voting rights in the shares of a union bank and the joint sale of shares of a union bank held by the safe companies and by the L.A.L.E.L., the Governor presented to the Minister of Finance the position of the Bank of Israel, according to which the separation of the Bank of The Union of M.L.L. would not destabilize B'L.L. and would not harm its business results; The Governor noted that splitting the Balaal Group and other banking groups as part of the sale of the banking shares in the arrangement would result in a desirable change in the structure of israel's banking system. The Governor also explained that the sale of a union bank separately from B'Al may increase the value of the government compared to its sale together with B'Al.

In the Treasury department's files and assets, no document was found regarding the determination of the position of the government or the Treasury department on the splitting of banking groups over the period since the steering committee's conclusions were submitted until February 1990. During this period, negotiations took place between assets and controlling shareholders, and memorandums of principle were signed with them at the end of 1989 and early 1990. A memorandon with the controlling shareholders of B'L.L. states that a union bank will be sold separately from B'Al. On the other hand, the Ministry of Finance and Assets agreed to the demand of the controlling shareholders of IDB to sell the group as a single piece. Memos signed with the controlling shareholders of Bank Hapoalim and B'Al stipulate that the list of their subsidiaries sold separately (other than a union bank) will be determined by agreement between the parties; In practice, no such lists were established, and in agreements signed by the government with the two largest banks and their controlling shareholders in the last quarter of 1991, the government was not given the authority to determine that a bank would sell its holdings in a banking corporation (other than a union bank) or a realistic one.

4. In February 1990, after the signing of the memorandums of principles with the controlling shareholders of the three largest bank groups, the Supervisor of Banks presented in a letter to the Chairman of Assets the position of the Bank of Israel that the banks in the arrangement of banking subsidiaries should be separated, provided that the following conditions were met:

(A) The bank that will be sold will be of a minimum size that ensures its business stability and enables it to function independently. Also, his contribution to the competition should be real.

(B) The split will not harm the stability of the parent company, will not reduce its capital to the extent that it impairs the ratio of capital liability required of it, and does not impair its operating capacity.

Based on these principles, the inspector recommended:

(1) Sell the Union Bank separately from B.L. and turn it into an independent bank.

(2) Cause the controls of Discount Bank to be sold in P.I.B.I. (the parent group of the first international bank), and of IDB Bisrup

(controlling shareholders of a general bank); And to explore the possibility of selling Barclays Discount Bank separately.

(3) Thoroughly consider the possibility of merging four small banks controlled by Bank Hapoalim, and selling them separately as a single unit.

(4) To have the government and the three largest banks at the same time sell their means of control over the L.A.P.A., so that it can act as an independent bank.

The inspector announced that if a thorough examination of these options was decided, the Bank of Israel would be willing to assist in doing so.

5. In July of that year, the Supervisor of Banks informed the Chairman of Assets that, according to the opinion of the Bank of Israel's legal advisor, the Governor was authorized to determine, as a condition of allowing the purchase of a banking corporation, that banking subsidiaries would be split from the parent company.The Supervisor of Banks stated that he intended to act in this matter in accordance with his letter to the Chairman of Assets from February 1990, mentioned above.

6. In November 1990, the Minister of Finance announced in a letter to the Governor that the Ministry of Finance would act to implement the agreement in the Memorandance of Principles with B'L.L., that a union bank would be sold separately. The minister rejected the supervisor's recommendation to consider merging four small banks controlled by Bank Hapoalim, citing the fact that being three of these banks is sectoral, their merger would cause a complication which, in the Treasury's opinion, is unjustified because of the benefits expected of it.

7. Since March 1990, the Chairman of Assets has contacted the Finance Minister several times, requesting that he decide on the splitting of the bank groups in the arrangement. In his March 1991 appeal, the Chairman of Assets noted, among other things, that the lack of a decision prevents progress in negotiating detailed agreements with B'Al and Bank Hapoalim and their controlling shareholders.

Until detailed agreements were signed with the controlling shareholders of the two largest bank groups - in October and December 1991, correspondence between the minister and the governor continued on the matter; No detailed decisions have yet been made regarding the splitting of the bank groups in the arrangement, with the exception of the directive to sell the IGU bank separately from B'Al and not separate Tefahot Bank from Mizrahi Bank.

In September 1992, during the planning of sales proposals of 10% of the shares in L.L. and Bank Hapoalim, which were supposed to take place towards the end of 1992, the Chairman of Assets requested in a letter to the Minister of Finance to call a hearing in his chambers, with the participation of representatives of the Ministry of Finance, assets and other parties as he deemed necessary, in order to formulate policies and guidelines for assets on the issue of fragmentation. He noted that the need for decision-making on this issue is taking on a matter of importance ahead of the expected offerings.

On 25 January 1992, the Finance Minister held a meeting on the splitting of the banks. The Finance Minister concluded the decision that the process of selling bank shares should not be linked to the issue of fragmentation in the banking system. Addressing the split issues in connection with the sale will slow down the process and will not help its success.

Therefore, the government will not exercise rights from the stock power to cause the splitting of companies in the banking groups.

### Control of banks in real corporations

1. A considerable time before the outbreak of the bank stock crisis in 1983, and before the problem of selling the settlement shares arose, the need to separate the real corporations from the banking corporations was recognized.

This need was expressed in Section 11 of the Banking (Licensing) Law,5741 -1981, which stated, among other things, that a bank would not control a realistic corporation unless it received approval from the Supervisor of Banks after consultation with the Licenses Committee.

The explanation for the bill[[52]](#footnote-52) indicates that the intention was to allow a commercial bank to directly engage in a wide range of financial activities, but to prohibit it from engaging in other areas, such as industry, construction and commerce.

It should be noted that in 1986 the clause was amended and the prohibition was also extended to holding as a "person of interest," we were those who possess twenty-five percent or more of a certain type of control.

It should be noted that various transitional provisions, which have been enacted over the years, have established special arrangements regarding banks that have already controlled or been interested in real corporations, in such a way that Section 11 does not apply to them. The transitional provisions stemmed from various considerations, such as: the fear of reducing the capital of the banks, etc., considerations that do not fall back from recognizing the necessary separation of real corporations from the banks.

The necessity of separation from all-farming considerations and the need to increase the resilience of the banks was expressed in the documents of the Bank of Israel and the Ministry of Finance. For example, the Treasury Department's January 1993 position paper on the benefits of realizing the investments of banking corporations in real companies reads:

" (1) Increasing the bank's active financial capital at the expense of investments in real assets will improve the bank's resilience.

(2) The realization of investments will contribute to reducing the control and involvement of the banking system in economic activity in the economy.

(3) The realization of the investments will result in a disconnect between the bank's considerations as a credit giver and its considerations as a stakeholder in businesscompanies."

2. In February 1990, the Supervisor of Banks proposed in a letter to the Chairman of Assets that the Ministry of Finance and Assets conduct a thorough examination of the possibilities to separately sell real corporations controlled by the banks in the arrangement. That same month, the issue was discussed in the Assets Board and the Chairman reported that an external accountant had been appointed to examine this question from the aspects of taxes and capital edicts. The Chairman announced that when the examination was completed, the issue would be brought, in all its effects, to the Finance Minister.

In July 1990, the accountant submitted two opinions relating to the possibility of Bank Hapoalim selling its holdings in Clal & Delek and B'Al to sell its holdings in African companies Israel and Migdal. The accountant based his calculations on a number ofassumptions.

(A) The sale of holdings in real corporations will result in the aforementioned banks having one-time redemption losses.

(B) The predicted return on active financial capital is lower than the forecasted return from the continued holding of their investments in nominated companies to be sold separately, therefore their profit will be reduced in the long term.

(C) Increasing the active financial capital of banks as a result of the realization of investments in non-bank assets will reduce the overall risk of banks, primarily by reducing exposure to interest and liquidity risks.

(D) The realization of investments will contribute to reducing banks' control over economic activity in the economy, and will cut off considerations of credit to the bank's clients from the bank's considerations regarding its investments. In relation to one of the two banks, the accountant added: "This is especially given the significant amount of credit that the bank provides to those companies."

The accountant's report further states that the government is not guaranteed full cooperation by the banks in selling their subsidiaries, and that selling them separately could result in an extension in the bank sales schedules. He also noted that the proceeds from the sale of the companies would remain in the banks themselves, so that the scope of the measures necessary to buy the banks would not be reduced due to the sale of the subsidiaries. Therefore, the sale will not increase the number of competitors for the purchase of the banks.

The accountant's aforementioned conclusions indicate that he saw the main difficulty in selling the real corporations to the impairment of the banks' capital adeciss as a result of the expected realization losses from paying tax to the government. Another disadvantage is that he saw a possible decrease in profit, due to the use of equity as financial capital, as a partial replacement for public deposits or a similar source of capital; However, compared to this disadvantage it is appropriate to take into account the risk reduction of the banks and their increased thyness.

3. In July 1990, the Supervisor of Banks brought to the attention of the Chairman of Assets the position of the Bank of Israel, Which relies on the accountant's opinion that the expected impairment of B'Elal's capital as a result of the separation of Africa Israel and Migdal and their sale, according to the accountant's estimate, is unreal, and in this respect there is no impediment to separating these companies from the group, while the expected harm to the capital fulability of Bank Hapoalim as a result of the separation of the two companies "clal" and "fuel" is real and therefore should be avoided.

After a year, the circumstances changed and with them , the position of supervisor of the banks changed. On the basis of an examination conducted by the inspector, following questions from the State Comptroller's Office, he announced that the expected reduction in bank capital of Hapoalim, if the two corporations (fuel and all) were split from it, would be at a total rate of 0.3% (from -9.2% to -8.9%).

" This relatively small impairment and improvement of the capital ratio at Bank Hapoalim since our previous recommendation warrant a reexability of the issue of fragmentation in this bank. This recommendation receives further reinforcement if proposed to carry out the above split without causing the bank's capital to be burned (e.g., by increasing capital by the government in the amount of tax charged)."

4. In July 1990, the Chairman of Assets presented the accountant's opinion before the Finance Minister, asking him for instructions on negotiations with the controlling shareholders of the L.A.L.A. and the Bank acting on lists of the companies that assets would require to sell separately.

In a letter to the Governor, dated November 1990, the Finance Minister raised, among other things, the accountant's main conclusions in the opinion he gave to the assets. He emphasized that because of the realization, Bank Hapoalim and the L.A.L.A. would incur one-time losses of considerable amounts, but did not specify that these losses would be the result of tax payments to the Treasury.

The minister noted that the main considerations for the separate sale of real corporations are macroeconomics, reducing the involvement and control of banks in the economy; And considering them could cause a considerable delay in the process of selling bank shares.

In agreements signed in 1991 regarding thecomparison of the rights of shares of Bank Hapoalim, Belal and Bank Association and their sale arrangements, nothing was said about the separate sale of the shares of the large banking corporations or real corporations owned by the banks, except for the Bank of Union.

The possibility of selling real corporations of the two largest banks separately depends,until October, 1993,on the consentof the banks and their controlling shareholders.

5. The Finance Minister, in his november 1990 letter to the Governor, relied on the accountant's examination, mentioning the expected losses to the banks from realizing the real investments and harming the capital blows. In no time, it beed clear from another examination by the Supervisor of Banks that the conclusions of the previous examination were valid for only a short period of time. In the opinion of the State Comptroller, the very consideration of

Paying tax should not be a factor against a separate sale when the state is the shareholder and when against the loss it will have as the owner the tax revenue stands. It also states above that it is possible to use the same income to prevent impairment of capital steadage, an injury that the supervisor believes is likely to be minimized.

The issue of separating real corporations from the banks is being examined again by the Joint Steering Committee of the Ministry of Finance and the Bank of Israel at the time of completion of the audit report.

When considering this matter, it is also worth remembering that banks enjoy special protection of the state, since the damage to the entire economy from the failure of the banks is greater than the damage that will apply to the owners or controlling the banks.

### Control of banks in provident funds and mutual funds

1. Bank provident funds and mutual funds (hereinafter – funds and funds respectively) manage a large part of the savings of Israeli households.

Until 1986, the registers invested mainly in designated bonds issued for them and the yield of which was determined by the Ministry of Finance. The fund managers could invest, at their discretion, only a very small portion of the[[53]](#footnote-53)fund's assets.

2. The Ministry of Finance and the Bank of Israel are naïve about holding conflicts of interest between the banks' action as fund managers and their other businesses in the capital market. It has already been mentioned above that banks are also engaged in signings for bond and stock offerings; they are investing in their own Nostro portfolio

 and manage investment portfolios for clients; They advise investors; And they also own realistic corporations whose securities are publicly traded.

As noted above, there is no dispute that the specified activity puts the banks in a conflict of interest situation. These acts allegedly involved favoring one fund over its evil" (Bisky Committee Report,p. 372).

In recent years, the reporting of the registers to peers has been improved according to the guidelines of the Capital Markets Division of the Ministry of Finance. The division has instituted a uniform formula for calculating the return achieved by each register and making it easier to compare the returns of the various registers. [[54]](#footnote-54)

The Ministry of Finance took a number of steps to narrow the possibility of a conflict of interest situation in provident funds. [[55]](#footnote-55) and act as faithfully, assiduously and carefully as a cautious trustee would in the same circumstances"; Amendments to the Regulations in 1988 and 1989 also included restrictions,in percentage terms, on the investment of cash registers in securities[[56]](#footnote-56)issued by one bank issuer, or in loans or deposits with one person.

In November 1987, the Capital Markets Division established criteria for approval of new provident funds (including new funds that will establish banks), according to these criteria: a new provident fund will be a company ltd. and will be managed by a managing company Ltd., which will not engage in any other occupation; The managing company will have equity in a certain minimum amount, and will purchase professional liability insurance for a certain minimum amount; The chairman of the board of directors of the managing company shall not be a member of the company's management nor a position therein; The board will have at least two directors from the public, and the number will not be less than a third of the board members; Each board committee, including the Investment Committee, will serve at least one public director. These criteria somewhat reduce the influence of banks on new funds, some of which are in total assets of

The banking provident funds are not [[57]](#footnote-57)yet many.

In contrast, capital markets reform has increased the danger of conflicts of interest. Prior to the reform, the box office managers could invest only a very small portion of the accumulation money in the shares, and most of the investment was in designated bonds. Since 1986, the registers have also purchased tradable bonds on the secondary market, including non-governmental bonds, and are entitled to invest up to 50% of their funds in convertible stocks or bonds. Fears of a conflict of interest may prevail when bank shares in a public settlement are sold. It should be expected that the registers and funds, like other investors, will include these shares in their portfolios. It is very important to ensure that the holding and trading of bank shares, as well as the use of voting rights, will be solely in the interests of the peers and not the controlling shareholders of the banks. Past experience shows that these concerns are real, in his may 1992 letter to the Governor of the Bank of Israel, The Finance Minister also raises the "concern that depositors' funds may be used directly and indirectly to purchase the shares of the banks themselves and thus the 'rule of directors' will be perpetuated."

The fear of banks' control over the registers and funds, especially after the reform of the capital markets, is therefore expressed in these two: concern about the possibility of harming the interests of savers and investors; And fears of harm to the proper functioning of the capital market when a small number of banks control the institutions that manage the large part of israel's household savings.

3. In light of the conflicts of interest in which the banks were found, the Bisky Committee recommended that they be prohibited, after a transition period, from managing funds and funds.

Managing the savings institutions involves, among other things, performing the following roles: marketing the service to savers and investors; managing and accounting; deciding on the investment of the adluted funds and filling loyal roles.

It is accepted by the Bisky Committee and most other bodies that dealt with the issue that banks have a great advantage in performing the roles of marketing, management and accounting, and holding loyal roles for funds and funds managed on

By others, including other banks. This advantage stems from the large array of branches, a skilled member of employees, a computer system, and equity necessary to fulfill a trustee'sduty of responsibility.

The proposals for changes and amendments, which were raised during the period under review, primarily addressed the area of investment management. This is the area in which conflicts of interest are expected with other bank operations and harm to the effectiveness of the allocation of capital markets. Furthermore, the relative advantage of banks in this area is not so significant.

4. Since the filing of the Biski Committee report, the matter of the relationship between the banks and the funds in the Ministry of Finance and the Bank of Israel, as well as the teams appointed by those bodies, have been discussed as much as possible regarding the conflicts of interest, but not with respect to the means undertaken by this need.

(a) prohibit banks from directly or indirectly managing funds and funds.

(B) Permit the management of funds and funds by corporations owned by the banks while establishing reservations about the management methods that will reduce the dependence of those corporations on banks, block the transfer of information and ensure a system of considerations and independent management for each corporation, so-called the establishment of "Chinese walls."

(C) Rely on "market control", by expanding the duty of disclosure, publishing metrics on the quality of performance of the various institutions and increasing competition.

5. Discussions between the various teams and between the Bank of Israel and the Ministry of Finance revealed disagreements regarding the measures to be taken. The Bank of Israel has tended to a combination of separating provident funds from banks with the creation of "Chinese walls" between the various units of banks that have the potential for conflict of interest.

Members of the Capital Market Reform Planning Team, which operated at the Bank of Israel, wrote in their December 1987 report that they thought separating ownership was preferable to the use of a "Chinese wall," given the "relative weakness of the 'Chinese walls' in achieving their goal," but because of economic considerations, resulting from the benefits of size in some capital market operations, they recommended separating ownership only in some cases. On the other hand, the Ministry of Finance believed that it was appropriate to rely more on market control and preferred not to keep the funds and funds away from the banks.

After representatives of the Bank of Israel, the Ministry of Finance and the Israel Securities Authority disagreed with the recommendations of the Bank of Israel's team to plan the reform, a joint team was established in January 1988 for these three bodies headed by a senior executive at the Bank of Israel. The chairman of the team submitted a report to the governor on the team's conclusions in March.

1990, but noted that no agreement had been reached on all issues. The main recommendations relating to managing funds and funds are as follows:

(A) Trust for mutual fund assets and provident **funds:** The team believes that a bank or corporation in a banking group that plays the roles of a trustee is not therefore in a conflict of interest situation and therefore recommended that it be permitted.

(B) **Mutual Fund Management:** The team recommended that a company that manages a mutual fund be removed from the bank to the rank of a sister company, at least.

(C) Management of provident **funds:**  Representatives of the Bank of Israel were of the opinion that exclusion within the banking group was insufficient to increase competition in the finance and capital markets and reduce the possibilities for a conflict ofinterest situation.

Representatives of the Israel Securities Authority and representatives of the Treasury on the team were of the opinion that the provident funds should also be kept only as far as a sister company, and that they should not be excluded from the banking group framework, which gives colleagues more confidence than alternative funds management bodies.

In June 1990, the Governor brought the recommendations of the Bank of Israel's staff to plan capital market reform for a hearing of the Bank of Israel's advisory committee. At the same hearing, some members of the committee, who are representatives of the major banks, expressed strong opposition to the committee's recommendations, particularly the separation of provident funds from the banks. Staff recommendations were also not supported by other members of the committee. The committee chairman concluded the hearing by saying the team's recommendations were immature to make a decision.

6. In December 1990, the Governor recommended, in a letter to the Finance Minister, to examine several options for promoting the sale of bank shares in the arrangement, including the sale of some of the shares in the capital market. The Governor noted the problem of buying bank shares by provident funds and related mutual funds, and proposed to overcome this by an amendment proposed by the Bank of Israel to the Banking (Licensing) Law, under which conditions and reservations for managing funds and funds would be determined by banks.

In fact, the amendment proposed by the Bank of Israel was not included in the bill. In October 1991, the Supervisor of Banks informed the Ministry of Finance that he intended to establish proper banking management provisions to prevent conflicts of interest in the management of funds and funds by banks. The Ministry of Finance asked him to refrain from doing so until their differences in this matter were settled and a recipe for regulating it was agreed.

7. In early June 1992, after consulting with the Advisory Committee on Matters Relating to Banking Business, the Supervisor of Banks set instructions

Proper banking management to prevent conflicts of interest in the business of a banking corporation. The introduction to the provisions states that it is important to have a mechanism to prevent conflicts of interest in order to increase public training in banks as fair intermediaries, in order to prevent abuse of the power of banks and the information they have and harm to banks that may result from lawsuits against them due to such abuse. The provisions set restrictions on the practice of banks in managing provident funds, mutual funds and client investment portfolios; And in signings and advising clients on investment matters, the provisions state, among other things, that a bank will not manage provident funds except through corporations it controls or has an interest in. The provisions also state "Chinese walls" to prevent, or at least reduce, the bank's influence on the corporations that will manage the provident funds, by limiting the participation of "insiders" in managing those corporations and their investment committees.

That same month, the Capital Markets Division informed the banks that it would not approve the changes to the existing provident funds' incorporation documents at this time, as required by the supervisor's instructions (however, the division would not object to the implementation of the provisions in new provident funds to be established). Since any changes to the incorporation documents and regulations of a loaded provident fund, according to income tax regulations, approval by the Division, was in this step to prevent banks from complying with the supervisor's instructions regarding existing provident funds. The division explained in its announcement that resolving the conflicts of interest problem in the way determined by the inspector raises concerns that the registers will be harmed by the exclusion of the registers from the banks; This may reduce a bank's responsibility to its managed register colleagues, which does not align with the identification of the register with the bank in the eyes of peers. In a letter to the supervisor from that month, the Treasury's CEO added that the banks' equity was idly larger than the equity on which a separate managing company's responsibility to provident fund peers might be based. The CEO has made it clear that the Treasury will not approve any changes to existing register incorporation documents unless arrangements are found to prevent harm to the best interests of peers.

In July 1992, the Inspector general of finance replied that he had set the aforementioned provisions because, in the status quo, after various improvements led by the Treasury and the Securities and Exchange Authority in recent years, there remained concern that a bank would prefer its own interest to that of provident fund colleagues and other clients whose savings it manages. He also noted that allegations were sometimes raised that a bank had made transactions, or used the voting rights of shares at the discretion of the banking group. In this situation, the peers' trust in the banks is compromised, and they may even file lawsuits against the bank. The supervisor noted that there was an opinion that the separation he had made in his orders was insufficient to prevent conflicts of interest, and that it was necessary to exclude the activities in the capital markets listed above from the bank groups; But given the potential harm to the capital markets and customers, he resorted to a more moderate system. The supervisor also noted that he believed that the bank had no legal obligation or guarantee against fellow provident funds, beyond the obligations he had expressly made. On the other hand, a bank, as noted, may be sued for managing the peer's money in conflict of interest.

Or not by professional standards. His instructions are designed to reduce this risk.

However, given the Treasury Department's position, the Supervisor of Banks that month, under the provisions of proper banking management, stated that a bank may continue to manage existing provident funds within the bank, but subject to certain provisions of the "Chinese wall" type. The Supervisor of Banks notified the State Comptroller's Office in December 1992 that these provisions had not yet been fully implemented.

By the time the audit was completed, the question raised by the Ministry of Finance had not yet been ascertained as one of the reasons for the objection to applying the supervisor's orders from June 1992 to existing bank provident funds. In this matter, the Supervisor of Banks wrote to the State Comptroller's Office in December 1992:

The Treasury's argument is that keeping management away from the bank will harm colleagues because there is a kind of guarantee of the bank to the registers managed by it. This argument has no traction in reality (beyond the direct obligations taken by the bank) and its fundamental[[58]](#footnote-58) error. The position of supervision of the banks is] that it is the prevention of conflict of interest that will ensure the safeguarding of peer affairs."

8. The provisions established by the Supervisor of Banks in June 1992 reflect a change in previous positions of the Bank of Israel, according to which banks are required to prohibit control or manage provident funds. The provisions require management through a company controlled by the bank and the existence of "Chinese walls" between it and the bank. However, it should be noted that the Planning Committee for Capital Market Reform, at the Bank of Israel, It is thought that" the main disadvantage of this approach is the relative weakness of the 'Chinese walls' in achieving their goal".

The inspector's orders were not implemented, in the end, in the face of opposition from the Treasury Department.

The Treasury Department's objection to such a partial expulsion applies to existing provident funds, in which it was possible, in his opinion, to "a question of retroactive harm to colleagues." The same injury, according to the Treasury, is due to the fact that a management company may have "zero capital," as the supervisor's directive does not include "minimum capital requirements and liability insurance

Professional" from the new corporation that will run provident funds. That is, if a colleague is created on grounds of action against the corporation that manages the register and the court determines that it has proved its claim, the corporation may not be able to compensate him due to lack of capital while the banks have a great deal of equity.

If the Objection of the Ministry of Finance stems only from the wording of the provisions that do not meet predictable problems, that then, in the opinion of the State Comptroller, it was appropriate to suggest to the supervisor of banks to amend the requiring amendment. It is inevitable that liability insurance would have answered the problem, without solely relying on a large equity investment.

9. The discussions between the Ministry of Finance and the Bank of Israel, which were reviewed above, dealt primarily with the issue of protecting the interests of savers and investors in provident funds. The management of funds and funds also affects the functioning of the capital market and its efficiency in allocating sources.

When the banks' shares are offered for sale to the public, it is presumed that the registers and funds will be among the largest purchasers of such shares; They might buy most of the shares. The Ministry of Finance and the Bank of Israel discuss proposals to prohibit, or restrict, the holding of funds and funds in shares of the bank in which they are linked. It has already been noted above that against such a reasonable restriction, there is an argument that investors in those funds and funds may be harmed by reducing the variety of investment options they face.

Despite such a restriction of holding bank shares, if it is decided, it is possible that the registers and funds of all major banks, as a group, will acquire a large portion, perhaps the majority, of all shares of all banks sold to the public. That is, there is the possibility that most of the shares of each bank sold to the public will be held by the registers and funds of the other banks. While provident funds are prohibited from appointing directors in corporations that invest in their shares, their vote, or abstaining from voting, can have a considerable impact.

Privatizing government corporations by selling shares to the public can also increase centralization in the economy, rather than reducing it, if the registers and funds associated with banks acquire a large portion, or the majority of the shares of the privatized corporations. As a result of the reform of the capital market and the removal of the limits on investment in shares by provident funds, the registers have become the main factor that has large financial reserves for investment and is expected to be able to purchase the shares of banks and the shares of the large corporations that the state will sell.

10. Against this background, the proposals raised by the Bisky Committee and the Bank of Israel's Reform Planning Team should be seen: separate the investment management of provident funds from the banks.

It is important to maintain advantages to size in banking and that there are other ways to reduce conflicts of interest arising from banks' involvement in managing funds and funds. In this context, "Chinese walls" were mentioned, and a reliance on "market control," as proposed by the Finance Ministry.

As mentioned above, "Chinese walls" are tools that are supposed to place barriers, administrative and organizational, in the face of a transition of influence and information between different units of the same organization, but these can, in many cases, be perceived as formal and unnecessary in the eyes of the people facing those "walls."

Market control is an important and worthy measure to rely on, but as its name indicates it - the same control can be more effective and effective as competition increases and centralization decreases.

One of the most important factors in market control, according to what can be learned from what is published about the U.S. capital markets, is the action of large institutional investors. These have the interest, tools and power necessary to act as "representatives" of investors, shareholders, against the managements whose power is very much with the small investors: but if a large portion of the provident funds are directly or indirectly controlled, of a small number of banks, the totality of their involvement in the capital market, and the economy in general, the smaller the chance that they will be able to properly fulfill the important role in the field of "market control."

As mentioned above, one of the important considerations raised against the separation of provident funds from banks is the existence of an advantage for size, especially in the field of marketing through the branch system. It is worth noting that this factor is likely to make it difficult for new competitors to enter this area of box office management. Therefore, market control will greatly reduce the efficiency of market control as a substitute for separating the registers from banks, and market control will therefore be more effective as a complement rather than a substitute for separation.

It is also worth mentioning that in light of the great centralization in banking and capital markets and against the great power of the bodies that manage the banking groups, the concern is raised about the reduction of power that regulators are supposed to ensure the compliance of the laws and regulations that are intended to regulate the operation of banks and other parties operating in the capital market.

It is worth mentioning in this context what was stated, among other things, in the conclusions chapter of the BayskyCommittee: "But we wish to reiterate that the absence of brake legislation enabled the regulation, but rather the violation of existing legislation by the banks and their non-enforcement bythe authorities charged with it."

11. Recently, near the conclusion of the audit report, the Ministry of Finance and the Bank of Israel had a lot of activity and there were many discussions regarding changes in the banking system and capital markets that must be made before, or in connection with, the sale of the banks.

At the end of writing of the audit report, mid-April 1993, still continue

Consultations with those bodies and the Joint Steering Committee of the Ministry of Finance and the Bank of Israel.

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### Reforms to the banking system and the sale of bank stocks

Over the period since the stock settlement, proposals have been raised to tie up the sale of shares of the banks in the arrangement with changes to the banking system. During the practical preparations for the sale of the shares, on various occasions some of which were mentioned above, the counter-argument is that such a link - between the sale of the shares and the reform of the capital market banking system - could delay the sale of the shares.

By the time this report was written, control of any of the banks in the arrangement had not yet been sold. There were certain reasons for this, but these had nothing to do with the government's desire to split the banks or initiate capital markets reform.

2. When the sale of bank shares has been rejected so far, the question arises as to whether it is undesirable and preferable, from the point of view of the national economy and the public good, to move forward the necessary changes in the banking system and capital markets to approve the sales proposals of the banks' shares to the public. As mentioned above, all public officials dealing with the issue are innocent about the importance of these changes, and the Ministry of Finance and the Bank of Israel have also recently worked jointly to plan them.

Therefore, it is appropriate to consider: (a) whether the introduction of the bank's share sales proposals outweighs the need for the necessary reform; (B) While making the sales proposals may make it difficult to carry out such a reform, thereby motivating or at least delaying it for a long time, or reducing it.

A reprieve in the sale of the shares was previously presented as undesirable for two main reasons:

(1) the delay will result in a financial loss as a result of the rejection of the receivables from the sale of the shares;

(2) The postponement will date the period in which the banks are controlled by parties who have not invested their money in purchasing a sufficient portion of the banks' money.

Rejecting the sales proposals can result in a loss to state coffers only when it cannot raise sufficient sources for its needs from the sale of state bonds, or when the cost of financing the amounts received is deferred greater than the expectedyield, in that time period, from the improvement in the value of the banks.

There's no telling if the whole addition to bank profits will find an expression in the price that will be achieved

For the shares to be sold: This also depends on the timing of the sales proposals and the state of the capital markets. It is quite possible that the improvement in the value of the shares will also be greater than the addition to the profits. However, no calculus was presented showing that postponing the sale would cause the Treasury a loss rather than a profit, even though this claim was raised in chapters.

The claim that postponing the sale of the shares would also delay the transfer of control to entities that invest their own money in banks was more valid when talking about the sale of controlling nuclear in banks. At this stage it is about selling some of the shares in the Israeli capital market, while control is expected to remain, at least in the short term, in the hands of the safe companies or another body that will receive the shares in trust on behalf of the state.

In the opinion of the State Comptroller, no compelling arguments were presented supporting the view that the introduction of the public offerings of bank stocks in a settlement trumps the need to bring about changes to the banking system, as the government will decide.

3. Changes in the banking system, which the government will decide upon, can be made in two ways. The one way is by acting as an owner. The other way is for the government to propose to the Knesset to enact laws that regulate the operation of banks in general and in the capital markets in particular. The state holds, through the safe companies, the vast majority of the bank stocks in the arrangement. The previous controlling shareholdershold approximately 3% of the shares of Bank Hapoalim and Mizrahi Bank – approximately 5% of the shares inL. and control about 13% of discount bank's shares (their ownership,in chain, is at a rate ofapproximately 7.5%-).

As long as the state, if not indirectly, holds shares, it is open to both ways to make changes that it decides. She is entitled to choose between them, at her discretion and in accordance with the circumstances. It is likely that at least some of the changes will make easier to make as owners, and that even the changes that are better made through legislation should be made as long as the government is the owner and therefore will bear the business results from such changes.

The reasons for the proposed changes are the good of the national economy and the protection of the interests of savers and investors. Changes in considerations in all farms may be perceived as contrary to the interests of banks or their shareholders.

When such changes are made according to a decision of most shareholders, the minority can oppose it, arguing that its rights are compromised. Such a minority could oppose, in public and legal ways, legislative proposals to introduce changes as described.

It is not the reality that any changes that benefit the public will severely harm the profitability of the banks and the value of their shares.

And control them. Opposition for such reasons generally serves the interests of controlling shareholders and management.

However, there may well be situations in which the economic strength of bodies with uliguapolisic status can be translated into great profitability and increased the value of banks.

The government is entitled, and is in the way, to intervene in economic activity in the economy in various ways. Any such intervention, in any way and in any field, affects the well-being and financial situation of many, for the better or for the worse. It would not be unnecessary to reiterate that the most notable case of such interference was the 1983 bank stock settlement, the same arrangement costing the Treasury billions of dollars, which were paid to shareholders, relative to the size of their holding in them, at the expense of all citizens. The arrangement was largely enjoyed by the banks themselves, who are responsible for the stock crisis, and the controlling shareholders of the banks. Once the same arrangement is made, at the expense of the Treasury, there is justification for reforming the banking system intended to benefit the entire economy, and its damages to banks, if any, will apply to the country that holds the majority of the shares.

If there is opposition to reform of the banking system by previous controlling shareholders who hold a tiny minority of the shares - much of which was given to them by the state in exchange for their consent to the comparison of rights, and which the stock arrangement has greatly benefited - it will have no moral and public validity. When there is public and moral justification, it must be assumed that the right way to do what is necessary will also be found.

If shares of banks are sold to the general public before making detailed decisions about reform and determining ways to implement them, a multiplicity of claims of "harm" to purchasers should be expected from any potential changes to the banking system. Towards the new shareholders, the state will not have the same moral and public validity that it faces with the previous controlling shareholders.

In the opinion of the State Comptroller, the Ministry of Finance and the government as a whole should consider carefully that economic benefits are expected from the introduction of the sales proposals for decision-making regarding the reform, even considering the cost of financing government debt against bank profits; And if such benefits are expected - do they outweigh the need to make, with fewer difficulties and delays, the changes to the banking system the government wants.

Summary

This accountability deals with the actions of the Ministry of Finance, the Bank of Israel and the M.I. Property Company to sell the shares of the banks that were included in the stock arrangement from October 1983, until the end of the preparation of the report, no controlling core was sold to any of the banks in the arrangement. Assets managed to sell only the shares of IDB Holdings, having separated most of the shares of Discount Bank that it owned; As well as the minority of shares of a general bank. However, the comparison of the voting rights of bank shares has been completed and proceedings have been set for the oversaling of the shares.

The share sale proceedings should be seen and evaluated against the backdrop of the actions and events that caused the October 1983 bank stock crisis and the arrangement that followed. That crisis shocked Israel's banking system and capital markets, and its implications exceeded the economic-financial sphere. The calculation of the direct damage caused to the Treasury from the implementation of the pledge to "redeem" the shares can only be done after the sale is completed. The indirect damages to the state economy and many of the civilians have also not yet been assessed, and it is doubtful that the full account will ever be held, but it is clear that they were very heavy.

The stock settlement also had negative implications in the public and social sectors. In a 1984 report on the stock crisis, the State Comptroller determined that the arrangement would have an impact "on the distribution of national income and wealth for the benefit of bank shareholders, relative to the size of their holding, and to the detriment of all others."

The terms of the arrangement were heavily influenced by the Fact that the Negotiating Teams of the Ministry of Finance and the Bank of Israel adopted "the trend to bring before the government a proposal acceptable to the banks, not to impose the arrangement on them." The arrangement was very good for the banks and the bodies and people who controlled the banks and managed them until the crisis, and which the Biski Committee found them responsible for.

The arrangement created an unacceptable and unreasonable situation in the banks. On the one hand, the state guarantees the share price and will bear the losses of banks from the regulation and business results of the banks until the date of the sale of the shares. On the other hand, the previous controlling shareholders, who had only a tiny minority of the banks' money, continued to control the banks and enjoyed the power to appoint their boards of directors. In this way, they remained very influential in israel's economic and financial activities. This position of bank managers and controlling shareholders gave them great financial and public power, and this could also strengthen their hands during negotiations over the sale of bank shares and discussions on proposals for changes to the banking system.

The decision to leave control of the hands of those who controlled the banks before the crisis had particular significance because it was known in advance that they considered themselves candidates to regain control, when the state would put the shares of the banks

For sale. This has caused a material contradiction between the country's objectives, as the actual shareholder and wants to sell them on the terms that are best for it, and the objectives of the bank managers and their controlling shareholders. The government had an interest in determining sales proceedings that would allow it to minimise the loss from the stock settlement. Minimizing loss can be done in two complementary ways to each other: one, achieving maximum monetary return from the sale of the shares; Thesecond is to achieve a not-so-financial goal: to take advantage of theopportunity, created at such a great cost, to make changes to the banking system that would seem necessary.

In contrast, the controlling shareholders, naturally, want sales proceedings that will give them priority in acquiring a share rate that will leave them in control, at as little expense as possible and without relinquishing their position in the capital markets and non-financial sectors.

It was essential, therefore, that the Ministry of Finance and an assets company do everything in their power to prevent the involvement of bank management and previous controlling shareholders in determining the sale processes, and to ensure that the government has maximum laitility in selling the shares and leading changes in the banking system and capital markets.

The sale of the shares of the big four banks included in the arrangement is a large and complex operation. These are assets worth billions of dollars. Based on such information, it was necessary to determine the timing of the sale and deployment of the various banks' shares over time.

No such planning was found to be conducted on all of the above aspects. These changes were rejected, among other things, because of fears that this would delay the sale and cause losses to the state from deferring receipt of proceeds. It did not find that the claim raised that the introduction of the sale would increase the proceeds to the state was examined at the preliminary planning stage or at any other time.

The stock arrangement created a one-time opportunity to reexability the structure of the banking system and the status of banks in the capital markets. The Bank of Israel and the Ministry of Finance, which oversee the banks and the capital markets, respectively, had to examine whether, while banking reform was necessary, and what the desired changes were, the viability of such changes and their impact on the banks' strength and stability. Such a reform should have included the maximum measures necessary to reduce as much as possible the danger that such a crisis would change

That occurred in 1983. To this end, it was appropriate to consider with full attention the findings, conclusions and recommendations of the Biski Committee.

Of all these, he pledged that immediately after the settlement, or as close to this date as possible, preparations for the sale of the shares would begin. These should have addressed the above issues and included studying the economic, locker and legal problems that might have arisen during the sale.

The audit report indicates that planning and preparations for the sale of the shares were not completed at the time necessary. When negotiations with the controlling shareholders began to compare the rights of the shares, negotiations that expanded and surrounded - miserablely - the determination of the banks' ways of selling, no preparations were completed and no working papers were in the hands of assets on all the issues on the agenda. Among other things, no summaries were prepared on the full range of aspects of possible splitting of the bank groups, a separate sale of the real corporations, and the various possibilities for this.

Although the Bank of Israel has proposed that the splitting of banking groups be a target in negotiations over the sale. But he did not prepare on time the research necessary to establish his proposal. The Bank of Israel has hung its refrain from such a thorough examination that negotiators have not adopted this issue as a destination. This explanation does not necrosis the Bank of Israel's refrain from thorough and thorough study of the subject and presents its position in a clear and well-established document.

Discussing proposals to separate real corporations from banks, assets and the Treasury Department gave considerable, unjustified, weight to a possible loss to banks incurred from paying taxes to the state; And this, too, is based on data for a particular time, which only a year later became inseter tantial to the same matter.

The steering committee that submitted its recommendations in 1988 did not address the potential effects of the introduction of nuclear sale control of banks on the possibility of causing the necessary changes in the status of banks in the capital markets and their relationship with mutual funds and provident funds. This is despite the recommendations of the Bisky Committee on the subject and the knowledge, It was already a thing of the banks that the reform of the capital market greatly changed the status of provident funds in the capital market and increased concerns about a potential conflict of interest between the roles of the banks in managing the funds and their other actions in the capital markets.

Near the conclusion of the preparation of the audit report, the discussions of a steering committee established by the Ministry of Finance and the Bank of Israel regarding changes in the banking system continued. The committee discusses proposals for structural changes in the banking system, ways to reduce conflicts of interest in the capital markets arising from banks' control of provident funds and mutual funds, and to reduce the control of banks in real corporations. In the opinion of the State Comptroller, it will make it easier for the government to institute the reforms on which it may decide following those discussions whether the detailed decisions regarding those changes will be made before the sale of a portion of the shares to the general public.

The report also found that in negotiations with the banks, government representatives did not achieve the best results: the banks did agree, after protracted negotiations, to compare the voting rights of the shares and thus waive the controlling rights of the special shareholders (although in practice they remained in control of the banks during the interim period), but for this the government needed not only to transfer to the controlling shareholders 3% of the bank's shares, but also to allow the controlling shareholders to participate in the decision. These had the added advantage over other contenders for buying nuclear controls at banks. They had complete and detailed information about the state of the banks, while other potential buyers had to make do with in-part information. This increased the risk they took and anyway reduced the addictive value and price they should offer. Obviously, any reduction in viability for the other contestants was there to inflict a loss on the state.

The willingness of the Ministry of Finance and assets to go towards the controlling shareholders found a prominent expression in the way in which control of IDB Holdings was sold: there was an uninterrupted adjustment to the will of the controlling shareholders and their needs. And under conditions that gave them priority and were not optimal for the state. When a situation was created that did not allow the controlling shareholders to purchase IDB as a single piece - due to the filing of criminal charges against them - the sellers agreed to a partial split of IDB Holdings, in a format specifically tailored to their needs.

The concessions made by properties to the controlling shareholders were explained by concerns about a lawsuit by buyers that could have caused, among other things, the sale to be rejected, but it is not at all clear that the government had more interest than buyers to complete the sale quickly, and the mere fear of such a claim could have encouraged the controlling shareholders to use it to their advantage.

State negotiators have come a long way toward banks and their controlling shareholders, reducing the likelihood of minimizing damage from the 1983 arrangement. Government officials in the negotiations explained that they sought to avoid any act that might be construed, rightly or wrongly, as nationaling the banks or the intervention of the government or its representatives in their management, if only for appearances. Of the same taste, legislation was also refrained from being used to protect the country's interests.

In fact, since the stock crisis in 1983, it has been the government's policy to refrain from nationalizeing the banks and interfering with their management. This imparted another bargaining chip in the hands of the controllingshareholders.

The same image of nationality they feared. In this context it was appropriate to examine the significance of concentrating such great power in the capital market by a small number of bankers; For concentrating power in the hands of private bodies can also have undesirable consequences. Nor was the question of why the only alternative to nationality was the handover of control of Israeli banking and capital markets to the parties that controlled the banks before the 1983 stock crisis.

In contrast to its refrain from nationaling the banks, the government "nationaled" the losses incurred by the banks in the past and those that might have been during the period until the share sale.

The results of negotiations with the controlling shareholders on the various issues were influenced, as noted, by the discourageance of non-consensual action with the banks. Of course, it would have been better to obtain consent and not need coercion through legislation or otherwise. But this recoil is less understandable under the special circumstances of the sale of bank shares. As mentioned above, there is a fundamental contrast between the government, as the shareholder, and the controlling shareholders of the banks. In this situation, when the government pre-corded its hands, and this was arrogant to the other side, the results could not help but be affected. In the case in question there was a public and moral justification for the use of any advantage that the state could make available to negotiators.

Appendix: Detailed Memorandums of Principles and Agreements

##### Bank Hapoalim

Memorandum of Principles

In January 1990, a memorandum was signed and approved to compare rights and determine an agreed sales process between the Ministry of Finance and Assets and the General Histadrut of Employees and the Company of Employees. Its contents are similar to a memo agreed with the controlling shareholders of IDB, with the exception of these differences:

1. Assets undertook to sell a controlling core at Bank Hapoalim within a year of approval of the memo by the competent bodies. The controlling core offered for sale will be at a rate of 25% - 51% of the share capital.

2. As long as it has not sold 75% of Bank Hapoalim's shares, or it has not been seven years since the sale of a controlling core of the bank, according to the earliest of them, Bank Hapoalim or the government or both will vote together with the purchaser of the controlling core, so that in the Bank Hapoalim meetings the purchaser will have at least 51% (hereinafter - the completion of the majority), provided that the proposals that are to be voted on will not be infringed upon.

3. Assets and Bank Hapoalim will conclude between them, within 30 days of the memo's approval, a list of corporations that will be split from Bank Hapoalim and sold separately.

Agreement from October 1991

In early October 1991, a detailed agreement was signed between the government and assets and the General Histadrut of workers in Eretz Israel, the Workers' Company, Bank Hapoalim and Bank Hapoalim Ltd. to compare voting rights in Bank Hapoalim, and an agreed sales process was established.

The following are the main points of the Agreement (except for terms similar to those set forth in the May 1990 IDB Agreement):

1. The sale of the controlling interest in the bank will begin within a year of comparing the rights, or at a later date, agreed upon by the[[59]](#footnote-59)parties.

2. The total sales of the bank's shares held by the Safe Company in public and employee offers should not exceed 48.8% of the bank's total share capital.

3. The company of employees and bank hapoalim and officers in which they will not engage in the sale of shares held by the safe company, and will not contact applicants who are not required by agreement.

4. Provisions regarding the appointment of external directors and their powers have been established (see this report, p. 00).

5. Notwithstanding the provisions of the loan agreements, the Safe Company may use the voting rights that its shares hold.

6. The Employees Company and Bank Hapoalim undertook to cooperate and provide information to assets and applicants; prepare prospectuses at the request of assets; refrain from any act or omission in order to thwart the implementation of the Agreement; And do their best to promote the sales process.

7. Although the memo states that the parties will determine an agreed list of corporations that will be split from Bank Hapoalim and sold separately, no such list has been determined.

##### Bank Leumi

Memorandum of Principles

On 30 January 1990, assets and the Ministry of Finance signed on the one hand, and the Treasury of Jewish Settlement (hereinafter – O.H.H.),which is the controlling shareholder of the B.L.A., on the other hand, signed a memorandum ofprinciples.

1. It was agreed that a union bank would be sold separately from B'Al, and that until the General Assembly convened to compare the rights, the parties would make an agreed list of other B.L.L. companies that would also be sold separately.

During the entire period of negotiations following the signing of the memo, the Finance Minister did not decide whether more B.L.A. corporations (other than a union bank) should be sold separately from B'Elal (other than a union bank) and if so, which corporations would be sold separately. Anyway, assets could not submit to the B.L.A. its demands on this matter, so that it would be agreed between the parties, as stipulated in the memo. The way it was about Bank Hapoalim.

2. The sale of a controlling core in the BLD will begin within 18 months of the memo's approval.

3. Assets will be entitled to terminate the sale process, if it becomes clear that it is impossible to sell a controlling core at a price that is at least equal to the minimum estimate it will set for itself, or if for some other reason it is impossible to reach an agreement whose terms are adequate and reasonable.

4. The completion of the majority of voting rights granted by the government to the controlling shareholder will be for a period of five years (not seven years, as stipulated in a memo signed with the controlling shareholders of Bank Hapoalim).

5. A controlling core of 25% to 75% of the share capital will be offered for sale.

6. The information provided to evaluaters and applicants approved by the Bank of Israel will be subject to the confidentiality arrangements established by assets, in coordination with the Supervisor of Banks and after hearing the position of L.L.A.

**Union**Bank: 1. O.H.H. undertook a memorandum from January 1990 to also act to ensure that the BLD (which is not a signatory to the memo) compares voting rights in union bank shares and agrees to asset requests regarding the sale of shares of a union bank in its hands, in all or part of it.

O.H.H. also pledgedthat unless voting rights are equal to the shares of a union bank or no agreement is reached for the sale of B'L.L.'s shares in a unionbank as stated, within 45 days of the memo's approval, The Safe Company and O.H. will convene the General Meeting of Shareholders in the B.L.L. to make a decision that the authority to act on the sale of the shares of B'Elal at The Union Bank will be in the hands of the General Assembly of B'L.L. instead of the Board of Directors of L.A.L., and assets will be entitled to instruct the Safety Company on how to exercise its rights in the matters stated in the General Assembly of the L.A.L.E.L.D.

2. The negotiations that held assets with B'L.L. and its controlling shareholders after the signing of the Memorandum of Principles in January 1990, in order to reach a detailed agreement, was delayed, among other reasons, for these reasons: (a) the refusal of the L.A.L.L. to allow the assets to separately sell the shares of a union bank held by the safe companies and its holdings; (B) The requirement of B'L.L. to be paid 3% of the union bank's equity in exchange for comparing voting rights in this bank, even though in a memorandum signed by assets and the Ministry of Finance with O.H.H. was not granted the right to receive a return in favor of comparing voting rights in a union bank.

In September 1991, the Minister of Finance informed the Chairman of the L.A.L.E.L.D. that he was adopting the principled approach of the Chairman of Assets and the Legal Advisor of the Ministry of Finance, According to which the Ministry of Finance is not obligated to pay compensation to the B.L.A., the minister requested that B'Elal make the voting rights compared without delay and without condition, and that assets and the L.A.L.P. jointly sell the shares of a union bank held by the Safe Company and the L.A.L.L., the minister informed the chairman of B.L.L., that if B'Elal did not respond to this request, he would resume legislative proceedings in the Knesset for the comparison of voting rights.

3. In November 1991, the Minister of Finance agreed to awardthe B'Al compensation equal to 1.5% of the shares of The Union Bank.

4. In the same month, the Supervisor of Banks informed the Minister of Finance of the Position of the Bank of Israel, according to which the preferred option at the time was the separation of the Bank of The Association of M.L.L. and its merger with another medium-sized bank in order to create a competitionable factor for the large banks.

In September 1992, the Bank of Israel approved the First International Bank as one of the candidates for the acquisition of a union bank. The Bank of Israel has determined that if the International Bank wins the contest, it will have to merge the business of a union bank in its business.

Agreements from December 1991

In December 1991, the government and assets signed two agreements: the first with O.H.H. and B.L. Safe, and the second with B'Elal, Bank Igud and B'Elah Safe.

1. O.H.H. and B'L.L. will compare voting rights in the B.L.A. and union bank, respectively.[[60]](#footnote-60)

That same month, the Knesset Finance Committee approved the payment to B'L.A. in exchange for comparing the rights in a union bank.

In March 1992, the Ministry of Finance explained to the State Comptroller's Office that the compensation was provided to the B'Al:

"constitutes an 'internal' transfer and not the removal of an asset out. The safe company has 98% of the B.L.A. before compensation and [[61]](#footnote-61)95%aftercompensation.

In the opinion of the State Comptroller, since B'L.L. is an independent business body whose level of expenses is also affected by its income, this compensation should not be considered a pocket-to-pocket transfer. There is no basis for the discount, that this transfer of funds from the state coffers to the B.C.L. will find expression in the abat of the bank's value and in increasing the proceeds to the state from the sale of its shares.

2. The agreement stipulates that a joint team of assets and the L.A.P.L. (two representatives for each party) will offer for sale, by way of dealing between candidates, a controlling core of a rate exceeding 50% of the origin share capital of a union bank. The team will also discuss and decide matters regarding all other banks under the sole authority of the government and assets, including: approval of applicants according to aspects - similar to those in the IDB agreement - which may somewise have an advantage over any other candidate; and the termination of the sale process, if it becomes clear to the team that the core control cannot be sold on reasonable and proper terms.

The Ministry of Finance explained to the State Comptroller's Office in March 1992 that in his opinion, the clause in which the finance minister's decision authority was established was practically the same as the determination that the government had the authority to decide on a particular matter.

Given Bala'l's ambition to acquire The Union Bank, and considering that it is known to the B.L.A. and the other candidates that unless the team sells a controlling core, the possibility of selling it to B'L.L., there would be no place, in the state comptroller's opinion, to establish the team in the aforementioned composition. It was appropriate for the government to be free to sell the shares of a union bank held by the Safe Company, and even the shares of a union bank held by B'Elal (as stipulated, as stipulated, in the Memorandm of Principles, if no agreement is reached in this matter) at its discretion, without giving the B.L.A. the option of influencing the sale. It is unlikely that anyone interested in buying an addictive one will at the same time also share the sale of the same addictive.

3. The memo states that the parties will formulate an agreed list of other companies (other than a union bank) that will also be sold separately. No such list has been determined.

##### Eastern Bank

Memorandum of Principles

In February 1990, a memorandum was signed between assets and the controlling shareholders of Mizrahi Holdings Bank (hereinafter – Mizrahi Holdings), which establishes an arrangement similar to that agreed with O.H. regarding L.L., except for these differences:

1. The controlling core will be at a rate of 25% or higher (in fact, up to 96.97% i.e. all share capitalexcept 3%- which the governmentwill hand over to the controllingshareholders and 0.03%- which were in the hands of the controlling shareholders in the first place).

2. No binding date has been set for assets to begin the process of selling the Eastern Bank.

3. Assets will decide, after consultation with the Bank of Israel, on the extent of the group's split.

Agreement from August 1990

In August 1990, an agreement was signed between the Government of Israel and Assets and Mizrahi Holdings and Mizrahi Safe to compare voting rights and an agreed sales process (hereinafter – the Agreement from August 1990).

Unlike the agreement signed with IDB, the agreement left the assets full discretion with regard to the dates of the sale process. In addition, the agreement stipulates a clause regarding the possibility of postponing the sale, which is similar to Article 16 of the May 1990 agreement with the controlling shareholders of IDB, but rather gives the government and assets freer discretion.

The following are the main points of the August 1990 agreement, in addition to those in the memo:

1. In regards to the issuance of shares or securities converted into shares of Mizrahi Bank, and the splitting of subsidiaries of Mizrahi Bank, the powers will be granted to the General Assembly of The Eastern Bank.

2. In light of the announcement by the Supervisor of Banks that in the status quo, Tefahot Bank should not be sold separately from Mizrahi Bank, but if the status of Mizrahi Bank changes, its position may also change, assets pledged that it would not initiate the splitting of Tefahot Bank, prior to a year after the agreement was signed. In fact, the Treasury department and assets chose to sell Eastern Bank in one piece.

3. Mizrahi Holdings will do its best to ensure that Mizrahi Bank cooperates fully with assets and the parties it authorizes, with regard to providing information for the purpose of evaluating the bank's valuation and shares, and for preparing documents that include detailed information about the bank.

4. Mizrahi Holdings has pledged that it and entities under its direct or indirect control will not engage in the sale of shares held by the safe companies or the government, and will not provide information to interested parties and candidates, except with written consent given by the government or assets.

Agreement from March 1991

Mizrahi Bank is not a party to the August 1990 agreement, in March 1991 an agreement was signed between Assets and Mizrahi Bank. Under the agreement, the bank undertook to cooperate with the government and assets to help the sale process of its shares, including handing over to an appreciative who had appointed assets to assess its value. The material he will require for his work, except for details of the bank's banking business and audit reports of the Supervisor of Banks. It is determined that the evaluater must sign a commitment to maintain confidentiality and refrain from using the material except for the purpose of making the assessment. Assets will not be able to obtain, without the bank's consent, the material used by the evaluater for his work, but only the opinion of the exponent and his explanatory notes.

The Bank has agreed to allow applicants approved by assets and the Bank of Israel to perform due diligence accordingto theseterms:

1. The examination will be conducted by an evaluater on behalf of the applicant, who will be approved by the Board of Assets and the Board of Directors of Mizrahi Bank.

2. The assesser will be entitled to check for the buyer only one-third of all loans made by the bank – one-third of which includes the loans given by the bank to its largest borrowers – and will also be entitled to review the audit reports of the Supervisor of Banks on credit and the bank's responses to these reports.

3. The evaluater will not transfer to the applicant, without the bank's consent, the material used by the evaluater for his work, but only his opinion and assessment of the bank's value and explanations for that assessment.

The sale process of Mizrahi Bank

Following the August 1990 agreement, voting rights in Mizrahi Bank shares were compared to a special meeting of shareholders convened at the Mizrahi Holdings 5770 a month later.

In October 1990, Assets issued an invitation to receive proposals to acquire a controlling core at Mizrahi Bank.

According to the public appeal to those interested, they were asked to announce, within two months of publication, their intention to participate in the contest. At the deadline for submitting a notice, five groups announced their participation. Following the events of the Gulf War, Properties decided to allow those interested in submitting questionnaires intended to test their competency as candidates.

At the end of February 1991, the Property Board decided to authorize four interested groups to participate in the contest, and to repay the fifth group because it did not give the required information to the assets.

At the end of August 1991, the Governor of the Bank of Israel approved the four challengers.

The sale process was delayed far beyond necessary, in part because of disagreements between assets and the Eastern Bank regarding the extent of the information provided by the bank to the assessor who appointed assets, and disagreements regarding the competency of the evaluator chosen by one of the bidders to perform a .due diligence examination.

In August 1992, at the end of negotiations with the three remaining candidates in the contest (after one withdrew from it), an agreement was signed between treasury and assets and the candidate who offered the highest price - $100 million for up to 25% of the bank's shares.

In December 1992, the Governor decided not to give this candidate a permanent permit to purchase control of the bank. As a result, the deal was not reached.

The State Comptroller's Office has not yet examined the process of selling the core control of the bank and the dangling of matters that resulted in the controlling core not being sold.

##### General Bank

The controlling shareholders of General Bank held75.29%of the share capital and 79.57%of the voting rights before comparing voting rights.

After the last "redemption" of bank stocks in October 1991, the Safe Company held about 24.7% of General Bank's shares.

1. See the State Comptroller's Report on Bank Stocks - October 1983 Crisis below - State Comptroller's Report on the Bank Stock Crisis), December 1984, Chapter 4, "The Economic and Public Implications of Regulating Bank Stocks" (p. 37). [↑](#footnote-ref-1)
2. See the State Comptroller's Report on the Bank Stock Crisis, People (sur)', 65-66. [↑](#footnote-ref-2)
3. The common phrase "redemption of bank stocks in the arrangement," mentioned in this report, is inaccurate: in fact, the government funded the purchase of the shares by "safe companies" (see below). [↑](#footnote-ref-3)
4. See the State Comptroller's Report on the Bank Stock Crisis, pp. 58-61 . [↑](#footnote-ref-4)
5. The value of the "redemption" promised to banks for shares The Nostro It was the same as that promised for shares held by the public, and which were not blocked, but were tradable until the date of "Padionen" in October 1988, see the State Comptroller's Report on the Bank Stock Crisis, p. 61).

Regarding "redemption" of shares The Nostro In October 1988, see Annual Report 40, pp. Take. [↑](#footnote-ref-5)
6. See the State Comptroller's Report on the Bank Stock Crisis, pp. 61-62 . [↑](#footnote-ref-6)
7. The shares held by El-Yim have bought her more than10%- From voting rights at IDB. A Memorandum of the Bank of Israel (which is unsigned and does not bear a date), which was writ ahead of the hearing in October 1983, stated that el-Yum Was One of three companies of interest, who cooperated regularly and held together in 15%- from IDB's share capital as a fixed investment; The same shares bought for the three companies together as37%- From voting rights in IDB Holdings (see more below, p. 00). [↑](#footnote-ref-7)
8. The employee company actually sold the shares, indirectly, to the government. An audit of the terms and conditions of this arrangement, see Annual Report 37, pp. 101-106. [↑](#footnote-ref-8)
9. The safe company established by the controlling shareholders of each of the banks in the arrangement is Company Ltd., which is designated to purchase the bank's shares from the public (and shares) The Nostro - from bank corporations) according to the terms of the "redemption" set forth in the arrangement, and holding them during the interim period. The only source of funding for the safe companies is in special loans from the state budget. [↑](#footnote-ref-9)
10. Property is a government company that the Finance Minister tasked in November 1988 with advising him on matters related to bank stocks and addressing various aspects of their sale (see below). [↑](#footnote-ref-10)
11. Inbal is a government company that performs various services for the General Accountant and government ministries (see Annual Report 42, p. Sue); Among other things, it manages for the government the records relating to the shares of banks that have been "cashed in." [↑](#footnote-ref-11)
12. Regarding the measures taken by the Treasury and the Bank of Israel to prevent harm to the economic value of bank stocks, see below, p. 00. [↑](#footnote-ref-12)
13. including shares of banks purchased by the government on and off the stock exchange prior to the scheduled "redemption" dates; See annual report 41, pp. Ki-vomit. [↑](#footnote-ref-13)
14. State Comptroller's Report on the Bank Stock Crisis, p. 67. [↑](#footnote-ref-14)
15. The "redemption" values were pegged to the dollar rate and were thought to be at a very low interest rate. As a result, "redemption" values were less high, in real terms, than the stock rates on the eve of the crisis. [↑](#footnote-ref-15)
16. The intention is that a mole would prevent the unwarranted preference of a particular candidate, including the preference of a candidate who enjoys a position of power in negotiations with the Treasury Department over comparing voting rights. On the other hand, it was justified for the Bank of Israel to rank the candidates according to equal standards of: integrity, professional ability of the management teams offered by the candidates, financial steadmostness, conflict of interest, etc.; and bring the quality rating of candidates to the attention of the Ministry of Finance and Assets, so that these will be taken into account, along with comparing the bids, in choosing the candidate who will win the contest. [↑](#footnote-ref-16)
17. On the conflicts of interest that banks control provident funds entails, and the need to address them, a critic pointed out The Midana Also in the State Comptroller's Report on the Bank Stock Crisis, pp. 34-35 , p. 82 and Annual Report 35, pp. 53-63 . [↑](#footnote-ref-17)
18. On the necessity of repairing the control structure of the provident funds due to the connection between the control of the banks in the provident funds and the preparations for the sale of bank shares, the State Comptroller's Office to the Ministry of Finance in October 1991 and again in October 1992. [↑](#footnote-ref-18)
19. See below, p. 00, 100, and 00. [↑](#footnote-ref-19)
20. See this matter below, 00. [↑](#footnote-ref-20)
21. See below, p. 00. [↑](#footnote-ref-21)
22. Mainly: disassembly, upsizing, or merging; Issuance of securities, any overall changes in the bank's business or the business of a company controlled by the bank. [↑](#footnote-ref-22)
23. In a committee report Bisky (sur) (pp. 376-377) states, "It is inconceivable that interests should be shared in such a sensitive decision or in the body recommending this matter." It also said that one of the recommendations of the staff appointed by the Governor (which is not presented here) was in it (had it been implemented) to indirectly benefit the stakeholders in the banks - "the same group of people who were not supposed to benefit from the arrangement." In fact the staff recommendation has not been implemented. [↑](#footnote-ref-23)
24. See the State Comptroller's Report on the Bank Stock Crisis, pp. 32-35 p. 82 and 89; And in annual report 35, pp. 53-63. [↑](#footnote-ref-24)
25. The document did not mention the steering committee and did not say it was intended to present its recommendations. The document was printed as a document of the Deputy Finance Minister, but not signed. [↑](#footnote-ref-25)
26. The phrase "government-held bank stocks" in the steering committee's document concerns the shares of banks held by the safe companies, which the government funded as "padionen." [↑](#footnote-ref-26)
27. See more on this matter there, pp. 337-339 . [↑](#footnote-ref-27)
28. The first right of refusal means that the right owner is entitled to purchase The Sellout On terms offered by the best bid holder in the competition. [↑](#footnote-ref-28)
29. The C.I.A. The 5770s, 62. [↑](#footnote-ref-29)
30. Under the same agreement, IDB transferred to Safe Company the majority of discount bank's shares (see below, p. 00). [↑](#footnote-ref-30)
31. Whereas the controlling shareholders held9%- From the shares (see more below, p. 00), their offer to purchase 42%, for example, is equivalent to John Doe's offer to purchase 51% (the largest nucleus that can be purchased in the tender). [↑](#footnote-ref-31)
32. Market evacuation - avoidance of the government from selling additional shares of the company, for six months from the date of the sale of the controlling core. [↑](#footnote-ref-32)
33. Regarding the importance of auditing the work of evaluaters in privatization transactions, see Annual Report 40, p. Kling (s) - Input. [↑](#footnote-ref-33)
34. Detail regarding memos and agreements signed with the other banks - see the appendix to this report. [↑](#footnote-ref-34)
35. HCJ 943,940,935/89 Ganor et al. v. Attorney General et al., P.D. Med(2) 485. [↑](#footnote-ref-35)
36. The offer is unsigned and does not carry a date. [↑](#footnote-ref-36)
37. The May 1990 agreement did not explicitly state that IDB must prepare a prospectus for a share sale offer, if requested by the government. This obligation was expressly set out in the August 1991 Agreement. In practice, there were delays in preparing the prospectus for the sales proposal made in November 1992, as a result of substantive disagreements between assets and controlling shareholders. [↑](#footnote-ref-37)
38. Attorney General's opinion from April 1991. [↑](#footnote-ref-38)
39. For clarity' sake, it should be noted that under the agreement the controlling core was supposed to be sold by way of competition, during which assets may allow candidates to improve their bids. [↑](#footnote-ref-39)
40. Their approval of the deal was needed because IDB Development owns83%- From the share capital of an investment firm, which held18%- Shares of a banking subsidiary of Discount Bank in New York (see below). [↑](#footnote-ref-40)
41. defined as 31.10.91, or later, if the necessary approvals are delayed to execute the agreement, but no later than the end of February 1992. [↑](#footnote-ref-41)
42. For clarity, it should be noted that in the interest of limiting the holding of controls in the bank, there are no computers in chaining the rates Attachments The partiality and the override. [↑](#footnote-ref-42)
43. The figures here are of the company's market value according to the share price traded on the stock exchange as set out on the last day of each month (Source: Tel Aviv Stock Exchange - "Stock &amp; Securities Tombstone The Converters listed for trading on the Stock Exchange"). It should be noted that in September 1990, when Assets decided not to postpone the deadline for applying for a controlling core acquisition of IDB Holdings, IDB Development's market capitalization was less than $400 million. [↑](#footnote-ref-43)
44. It should not necessarily be concluded that the price would have decreased had IDB Development shares been offered for sale on the stock exchange; Experience in recent years shows that the opposite could have been true, too. [↑](#footnote-ref-44)
45. The chart itself did not show the connection between IDB Holdings, through IDB Development and its subsidiaries, and El-Yam and the controlling shareholder company. [↑](#footnote-ref-45)
46. "The cluster of companies consisting of IDB, the companies controlled by it directly ..., and the subsidiaries and related companies of the controlled companies as stated ..., all if not stated otherwise in this agreement ...". [↑](#footnote-ref-46)
47. The acquisition of shares of a company by a subsidiary, a granddaughter company, etc. of that company is considered a kind of reduction in the company's capital. It should be noted that such action is not prohibited per se; Section 139 of the Companies Ordinance states: "You will not give a company to any person directly or indirectly with financial assistance ... To buy her shares. [↑](#footnote-ref-47)
48. Including shares in the settlement that were "redeemed" - see above. [↑](#footnote-ref-48)
49. See this matter below, p. 00. [↑](#footnote-ref-49)
50. According to figures from the Capital Markets Division, the remaining assets of provident funds - including advanced study funds, but excluding pension funds and insurance funds (special provident funds for life insurance, managed by insurance companies) - Was At the end of December 1992, worth NIS 84.1 billion; And the weight of said provident funds from the public's total financial asset portfolio was 25%. About two-thirds of all these provident funds - which have 81% of the remaining assets of these provident funds - are managed by financial institutions - mainly banks (the rest are provident funds of various enterprises and institutions).

According to a publication by the Bank of Israel - "Capital Market Developments - 1992" - The remaining assets (in market values) of mutual funds for the end of December 1992 Was NIS 28.7 billion; More than 90 percent of mutual fund assets are in the hands of bank management companies. [↑](#footnote-ref-50)
51. Securities Law (Amendment No. 9), 5748- 1988. [↑](#footnote-ref-51)
52. The C.I.A. The 1990s, 53. [↑](#footnote-ref-52)
53. In a report on the bank stock crisis (pp. 24-25 and p. 82), the State Comptroller pointed out that many provident funds purchased shares of the banks that control them, and that the Capital Markets Department did not act to prevent this phenomenon.

In annual report 35 pp. (53-63), the comptroller pointed to numerous deficiencies in the supervision of the Capital Markets Division on provident funds in regards to the conflicts of interest between them and the banks that control them, particularly in connection with the purchase of bank shares during the period of stock regulation. In the summary of this audit, the comptroller determined:

"The importance of applying the lessons of the audit will increase if the government decides to reduce the investment rates of the registers in treasury obligations, and to expand the discretionary area of the register managements in choosing the financial assets in which their funds will be invested." [↑](#footnote-ref-53)
54. In October 1992, the State Comptroller's Office voted before the Department on real deficiencies in the reporting of provident funds for their dealings with related parties in the framework. The Lights For their financial statements, and the need for the wing to improve the format The Lights. In this matter, see also Annual Report 40, p. 25. [↑](#footnote-ref-54)
55. Amendment to income tax regulations (rules for approval and management of provident funds), 5744- 1964. [↑](#footnote-ref-55)
56. The State Comptroller's Office pointed to Loophole (syringe) Broad in the formulation of this restriction (see Annual Report 38, pp. 43-44). [↑](#footnote-ref-56)
57. The Capital Markets Division informed the State Comptroller's Office in April 1993 that provident funds that these criteria had not been met were also attached by external directors to their investment committees. [↑](#footnote-ref-57)
58. This refers to the obligations under which a bank vouches for each colleague in a provident fund under his control, to pay the nominal amount (without linkage and without profits) that the peer has placed in the register. [↑](#footnote-ref-58)
59. In fact, the sale of a controlling core was not applied within a year of comparing the rights. [↑](#footnote-ref-59)
60. The agreement stipulates that for this purpose, the share price will be determined by the price determined in the agreement of the sale of the controlling interest in a union bank, and if shares are offered first by way of prospectus or by tender, the share price will be determined according to the price determined in the prospectus or tender, as applicable. The agreement also stipulates that the proceeds will be paid only if the purchaser of the controlling core is not in L.A.L., or a body under his control or on his behalf, or a purchaser with whom B.L. participates in the acquisition directly or indirectly. [↑](#footnote-ref-60)
61. This means that only 5% of compensation - which is 0.078% of the share value of a union bank - will come indirectly Lao H.H.. [↑](#footnote-ref-61)