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Israel: Detailed Assessment of IOSCO Objectives and Principles of Securities Regulation

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FINANCIAL SECTOR ASSESSMENT PROGRAM UPDATE

ISRAEL

IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION

DETAILED ASSESSMENT OF OBSERVANCE

MARCH 2012

INTERNATIONAL MONETARY FUND
MONETARY AND CAPITAL MARKETS DEPARTMENT

Contents Page

GLOSSARY

AEC	The Administrative Enforcement Committee under Chapter 8D of the Securities Law
Bachar Committee	The Bachar Inter-Ministerial Committee on Structural Reform of the Capital Market
Bachar Law	The Law for Enhancing Competition and Reduction of Concentration and Conflicts of Interest in Israel's Capital Market—2005
BCH	Banks' paper-based clearing house
BI	The ISA's Business Intelligence market surveillance system
BOI	Bank of Israel
CCMIS	Commissioner of Capital Markets, Investment, and Savings
CEOs	Chief executive officers
CFO	Chief financial officers
CMISD	The Ministry of Finance's Capital Markets, Insurance and Savings Division
CIS	Collective investment scheme
Companies Law	The Companies Law—1999
CPA Law	The Certified Public Accountants Law 1955
Economic Court	Economic Section of the Tel Aviv District Court
ETN	Exchange traded notes
FSAP	Financial Stability Assessment Program
GAAP	US General Accepted Accounting Principles
IA Equity and Insurance Regulations	The Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management—Regulations (Equity and Insurance)—2000
IA Internal Procedures Directive	The directive to licensed corporations concerning the duty to determine work procedures for their operation and management under the Investment Advice Law
IA Records Regulations	The Regulation of Investment Advice, Investment Marketing, and Investment Portfolio Management Regulations (Recording of Transactions and Investment Advice Activity)—2007
IASB	The International Accounting Standards Board
ICPAS	Institute of Certified Public Accountants in Israel
IFRS	International Financial Reporting Standards
Investment Advice Law	The Regulation of Investment Advice, Investment Marketing, and Investment Portfolio Management Law 1995
IOSCO	International Organization of Securities Commissions
IOSCO MMOU	The IOSCO Multilateral Memorandum of Understanding
IPO	Initial Public Offering
ISA	Israel Securities Authority
Israeli SOX	Internal controls on periodic disclosure in financial statements

IT	Information technology
MAGNA	The ISA's automated regulatory filing system
MAOF	The Tel Aviv Stock Exchange's MAOF derivatives exchange
MAOFCH	MAOF Clearing House
Manof funds	Government-owned investment funds
Masav	Automated clearing house
MF Asset Valuation Regulations	Joint Investment Trust (Purchase and Sale Prices of a Fund's Assets and Value of a Fund's Assets) Regulations 1995
MF Conflict of Interest Regulations	Joint Investment Trust (transactions that may involve a conflict of interests, substantial transactions and transactions outside the stock exchange) Regulations—1995
MF Equity, Insurance and Suitability Regulations	Joint Investment Trust (Equity and Insurance of the Fund Manager and Trustee and Criteria for Suitability of Directors and Members of the Investment Committee) Regulations 1995
MF Financial Statements Regulations	Joint Investment Trust (Financial Statements of a Fund) Regulations 2009
MF Prospectus Regulations	Joint Investment Trust (Details, Structure and Form of a Fund Prospectus) Regulation -2009
MF Reporting Regulations	Joint Investment Trust Regulations (Reports) 1994
MOF	Ministry of Finance
MOU	Memorandum of Understanding
MOU on Coordinated Capital Market Regulation	The Memorandum of Understanding concerning cooperation and exchange of information between the supervisor of banks, the Israel Securities Authority and the Capital Markets, Insurance & Savings Division of the Finance Ministry 2006
MTS Israel	Government bond auctions
Mutual Fund Law	The Joint Investment Trust Law 1994
NIS	New Israeli shekel
OTC	Over-the-counter
PCAOB	US Public Company Accounting Oversight Board
Private Placement Regulations	The Securities Law Regulations (private offering of a securities in a listed company) 2000
Prospectus Regulations	The Securities Law Regulations (details, structure, and form of prospectus and draft prospectus) 1969
Proxy Regulations	The Companies Law Regulations (proxy voting and position statement)—2005
REIT	Real Estate Investment Trust
Related Party Regulations	The Securities Law Regulations (transaction between a company and A controlling shareholder therein)—2001
REPO	Repurchase
Reporting Regulations	The Securities Law Regulations (Periodic and Immediate Reports), 1970
Securities Law	The Securities Law 1968
SRO	Self-regulatory organization

Statement of Reasons Law	Administrative Procedure Amendment (Statement of Reasons) 1958
Supervisor of Banks	Bank of Israel's Bank Supervision Department
TACT	Tel Aviv Continuous Trading automated traded system
TASE	Tel Aviv Stock Exchange Ltd
TASECH	The Tel Aviv Stock Exchange Clearing House Ltd
Tender Offer Regulations	Securities Law Regulations (Purchase Offers) – 2000
Zahav	Bank of Israel's real time gross settlement payments system

I. SUMMARY, KEY FINDINGS AND RECOMMENDATIONS

1. **The regulatory regime is well developed and in most respects is comparable to that in major jurisdictions.** For the most part, it is compliant with international standards and regulation and oversight by the Israel Securities Authority (ISA) is robust and effective. Significant changes have been made to the regime in recent years and a large number of initiatives are in the process of being finalized, or are at the planning stage. At the time of the assessment, the ISA had already begun work to address many of the deficiencies noted in this report; when these efforts are completed, the degree of compliance should be significantly higher, and certain risks reduced.

2. **The regulation of broker dealers is a significant gap in the coverage of the regulatory regime**. Broker-dealer activity can be undertaken without falling within the regulatory framework, if the activity does not involve membership of the stock exchange or the provision of advice services to retail clients. Similarly, additional over-the-counter (OTC) derivatives activity, including the sale of products to retail investors, can take place outside the regulatory regime. The absence of a licensing framework for intermediaries of this kind could have serious implications for investor protection and (if unregulated activity grew to a significant size) could potentially have an impact on overall market stability. It also means that comparable regulation does not apply to like activities, since, for example, the broker-dealer activities of members of the Tel Aviv Stock Exchange (TASE) are regulated though the securities laws. Note, however, that the ISA has initiated a legislative proposal to regulate the activity of investment intermediaries in Israel by creating a comprehensive regulatory framework designed to encompass all investment intermediaries and all products associated with investment activity. A draft of the proposed legislation was published for public comment in October 2010.

II. INTRODUCTION

3. **This assessment was carried out as part of the Financial Stability Assessment Program (FSAP) Update mission to Israel that took place between November 6 and November 22, 2011.** The assessor[1] relied on number of sources in carrying out the assessment, including a review of the relevant legislation, a self-assessment and other material prepared by staff of the Israel Securities Authority (the ISA), detailed discussions with the staff of the ISA and other regulatory authorities, a range of market participants and representative bodies, and others expert in the securities market in Israel.

4. **The assessor thanks the staff of the authorities for their participation in the process and for their comprehensive self-assessment.** Staff of the ISA were particularly

[1] The assessment was performed by Malcolm Rodgers, former Executive Director and Acting Commissioner of the Australian Securities and Investments Commission.

generous in making themselves available for discussions that were helpful and frank, and in providing requested information and copies of the relevant legislative and regulatory texts. The assessor also values the assistance and information provided by other regulators and market participants.

5. **This is the second assessment of the Israeli system against the International Organization of Securities Commissions (IOSCO) Principles, with the first being conducted 2001.** That assessment against IOSCO Objectives and Principles concluded that securities regulation in Israel was on a sound footing and achieved a high degree of compliance with IOSCO principles. Twenty five Principles were rated implemented, and four Principles were rated partially implemented; one Principle (Principle 30) was not assessed. It should be noted that the first assessment was undertaken before IOSCO had finalized a detailed methodology for assessment, including the assessment categories described below.

III. Information and Methodology Used for Assessment

6. **The assessment was conducted based on the IOSCO Objectives and Principles of Securities Regulation and the associated methodology adopted in 2003, as updated in 2008.**[2] An assessment of Principle 30, which deals with securities settlement systems, was not carried out as part of this assessment. A review (but not a formal assessment) of Israel's clearing and settlement systems was carried out as part of the overall FSAP assessment.

7. **During the assessment, the new principles adopted by IOSCO and published in June 2010 were also discussed.** Discussions about them were informal and not part of the assessment. Those discussions are reflected Appendix I.

8. **The assessment of a country's observance of each individual Principle is made by assigning to it one of the following assessment categories: fully implemented, broadly implemented, partly implemented, not implemented and not applicable.** The IOSCO assessment methodology provides a set of detailed criteria to be met in respect of each Principle to achieve the designated benchmarks. The methodology recognizes that the means of implementation may vary depending on the domestic context, structure, and stage of development of the country's capital market and acknowledges that regulatory authorities may implement the Principles in many different ways.

- A Principle is considered **fully implemented** when all assessment criteria specified for that Principle are generally met without any significant deficiencies.

- A Principle is considered **broadly implemented** when the exceptions to meeting the assessment criteria specified for that Principle are limited to those specified

[2] A new IOSCO methodology (including methodology for the assessment of new principles) was adopted in September 2011 but was not used for the current assessment.

under the broadly implemented benchmark for that Principle and do not substantially affect the overall adequacy of the regulation that the Principle is intended to address.

- A Principle is considered **partly implemented** when the assessment criteria specified under the partly implemented benchmark for that Principle are generally met without any significant deficiencies.

- A Principle is considered **not implemented** when major shortcomings (as specified in the not implemented benchmark for that Principle) are found in adhering to the assessment criteria specified for that Principle.

- A Principle is considered **not applicable** when it does not apply because of the nature of the country's securities market and relevant structural, legal and institutional considerations.

9. **The conclusions set out below are based on information and findings as of November 2011.** Is should be noted that the assessment takes place against a background of continuing change in the legislative framework and the regulatory environment for securities regulation.

A. Institutional Structure—Overview

10. **Regulation of the financial sector is divided along institutional lines.** The three main regulators are:

- the Supervisor of Banks, located within the Bank of Israel (BOI) and responsible for regulation of banks and banking groups;

- the Capital Markets, Investment and Savings Division (CMISD), located within the ministry of finance and responsible for regulation of insurance, and the retirement savings sector (pension and provident funds);

- the ISA, an independent agency responsible for the regulation of the securities sector, including exchange markets, capital markets, mutual funds, portfolio managers and advisers and marketers of securities.

11. **In addition, the competition authority has broad responsibility for anti-trust issues, including in the financial sector.**

12. **The TASE plays a significant role as a self-regulatory organization (SRO).** It has responsibility for the authorization (licensing) of stock exchange members, and for the supervision of their obligations under TASE rules and regulations. It also supervises trading activity on exchange markets, although the ISA has direct responsibility for detecting and responding to insider trading and other forms of market abuse.

Given the role played by banks in the Israel securities market (see below), it should be noted that a bank active in the securities market is subject to regulation by three different authorities:

- prudential (stability) and consumer protection regulation by the Supervisor of Banks. This supervision is on a group-wide basis and extends to the subsidiaries of the bank. Conduct regulation is carried out by a separate section of the Supervisor of Banks and looks to the conduct of banks in relation to their clients, including clients of the bank's securities market activity;

- direct regulation by the ISA in respect of insider trading and other forms of market abuse such as market manipulation. Banks that issue equities or debt, or engage in underwriting, takeover or merger activity, are also regulated by the ISA in respect of these capital market activities;

- regulation by TASE (under the overall supervision of the ISA) in respect of compliance with TASE rules and regulations.

B. Market Structure and Activity

13. **The Israel securities markets have undergone very significant change in recent years.** These reforms fall under two broad headings, which are sometimes interrelated:

- changes brought about by major changes in policy which have had an impact on the structure of the securities markets;

- changes flowing from the development of new products and activities.

14. **The mutual fund industry has undergone extensive structural change over the past decade.** As a result of the Bachar reform, banks were forced to divest their holdings in mutual fund management firms. The transition period was short and in practice most of the divestment took place within the first year following ratification of the Bachar Law. Before these reforms the two largest banks, Bank Hapoalim and Bank Leumi, held a 60 percent market share and the market share of Israel's 5 largest commercial banks was more than 80 percent. One year into the reforms, 9 mutual fund managers shared 85 percent of the market, with the largest company (subsequently liquidated) holding a 20 percent market share. The top 5 managers held 68 percent of the market. As of June 2011, 9 groups still lead the market but their identity and market share differ. The largest has a 16.6 percent share and the top 5 have a cumulative market share of 61.8 percent. Insurers and groups that include insurers now have a market share of 36 percent, with 64 percent held by other investment houses.

15. **Recent years have seen rapid growth in a number of product areas.** These include:

a. the market for exchange traded notes (ETNs) has grown rapidly since 2006. At the end of 2010, there were 437 ETN series (up from 133 in 2006) with a float adjusted market capitalization of almost 55 billion new Israeli sheqels (NIS) (NIS 13 billion in 2006). There were 7 issuing groups. Retail investors hold almost 66 percent of ETNs, with the remainder held by professional fund managers, including mutual funds, provident and pension funds, and insurance companies.

b. portfolio management activities (in which managers manage portfolios for individual investors on a discretionary basis) have more than doubled in size since 2005. At the end of 2010, NIS 242 billion was managed in this way by 164 portfolio management firms, up from NIS 103 billion in 2005. The top 10 firms (which include banks and bank subsidiaries) account for round 70 percent of this activity.

c. the corporate bond market grew rapidly in the period from 2005 to 2007 (market capitalization increased from NIS 66 billion in 2005 to NIS 174 billion in 2007), and—after problems in 2008—grew again to NIS 242 billion in 2010. It is worth noting that corporate bonds market in Israel is publicly listed and therefore subject to the securities law and regulations disclosure requirements.

The following is a summary of the main components of the Israel securities market.

The stock market

16. **TASE is the only exchange market in Israel.** It has a well-developed equities market with over 600 issuers, a corporate bond market with over 250 issuers, a government debt market, a derivatives market (dominated by trading in 2 option products, the TA-25 and the NIS/USD FX), and an institutional trading platform for debt securities that have not been publicly offered.

17. **TASE has 29 members, 15 of which are banks (including 3 foreign banks) and 14 nonbanks (including one remote member) (+citygroup financial services Israel joined at the end of 2011).** Banks dominate brokerage activity on TASE markets, accounting for two thirds of all equity trading, 74 percent of bond trading and over 80 percent of derivatives trading.

18. **TASE owns two clearing houses, the TASE Clearing House (TASECH) and the MAOF Clearing House (MAOFCH).** TASECH carries out a range of functions: it clears and settles TASE transactions; serves as a central depository for public securities; handles the creation and redemption of mutual funds; and provides clearing and settlement for other trading platforms such as MTS Israel (government bond auctions), OTC trading between institutional investors, and block trading in TASE traded securities. MAOFCH clears and settles the derivatives market. TASECH has 12 bank and 9 nonbank members. MAOFCH has 9 members, all banks at this time.

19. **The following tables summarize the main components of the Israel's exchange market activity:**

Table 1. Israel: Market Capitalization of TASE-listed Securities, 2005–6/2011 (NIS Billions)

	The Equity Market		Debt Market					
Year	Shares & Convertibles	ETN Assets 1/	Govt. Bonds	Corp Bonds	TACT Institutional	Structured bonds 2/ & CD Notes 1/	ETN Assets 1/	T-Bills
2005	594	8	299	66	19	28	0	100
2006	681	14	304	97	30	25	1	101
2007	843	21	303	164	47	27	8	77
2008	433	9	342	139	46	28	15	77
2009	715	25	367	201	34	23	19	85
2010	806	33	389	239	35	18	21	135
6/2011	712	34	380	242	37	17	19	123

Source: Israeli authorities.

1/ Assets under management (public holdings).
2/ Public holdings.

Table 2. Israel: Ownership Structure of TASE-listed Companies, 2001 and 2010 (Percent)

Shareholders	2001		2010	
	Principal Holdings 1/	Public Holdings	Principal Holdings 1/	Public Holdings
Israeli Public	42	29	40	11
Foreign Investors 2/	8	2	5	30 3/
Institutional Investors 4/	-	10	-	12
Mutual Funds	-	3	-	2
Government of Israel	6	-	0 5/	
Total	56	44	45.4	55

Source: Israeli authorities.

1/ Principal holding refers to the aggregate ownership of shareholders who each hold at least 5 percent of equity in an issuer.
2/ Including institutional investors.
3/ Of which 22 percent dual listings abroad.
4/ Provident funds, pension funds, and insurance companies.
5/ Rounded down from 0.4.

Table 3. Israel: Sectoral Composition of the TASE Equity Market, June 2011

	No. Companies	Market Cap US$ billion	Relative Market Cap (percent)
Manufacturing	96	35	16
Real Estate	126	21	10
Commerce & Services	112	27	12
Oil & Gas	18	10	5
Investments & Holdings	77	22	10
Pharmaceuticals	3	56	26
High Tech	149	18	8
Banks	10	22	10
Insurance	7	6	3
Total	598	217	100

Source: TASE

Table 4. Israel: TASE Brokerage Activity
Distribution of Turnover by TASE Members, 2005–2010
(Percentage share of brokerage activity)

	Equity		Bonds			Derivatives	
	Bank	Nonbank	Bank	Nonbank	Bank of Israel	Bank	Nonbank
2005	65.0	35.0	77.5	22.0	0.0	69.9	30.1
2006	59.2	40.8	73.3	26.7	0.0	71.2	28.8
2007	56.0	44.0	61.4	38.6	0.0	73.9	26.1
2008	56.4	43.6	61.3	38.7	0.0	75.0	25.0
2009	64.2	35.8	66.4	32.8	0.8	76.7	23.3
2010	67.0	33.0	74.1	25.9	0.0	81.9	18.1

Source: TASE

The mutual fund industry

20. **The mutual fund industry has undergone extensive structural change over the past decade.** Consolidation and competition marked the industry, precipitated by both the Bachar reform and the emergence of the ETN market.

21. **The consolidation of the industry is reflected primarily in the sharp decline in the number of mutual fund managers.** In 2005 there were 42 managers in the industry, but

by June 2011 only 27 remained. This is the result of mergers and acquisition activity, not all directly related to the Bachar reform divestments. Since the reform leading mutual fund managers developed higher profile and more costly operations, which led to mergers within the industry, fueled in part by falling profit margins.

22. **The emergence of the ETN industry poses another competitive challenge to the mutual fund industry.** As is the case in foreign markets, passive investment in index-tracking instruments provides a cost-effective alternative to investment in actively managed mutual funds. In addition, although over 70 percent of the ETNs track TASE share price and bond price indices, the introduction of instruments tracking foreign markets and providing diverse trading strategies catalyzed diversity in the mutual fund market as well. In 2007, new types of mutual fund products entered the market, including money market funds, fund of funds and fund of foreign funds, leveraged funds, and tracking funds.

23. **The following tables summarize the main components of the Israel's mutual fund activity:**

Table 5. Israel: The Mutual Fund Industry 2005–2011

All Funds	2005	2006	2007	2008	2009	2010	2011
Number of funds (end of year)	918	1,035	1,167	1,185	1,202	1,247	1,272
Change from previous year	123	117	132	18	17	45	25
Percentage change	15.47	12.75	12.75	1.54	1.43	3.74	2.00
Net total assets value (Million NIS, end of year)	124,833	111,902	120,175	98,094	133,159	156,581	154,176
Change from previous year (Million NIS)	23,575	-12,931	8,273	-22,080	35,065	23,422	-2,405
Percentage change	23.28	-10.36	7.39	-18.37	35.75	17.59	-1.54
Net creation (Million NIS)	17,292	-19,799	4,822	-9,651	19,742	16,046	-560
Change from previous year (Million NIS)	2,757	-37,091	24,621	-14,473	29,394	-3,697	-16,606
Active mutual fund managers	42	36	40	37	31	27	26
Active mutual fund trustees	7	7	7	7	7	7	7

Source: ISA.

Table 6. Israel: The ETN Industry 2006–2011

	2006	2007	2008	2009	2010
No. of ETN Series	133	265	380	412	437
Float-adjusted Market Cap (billion NIS)	13.1	25.7	23.2	44.8	54.9
of which:					
equity-linked	12.6	18.8	8.9	25.4	33.4
debt-linked	0.5	6.9	14.3	19.4	21.4
Number of Issuing Groups	6	8	9	9	7
Number of SPVs	26	32	33	33	32
Distribution of Holdings:(percent)					
Retail investors	58.5	65.5	67.1	66.7	65.5
Institutional Investors	41.5	34.4	32.9	33.4	34.5
of which:					
Mutual Funds	0.5	0.8	2.0	3.3	3.3
Provident Funds	25.1	16.0	13.3	16.4	15.5
Pension Funds	12.9	14.8	13.4	10.4	10.9
Insurance Companies	3.0	2.8	4.2	3.3	4.8

Source: ISA and BOI

Intermediaries in the securities sector

24. **Portfolio managers, investment advisers and investment marketers are active in the market in Israel.**

25. **The Bachar reforms played a key role in shaping the industry.** In areas such as investment advice and brokerage services, where commercial banks were allowed to remain, they continue to dominate the market. In areas, notably fund and portfolio management, from which banks were excluded, independent investment houses now occupy the arena vacated by the banks. The largest of these investment houses offer multiple asset management services through separate corporate entities, including portfolio management, mutual fund management, provident fund management, and underwriting. Most of the large investment houses are also TASE members and, in addition to handling the TASE transactions of the financial group, also provide third-party brokerage services. The independent investment houses pioneered Israel's ETN industry and maintain dominance in this market.

Table 7. Israel: Licensed Securities Firms, 2005–2010

	2005	2006	2007	2008	2009	2010
Assets under management by portfolio management companies (billion NIS)	103	115	128	118	198	242[1]
Number of firms	182	204	241	235	214	201
Portfolio management firms	159	177	205	198	176	164
Investment advice firms	23	15	11	11	16	12
Investment marketing firms	--	12	25	26	22	27
Market share of top-ten companies (In percent)	60	53	55	57	69	70
Equity (NIS billion)						
Top ten portfolio management firms	0.50	1.01	1.22	1.0	0.93	0.77
Investment advice & marketing firms	0.36	0.99	1.67	NA	3.25	3.22

Source: ISA

1/ Until 2010, not all companies reported holdings in mutual funds as part of their assets under management. In 2010 all companies included mutual fund holdings in their reports to the ISA.

C. Recent Developments

26. **The global crisis affected Israel's economy, but no domestic financial institution got into serious difficulties during the crisis.** Financial institutions weathered the storm of the global crisis, although profitability suffered. The corporate bond market suffered especially large falls in prices, and new issuance came to a halt.

27. **The authorities preempted the spread of financial stress with a slew of crisis-intervention measures.** The BOI aggressively cut its policy interest rates, and expanded liquidity facilities. The BOI also tightened bank supervisory measures in areas of reporting, capital, and liquidity. In areas of capital markets, the MOF established various back-stop mechanisms, such as a "safety net" program for provident fund savings, a guarantee program to banks for raising capital, and the creation of the government owned investment funds ("Manof" funds); while the ISA set up a debt settlement framework. Furthermore, this episode led to the establishment of the Hodek committee, which in February 2010 presented a set of recommendations to the government to improve market transparency, conduct, and the corporate government of institutional investors.

28. **At the time of the mission, the health of the financial sector was generally satisfactory.** Financial soundness indicators for banks and insurance companies are currently generally satisfactory.

29. **In 2008 significant problems were experienced in the corporate bond market.** Bond issuers exposed to real estate assets, especially in part of Eastern Europe and North

America. In response to these problems, increased disclosure requirements were imposed and there are currently proposals to enhance the oversight role of trustees for bondholders and the rights of bondholders.

30. **There have been many changes to the securities regulation regime in recent years and a large number of proposals are in process.** Current initiatives include proposals to regulate custodians and credit ratings agencies; to amend the regulation of underwriters and mutual funds; and to enhance the rule making power of the ISA.

IV. Preconditions for Effective Securities Regulation

31. **The general preconditions for effective regulation of securities markets appear to be in place in Israel.** The legal and accounting system supports the implementation of requirements and effective regulation of market participants. The commercial law is modern, as are corporate governance standards. The regulator has legally enforceable powers.

32. **Israel has a solid institutional framework supporting the conduct of sound macro-economic policies.** Monetary policy is based on an inflation targeting framework, and the BOI's independence has been recently strengthened following the enactment of the 2010 BOI Law. Budgetary policy too has been strengthened in recent years, with the establishment of a fiscal rule that gives credibility to the authorities' fiscal consolidation plan.

33. **The Israeli legal framework for the financial sector is comprehensive and regularly updated.**

34. **The auditing and accounting rules applicable to financial institutions generally comply with international standards.** Listed companies and most nonbank financial institutions have applied International Financial Reporting Standards (IFRS) since 2008 (early adoption was possible from 2006). The Israeli banking system uses US General Accepted Accounting Principles (GAAP), with some IFRS elements for non-core activities.

35. **The Israeli legislative framework with regard to the audit profession requires internal and external auditors to be independent in both fact and appearance.** Furthermore, the Companies Law and the Accountants Law assure the independence of external auditors, including qualification requirements. However, the audit profession is self-regulating.

36. **The judicial system, including that for bankruptcy and the enforcement of property rights, is well-developed.** The Israeli legal tradition is based mostly on English common law, which is reflected both in the nature of its corporate legislation and the role of the judiciary.

37. **The payment and settlement system is reliable and efficient.** The BOI regulates Israel's payment systems. It operates the Zahav (a real time gross settlement system) system, which is considered to be secure and fast. The Zahav system is linked to banks' paper-based clearing house (BCH), the automated clearing house (Masav), and the TASE clearing houses.

38. **Competition is encouraged and the market is open to foreign participation.** There are no significant non-prudential barriers to entry by domestic or foreign firms.

39. **A freeze in capital markets in late 2008 revealed weaknesses in the corporate governance regime of bond issuers, and market disclosure and transparency.** Efforts to improve the quality and timeliness of disclosure were initiated. A number of disclosure directives imposed on bond issuers were issued in 2008-9, of which most have since been adopted permanently in legislation (for example: disclosure of projected cash flows for the coming two years etc.). In addition, an amendment to the Companies Law, strengthening corporate governance requirements in order to enhance bondholder protection, was adopted in August 2011.

40. **The corporate governance of financial institutions in Israel is governed by the Companies Law and the Securities Law.** In addition, sectoral legislation has been introduced to regulate the operation of each financial sector, such as banks (the Banking Licensing Law and the Banking Ordinance), mutual funds (Joint Investment Trust Law), portfolio managers, investment advisers and investment marketers (the Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management Law) provident funds (Provident Funds), and pension funds (Pension Counseling and Pension Market Law).

41. **The basic principles of financial reporting are laid out in the Securities Law.** The law addresses the content of a prospectus, the prohibition against the use of insider information, and the penalties applicable for the breach of the law. The law also sets out the contents of annual reporting requirements for listed companies. To facilitate the disclosure in line with those required by the Securities Law, the ISA provides an online filing system which is accessible to the public.

42. **Israel does not have formal deposit insurance.** However, in the past, the government and the BOI provided an extensive degree of de facto protection to depositors. For example, in response to the public's increasing concern about deposits during the latest global crisis, the MOF stated that the BOI and the government would protect depositors. For the non-systemic bank failure cases in 1985 and 2001, the BOI compensated depositors almost in full. In the severe financial crisis of the early 1980s, the government nationalized the entire system, and depositors did not suffer any losses and no bank was allowed to fail outright.

V. MAIN FINDINGS

A. Summary

Principles for the regulator (Principles 1–5): Within an overall framework organized regulation along institutional lines, the securities regulator works under a clear mandate, with its responsibilities and powers established by legislation. The ISA has a high degree of operational independence, although some powers of a regulatory character are reserved for the minister of finance. A notable gap in the regulatory framework is that broker-dealer activity can be undertaken without falling within the regulatory framework, if the activity does not involve membership of the stock exchange or the provision of advice or marketing services to retail clients. In addition, regulation of OTC derivatives activity, including the sale of products to retail investors, can take place outside the regulatory regime. Responsibility for supervision of the conduct of business obligations of members of the stock exchange is split between the TASE (for nonbank members) and the supervisor of banks (for bank members), with the securities regulator not having a direct role in this area, except for advice giving and marketing activities. The level of accountability to the government, parliament, and the public is high. Decisions of the regulator are required to be transparent and are amenable to judicial review, and the ISA is subject to comprehensive rules relating to procedural fairness. The ISA has adequate powers to carry out its regulatory functions, and has rulemaking authority, although this is time limited in one area. ISA members and staff are subject to integrity policies that ensure high standards of professional conduct and compliance with these standards is monitored effectively. Arrangements for cooperation and information sharing between regulators exist, but there may be a need for further effort to ensure they work fully effectively in practice.

Principles for self-regulation (Principles 6–7): The TASE plays a significant role as an SRO, with responsibility for authorizing and supervising its members (which are not required to be licensed by the ISA), as well as supervising the conduct of its markets and clearing and settlement activities. Bank members of TASE are also regulated by the supervisor of banks, who is responsible for prudential supervision and the conduct of business obligations of bank members. Regulation of insider trading and other forms of market abuse is done directly by the ISA. TASE has adequate powers to supervise its members and markets, including powers to impose a range of disciplinary sanctions. The ISA has broad powers to supervise TASE's compliance with its responsibilities, although it has limited powers to act against members of the exchange except where they also hold an ISA license, unless market abuse is involved.

Principles for enforcement (Principles 8–10): The ISA has extensive and appropriate powers to obtain information and records, and can exercise these powers on a routine basis to ensure compliance with the laws it administers. Regulated entities are subject to detailed record keeping and retention requirements, including records relating to the identity of clients and records that enable the tracing of funds and securities. The ISA has responsibility for administering anti-money laundering and combating the financing of terrorism legislation in

relation to portfolio managers and nonbank members of TASE. It has comprehensive powers to investigate both administrative and criminal violations of securities laws. Criminal sanctions are available for serious violations. Until recently, the ISA had only limited ability to impose sanctions for non-criminal violations but now has new powers, which became fully operative shortly after the assessment mission, through an Administrative Enforcement Committee, to impose a broad range of sanctions. The ISA is an active regulator and carries out well-planned programs of supervision that include on-site and off-site reviews of regulated entities. It is also active in investigating and taking enforcement action for breaches of the legislation it administers. It has sophisticated technology systems to assist in identifying potential breaches of the law. Achieving this level of effectiveness is facilitated by the relatively small number of supervised entities.

Principles for cooperation (Principles 11–13): Major changes have occurred in this area since the 2001 assessment. The ISA has power to share information both domestically and internationally on matters relating to its regulatory functions, including its investigative and enforcement activities. Concerning domestic cooperation, the authorities will need to continue to work towards enhanced exchange of information and analysis in the context of the development of a macroprudential framework. A precondition for sharing information internationally is the existence of a Memorandum of Understanding (MOU) with the relevant regulator. Government approval is required for the signing of an MOU with a foreign regulator, but this is readily given and the ISA now has individual MOUs with 19 foreign regulators. It is also a full signatory to the IOSCO multilateral MOU. There is evidence of its cooperation under these arrangements. The ISA is able to provide assistance to foreign regulators who need to make inquiries in carrying out their functions.

Principles for issuers (Principles 14–16): Issues to the public of equity and debt securities require a prospectus approved by the ISA. Disclosure requirements for prospectuses are in line with IOSCO principles.[3] Issuers submit annual and quarterly reports, and immediate reports about material developments. Financial statements must be prepared in accordance with IFRS (other than banks who must comply with standards set by the BOI). Auditors that conduct statutory audits are subject to the oversight of a registration authority and the relevant professional body. The framework requires that auditors be independent. The ISA has broad powers to enforce issuers' compliance with financial reporting standards. Changes of control transactions are required to comply with disclosure requirements and obligations to treat shareholders equally. Given the structure of the Israeli market, special emphasis is given to the rights of minority shareholders, especially in critical areas such as related party transactions.

[3] However, the 2006 "shelf prospectus" provision allows rapid issuance of a prospectus, which in practice may reduce the ability of underwriters to conduct a thorough analysis.

Principles for collective investment schemes (Principles 17–20): Collective investment schemes (CIS) are subject to licensing by the ISA. The regulatory system sets eligibility standards, including integrity standards. The ISA does not currently have the power to examine the adequacy of internal management procedures at the time of licensing. Managers are subject to minimum capital requirements, and insurance requirements. All CIS must have a trustee who holds fund assets and supervises the actions of the manager. There are clear rules governing the legal form and structure of CIS. The ISA carries out a systematic program of on-site and off-site inspections. CIS must have a prospectus that complies with IOSCO Principles. Detailed rules apply to valuation of assets (including assets for which a market price is not readily available), and the pricing of units, and there is full transparency about these issues.

Principles for intermediaries (Principles 21–24): The ISA licenses portfolio managers, advisers and marketers of securities. The TASE authorizes its members. Potentially significant activity that does not fall within either of these two categories remains unregulated (including broker-dealer activity and OTC derivatives activities). (See the above comment of the ISA) For the entities it licenses, the ISA has power to ensure minimum criteria are met. Licensees are subject to comprehensive ongoing requirements, and the ISA is systematic and active in monitoring compliance with these obligations. TASE licensees are subject to an authorization process. TASE supervision is focused primarily on nonbank members and their compliance with capital standards and systems that interact with exchange systems. Responsibility for supervising bank members' dealings with their clients rests with the supervisor of banks. Minimum capital and insurance standards apply to ISA licensees (though it does not address risks from outside the regulated firm), and risk based capital standards apply to nonbank members of TASE. Capital standards for TASE members allow long term unsubordinated debt to count as capital; this is out of line with common international practice. Detailed standards for internal organization and operational conduct apply to both ISA licensees and TASE members, although for ISA licensees there is no requirement for an independent periodic evaluation of internal controls and risk management processes. Adequate procedures exist for dealing with the failure of an intermediary.

Principles for secondary markets (Principles 25–30): TASE is the only secondary market in Israel, and operates both securities and derivatives markets, and (through two subsidiaries) clearing and settlement facilities for each type of market. It holds a license issued by the minister of finance and is subject to the supervision of the ISA, which has extensive powers to ensure TASE acts in accordance with regulatory requirements. Market participants are supervised by TASE and (for banks) the BOI. The clearing and settlement entities are not required to hold a license but are subject to specific provisions in the Securities Law administered by the ISA. The ISA is closely involved in TASE decision making processes and maintains an effective supervision program. Trading on the markets is transparent. The ISA has direct responsibility for detecting insider trading and other forms of market abuse and uses an impressive technological system to assist. The management of large exposures, default risk and market disruption is achieved through the rules of TASE and its clearing

houses. Proposals are advanced for regulating dealer trading platforms through the provisions of the Securities Law.

Table 8. Israel: Summary Implementation of the IOSCO Principles

Principle	Grading	Findings
Principle 1. The responsibilities of the regulator should be clearly and objectively stated.	**BI**	The responsibilities of the ISA and TASE are clearly established by law. The mandate is also well understood by market participants. Arrangements for cooperation and information sharing between the financial sector regulators exist, but there may be a need for further effort to ensure they work fully effectively in practice. There is a notable gap in the regulatory framework that permits broker-dealer activity and OTC derivatives activity to take place outside the regulatory regime.
Principle 2. The regulator should be operationally independent and accountable in the exercise of its functions and powers.	**PI**	The ISA has a high degree of operational independence, although some powers of a regulatory character are reserved for the minister of finance, and the minister has control over staffing levels. The level of accountability to the government, parliament, and the public is high. Decisions of the regulator are required to be transparent and are amenable to judicial review, and the ISA is subject to comprehensive rules relating to procedural fairness.
Principle 3. The regulator should have adequate powers, proper resources, and the capacity to perform its functions and exercise its powers.	**FI**	The ISA has adequate powers and resources to carry out its regulatory functions, and has rulemaking authority, although this is time limited in one area.
Principle 4. The regulator should adopt clear and consistent regulatory processes.	**FI**	The ISA has clear and consistent regulatory processes, and operates in a transparent way.
Principle 5. The staff of the regulator should observe the highest professional standards.	**FI**	ISA members and staff are subject to integrity policies that ensure high standards of professional conduct and compliance with these standards is monitored effectively.
Principle 6 The regulatory regime should make appropriate use of SROs that exercise some direct oversight responsibility for their respective areas of competence and to the extent appropriate to the size and complexity of the markets.	**FI**	The TASE plays a significant role as an SRO, and members of the TASE do not require to be licensed by the ISA unless they engage in advisory or marketing activities.
Principle 7. SROs should be subject to the oversight of the	**FI**	TASE is subject to regulatory oversight by the ISA. Its rulemaking requires approval and the ISA has an

Principle	Grading	Findings
regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.		active oversight presence. TASE has the attributes required of an SRO and is bound by standards appropriate for a professional regulatory body. Its regulatory decisions are subject to judicial review.
Principle 8. The regulator should have comprehensive inspection, investigation and surveillance powers.	**FI**	The ISA has comprehensive information gathering, inspection and surveillance powers. Regulated entities are subject to extensive record keeping and retention requirements.
Principle 9. The regulator should have comprehensive enforcement powers.	**FI**	The ISA has extensive evidence gathering and other investigative and enforcement powers. Criminal sanctions are available for serious violations. Until recently, the ISA had only limited ability to impose sanctions for non-criminal violations, but it now has new powers (not yet fully operative), through an Administrative Enforcement Committee, to impose a broad range of sanctions.
Principle 10.The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance, and enforcement powers and implementation of an effective compliance program.	**FI**	The ISA has a credible and effective supervisory and enforcement program. It is an active regulator and carries out well planned programs of supervision that include on-site and off-site reviews of regulated entities. It is also active in investigating and taking enforcement action for breaches of the legislation it administers.
Principle 11 The regulator should have the authority to share both public and non-public information with domestic and foreign counterparts.	**FI**	The ISA has power to share information both domestically and internationally on matters relating to its regulatory functions, including its investigative and enforcement activities. It can share both public and non-public information with a minimum of procedural restrictions.
Principle 12. Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts.	**FI**	The ISA has domestic information sharing arrangements with other financial sector regulators. It is also a full signatory to the IOSCO multilateral MOU and has signed numbers MOU with foreign counterparts. There is good evidence that these arrangements are working in practice.
Principle 13. The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers.	**FI**	The ISA can provide effective and timely assistance to foreign regulators to assist them in their regulatory and enforcement activities. With one exception, the ISA does not have to have an independent interest in a matter on which a foreign regulator seeks assistance, or for the conduct being investigated to be a breach of law in Israel.
Principle 14. There should be full, timely, and accurate disclosure of financial results	**FI**	Public issuers are subject to comprehensive disclosure requirements, including prospectus disclosure and annual, quarterly and immediate reporting

Principle	Grading	Findings
and other information that is material to investors' decisions.		requirements. Financial statements are prepared in accordance with IFRS. Strict rules apply to the timing of disclosures and reports. Preparers of disclosure documents and reports are required to take responsibility for them.
Principle 15. Holders of securities in a company should be treated in a fair and equitable manner.	**FI**	There is a strong regulatory framework that requires fair treatment of securities holders. The Companies Law and the Securities Law facilitate shareholder decision making and protect the rights of minority shareholders, especially in groups with controlling shareholders. Takeovers and other change of control transactions are regulated to ensure equal treatment and full disclosure,
Principle 16. Accounting and auditing standards should be of a high and internationally acceptable quality.	**FI**	Israel has adopted IFRS in full and financial statements are of international quality. Audit standards appear to comply with international standards though they are not yet fully aligned with them. Auditors are subject to tight independence rules.
Principle 17. The regulatory system should set standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme.	**PI**	CIS are subject to authorization standards and ISA licensing. The ISA does not currently have the power to examine the adequacy of internal management procedures at the time of licensing. Managers are subject to minimum capital requirements, and insurance requirements. The ISA carries out a systematic program of on-site and off-site inspections.
Principle 18. The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.	**FI**	All CIS must have a trustee who holds fund assets and supervises the actions of the manager. There are clear rules governing the legal form and structure of CIS. Client assets are protected through their being held by a trustee.
Principle 19. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme.	**FI**	CIS must have a prospectus that complies with IOSCO Principles. The ISA approves prospectuses and has power to hold back or intervene if there is inadequate disclosure. CIS are also subject to regular reporting requirements, and their accounts must be prepared in accordance with Israeli GAAP.
Principle 20. Regulation should ensure that there is a proper and disclosed basis for assets valuation and the pricing and the redemption of units in a collective investment scheme.	**FI**	Detailed rules apply to valuation of assets (including assets for which a market price is not readily available), and the pricing of units, and there is full transparency about these issues.
Principle 21. Regulation should	**NI**	Not all intermediaries are subject to an authorization

Principle	Grading	Findings
provide for minimum entry standards for market intermediaries.		process (see under Principle 1). Entities that are licensed are subject a minimum entry standards and subject to ongoing obligations. For entities it licenses, the ISA has comprehensive powers. TASE has similar powers with respect to its members. Advisers are fully regulated. The ISA has a systematic and active monitoring and compliance program for licensed entities.
Principle 22. There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.	**BI**	Licensed entities are subject to limited initial capital requirements. Nonbank members of TASE are subject to a full risk weighted capital regimes. ISA licensees must hold insurance designed to enable them to compensate investors. The capital requirements set for ISA licensees do not address risks from outside the regulated entity, though this is unlikely to give rise to serious problems given the nature of these licensees' activities. Unusually, long-term non-subordinated debt counts towards capital for TASE members.
Principle 23. Market intermediaries should be required to comply with standards for internal organization and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters.	**BI**	Standards for internal organization and operational conduct apply to both ISA licensees and TASE members. For ISA licensees the requirement for an independent periodic evaluation of large portfolio managers' internal controls and risk management processes, while recently legislated for, is not yet implemented.
Principle 24. There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.	**FI**	Adequate procedures exist for dealing with the failure of a licensed intermediary or a TASE member. Insurance is available in the case of ISA licensees.
Principle 25. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.	**FI**	TASE is the only secondary market in Israel, and operates both securities and derivatives markets, and (through two subsidiaries) clearing and settlement facilities for each type of market. It holds a license issued by the minister of finance and is subject to the supervision of the ISA, which has extensive powers to ensure TASE acts in accordance with regulatory requirements. Market participants are supervised by TASE and (for banks) the BOI.
Principle 26. There should be ongoing regulatory supervision of exchanges and trading systems, which should aim to ensure that the integrity of	**FI**	The ISA is closely involved in TASE decision making processes and maintains an effective supervision program.

Principle	Grading	Findings
trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.		
Principle 27. Regulation should promote transparency of trading.	**FI**	Trading on TASE's markets is appropriately transparent.
Principle 28. Regulation should be designed to detect and deter manipulation and other unfair trading practices.	**FI**	All forms of market abuse are prohibited by the Securities Law. The ISA has direct responsibility for detecting insider trading and other forms of market abuse. It uses an impressive technological system to assist it to detect all forms of market abuse.
Principle 29. Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.	**FI**	The management of large exposures, default risk and market disruption is achieved through the rules of TASE and its clearing houses.
Principle 30. Systems for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that they are fair, effective and efficient and that they reduce systemic risk.	**NA**	

FI: Fully implemented
BI: Broadly implemented
PI: Partially implemented
NI: Not implemented
NA: Not applicable

B. Recommended Action Plan and Authorities' Response

Recommended action plan

43. **The following recommendations aim to suggest measures to further improve the securities regulation framework and supervision.**

Table 9. Israel: Recommended Action Plan to Improve Compliance with the IOSCO Objectives and Principles for Securities Regulation

Reference Principle	Recommended Action
Principle 1	Steps should be taken to close gaps in the legislative framework for broker dealer and for OTC derivatives activity. Authorities should consider measures to ensure that there is a more comprehensive and consistent approach to regulation of the whole spectrum of securities market activities. Proposals to introduce a new regime for broker dealers generally should be proceeded with. Steps should be taken to ensure that the regulatory approaches taken by TASE (for nonbank members) and by the bank supervisor (for banks) is consistent. Authorities should ensure that the framework for cooperation works effectively in practice, especially in areas where more than one regulator has responsibility for a regulated entity,
Principle 2	Authorities should proceed with proposals to amend the legislation to make clear that decisions of a purely regulatory character are to be made by the ISA. Authorities should consider whether is necessary to maintain the minister of finance's power to set staff ceilings for the ISA, in addition to his or her power to approve the ISA's budget.
Principle 14	The ISA should proceed as a matter of priority with proposals to improve the quality of underwriting and the role played by underwriters in the issuance process.
Principle 17	Proposed amendments to the Mutual Fund Law to permit the ISA to assess a CIS operator's systems and processes at the time the application for a license is being assessed should be proceeded with.
Principle 21	For regulation of currently unregulated intermediaries, see recommended action under Principle 1. Steps should be taken to ensure that supervision of TASE members is consistent and coherent for both bank and nonbank members.
Principle 22	The ISA should consider requiring licensees to provide it with notice of a decline in capital levels before the minimum requirement is reached. It should also consider taking into consideration of potential risks from outside the regulated entity when setting capital standards, especially for larger portfolio managers. Consideration should be given to amending TASE capital rules, such that only fully subordinated debt would be treated to be treated as capital.

Reference Principle	Recommended Action
Principle 23	Legislation requiring large portfolio management licensees to have an independent evaluation of internal controls and risk management processes is now in place and will be implemented as of May 2012. Consideration should be given to applying this obligation to other licensees.

Authorities' response

44. **The ISA would like to thank the IMF's staff for all their efforts and for their professional and hard work in Israel.** We have found the reports and comments provided to us very comprehensive and helpful, and the exchange of views as a useful and efficient process.

45. **The regulation of broker-dealer activity received high priority at the ISA.** The ISA has established an internal working group dedicated to examine and propose a legislative framework to regulate the broker-dealer activity in Israel. This process will be closely coordinated with the BOI.

46. **It should be emphasized that notwithstanding the differentiation between TASE member categories, all TASE members are currently subject to TASE rules pertaining to conduct towards customers, disciplinary violations, compliance with TASE enforcement and with the general provisions pertaining to member obligations towards TASE.**

47. **According to the data the ISA has, most of the OTC derivatives activity is performed in trading platforms within the banks.** The exposure of retail clients to OTC derivatives is limited by law, and their indirect exposure is also low (mutual funds are prohibited from investing in OTC derivatives, however ETNs are not).

48. **The ISA currently acts to extend liability of underwriters**. In addition to what was stated in the IOSCO Detailed Assessment, the amendment proposed by the ISA, if approved, will impose a mandatory duty to have an underwriter in every public offering, for the purpose of external due diligence.

49. **As to the comment of the assessor that the capital requirements set for ISA licensees do not address risks from outside the regulated entity (principle 22), the ISA believes that due to the specific regulation of these licensees, there is no need in changing the capital requirements and impose unnecessary burden on the industry.**

VI. DETAILED ASSESSMENT

Table 10. Israel: Detailed Assessment of Implementation of the IOSCO Principles

Principles Relating to the Regulator	
Principle 1.	**The responsibilities of the regulator should be clear and objectively stated.**
Description	**Structure of the securities regulation regime** Regulation of the financial services industry in Israel is organized along institutional lines, with different regulatory authorities for each of: the securities sector—the Israel Securities Authority (ISA); the banking sector—the Bank of Israel's Bank Supervision Department (the Supervisor of Banks); and the insurance and retirement savings sectors—the Commissioner of Capital Markets, Investment, and Savings (CCMIS) in the ministry of finance's Capital Markets, Insurance and Savings Division. **ISA responsibilities, powers, and authority** ISA is responsible for regulation of both securities and derivatives markets. In particular it has regulatory responsibility for regulation of primary markets (issuance); secondary markets; disclosure obligations of issuers; mutual funds; portfolio management; investment advice; and the marketing of financial products. Regulated persons and entities for which ISA has responsibility include: securities exchanges and (as of 2011) dealer intermediated trading platforms; issuers; underwriters; mutual funds and their managers, controlling shareholders and trustees; issuers of index products and their managers, controlling shareholders and trustees; portfolio managers; investment advisors; marketers of publicly traded financial assets. ISA is also responsible for enforcing the Prohibition on Money Laundering Law—2000 (Money Laundering Law) and the Prohibition on Terrorist Financing Law—2004 (Terrorism Financing Law) in so far as these relate to portfolio managers and non-bank stock exchange members. ISA is also the Company Registrar for public companies under the Companies Law—1999 (the Companies Law). ISA also has broad authority for regulation of misconduct in the capital and derivatives markets, for example for prohibitions against insider trading and other forms of market abuse. A number of current law reform initiatives will expand the ISA's authority, for example for regulation of a broader range of financial intermediaries; credit rating agencies, and securities custody. ISA's powers and authority derive from the legislation it administers. There is a large body of legislation and regulations but the three key laws are: the Securities Law—1968 (under which the ISA was established); Joint Investment Trust Law—1994 (Mutual Fund Law); and the Regulation of Investment Advising, Investment Marketing, and Investment Portfolio Management Law—1995 (Investment Advice Law).

These laws confer extensive powers on ISA and the use of those powers may be enforced through the legal system.

Discretion to interpret its authority

ISA's discretion to interpret its authority is set out in the laws it administers, and discretions relating to the application of the legislation can be exercised only if permitted by the law.

The Securities Law (section 9B) requires ISA to publish decisions which it believes are of fundamental importance. More generally, ISA adopts a transparent approach to the exercise of its discretions and to its interpretation of the laws it administers. This approach includes:

publishing exposure drafts of bills and regulations for public comment;
establishing processes for providing pre-rulings and no action positions, and publishing responses to pre-ruling requests on its website;

Requests for Pre-rulings, 2008–2010

Year	Accounting Requests	Legal Requests	Mutual Funds	Total
2008	49	79	31	159
2009	25	59	15	99
2010	51	32	10	93

Source: ISA 2010 Annual Report and ISA website

making use of Staff Legal Bulletins and Staff Accounting Bulletins to make public its approach to legal and accounting issues likely to be of relevance to a number of stakeholders; and
publishing FAQs on technical issues, mostly in the accounting area.

Gaps or overlaps

The responsibilities of the three specialist financial sector regulators (and the TASE) are set out in legislation. These provisions are generally coherent and help reduce the potential for gaps, overlaps or inconsistencies in oversight responsibilities and practice, but there are several areas of potential concern. There is a risk of differences in approach by regulators responsible for supervision of what are in fact very similar operational activities. An example is the responsibility the TASE has for supervision of nonbank members' compliance with conduct of business rules, and the responsibility the bank supervision area of the BOI has for supervising banks dealings with their customers, including their securities customers.

Members of TASE do not require a license issued by the ISA and responsibility for their authorization rests with TASE. Banks and bank subsidiaries who are TASE members are not subject to the full regulatory regime that applies to nonbanks under the TASE rules and regulations.

A notable gap in the regulatory framework is that broker-dealer activity can be undertaken without falling within the regulatory framework, if the activity does not involve membership of the stock exchange or the provision of advice or marketing services to retail clients. In addition, regulation of OTC derivatives activity, including the sale of products to retail investors, can take place outside the regulatory regime. Responsibility for supervision of the conduct of business obligations of members of the stock exchange is split between the TASE (for nonbank members) and the Supervisor Banks (for bank members), with the securities regulator not having a role in this area, except for advice giving activities.

In areas of possible duplication, exceptions in the legislation help to delineate areas of authority. For example, under the Investment Advice Law banking institutions are exempt from ISA licensing and are prohibited from engaging in portfolio management (though bank subsidiaries can do so).

	Investment advisors employed in the banks, however, are subject to ISA licensing as individuals and the conduct obligations under the Investment Advice Law apply to them. Banks are not permitted to operate mutual funds. All individuals and market participants are subject to the prohibitions against market misconduct administered by the ISA. The Securities Law applies to all nonfederal government issuers, all publicly traded asset classes—cash and derivatives—and all securities violations regardless of perpetrator. The Investment Advice Law extends to all investment advisors and portfolio managers, whether employed by commercial banks (regulated by the Supervisor of Banks), ISA-regulated investment houses or operating as self-employed individuals. Recently adopted legislation deals with the regulation of alternative trading platforms by making those subject to special provisions of the Securities Law and requiring them to be licensed by the ISA. There are also additional provisions in the new legislation, specifically dealing with the obligations of licensees in this category. In practice, there are around 10 providers of these services in the Israel market, for the most part offering trading in foreign exchange products. The authorities have endeavored to harmonize regulation across different financial sectors. For example following the report of the Bachar Committee, the Control of Financial Services (Provident Funds) Law—2005 (Provident Fund Law) and the Control of Financial Services (Pension Counseling and Pension Marketing) Law—2005 (Financial Planning Law) were modeled on the laws on portfolio management and investment advice and marketing administered by ISA. The laws regulating retirement savings advice are modeled after the Investment Advice Law. Similarly, the regulation of long-term savings schemes is broadly modeled after the Mutual Fund Law. **Coordination and cooperation between regulatory authorities** A number of formal mechanisms are designed to enhance cooperation and the flow of information between regulatory authorities. These include: *Cross representation on boards*: The BOI and ministry of finance are represented on the ISA plenum. The ISA chairman is a member of the advisory board of the Bank Supervision Department; and an ISA representative sits on the BOI's National Committee for Payments and Settlements. *Coordinating committee*: In 2006 a regulatory coordinating committee was established under a MOU between the ISA, Supervisor of Banks, and the Capital Market Division.[4] The purpose of the committee is to coordinate regulation and enhance the exchange of information between the three regulators. It meets regularly to discuss regulatory developments, and when necessary, establishes task forces to address specific regulatory initiatives that affect the industries regulated by the agencies. For example, in December 2010 the committee adopted common standards for applying "fit and proper" tests for licensees under the jurisdictions of the three financial services regulators. *MOU on supervision of the TASE clearing houses*: There is an MOU between the ISA and the BOI regarding supervisory authority shared between the two in the enforcement of the Payment Systems Law—2008 (which is under the jurisdiction of the BOI). *Interministerial/agency cooperation*: the ISA participates in committees and other mechanisms dealing with cross-jurisdictional issues. This is particularly true in areas of systemic or macroeconomic importance. The most prominent example to date has been the Bachar committee. The governor of the BOI has recently proposed to the ISA chairman and the commissioner of the Capital Market Division that a forum be established to foster cooperation in identifying, analyzing, and managing systemic risks engendered in the current volatile market conditions. Conversations with authorities and market participants suggest that, while these mechanisms are

[4] T*he Memorandum of Understanding Concerning Cooperation and Exchange of Information Between the Supervisor of Banks, the Israel Securities Authority and the Capital Markets, Insurance & Savings Division of the Finance Ministry* (MOU on Coordinated Capital Market Regulation).

	valuable, further effort on the part of all authorities is required to optimize cooperation and the flow of information between authorities. This applies not only to cooperation and consultation on macro issues, but also to proactive information sharing about regulated entities whose activities are subject to supervision by more than one regulator, such as banks and bank subsidiaries active in the capital market as issuers of securities and as market participants.
Assessment	Broadly implemented.
Comments	The area of concern under this Principle relates to whether substantially the same conduct is subject to consistent regulatory requirement. The gaps in the legislative framework referred to in the description suggest that the regime does not operate in a conceptually consistent way across the spectrum of capital market activity because some potentially significant areas of activity fall outside the current regulatory regime. In particular, a broker dealer can operate without being subject to the securities regulation regime if it is not a member of the stock exchange and does not provide advice to retail clients, and OTC derivatives can take place in an unregulated environment, even if it involves retail clients buying products from market participants. It also means that comparable regulation does not apply to like activities, since, for example, the broker-dealer activities of members of the TASE are regulated through the TASE rules and regulations (under the overall supervision of the ISA), but an entity providing similar services away from the TASE market is unregulated. (According to available data, most of OTC derivatives activity is performed in trading platforms within banks.) The authorities should consider measures to ensure that there is a more comprehensive and consistent approach to regulation of the whole spectrum of securities market activities. In addition to this concern about the existing coverage of the regime, there is also a risk of uneven application of regulation to bank and nonbank members of the stock exchange. Steps should be taken to ensure that the regulatory approaches taken by the stock exchange (for nonbank members) and by the bank supervisor (for banks) is consistent. In this context, it should be noted that the ISA has been developing an amendment to the Investment Advice Law to deal with the regulation of investment intermediaries. The proposed amendment would extend ISA supervision of investment intermediaries to include broker-dealers and establish an SRO style council to play a role in supervision of all investment professionals. It will regulate entities that provide broker dealer services and who are not members of the TASE, as well as TASE members. The proposal will also extend the ISA power to regulate any broker-dealer activity in a wide range of assets. The definition of assets covered is broad, to include "securities and financial instruments," including derivatives; and the definition of brokerage and dealing are equally broad. A draft of the proposed legislation was published for public comments on October 2010. Authorities should ensure that the framework for cooperation works effectively in practice, especially in areas where more than one regulator has responsibility for a regulated entity.
Principle 2.	**The regulator should be operationally independent and accountable in the exercise of its functions and powers.**
Description	**Independence** *Governance* Chapter 2 of the Securities Law contains the main provisions dealing with the establishment and operation of the ISA. The legislation requires the minister to appoint up to 13 members of the authority, including a chairman and a deputy chairman. Members are appointed from the public and the civil service, and one must be an employee of the BOI. In practice, at the date of the assessment there were 10 members, including the chairman. Of these, three are civil servants (including the two statutory appointments from the BOI and the ministry of finance); four are academics specializing in law and business administration; and two are from the

	private sector (one a legal professional and one an accountant). Meetings of all members of the authority (the ISA plenum) usually occur once a month. The ISA plenum also deals, through committees, with granting applications for permission to publish prospectuses; granting exemptions and extensions; stock exchange issues; issues relating to the ISA's finances and budget; the independence of auditors in companies subject to the Securities Law; issues relating to the licensing of investment advisors, investment marketers, and investment portfolio managers; and issues relating to the imposition of civil fines on mutual fund managers, as well as other issues as needed. The ISA has a number of standing committees. These include: the regulation and supervision committee (responsible for decisions about the regulation and supervision of market participants including underwriters, and for licensing and authorization under the Mutual Funds Law and the Advice Law); the secondary market committee (responsible for the ISA's decisions about regulation of the stock exchange, including approval of TASE rules and regulations); the disclosure and financial statements committee (responsible for matters relating to issuers' disclosure and presentation in financial statements); the financial sanctions and fines committee (responsible noncriminal financial sanctions imposed by the ISA under the Securities Law, the Mutual Funds Law, and the Advice Law, and ISA decisions to fund class and derivative actions. [Note that this committee deals with the relatively low level sanctions, not the sanctions imposed by the new Administrative Enforcement Committee.]; the ISA audit committee; the ISA's budget Committee; and the ISA's tender committee. The chairman of the ISA chairs a number of these committees and the number of members on each varies between committees. *Interaction with government* There are a number of examples in the Securities Law where the minister of finance (rather than the ISA) must make a decision that is regulatory in character. Examples include: section 12(d), under which the minister approves rules for applications to publish a prospectus; section 20A, under which the minister approves ISA procedures for examining draft prospectuses; section 15E, which provides that the ISA may, with the approval of the minister of finance, promulgate rules that shall enable it to exempt an offeror from any or all of the provisions pertaining to the details, structure or form of a prospectus, or with regard to particular types of offers, offerors, corporations or securities; these rules shall be published in the official gazette; section 39, which provides that issues of securities and their offer to the public require the approval of the minister of finance or of a person appointed by him for this purpose. [Note: The assessor was advised that since 1987 the requirement for the minister's approval for the issue of securities has effectively been removed by a decision of the government to give a general approval for the issue of securities by any person. This means that issues can be made subject only to having a prospectus approved by the ISA. In addition, proposals are currently before the Knesset to amend the provision to reflect the current practice.] section 45A, under which it is the minister which grants a stock exchange license; section 48, under which the minister (and the Knesset Financial Committee) approves changes to stock exchange rules; and section 50, under which closure of the stock exchange requires the consent of the minister. A number of these provisions enable the ISA to give the minister advice on the regulatory decision. Nonetheless, some provisions are regulatory in nature and it potentially intrudes on the independence of the ISA for decisions of this kind to be made at the political level. In the case of section 39, it is unsatisfactory for the legislation to continue to empower the minister to make a regulatory decision when in practice this power is exercised by the ISA.

Funding

The ISA budget is subject to the approval of the minister of finance and the Knesset Finance Committee.

The ISA is funded entirely by fees levied on regulated entities for services and receives no allocations from the government budget. Under Section 55A of the Securities Law, fee schedules are set by regulations made by the minister of finance and approved by the Knesset Finance Committee. Fines collected by the ISA for violations of laws under its jurisdiction are not part of ISA's revenue and are remitted to the treasury.

The ISA approved budget for 2010 was NIS 144.2 million. Budgeted income for that year was NIS 133.0 million derived as follows:

Category	Amount (NIS m)
Prospectus fees	47.0
Annual fees (mostly mutual fund transfer fees, and fees from other regulated entities and TASE)	60.0
Net financing income	15.0
Investment advisors licensing fees	11.0

In practice, the ISA has achieved surpluses over some years and now has substantial reserves. Following a decision of the ISA Finance Committee, with the approval of the Knesset Finance Committee, the ISA will reduce its fixed fees by 40 percent, for the next 4 years. This reduction is expected to result in a deficit budget which will be financed through surpluses from previous years.

As well as the minster's role in the approval of the ISA budget, section 10 of the Securities Law makes the minister responsible for the size of the ISA's staff.

Legal protection

Section 56G of the Securities Law provides that the ISA has the same status as the State of Israel under the Civil Wrongs (Liability of the State) Law—1952. Under section 3 of that law, the state is not civilly liable for actions undertaken within the scope of its lawful authority or within the bona fide exercise of that authority. Civil action can be brought against the state when the duty of care is breached. Three common law standards have been developed about breach of care, which together create a basis for a claim of government negligence or breach of care:

the absence of a rational connection between the measure taken and the intended result;
the existence of a less damaging alternative to the measure taken; and
the degree of damage incurred relative to the benefit gained from the measure.

Under the Torts Ordinance (New Version) (hereafter Torts Ordinance) members and employees of the ISA are immune from civil action for actions (or failures to act) performed in the exercise of their lawful authority, unless the damage incurred was caused knowingly and intentionally by the ISA employee. Employee immunity does not exempt the ISA from civil liability in cases in which breach of care can be established. In practice only one (unsuccessful) action has been commenced under these provisions.

Mechanisms to protect independence

Members of the governing board of the ISA are appointed by the minister of finance for fixed terms (three years for members; five years for the Chairman): section 4 of the Securities Law.

Once appointed, members can only be removed from office for specific causes:

repeated failure to be present at four consecutive meetings or six meetings within a calendar year;

	failure to continue meeting the conditions qualifying him/her for membership, including conflict of interest restrictions; and violation of the restrictions placed on engaging in securities transactions. (Sections 4(d) and 6(a) of the Securities Law.) **Accountability** For the performance of its functions, ISA is accountable to the minister of finance and the Knesset Finance Committee. Section 14 of the Securities Law requires the ISA to provide a report on its activities on demand and at least once a year to the minister of finance and the Knesset Finance Committee. In practice the ISA produces a comprehensive annual report which it publishes on its website. As a public body the ISA is accountable to the government Comptroller's Office, which is responsible for review of all actions by state authorities. Section 9B of the Securities Law requires the ISA to publish decisions it deems as key to the public. In practice, the ISA publishes all its decisions and the minutes of its meetings on its website. As a public authority, the ISA and its staff are also subject to the Administrative Procedure Amendment (Statement of Reasons)—1958 (the Statement of Reasons Law) which requires civil servants replying to a written request, to set out the reasoning behind decisions which may have an adverse effect on the applicant. Transparency is also applied in the appeal of fines, administrative sanctions and licensing decisions, which under recently enacted legislation are handled by an independent committee rather than the ISA itself. *Review of ISA's decisions* Decisions of the ISA are subject to administrative law requirements applying to decision making by government bodies generally, as well as specific provisions in the legislation it administers. A person adversely affected by an ISA decision can seek administrative review under Section 42C(a) of the Courts Law—1984. That law provides that for challenges to ISA decisions to be heard by the newly established Economic Section of the Tel Aviv District Court (Economic Court) as administrative actions. This also applies to most decisions of TASE under section 47(b) of the Securities Law. In such a case, the court will review the validity of an ISA decision under administrative law principles. If a court finds a decision was not made in accordance with the law, it can overturn the decision and remit the matter to the ISA for a proper decision. The right to appeal is broad-based, and as interpreted in case law, applies not only to persons directly the subject of by ISA decisions, but also to third-party stakeholders affected by them. There are a number of exceptions, such as an ISA decision not to open a criminal investigation and the appeal of disciplinary ruling of the TASE disciplinary board. Actions challenging the validity of regulation or ISA directives can also be brought to the supreme court in its capacity as the High Court of Justice. In practice, over time a fairly large body of civil cases involving administrative actions and appeals against ISA decisions and procedures has accrued. A relatively large range of issues have been addressed in these civil actions, ranging from technical considerations, such as the cost of fees to the constitutionality of new securities laws. Complaints about ISA's actions can be made to the State Comptrollers Office in its capacity as the government ombudsman. Under the Statement of Reasons Law—1958, ISA staff are required to set out the reasons for rejecting any written request. Although the ISA has power under that law to do so, it has not created

	any exemptions to this obligation for the laws it administers. In addition to these broad administrative law provisions, the legislation the ISA administers contains a variety of procedural fairness provisions. For example, section 15(a) of the Mutual Funds Law requires the ISA to give a fund manager the opportunity to be heard before a decision to revoke the manager's authorization (similar provisions apply to licenses issued by the ISA to portfolio managers, advisers and marketers—see section 10(a) of the Advice Law). Statutory provisions of this kind are supplemented by procedures adopted by the ISA. These include an internal appeal mechanism entitling applicants to ask the ISA to review its decision. Where the operation of the legislation is uncertain or potentially ambiguous, ISA issues clarifying guidelines. It also uses processes that limit the potential for abuse of process, for example by using a licensing committee to make decisions about licenses, and a committee to make decisions about sanctions involving fines directly imposed by the ISA. Where ISA discretionary decisions powers are involved, affected persons are entitled to present their case and in some cases, be represented by counsel, prior to a decision being made. The right to be heard does not necessarily imply the right to be heard in person**,** although under Section 52WW of the Securities Law, in administrative enforcement cases, defendants have the right to be present at all proceedings, to appear before the new Administrative Enforcement Committee (AEC) and, if witnesses are called in the proceedings, to respond to their testimony**.** An ISA decision to open an investigation is not subject to the right to be heard prior to the decision, but the rights of the suspect or the potential offender are built into the investigation process prior to indictment, and later in court proceedings. *Confidentiality* Section 13 of the Securities Law requires confidentiality of documents and materials submitted to the ISA, its members or staff. Release of any information is subject to the approval of the ISA or its chairman, except where required by a court order or an order of the attorney general for the purpose of criminal proceedings. Section 56E also requires information obtained in the course of an investigation to be kept confidential and section 52OO makes similar provision with respect to the operation of the new AEC.
Assessment	Partially implemented
Comments	The ISA enjoys a high degree of operational independence and is fully accountable for its activities. The issue under this Principle is the fact that the legislation gives the minister of finance (rather than the ISA) the power to make some decisions that are of a regulatory character. A list of decisions of this kind is given in the description. There is no suggestion that the existence of these powers in practice undermines the regulatory autonomy of the ISA. The minister has obligations in some areas to seek the advice from the ISA and in practice places great reliance on its advice. Nonetheless, the IOSCO principle requires that decision making on day to day technical matters should rest solely with the regulator. In the case of the approval of stock exchanges, the assessor accepts that the decision may be viewed as having a political character as well as a regulatory one. An exposure draft bill, Administrative Powers of the Israel Securities Authority Bill (Legislative Amendments) 2010 was circulated last year by the ministry of finance. It deals with the involvement of the minister of finance in the areas described above and significantly reduces it. Under the proposed amendments, most of the minister's approval powers will be eliminated, and the ISA will have the power to promulgate those rules. For example, the powers in sections 12(d), 20A, and 15E of the Securities Law will become ISA powers. Section 39 will be removed. Some approval powers relating to the boundaries of regulation will remain with the Minister. Approval of stock exchanges will remain with the minister. The authorities should proceed with these proposed amendments.

	The minister's power to set staff ceilings for the ISA, in addition to his or her power to approve the ISA's budget, potentially limits the operational autonomy of the regulator. Authorities should consider why this restriction is necessary and consider removing it altogether.
Principle 3.	**The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.**
Description	**Power and authorities** The ISA has extensive powers and authorities to carry out its functions. These include the power to: issue authorizations (licenses) to entities carrying on business as financial services institutions in the capital markets; approve capital market activities, such as fundraising and takeovers; monitor trading on secondary markets; obtain information to enable it to monitor compliance by regulated entities and issuers in the capital market and to detect market abuse; conduct investigations, including by searching and seizing evidence and detaining suspects; and take corrective action to remedy breaches and reduce the risk of noncompliance, including by initiating civil or criminal proceedings, imposing monetary and other sanctions, suspending or revoking licenses, requiring disgorgement and banning individuals from beneficially owning or serving as officers in regulated entities. ISA also plays an active role in initiating securities-related legislation and related regulations. The ISA also has power to issue directives. Under the Securities Law (section 36A), this power have a limited life of one year, which may with the approval of the finance minister be extended by up to a further year. Under the Mutual Fund Law and the Advice Law, the ISA has similar powers but they are not limited in time. A directive under section 36A(b) of the Securities Law is enforceable both administratively and criminally (for criminal enforcement of directives—see section 53(b)(5a)). An instruction under section 28(b) of the Advice Law is enforceable and makes a person liable to administrative fines, which can escalate for repeated breaches. (Section26 of the Second Schedule of the Advice Law, and section 1 of the Fourth Schedule of the Advice Law.) It is not enforceable criminally. An instruction under section 97(b) of the Mutual Funds Law is enforceable administratively (section 1 of Part B of the First Schedule of the Mutual Fund Law, and see specially section 1(i)). It is not enforceable criminally. **Funding** ISA appears to have a stable source of funding through the fees it collects from regulated entities and prospectus transactions. It has made substantial surpluses for each of the 4 years to 2010 through a combination of spending less than its approved budget and collecting fees in excess of estimated income. Fees from prospectus registration can be expected to fluctuate in line with increases or decreases in capital market activity, but annual fees from regulated entities that account for a little over half its total income can be expected to be reasonably stable. The ISA has substantial reserves from previous years' surpluses, and earns substantial interest income on these retained surpluses. The ISA's budget can be adjusted throughout the year but significant changes require the approval of the minister of finance.

Staff resources

As at end November 2011, the staff of the ISA was as follows:

Organizational unit	No. of positions filled
Chairman's Bureau	4
Legal Counsel	9
Department of International Affairs	4
Corporate Finance Department	47.5
Investment Department	50
Securities Department at the Tel Aviv District Attorney's Office	22
Investigations and Intelligence Department	40
Research, Development and Economic and Strategic Counseling Department	7
Information Systems Department	7
Department of Supervision over the Secondary Market	8
Administration, Finance and Human Resources	23.5
Administrative enforcement	4
Total	**226**

Approximately 90 percent of the staff of ISA are university graduates, mostly professional in law, accounting and finance. ISA can also seek external professional assistance when required.

Pay scales and other conditions are required by section 10 of the Securities Law to be analogous to those of civil servants. Nonetheless, because of the high proportion of professional staff it employs, salaries for most staff tend to be higher than the norm for the civil service. Under a special agreement between the ISA and the ministry of finance, the ISA can also pay bonuses to its staff.

Training

The ISA runs internal training for new employees and finances ISA employee participation in seminars and conferences in Israel and abroad, including programs operated by the SEC, the EU, and IOSCO. The ISA operates an annual study trip the U.S., which includes meetings at the SEC, U.S. securities exchanges, accounting and legal firms. The ISA recently appointed a professional training coordinator and a comprehensive training program comprised of internal and external seminars and courses has been developed. Over the past 5 years the average expenditure on ongoing staff training came to approximately 1.8 percent of total net salaries and 0.8 percent of the total ISA budget.

Assessment	Fully implemented
Comment	The ISA is promoting measures, through proposed legislation, to increase the scope of its rulemaking authority. The exposure draft bill, Administrative Powers of the Israel Securities Authority Bill (Legislative Amendments) 2010, deals with rulemaking procedures. The assessor understands that this includes proposals to remove the time limitation on directives issued under the Securities Law, and supports that proposal.
Principle 4.	**The regulator should adopt clear and consistent regulatory processes.**
Description	**Clear and equitable procedures** *Procedures rules and regulations* The ISA is bound by general administrative law principles that require consistent and fair processes. These include common law court decisions and specific legislation such as the Administrative

	Procedure Amendment (Statement of Reasons)—1958; the Courts Law (providing for judicial review of ISA decisions); and the Freedom of Information Law—1998. In some cases, they are supplemented by specific procedural requirements in the legislation the ISA administers such as the Securities Law, the Mutual Funds Law and the Investment Advice Law. See also the discussion on accountability under Principle 2. *Consultation and transparency* The ISA consults publicly, through its website, and invites comment on reports, policy position papers and proposed legislation. It commonly issues press releases to publicize policy changes. It also regularly invites representatives of those affected by policies to take part in staff deliberations prior to drafting proposed legislation and rules. Similarly, it meets with industry and other groups. The ISA also holds seminars and conferences for the general public as well as for investment, legal and accounting professionals. The ISA is not obliged as a matter of law to conduct an economic impact analysis of its regulatory policies and actions. As a matter of practice, potential costs of compliance is relevant to its decision making, and the comments solicited during public consultation processes enable market participants and regulated entities to draw attention to cost and efficiency issues in proposed legislation, regulations and ISA policies. In some cases (such as the recent formulation of draft regulations for issuers of exchange traded notes), it commission work by economic consultants to assist in the formulation of policy. All rules and regulations are made publicly available on the ISA website. In addition, the ISA makes databases of regulatory filings, mutual funds and licensed investment advisers publicly available on its website. Section 6 of the Freedom of Information Law—1998 requires the ISA to provide public access to written administrative guidelines governing its operations that relate to or are important for the public. For primary legislation, the ISA must use the guidelines established by the office of the attorney general. These guidelines require exposure drafts to be circulated and made available for public comment. For its own policy making, the ISA does not yet have formal guidelines but, as a matter of practice, draft ordinances and directives are posted on the ISA website and public comment is sought. *Procedural fairness* A variety of obligations, and measures taken administratively by the ISA, contribute to procedural fairness in the carrying out of its functions. These include: the use of committees rather than individual staff member to make some key decisions, such as the issuing of licenses and sanctions decisions; the right to be heard in respect of regulatory and enforcement decisions; the power of the state ombudsman to hear complaints about the ISA; the requirement that ISA give written reasons for its decisions; and the availability of judicial review of ISA decisions. The TASE rules and regulations set out criteria to be applied to applicants for membership. **Transparency and confidentiality** The procedures for administrative (civil) and criminal proceedings require transparency for the benefit of accused parties, entitling them to rights of discovery, and subsequently, to the right to obtain a copy of the transcript of the hearing. The procedure governing criminal prosecution, from initial investigation through trial and sentencing, is stipulated in the Criminal Procedures Law—1982 and case law, which ensure the civil rights of suspects and accused persons are protected.

	These include the right to remain silent, to discovery, right of representation, and so on. In administrative prosecutions, defendants' rights are built into the proceedings. Defendants are entitled to representation, discovery, a right to attend the proceedings and, if applicable, hear the testimony of witnesses. Proceedings are conducted in private, but the outcome of ISA administrative hearings is generally published on the ISA website. In the case of regulatory inquiries and inspections ("audits"), neither the existence of an audit nor its findings are published unless warranted by public interest, or if the audit results in the imposition of sanctions. The ISA's general policy is not to publicize investigations until they reach the court process, or otherwise become public. **Investor Education** The ISA has undertaken a number of investor education initiatives in conjunction with other bodies. In 2007, ISA and the Tele Aviv Stock Exchange launched a dedicated website including materials designed to further understanding of the stock exchange and the securities traded on it as well as information regarding the avoidance of victimization by fraud. The ISA also participates in an inter-ministerial committee headed by the chairman of the National Economic Council convened to articulate measure to promote "financial awareness" among Israelis, including investor education for informed financial consumerism. Among other initiatives, the committee developed and introduced a financial educational course in 24 high schools in the 2010 school year. The pilot has received positive feedback and is planned to be rolled out to 250 schools, starting in late 2011. The committee also prepared a survey to measure financial literacy, which is in its final stages of design. The ISA has a budget for investor education which it uses to participate in the activities described above. It does not, however, have a particular focus on investor education, and its website is devoted almost entirely to information for regulated entities.
Assessment	Fully implemented.
Comments	Given the active retail investment base in Israel, the ISA should consider taking a more active role in investor education, for example by using its website to communicate with retail investors as well as the regulated population.
Principle 5.	**The staff of the regulator should observe the highest professional standards including appropriate standards of confidentiality.**
Description	Staff of the ISA are subject to a variety of mechanisms to ensure their integrity and proper conduct: The Penal Code—1977 (Titles D and E) makes specific provisions relating to malfeasance by civil servants (which in this context includes ISA staff). As well as dealing with bribery, the Code prohibits abuse of or arbitrary use of authority; the use of authority for personal gain; fraud and the violation of public trust. The Civil Service Law (Discipline)—1964 establishes the framework for enforcing disciplinary offences, a term which includes behavior unbecoming a civil servant or damaging to the good standing of the civil service; unfair behavior in the performance of duties; and the commission of a crime involving moral turpitude. Sections 5 and 10A of the Securities Law deal with restrictions on securities transactions both during and after service with the ISA. Section 53 of the Law makes violation of these rules a criminal offence. The ISA has a code of ethics that applies to members of the ISA plenum and to ISA staff. The code reinforces the principles of law in the exercise of power and administrative propriety, including transparency, commitment to public service and ISA objectives; professionalism and accessibility; and sensitivity to the principles of proper public administration.

	Conflicts of interest The Securities Law prohibits the appointment or employment of individuals whose other activities engender conflicts of interest (sections 3(c) and 10(b)). This applies to ISA plenum members, members of the AEC and to the ISA staff. All appointments to the ISA plenum are subject to vetting and approval by the Ministry of Justice Committee for the Prevention of Conflicts of Interest. The avoidance of conflicts of interest starts at the recruitment stage, continues through the period of employment and continues after employment ceases (through mandatory “cooling off” periods). *Securities trading by ISA staff* Section 5 of the Securities Law prohibits ISA staff members from executing unauthorized securities transactions and requires that the employee disclose their securities holdings and permitted transactions. Under the Permit to Transact in Securities—2006, the minister of finance authorizes ISA employees to hold and execute transactions in foreign government bonds, mutual fund units, exchange-traded index products, securities of non-ISA regulated entities (excluding subsidiaries of regulated entities) and securities portfolios managed by a fiduciary in blind trust. Other securities acquired prior to ISA employment or by way of inheritance or securities that were non-regulated at time of acquisition can be held or sold, under the condition that the employee gives a seven day notice prior to the sale and securities portfolios managed by a fiduciary as a blind trust. ISA employees may also hold and transact in financial instruments issued by the government or BOI. *Use of information* Inappropriate use of information is prohibited in the Penal Code and the Securities Law. Section 117 of the Penal Code prohibits the unauthorized delivery of information obtained by a public servant by virtue of his/her office to unauthorized persons, and includes to negligence in protecting information and to the unauthorized possession of information both during and after the period of public service. In the Securities Law inappropriate use is covered in the sections of the Law relating to confidentiality (see below) and Chapter 8A of the Law, which deals with inside information. "Use" is defined in Section 52B(a)(2) of the Law to include not only use by the possessor of inside information for his/her own benefit, or the delivery of the information to a third party but, the delivery of an opinion based on inside information. *Confidentiality and secrecy* In addition to the provisions of the Penal Code described above, Sections 13, 52OO, 54K4(b) and 56E of the Securities Law mandate the confidentiality of information submitted to the ISA or its staff, or an AEC panel, as well as information gathered in the framework of an investigation, including investigations conducted on the behalf of a foreign securities commission. *Procedural fairness* Breaches of procedural fairness obligations would be covered either under the abuse of power provisions of the Penal Code and/or the fairness provisions of the Civil Service Discipline Law. **Processes for dealing with violations** The ISA General Secretary's Office and the Legal Counsel Department supervise adherence to proper conduct standards at the ISA. The general secretary and chief legal counsel are responsible for checking possible conflicts of interest on recruitment of employees for sensitive positions at the ISA, and for examining requests to shorten cooling off periods. Any employee accepted for a sensitive position at the ISA is subject to an in depth investigation of his or her private business dealings and personal relations. The Civil Service Discipline Law has been adopted (with appropriate modification) by the ISA and establishes the framework for investigating and resolving potential breaches of the standards that

	apply to ISA employees. The ISA internal auditor conducts targeted inspections regarding various aspects of ISA conduct and that of its staff, at its sole discretion under the supervision of the ISA Audit Committee. The findings of inspections are handled, as necessary, by the ISA general secretary under the authority granted it for this purpose. The ISA makes use of information technology (IT) systems to prevent the unauthorized disclosure of information. The ISA also requires all staff members to personally sign a confidentiality agreement, the breach of which may be subject to criminal enforcement The ISA chairman is responsible for handing the investigation of disciplinary violations of the type mentioned above. Under Section 31 of the Law, the ISA chairman is entitled to censure or issue a warning to an employee suspected of a disciplinary violation, after giving the employee an opportunity to be heard. Alternatively, under Section 32, the ISA chairman can file a complaint to the prosecutor of the disciplinary court, either at his or her initiative or in response to a complaint against the employee. If warranted, the prosecutor submits an action to the disciplinary court, which is responsible for adjudicating the case] **Sanctions** Some breaches of standards involve criminal offenses and are subject to criminal sanctions. An ISA employee suspected of a disciplinary offence under Section 17 (3) (behavior unbecoming), 17 (4) (unfair behavior) or 17 (6) (crime involving moral turpitude) of the Civil Service Discipline Law, can face civil charges in the disciplinary court established under that law. A wide range of sanctions is available.
Assessment	Fully implemented.
Comments	
Principles of Self-Regulation	
Principle 6.	**The regulatory regime should make appropriate use of SROs that exercise some direct oversight responsibility for their respective areas of competence, and to the extent appropriate to the size and complexity of the markets.**
Description	**SROs** Israel's only stock exchange, TASE, plays a significant role as an SRO. As well as being responsible for regulation of its markets and clearing houses under the supervision of the ISA, TASE authorizes its broker-dealer members, who are not required to hold a license issued by the ISA (other than in relation to their advice giving activities). TASE: establishes eligibility rules which must be met by: broker dealers who are members of TASE; and members of the two clearing houses that are wholly owned subsidiaries of TASE: TASECH, which clears and settles TASE transactions; serves as a central depository for public securities acts; handles the creation and redemption of mutual funds; and provides clearing and settlement for other trading platforms such as MTS Israel, OTC trading between institutional investors, and block trading in TASE traded securities; and the MAOFCH, which clears and settles derivatives markets. establishes and enforces binding rules relating to trading on its markets and the conduct of business of members of TASE and the clearing houses. establishes a framework for dealing with members' breaches of its rules, and conducts disciplinary proceedings through a disciplinary board.

	Membership of TASE is currently comprised of 15 banks (including the BOI) , 14 nonbank brokerage firms (including one remote member) + one remote member (merryl)+ TASECH has 12 bank and 9 nonbank members, while MAOFCH has 9 members, all banks. Only members of TASE can trade on the markets it operates. Entities admitted to membership of TASE and its clearing houses are not required to hold a license issued by ISA, so TASE rules provide the complete framework for regulation of members' eligibility criteria and ongoing obligations, including capital, insurance, and conduct of business obligations. TASE's responsibility for supervision of its members to ensure compliance with stability (capital) requirements and some other obligations does not include ongoing supervision of bank members, which are the responsibility of the BOI. See further under Principle 21. Notwithstanding the differentiation between member categories, all TASE members are subject to the provisions of the rules pertaining to conduct towards customers, disciplinary violations, compliance with TASE enforcement and with the general provisions pertaining to member obligations to TASE. The market abuse provisions (insider trading, market manipulation and so on) apply to all persons regardless of their institutional status and are exclusively administered by the ISA, rather than by TASE.
Assessment	Fully Implemented.
Comments	
Principle 7.	**SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.**
Description	**Authorization** The Securities Law sets out TASE's authority and obligations as a self-regulatory body. A stock exchange may only be operated an entity licensed by the minister of finance after consultation with the ISA (section 45(a)). *Rules* Section 45(3) requires a securities exchange to have written rules that have been approved by the minister of finance after consultation with the ISA, and by the Knesset Finance Committee. Section 46 sets out detailed requirements for these rules, including details relating to rules for: membership, covering eligibility requirements and ongoing obligations, including disclosure, reporting and conduct of business obligations; the listing of securities for trading; trading on the stock exchange ; and the obligations of corporations whose securities are listed for trading. All changes to TASE rules require approval by the minister of finance, after consultation with the ISA, and by the Knesset Finance Committee (section 48(a) of the Securities Law). Regulations under the rules as well as temporary measures adopted by the TASE board are subject to ISA approval (section 46(d)). Under Section 48 (b) of the Law, if the ISA believes that, for the purpose of ensuring proper and fair management of TASE, an amendment should be made to its rules, it must notify TASE. If TASE does not amend its rules in accordance with the notice, the minister of finance in accordance with an ISA proposal is entitled, with the approval of the Knesset Finance Committee, may make an order amending the rules. TASE may not alter or repeal an amendment ordered in this way without the consent of the minister of finance.

	TASE membership TASE rules create different classes of membership. All TASE members are subject to TASE supervision but classes of members are subject to some different requirements. There are distinctions between: banks and nonbank members. Bank members are not subject to TASE capital rules and requirements relating to internal control, risk management, and compliance mechanisms. In these areas, they are subject to BOI requirements and supervision; within the nonbank category, institutions whose securities are publicly traded and privately held institutions. Publicly traded institutions are subject to lesser requirements relating to disclosure, corporate governance, enforceability, and familiarity with the local capital market. This is on the basis that, as publicly traded corporations, they are already subject to requirements to at least the standard of those imposed on privately held TASE members; local and remote members; and local banks and foreign banks. An applicant who meets eligibility meets the eligibility criteria in the TASE rules may nonetheless be refused membership if a75 percent majority of the TASE board so determines. Such as decision can be appealed to a court. *Obligations of members* Chapter 5 of the TASE rules sets out the fiduciary responsibilities of TASE members towards their customers. These include: a duty of trust and professionalism; a duty of care; an obligation to place the customer's interest over self-interest or that of a third party; an obligation to avoid conflicts of interests; and an obligation not to prefer one customer over another. The rules mandate that customers' securities be held in trust on behalf of the customer, that separate accounts be held for each customer, and that the member assets are held separately from customer assets. The rules also require that member-customer relations be formalized in a written contract and that the member issue periodic statements regarding portfolio composition and returns. *TASE oversight responsibilities and disciplinary functions* Chapter 6 of the TASE rules (Supervision and Control of the Stock Exchange Members' Performance of the Stock Exchange Rules and Regulations), sets out the mechanisms TASE uses in its self-regulatory role. TASE members are required to provide TASE with all the information necessary to execute supervision and control. TASE is given broad discretion in determining the scope of this information, and TASE members are required to inform their customers of TASE's discretion in this matter. TASE also is entitled to enter the offices of its members for the purposes of its supervisory functions. TASE's disciplinary powers are specified in Chapter 7 of Part I of the rules. Disciplinary violations include violation of a provision of the TASE rules, regulations or a board decision, and conduct unbecoming a TASE member. Disciplinary action can be taken against a member (including its securities industry subsidiaries, which are subject to the TASE membership rules), its senior executive, or one of its employees for violations of TASE rules, regulations, or TASE board decisions, or for conduct unbecoming a TASE member. TASE is entitled to waive disciplinary action if enforcement of the same violation is being handled by ISA or another relevant regulatory agency. Disciplinary complaints are vetted initially by a person acting as an ombudsman, and if accepted, are referred to a disciplinary board of at least three members appointed by the chairman of the

	TASE board and comprised of board members (of which, at least one is an external board member), TASE members and at least one person with legal training. The disciplinary board can impose: a warning; a reprimand; a fine of not more than NIS 1,000,000; a fine of up to four times the benefit derived from the commission of the offence; temporary or permanent restrictions or prohibition of an individual's continued engagement in securities with a member; temporary prohibition from the member engaging in various or certain types of securities transactions; temporary suspension of membership; and revocation of membership. The TASE regulations also specify that certain offences are finable without disciplinary board adjudication. During the year 2010, TASE imposed a total of approximately NIS 325,000 in fines from 10 TASE members. TASE disciplinary decisions can be challenged in court. *Reporting to the ISA* Under the Chapter 6 of the TASE Rules, if TASE uncover prima facie evidence of a suspected violation of the Securities Law, Investment Advice Law or Money Laundering Law, it must inform the ISA of this information. The ISA is also entitled to demand additional information and documents from TASE. The findings of audits conducted by TASE at its members' offices are submitted to the ISA at least once a year. The ISA conducts market watch activities and operates a data analysis system, which integrates information from multiple sources including real-time TASE market data. *Governance* Section 45A of the Securities Law sets out requirements for the composition of the board of directors of a licensed securities exchange. It requires a board of 16 directors comprised of: seven directors appointed by the members in accordance with the exchange's incorporation documents. Under the TASE Articles of Association (each of the five largest banks is entitled to elect one director, and two other directors are elected by nonbanks members); five external directors appointed by an appointment committee, with the approval of the ISA chairman (the composition of the appointment committee, which includes the ISA chairman, is set out in section 45A(d); one director appointed by the minister of finance; one director appointed by the commissioner of the BOI; a chairman appointed by the board with the approval of the ISA chairman. The chairman must be qualified as an external director; and a general manager elected by the board. The general manager must be qualified as an external director. *Avoiding anticompetitive situations and misuse of oversight role* TASE regulations require ISA approval. In addition, under section 51 of the Securities Law, the ISA has power to supervise the orderly and fair operation of TASE. If the ISA considers, after giving the TASE chairman of the board of directors the opportunity to be heard, that TASE is operating contrary to the provisions of its by-laws or its directives, or in a manner that undermines its orderly

	and fair operation, the ISA can direct TASE as to the proper manner of operation. The ISA interprets section 51 as including a duty to ensure that TASE shall not act in an anticompetitive manner and that it will not abuse its position to allow a market participant unfairly to gain unfair advantage in the market. There are examples of when the ISA has acted on this interpretation, for example in relation to the use of market data by third parties to calculate indices, and the qualification criteria for remote membership. **ISA oversight** *ISA powers* Section 45 D of the Securities Law requires a stock exchange to submit annual reports to the Corporate Registrar and the ISA. In other respects the ISA is given broad discretion in setting the terms of supervision. A stock exchange must submit reports on its activity as set by the ISA and additional information upon ISA demand (section 51(c)). The ISA also has powers to initiate changes to the rules of an exchange (section 48(b)) and effect operational changes if it considers that orderly and fair management may be compromised (section 51(b)). *Oversight of TASE decision making* The ISA has powers directly to monitor much of the decision making of TASE. Section 51(d) of the Securities Law permits a representative of the ISA to be present at general meetings of TASE, at board meetings and at meetings of board committees. Presence at these meetings allows the ISA to be aware on an ongoing basis of the issues that are on the agenda of the TASE. It allows the ISA to comment on issues before any decisions are taken by the TASE board, and enables TASE to consult with representatives of the ISA. As a result, the ISA rarely used its powers of intervention under section 51(b) of the Securities Law. Two representatives of the ISA regularly attend the meetings of the TASE's decision making bodies as observers. ISA representatives also attend meetings of the TASE computerized systems committee, its budget and balance sheet committee and its audit committee. The ISA's ongoing oversight is active and ISA staff have direct engagement with TASE's high level decision-making and operational management. TASE has been proactive in improving its trading systems, risk management, member supervision, and clearing house operations. The ISA Department of Supervision of Secondary Markets has internal procedures that require a work plan for supervision and set out the supervisory functions and duties of the department. The procedures specify in detail the obligations of ISA staff members. TASE submits internal audit reports, audit reports that TASE conducts on its members, work plans, reports on specific events, and reports on deficiencies to the ISA on an ongoing basis. For example, during the global financial crisis of 2008, the ISA asked TASE to inspect TASE members' exposure to this crisis and to the entities and markets at risk as a result of it. The ISA also required TASE to discuss the means undertaken by TASE members to reduce exposure, and to report to the ISA on its findings on an ongoing basis as detailed above. The internal procedures of the ISA Department of Secondary Markets describe the reporting obligations of TASE towards the ISA. *Clearing houses* Clearing houses do not require to be separately licensed under the Securities Law. ISA oversight of the TASE clearing houses is established under Section 50C of the Securities Law. The objective of ISA supervision of clearing houses is assurance of their stability and efficient operation as articulated in Section 10 of the Payment Systems Law. Section 50B of the Securities Law requires that the clearing houses establish rules and operational procedures, as well as risk management policies and emergency backup systems to ensure financial and operational soundness. ISA

	supervision focuses on assuring that these obligations are met. Under section 50C, if the ISA determines that a clearing house has failed to carry out one of its requirements, it may order the clearing house to comply with the said requirement and instruct it to amend its by-laws or operations. If a clearing house fails to comply with such an order, the ISA is authorized to amend the by-laws itself. To carry out its supervisory function, the ISA chairman or a person authorized by him or her can demand information from the clearing house or a clearing house member (section 50C(d)). The ISA requires TASE to conduct a risk management survey of the clearing house at least every five years. The BOI is responsible for the sound performance of the payments systems in Israel and on their efficiency and safety. The ISA has an MOU with it that clarifies the scope of responsibilities of each entity and establishes a mechanism for cooperation and the sharing of information between the two entities. *ISA's power to take action independently of TASE* The ISA's general powers to require information and documents (section 56 of the Securities Law) apply to conduct relating to stock exchange activity. In addition, section 56A1 gives power to the ISA chairman or an employee authorized by him to demand any information or document pertaining to transactions involving exchange-listed securities from a stock exchange, exchange members, licensed trading platforms, or portfolio managers. This provision is complemented by Paragraph 49 b of the TASE Rules, under TASE must give the ISA information relating to possible violations of the Securities Law, the Investment Advice Law or the Money Laundering Law. The authorities provided a number of examples where ISA has exercised its authority to deal with both overall market fairness issues (such as TASE charges to members); the quality of corporate governance in listed entities; more specific problems affecting the integrity of market trading (such as errors in short sale reports; and the effect of unintentional large orders on the volatility of the TA-25 share price index). In addition to its authority to make inquiries and intervene, the ISA has extensive authority over the regular course of TASE's business. For example, all changes in trading and clearing fee schedules that the TASE charges from its members must be approved by the ISA; and it is involved in the design of the new TASE executive compensation model from the standpoint of methodology and corporate governance. During the financial crisis of 2008, on several occasions unusual price fluctuations in various indices were apparently precipitated by issuers of leveraged ETNs, which, in order to comply with their obligations to ETNs holders, executed a high volume of transactions. To avoid jeopardizing the orderly operation of trading, the TASE and the ISA decided, among other things, to impose maximum ceiling on the leverage permitted for ETNs. In relation to misconduct by TASE members, the ISA's authority to enforce the Securities Law is independent of TASE disciplinary actions and action can be taken in addition to any measures TASE may take. Paragraph 74 c of the TASE rules stipulates that should a member be under investigation or prosecuted for the same disciplinary violation by a regulatory authority, TASE can opt to discontinue or suspend its own disciplinary handling of the case. . **Professional standards** TASE and its employees are subject to most of the key restrictions placed on the ISA, its members, and staff. A decision of Israel's supreme court decision made it clear that, although TASE was incorporated as a private corporation, it is deemed to be a public authority. TASE, therefore, acts in accordance with the norms required of other public entities. Under Section 47 of the Securities Law, TASE decisions can be appealed to the court system. Most

	TASE decisions can be appealed to the newly established Economic Court. Other decisions can be appealed to regular courts. Under section 45C of the Securities Law, the restrictions placed on holding and transacting in securities under Sections 5(a) and (b) apply to TASE directors and employees, and transaction must be notified to the ISA chairman and the TASE chairman. Under TASE rules, the TASE must not divulge information given to it by a member. Paragraph 49 of the rules requires that TASE can deliver information only in response to a legally valid demand of a competent authority; to the ISA in the event of a suspected prima facie violation of securities laws; and to the TASE ombudsman or disciplinary committee in disciplinary proceedings. Each new employee of the TASE signs a nondisclosure document; a document regarding data security in the working environment; and a document regarding the restrictions on TASE employees' transactions in securities. Abuse of information by TASE obtained in the course of its exercise of power could be grounds for ISA intervention in TASE operations under Section 51 of the Securities Law. Abuse of nonpublic information regarding a company by a TASE employee could be grounds for prosecution Chapter 8A of the Securities Law (Use of Inside Information). **Conflicts of interest** The mandatory composition of the board (described above) is designed to minimize the potential for conflicts of interest at the governance level of the exchange. In addition, TASE's articles of association deal explicitly with conflicts of interests arising from directors' personal interests in board resolutions. Before any discussion of the board of directors of an action or a transaction, each director is required to notify the board of directors or the chairman of the board of any interest that they may have in the matter. A director who has either a personal interest or an institutional interest (as defined in the articles of association) must not be present at the discussions regarding the corporation in which he or she has an interest, or in a discussion in which the corporation which he/she has interest in has personal interest in the resolution discussed. Under Chapter 7 of Part I of the TASE rules, when a hearing on a disciplinary offence is to take place, the TASE chairman of the board must appoint—from the members of the board of directors and from members and their employees—a panel of three persons or a greater uneven number, at least one of whom is an external director of the TASE and one of whom has a legal education, to hear the offence and shall determine which of the panel's members shall chair the panel. The obligation to nominate at least one external director to the panel is designed to ensure conflicts of interests in enforcement decisions are avoided.
Assessment	Fully implemented
Comments	
Principles for Enforcement	
Principle 8.	**The regulator should have comprehensive inspection, investigation and surveillance powers.**
Description	**Special Note** Significant amendments have recently been made to the main legislation administered by the ISA. These amendments came into effect in February 2011. They fall under two main headings: administrative enforcement reforms; and the establishment of a specialized economic court. *Administrative enforcement reform* Significant additions have been made to the suite of remedial actions available to the ISA under the Securities Law, the Managed Fund Law, and the investment Advice Law. The new legislative provisions introduce two primary mechanisms:

	Administrative enforcement—this mechanism applies to offenses under the securities laws, where the level of intent rises no higher than negligence. These cases will first be investigated by the ISA and will then be adjudicated by the AEC, a newly established committee which is authorized to impose various sanctions. The AEC will consist of six persons divided into two panels each of three persons each. Two members, who are ISA employees qualified to serve as district court judges, are to be appointed by the ISA chairman. The minister of justice is to appoint the four other members, two of whom must have expertise in the capital markets and two of whom must be attorneys with expertise in securities law and companies law. See section 52FF of the Securities Law. At the time of the assessment, appointments to the AEC were in the process of being made, and procedures for its operation were being drawn up. The ISA indicated it had a number of cases that could potentially be considered by the AEC if the ISA chairman approves. *Non-prosecution Agreement*—this mechanism enables the ISA to impose sanctions on securities offenses with the consent and cooperation of the offender. Non-prosecution procedures may replace criminal proceedings or administrative proceedings at any stage prior to the initiation of the investigation or the filing of an indictment. In addition, following the finalization of a criminal investigation and the transfer of the investigation file to the districts attorney's office, the district attorney may elect not to indict a suspect for the commission of a securities offense, and to enter into an arrangement with the suspect to conclude proceedings subject to conditions. *A specialized economic court* This reform established an "Economic Court," an economic department within the district court of Tel-Aviv. It is designed to improve and enhance the enforcement process relating to economic issues and to establish an appropriate forum for civil claims on securities issues. The economic court commenced operation in December 2010 with ratification of Amendment No. 59 to the Courts Law. The new court facilitates coherence in rulings on economic issues and is designed to increase consistency in adjudication about economic actions. The jurisdiction of the economic court includes claims about or under corporate and securities law. The economic court is comprised of judges specializing in these fields and hears all criminal and civil cases (including class actions and derivative claims) in these areas. Its jurisdiction includes appeals about ISA administrative decisions (including the AEC) as well as appeals of most TASE decisions and decisions of the companies registrar. Because of the newness of these arrangements, the ISA has to date not yet had much practical experience in their operation. **Information gathering and inspection powers** The ISA has extensive information gathering and inspection powers. It can request information both on a routine basis and in specific circumstances without notice or judicial action. *General powers* Under Section 56A of the Securities Law, the ISA chairman or a person authorized in writing by the chairman for this purpose has power to: require any person to provide any information or document relating to the business of a corporation which is subject to the Securities Law, or which relates to a criminal or administrative offense; and enter premises (other than premises that are exclusively a residence), where he/she has reasonable grounds to believe that there is an activity of a regulated entity is taking place, and demand to receive documents. These powers can be exercised to secure the execution of the Law (a term enabling ISA to seek

	information relating to the administration of the law it is responsible for administering); or if there are reasonable grounds to believe that an administrative offense has occurred, or in the event that a suspicion of a criminal violation of the Law has arisen. Section 97A (b) of the Mutual Funds Law and Section 29 (b) of the Investment Advice Law grants similar authority in monitoring compliance with enforcement of those laws. Although section 56A of the Securities Law grants the ISA the authority to require information from any regulated corporation—including banks—without a court order, in practice, in consideration of bank confidentiality, the ISA routinely seeks a court order to demand information from banks. As well as these broad powers, the ISA has a number of specific powers to seek information. *Stock exchange transactions* Section 56A1(a) of the Securities Law gives the ISA power to require a stock exchange member or an investment portfolio manager to provide information and documentation relating to securities transactions involving exchange-listed securities (including information about the identification of the party on whose behalf, or on whose instructions, the transaction was executed). Under section 97A of the Mutual Fund Law and section 29 of the Investment Advice Law, the Securities Law information gathering powers stated in Section 56A1 are applied to mutual fund and investment advice activities. . In practice, the ISA uses a sophisticated market surveillance and data analysis system using business intelligence (BI) technology. This system is designed (among other things) to highlight unusual market activity that may indicate market abuse or the use of inside information. The BI system integrates information from a wide range of sources: TASE (real time market data); the ministry of finance; TASE members; other ISA systems; as well as spreadsheets and manually keyed information. The type of information available on BI includes trade orders, executed transactions, price quotes, index data, corporate actions, data on issuers and mutual funds, and data about the trading activity and holdings of controlling shareholders and interested parties. The market watch system uses pre-designed algorithms to monitor activity on TASE to identify irregularities in price movements, turnover, and other parameters. It cross-references trade data with the parties carrying out the trading (for example if the investor is a potential insider such as a senior officer or a principal shareholder). It also cross-references trading data with regulatory filings by or about the relevant issuers on the ISA's web-based reporting platform, MAGNA. Each potentially suspicious trade or series of trades is assigned a risk score (in a range of 0–100) indicating the likelihood that a trading or other violation has occurred. Activity scored in this manner is sent to the member of the ISA staff assigned as reference person to the issuer in question as well as to the Supervision of Secondary Markets Department and the ISA enforcement staff. All trading data transferred to the system include a coded number, representing the account number of the investor carrying out the activity. For entities regulated by the ISA (mutual funds and portfolio management firms) the ISA has access to the coded identity of entities. It is therefore able in real time to monitor their trading activity and cross-reference it to regulatory filings. The ISA also has code numbers from ETN issuers. The system detects activity that may indicate a violation of regulations has occurred, (for example if a fund purchases shares even though its stated investment policy is "strictly bonds"). The system then sends alerts to the appropriate ISA supervisor. The ISA also has the coded identity of entities regulated by the Capital Markets Division of the ministry of finance (pension and provident funds and insurance companies), *Issuers* Section 36 of the Securities Law empowers the ISA to require issuers to give the ISA explanations, details, information or documents relating to any item included in a report or notice submitted to the

	ISA; and to give the ISA an amendment to any report or notice submitted as required. Section 56F of the Securities Law give the ISA power to appoint a person (including persons not employed by the ISA) to conduct an audit and demand documents and information set out in section 56A if the ISA considers that, for purposes of protecting the interests of the investing public, it is appropriate to conduct an audit of a corporation which is subject to the provisions of the Securities Law. This section does not apply to stock exchanges, banking corporations or insurers. *Mutual Funds* Section 97(c) of the Law gives the ISA power to authorize a party who is not an ISA employee to carry out inspections and to demand documents and information relating to mutual fund activity regulated by the legislation. *Licensees* Section 28 gives the ISA power to supervise licensees (which includes the power to conduct inspections), and also the power to authorize a person who is not an ISA employee to carry out such inspections. As with the other laws, this agent is authorized to carry out inspections and demand documents and information relating to a licensee and the fulfillment of its duties under the Law. *Information gathering—criminal investigations* The Securities Law gives the ISA extensive powers to gather evidence if it suspects a criminal offence has been or is being committed. Under Section 56B, an investigator may: apply to a magistrate court judge to issue a warrant allowing the investigator to enter any premises, to conduct a search of that premises and to seize any item related to the offense; and enter premises (that are not exclusively residential premises), carry out a search, and seize any item related to an offense classified as a felony without a warrant, if a senior investigator approves the search and there is insufficient time to obtain a warrant. Section 97A(c) of the Mutual Funds Law and Section 29 (c) of the Investment Advice Law give an ISA investigator the same search and seizure powers in relation to mutual funds and ISA licensees. *Information gathering—administrative offenses* If an investigator has reasonable grounds to believe that administrative offense was committed, they may apply to a magistrate court judge to: issue a warrant instructing a person to surrender an item required for the inquiry of the alleged administrative violation to the investigator; and issue a warrant allowing the investigator to enter premises (that are not exclusively residential premises) to carry out a search of that premises and to seize any item required for the inquiry of the administrative violation. A search warrant can only be granted if either: a person failed to deliver a document or an object requested by an investigator or an employee of the ISA; or a request by the ISA to surrender the required document or object is likely to impede the inquiry of the administrative violation because of the risk that evidence will be removed or damaged. (Section 52QQ (a) of the Securities Law, Section 120(q) of the Mutual Funds Law and Section 38G of the Investment Advice Law.) **Record keeping requirements** The legislation administered by the ISA contains record keeping requirements, including records

	concerning client identity and records enabling the tracing the movement of funds and securities in and out of brokerage and bank accounts resulting from securities transactions. *Issuers* Section 124 of the Companies Law requires all companies (including those regulated by the ISA) to keep documents such as the minutes of the general meeting, minutes of board of directors meetings, and resolutions record must be kept at a corporation's registered office for seven years from the date of the meeting. It also requires that copies of notices from the company to shareholders over the previous seven years, financial statements; the shareholders register, and, for public companies, the register of principal shareholders. Section 4 of the Securities Law Regulations (Electronic Signature and Reporting)—2003, provides that, if a document or accompanying page is reported electronically to the ISA, a copy of the document or accompanying page must be kept electronically at the head office of the reporting entity. The Companies Law requires all companies to maintain a shareholders registry which is available for view by the public. A shareholder who is a trustee on behalf of a beneficial holder must be registered as such. For most TASE-listed companies, the entity registered as the shareholder of the company (in addition to shareholders who did not register their shares for trade) is a nominee company (a subsidiary of one of four TASE bank members). Physical securities certificates are immobilized and held in by the parent banks of nominee companies. At the clearing house level securities custody is dematerialized. The transfer of "ownership" between members is registered at the TASECH but does not result in a transfer of certificates between securities holders or a change in the securities ownership register managed by the issuing company. *Members of TASE* TASE rules and regulations require all nonbank TASE members to keep orders relating to securities for a period of seven years. Pursuant to the supervisor of banks: Proper Conduct of Banking Business Rule No. 1/06, banks are required to keep all documents related to a transactions executed in negotiable securities (as defined under Section 52 of the Securities Law and including options and futures) for at least seven years. *Mutual funds* Section 129 of the Mutual Funds Law requires a mutual fund manager to keep fund records in a fund book, in a manner that incorporates all the information relating to the fund, for at least seven years. The information held in these fund books include: the assets held by the fund; transactions conducted on its behalf, the decisions made with regard to its management, computer reports containing details of the above, and other details. *ISA licensees* Section 25 of the Investment Advice Law sets out record keeping requirements for entities licensed by the ISA. Portfolio managers to must maintain records of all transactions executed on behalf of a client. All licensees must maintain records of each communication in which investment advice is provided to a client. Investment marketing agents must maintain similar records relating to the marketing of investments. These provisions also apply to instances of giving advice or marketing, which do not result in a transaction. Records must be kept for seven years. The Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management Regulations (Recording of Transactions and Investment Advice Activity)—2007 (hereafter: IA Records Regulation) describe the details which these records must include. The records of a portfolio manager must include identifying information about the client on whose behalf a transaction was conducted, whether the transaction is the result of advice given to the client or the result of

	instructions initiated by the client without portfolio manager discretion, and details about the transaction and instructions given in relation to it. If any item of information is recorded with a TASE member in a way that allows for its retrieval at any time on the demand of the portfolio manager, the portfolio manager is exempted from recording that item. **Customer identity** Since 2001 the ISA has been responsible for monitoring potential money laundry activity in relation to portfolio managers and nonbank stock exchange members. Its supervision and enforcement powers for this function are set out in ordinances issued under the Money Laundering Law. Updated ordinances were issued in 2010 and implemented in accordance with FATF recommendations. The ISA has power to obtain records kept pursuant to this legislation. Under the Money Laundering Ordinance (Portfolio Manager Requirements Regarding Identification, Reporting and Record Keeping)—2010, portfolio managers must conduct due diligence on their customers (know your customer). They must document and verify details regarding their customers, including details about the beneficial owner and controlling shareholders if the customer is a corporation, including name, identity number, date of birth (or incorporation), gender, and address. Identification documents must be recorded and kept for a period of at least seven years from the date of termination of the agreement. Portfolio managers must monitor customers on an ongoing basis and report unusual actions. Documents recording the execution of transactions initiated by the customer or reported by the portfolio manager must be kept for a period of at least seven years. Similar duties apply to nonbank stock exchange members, under the Money Laundering Ordinance (Exchange Member Requirements Regarding Identification, Reporting and Record Keeping)—2010. In addition, TASE members have an obligation to report unusual activities and activity of a certain size (such as cash deposits or withdrawals of at least NIS 50,000 and the transfer of securities or other financial assets from one account to another equaling at least NIS 50,000). In 2010, the ISA conducted audits on portfolio management companies that are also stock exchange members focused on compliance with the Money Laundering Law. Section 7a(1) of the Money Laundering Law requires all banks to obtain and record the identities of persons who receive services from a bank—including the beneficial owner of a transaction—and, for transactions conducted at the request of a corporation or by means of a corporate account, the identities of the persons controlling the corporation. Section 7(a)(3) of the Money Laundering Law requires banks to maintain records as prescribed in the Money Laundering (Banking Corporations' Requirements Regarding Identification, Reporting and Record Keeping) Order. Accordingly, banks are required to keep all documents attesting to transactions reported to the Money Laundering Prohibition Authority for a period of at least seven years from the date on which the transaction was recorded in the bank's books. The Supervisor of Banks: Proper Conduct of Banking Business Rule No. 411 (which is now pending Knesset ratification) sets the rules for banking corporations regarding money laundering. **Inspections outsourced to SROs and other third parties** Criminal investigations and administrative inquiries are made by ISA employees and are not outsourced. Routine ongoing supervision is carried out directly the relevant ISA department. In cases in which special professional skills are required, and for most onsite inspections, outsourcing to third parties is used.

	To be engaged by the ISA, third parties must fulfill strict conditions and requirements (including professional, confidentiality and conflict-of- interest conditions) as set out in the public tender. The agreement signed between the ISA and third party inspectors is for a limited period of time. By section 56E of the Securities Law, section 28(2) of the Investment Advice Law, and section 97(d) of the Mutual Funds Law, these third parties are subject to confidentiality restrictions and may not disclose the content of any information or document received by virtue of their position, other than to the ISA chairman or to an ISA employee. Under ISA internal procedures, the ISA supervises the functions of these third parties throughout the audit process, has full access to information kept or obtained by them and can require changes in the way they conduct their audits.
Assessment	Fully implemented
Comments	
Principle 9.	**The regulator should have comprehensive enforcement powers.**
Description	**Investigative and enforcement powers** The ISA has an extensive range of administrative and criminal enforcement powers. The chairman of the ISA is authorized under Section 52RR of the Securities Law to decide whether to pursue administrative or criminal investigations. The Investigations and Intelligence Department is responsible for investigating any suspicion of criminal and administrative violations of the Securities Law, the Mutual Fund Law, or the Investment Advice Law. ISA investigators are also authorized to investigate certain offenses under the Penal Code and the Money Laundering Law if these relate to securities violations. In less serious cases the ISA has the power to impose monetary sanctions on violations related to securities activity. The ISA can obtain data, information, documents, books, records, and statements from any person involved in relevant conduct or having relevant information regarding an investigation and enforcement inquiry. *Civil proceedings* Under section 56D to the Securities Law, the chairman of the ISA has power to apply to the district court for an order prohibiting an offense or violation (or of the continuation of acts amounting to an offense or violation), if he or she has reasonable grounds to assume that a securities offense or an administrative violation is being committed, or that an offense or an administrative violation is about to be committed. Analogous provisions are contained in section 97A(c) of the Mutual Fund Law and section 29 (c) of the Investment Advice Law for violations involving criminal liability. The application of this section with regards to criminal violations is merely a consequence of scrivener's error and will be corrected in a future amendment to apply this authority also on administrative violations. *ISA powers to take corrective actions* The ISA has extensive regulatory, administrative and investigative powers to ensure compliance with the laws it administers. The most important of these powers are the power to: order an offeror to publish an amendment to the prospectus or an amended prospectus (Section 25 of the Securities Law); order reporting companies to issue or amend immediate or periodic reports pertaining to any event or matter that it deems important to a reasonable investor. This includes the authority to order a restatement of previously submitted financial statements (section 36 of the Securities Law); instruct reporting companies as to the manner in which accounting and other information is presented. In practice, since the ISA holds discussions with the companies regarding problems related to disclosures, companies usually amend their reports without the need for the ISA to so order (section 36A of the Securities Law);

	apply to the district court for an order requiring a corporation and its directors to submit a report or amend a report, or to submit an additional or alternative opinion, if a corporation fails to submit or amend a report at the prescribed time, or fails to submit an explanation, detail, information or document, or an additional or alternative opinion as ordered by the ISA (section 38 of the Securities Law); demand information from a licensee or banking corporation. If the ISA requests, these entities must provide the ISA with written explanations, elaborations, information or documents relating to the details included in a report or notice filed (section 27 of the Investment Advice Law); order mutual funds to change their name if it is of the opinion that the name may be misleading. The ISA has used this authority only once. The ISA has published a circular on its website, which sets out its interpretation of what constitutes a misleading name. (Section 6 of the Mutual Fund Law); order mutual fund managers to amend prospectuses. Under Section 28 of the Law, mutual fund managers must—if required by the ISA—provide explanations, details, information and documents with regard to disclosures in a prospectus. In practice, The ISA rarely uses its authority to order mutual fund managers to amend mutual fund prospectuses since it expresses its opinion in its ongoing discussions with the fund managers. (Sections 27-28 of the Mutual Fund Law); order corrections to a mutual fund prospectus. If details, which may be important to a reasonable investor are not included in a prospectus, or a misleading item is included, or an event has occurred that may be important to a reasonable investor considering the purchase or redemption of a unit, and the fund manager fails to file a report or publish a correction in a newspaper, the ISA can order the mutual fund manager to file and publish such a report (section 34 of the Mutual Fund Law). In practice, the ISA usually employs its general authority under section 72 of the Mutual Fund Law, since the specific authority under section 34 is incorporated in section 72 of the Law; demand additional disclosures from mutual fund managers and trustees. If the ISA considers an event or issue is important to a reasonable investor it may demand its disclosure by the fund manager and/or trustee. The ISA may order submission of an amended report if it deems a report noncompliant and the ISA chairman may order mutual fund managers to send reports to unit holders, if he or she believes that information included in a report filed under the Mutual Fund Law is of particular importance. (Section 72 of the Mutual Fund Law); and demand information or documents in investigations of mutual fund violations. The ISA may—in order to ensure implementation of the Law, or if there is a reasonable basis for assuming that a violation has been committed, or if suspicion has arisen regarding the commission of an offense—require any person to provide information or documents relating to the fund manager's or trustee's operations, or relating to the alleged violation or offense. (Section 97A (b)(1) of the Mutual Fund Law). *Administrative sanctions* Until the recent reforms described under Principle 8, the ISA had limited powers to impose monetary sanctions for violations that were of a relatively minor and straightforward nature (for example, for failure to meet a reporting timetable required by the legislation). The powers introduced by changes to the Securities Law, the Mutual Fund Law, and the Investment Advice Law now mean it has an extensive range of sanctions available for a much wider range of violations. These powers will be in full effect when appointments to the AEC and the procedures for its operation are finalized. *Monetary sanctions:* The ISA has the power directly to impose monetary sanctions on any legal or natural person violating specified sections of the laws it administers: Under section 52O of the Securities Law, the ISA can impose monetary sanctions for a range of violations of the Securities Law. Examples include: offering securities to the public other than under a prospectus approved by the ISA, or failure to file a report to the ISA or to the TASE. The fine for an individual is NIS 6,000 NIS, and for a corporation ranges between NIS 20,000–1,000,000. By section 52AA, the ISA must publish decisions to impose fines on its website. Under section 114 of the Mutual Fund Law, the ISA can impose monetary sanctions on any person or corporation violating certain sections of this Law. Examples of violations include: omissions in a fund prospectus and noncompliance with ISA ordinances. Fines range between NIS 10,000–1,000,000.

Under section 38A of the Investment Advice Law, the ISA has power to impose fines on any legal or natural person violating the Investment Advice Law. Examples of finable offenses include: failure to formalize a written agreement with a customer or failure to comply with client confidentiality rules. Fines for an individual range between NIS 10,000–15,000 and for a corporation, (depending on its category under the Investment Advice Law and on the violation) ranges between NIS 50,000–1,000,000. If a fine is imposed on a licensee under the Investment Advice Law or on a banking corporation, the ISA chairman may instruct it to inform its customers of the violation and the fine.

The following table sets out the total fines imposed by the ISA, 2008–2010 (figures are in NIS):

	2008	**2009**	**2010**
Securities Law	1,739,280	1,440,000	2,250,000
Mutual Fund Law	619,200	1,009,296	1,468,800
Investment Advice Law	493,260	2,468,278	817,000
Total	**2,851,740**	**4,917,574**	**4,535,800**

Source: ISA Annual Reports.

Note that this table refers to sanctions imposed before the amendments to the legislation came into effect.

The new administrative enforcement mechanism: A new chapter in the Securities Law (Chapter 8-D) came into force in February 2011 and gives the ISA (through the AEC) new administrative enforcement tools. The new chapter expands the cases in which ISA can impose administrative sanctions, and grants the ISA powers to impose a range of new administrative sanctions. The ISA has not yet had practical experience in administrative enforcement. This new reform provides an administrative alternative to the existing criminal enforcement process that until now the ISA used for enforcing securities laws and regulations.

The new mechanism addresses most offenses under the securities laws, where the level of intent rises no higher than negligence. These cases are first investigated by the ISA. The ISA chairman has the authority to determine, according to criteria specified in the law, whether a case is to be investigated as a criminal violation or as an administrative offense. Once the administrative inquiry is completed, the case is adjudicated by a panel of the AEC.

An AEC panel may take the following measures as sanctions for administrative offenses:

impose fines ranging from:
NIS 400,000–1,000,000 for an individual (depending on the violation);
NIS 2,000,000–5,000,000 for a corporation (depending on the violation);
up to NIS 25,000 on individuals who do not hold a senior position. These amounts are the maximum amounts that the panel can impose.
order payments to third parties injured as a result of the offense;
compel an offender to take actions to correct the violation and to prevent its repetition;
prohibit offenders in certain cases from serving as a senior officer in a regulated entity for a period of up to one year (or up to five years with court approval); and
suspend a license, approval or permit issued under the laws enforced by the ISA for a period of up to one year (or up to five years with court approval) for specified offenses
(Section 52ZZ-52GGG of the Securities Law).

Non-prosecution Agreement: This mechanism was also introduced under the administrative enforcement reform described under Principle 8. It enables the ISA (and the District Attorney) to impose sanctions on securities offenses and administrative violations with the consent and cooperation of the offender.

ISA's authority to revoke licenses or approvals: As part of its authority to assess fit and proper

suitability of licensees on an ongoing basis, the ISA has administrative authority to revoke licenses for breaches of fit and proper standards. In addition to circumstances specified in the relevant laws, the ISA has published a list of considerations which will be considered in these proceedings.

The following table illustrates the use the ISA has made of this power:

Revocation and Suspension of Licenses Granted under the Investment Advice Law 2006–2010

Reason for action	**2006**	**2007**	**2008**	**2009**	**2010**
Insurance	7	3	5	43	18
Annual Fees				115	122
Fit & Proper	2	1		1	
Capital Adequacy	1			1	
License Fraud				1	

Source: ISA Annual Reports.

Sections 10A, 15 and 23D of the Mutual Fund Law give the ISA power to revoke or suspend ISA approval to act as a mutual fund trustee, mutual fund manager or controlling shareholder of a mutual fund manager**.** There have been few cases of approval revocation under the Mutual Fund Law but there are several high-profile examples.

ISA's power to compel fund trustees to act: Section 11 of the Mutual Fund Law gives the ISA power to order a fund trustee to correct defects if the ISA considers the trustee is not carrying out its responsibilities and that the interests of unit holders are being, or may be, harmed. If the defects are not corrected, the ISA may apply to the court to remove the trustee from office. In practice, the ISA has not yet used this authority.

Criminal investigations and sanctions

Under section 52RR of the Securities Law, if the ISA chairman has reasonable grounds to believe that there has been an act or omission for which either a criminal investigation or an administrative inquiry could be conducted, he or she must decide whether either an investigation or an inquiry is to be conducted. The section specifies the factors which must be taken into account in making this determination:

the severity of the act and its circumstances;
an assessment of the nature and the strength of the evidence regarding the act; and
the ISA's enforcement policy.

At the time of the assessment, the ISA was in the process of consolidating criteria for the decision as to whether to pursue a criminal investigation or an administrative inquiry.

A criminal investigation is initiated by order of the ISA chairman, and is completed when the investigation file is sent to the district attorney (Department of Taxation and Economics), together with a recommendation to either file an indictment or to close the file. The decision to file an indictment rests with the district attorney. During an investigation, the ISA is authorized to detain, arrest and release suspects (Section 56C1 of the Securities Law), and to carry out searches and seize the property related to securities offenses (section 56B and 56B1 of the Securities Law). Some of these actions require court orders.

In criminal Securities Law cases the ISA is represented by prosecutors specializing in securities law, and the cases are heard by the newly established economic court. The ISA funds a number of positions in the district attorney's office to ensure securities law matters can be dealt with.

	Criminal sanctions for violations under laws administered by the ISA include: *Use of inside information*—by Section 52C of the Securities Law, the use of inside information by an insider in a company is punishable by imprisonment for a term of up to five years or by a fine. Under Section 52D, the use of inside information by a third party that was received, directly or indirectly, from a person whom that party knows to be an insider in the company is punishable by two years imprisonment or by a fine. *Market abuse*—under Section 54 of the Securities Law**,** securities fraud is punishable by a five-year prison term or to a fine. *Misleading disclosure*—Section 53 of the Securities Law provides that misleading disclosure in public reports and in financial statements is punishable by a five-year prison term or a fine. This section of the law also describes other criminal violations and the maximum punishment for such violations. *Investment Advice Law*—section 39 of the Investment Advice Law includes a detailed list of offenses for which punishment ranges from one to three years imprisonment or fines. *Mutual Fund Law*—section 124 of the Mutual Fund Law lists offenses for which punishment ranges from one to five years imprisonment or fines. *Suspension of trading* If an issuer fails to submit a report or notice within the prescribed time or submits a report or notice which does not materially comply with the provisions of the law, the ISA may order a trading suspension. The exercise of this authority is subject to consultation with the chairman of the TASE board of directors. (Section 38A of the Securities Law). **Power to require information** In addition to having the powers described above (including powers to require document and records, to enter premises and in some cases to seize documents), the ISA has other powers to obtain information in a criminal investigation. *Telecommunications data* An ISA investigator has power under the Criminal Proceedings Law (Enforcement Authorities-Communication Data) to apply to a magistrate court judge for a warrant entitling the investigator to receive records and data from telecom companies pertaining, inter alia, to telephone calls, the identification of telephone holders, and IP addresses. The ISA can also apply to a court for an authority to record telephone conversations. *Power to compel a person to provide information* Section 56C of the Securities Law provides that, if a suspicion has arisen regarding the commission of a securities violation, an investigator may: investigate a person whom the investigator believes to be connected to the violation or who could have information relating to it; and demand that a person appear before the investigator or before another investigator for the purpose of providing any detail, document, or information relating to the said offense or for questioning, and to demand of any person that they accompany the investigator to a location at which the material is to be provided or the questioning take place. The persons investigated under this authority are investigated either as suspects or as witnesses. These Securities Law powers are available for use in relation to violations of all the laws for which the ISA is responsible. For administrative inquiries, the ISA has power to summon any person that is believed to have knowledge about an offense or to a fact that might lead to the identity of the offender, and question them about it (section 52QQ (a) of the Securities Law, see also section 120(q) of the Mutual Fund

Law and section 38G of the Investment Advice Law). This power arises if an investigator has reasonable grounds to believe that an administrative offense has occurred.

Questioning under a summons issued to a person who is not the suspected offender must be conducted at a reasonable time as coordinated with that person. If an individual has been summonsed, the investigator must inform him or her, prior to questioning, of the acts about which the person is being questioned. A person's responses about these acts cannot be used as evidence in criminal proceedings against them.

Private rights of action

Individuals can seek private remedies for misconduct relating to securities laws through various actions. Private remedies can be sought for securities violations either by way of private action or through class actions. Under the Class Actions Law—2006 (the Class Actions Law), a person may file a class action for a cause of action pertaining to securities or mutual fund units.

For losses resulting from poor advice under the Investment Advice Law, the general law of torts applies and damages can be recovered by an action in negligence or for breach of statutory duty.

Under Section 209 of the Companies Law, a plaintiff seeking relief in a class action as described above may request the ISA to participate in the cost of the class action. Where the ISA is convinced that the class action is in the public interest and that there is a reasonable chance that the court will approve it as a class action, the ISA may bear the plaintiff's costs for an amount and under conditions it determines.

Section 41 of the Mutual Fund Law states that a unit holder may sue on behalf of a group of unit holders, the fund manager, the trustee, a director of any one of these, or a member of a committee of the board of directors, for any cause of action under the Mutual Fund Law.

The ISA regards class actions as an important component in the overall enforcement system in the Israeli capital market and as a way of facilitating shareholder activism and private civil enforcement. The ISA actively support the development of private rights of action.

Private rights of action relating to the securities market are heard by the economic court. The first ruling of that court in a class action was handed down in May 2011.

To ensure streamlined hearing of class actions, under the amended Courts Law a court decision to approve an action as a class action cannot be directly appealed to the Supreme Court.

Securities Class Actions Supported by the ISA, 2008—2010

	2008	2009	2010
No. applications for financing class actions lawsuits	2 [1/]	6	4
No. pending class actions lawsuits receiving financing from ISA	7	6	9
ISA budget for supporting class actions (NIS)	350,000	350,000	450,000 [2/]

Source: ISA Annual Reports.

[1/] One of which withdrawn following ISA decision against financing.

[2/] NIS 450,000 also budgeted for 2011.

Under the Companies Law and subject to its conditions, any shareholder and any director of a company may file a derivative action on behalf of a company.

	Under a new amendment to the Companies Law, initiators of derivative actions may request the ISA to bear their costs. If the ISA is convinced that the derivative action is in the public interest and that there is a reasonable chance that the court will approve it as a derivative action, the ISA may bear the plaintiff's costs, in the amount and conditions set by it. This provision has not yet been enacted and will become operative when regulations under it are completed. **Information sharing** Under Section 13 of the Securities Law, the ISA chairman has discretion to share information with a third party (except where compelled by law to do so). The ISA is authorized to disclose information to other ministries or government agencies. The Law does not limit the type of information that may be transferred and the transfer of information gathered during investigations and regulatory enforcement is within the discretion of the ISA chairman. The ISA must disclose information in response to a court order in criminal, civil, or administrative procedures and must disclose information to the attorney-general upon request for the purposes of a criminal trial. In addition, Section 3 of the Basic Law- State Comptroller establishes the right of the state comptroller to demand information from an audited government authority, which includes the ISA.
Assessment	Fully implemented
Comments	
Principle 10.	**The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance, and enforcement powers and implementation of an effective compliance program.**
Description	**Inspection, surveillance and compliance monitoring** The main regulatory departments responsible for regulated entities (for issuers, the Corporate Finance Department, for mutual funds, ETN issuers, portfolio managers, and investment advisers and marketers, the Investment Department) have annual supervision plans and use risk scoring methodologies to identify entities that will be subject to more intensive oversight. These departments review the disclosures and reports of regulated entities, and intelligence reports from the ISA's BI system, and are responsible for audits of regulated entities (in this context, "audits" means desk based reviews and onsite inspections). The Intelligence and Investigations Department is responsible for carrying out investigations of conduct that may indicate violations for which a criminal or administrative penalty may be imposed. *Corporate finance* The Corporate Finance Department handles prospectus disclosure and regulatory disclosures lodged under the Securities Law, and monitors regulatory filings by issuers in real time (including immediate reports, interim reports and annual reports, and disclosure relating to takeover activity and related party transactions). Monitoring includes an assessment and examination from a legal and accounting perspective, with emphasis on compliance with the requirements of the law and enforcement of accounting rules. With regard to immediate reports, special emphasis is placed on reports on related party transactions, private placements, tender offers, debt restructuring and mergers. The department's annual work plan specifies topics on which the department wishes to focus, such as oil and gas companies, corporate governance and internal corporate controls, and property valuation of foreign real estate. The selection of companies to be inspected is based on (among other factors) on the size of the company, its impact on the market, and the issuer's financial condition. The professional staff charged with ongoing monitoring is divided along expertise lines (such as biomed, oil and gas, real estate), and, in accordance with their familiarity, with the company and the industry. Around 160 companies per year are scheduled for detailed review.

	For annual financial statements, the department has program under which annual financial statements of issuers are closely scrutinized over a four year cycle. Currently, the 160 review companies are in the pool for review of financial statements, with intensive reviews scheduled for 55 issuers. As well as the financial statement, other factors examined include the size of the company, its scope of business, financial condition (including as reflected in future cash flow reports and going concern notices), and account complexity. Department staff also take into consideration red flags raised through ongoing contact with reporting companies, from the media and from complaints received from the public. *Investment activity* The Investment Department deals with the licensing, supervision, and regulation of fund managers, trustees, portfolio managers, investment advisers and marketers. It is also responsible for supervision on ETN issuers, and carries out ongoing monitoring and inspections of the regulated entities. To detect noncompliance, the department monitors immediate reports and uses information from the ISA's systems. For fund managers, these systems help detect possible breaches of the provisions of the Mutual Funds Law and unusual unit price fluctuations. The department also engages in ongoing supervision of portfolio manager, investment adviser, and investment marketing agent compliance with the provisions of the Investment Advice Law. It conducts onsite and desk- based audits to examine licensees' compliance and audits portfolio management companies and nonbank stock exchange members for compliance with the provisions of the Money Laundering Law. It also handles complaints filed by the public against licensees. Intelligence about activity by unlicensed entities in breach of the obligation to hold a license is detected by using complaints, monitoring the internet and using general intelligence. *Licensees*: The unit responsible for the supervision of licensees has a risk-based model, according to which each corporate licensee is graded on a scale of 1 to 100 against parameters such as the value of assets under management (portfolio managers) or assets under advice (advisers), convictions, indictments, the results of previous inspections, changes in the management or ownership, the number of inspections previously conducted, information published in the media, and alerts from the Corporate Finance Department. Depending on the grade the licensee receives, the licensee unit staff decides on the scope of supervision and its intensity based on a scale of one to three. For a licensee receiving the most problematic risk rating, a specific staff member is assigned for the purpose of its supervision. That staff member supervises the licensee on an ongoing basis and maintains contact with its management and compliance officer. He or she is responsible for inspecting the licensee, focusing on topics set by the unit in line with warning signs encountered during current supervision of the licensee. The number of these inspections is determined by the unit. In the current planning year, the unit round 12 portfolio managers (including both bank and nonbank entities) are scheduled for intensive inspections. For licensees not rated in the intensive supervision category (where a specific staff member has not been assigned), the main criterion for conducting such inspections is the time elapsed between inspections and the unit aims to carry out desk-based reviews on a two to four year cycle, depending on their size. The licensee unit conducts cross-sectional (thematic) inspections of several licensees on selected issues. The unit also carries ad hoc inspections licensees on specific subjects, as a result of a complaint or other information received about the licensee. To improve compliance, the ISA provides training to all new corporate licensees. Training sessions are conducted with each company separately, close to the occasion of granting the licenses. An

	onsite inspection is then carried out within the first year of the new licensee's operations. The licensee unit is currently carrying out a pilot project to use the BI system to identify potential violations. This use of the system is intended to predetermined risk factors and is designed to flag licensees for potential inspection. For example, it will identify instances where a portfolio manager has an unusually high level of turnover of assets (which may indicate churning), or an unusually low turnover (which may indicate poor management). For advisers (where round 90 percent are individually licensed employees of banks) the unit has a special category of "problem advisers" based on criteria such as the level of complaints, adverse publicity or because individuals are adversely known to the unit. If a person becomes a problem adviser, he or she is subject to an immediate audit. *Mutual funds*: The unit responsible for the supervision of mutual funds carries out ongoing monitoring of mutual fund transparency. Annual financial reports of mutual funds are examined based on a model, according to which all reports are checked, and 50–60 annual financial statements per year are examined in detail. The model is designed to select reports in a manner that covers all persons involved in preparing the financial statements (fund managers, trustees and auditors). Prearranged transaction reports and off-floor block trading reports are examined and other factors are considered, such as the volume of the transaction, the price of transaction (compared to the market price) and compliance with the instructions of the law and regulations. The inspections conducted by the unit take into consideration parameters such as the scope of fund assets and the quality of internal control systems. According to the model, each regulated entity is inspected at least once every three years (for larger entities) to five years (for smaller entities). The mutual fund unit uses the BI system to identify instances where a fund manager acquires assets outside its investment mandate on a near real time basis. *TASE members*: The inspections and audits carried by TASE are described under Principles 21 and 25. **Unusual transactions on regulated markets** The ISA uses a market surveillance and data analysis system, Business Intelligence (BI), described under Principle 8. The system provides ISA staff with flexibility in the collection, comparison, and analysis of data. Each department uses the data in the system for its own purposes. It is primarily used to uncover possible violations, but information from these tools is also used by other departments not directly involved in enforcement (the Corporate Finance, Mutual Funds and Economic Research departments) to more effectively monitor and regulate the entities under their supervision and to monitor events and trends in the capital market. The ISA uses the BI system on a daily basis. The system was deployed in 2010, replacing another computerized surveillance system. Since deployment there has been an increase of 25 percent in suspicious activity uncovered by the ISA in comparison with previous years. Around 60 alerts are produced each day. **Mechanisms to detect and investigate insider trading and other forms of market abuse** Market abuse, price manipulation and insider trading are primarily detected by the BI system described under Principle 8. The ISA Investigations and Intelligence Department investigates any suspicion of a violation under the Securities Law, the Mutual Funds Law, and the Investment Advice Law. The department collects information from internal and external sources. This information, including information collected from

local and international data bases is examined, analyzed and evaluated by the staff with the aid of computerized systems. Based on an initial evaluation, decisions to gather further intelligence and to consolidate and verify information already collected.

These activities are normally conducted by the intelligence unit of the department. Cases, for which substantive evidence is found, are forwarded to the ISA chairman, who decides whether to pursue a criminal investigation, an administrative inquiry or to close the file. If the ISA chairman orders the opening of an investigation or administrative inquiry, the department's investigation unit exercises its authority. The following charts demonstrate the results of these activities:

Investigations conducted by the ISA Investigations and Intelligence Department 2006–2010

Type of Offense	2006	2007	2008	2009	2010	Total
Securities Fraud	5	1	2	4	4	16
Use of Inside Information	4	3	2	6	2	17
Misleading Information	2	2	5	4	5	18
Delinquent and non-Filing	1	1	1			3
Unlicensed Portfolio Management or Investment Advice	2					2
Offenses by a stock exchange member employee or portfolio manager	1	1				2
Disciplinary Offenses		1				1
Offenses under the Mutual Funds Law		1		1		2
Offenses under the Penal Code				2	1	3
Total	**15**	**10**	**10**	**17**	**12**	**64**

Source: ISA

A criminal investigation is commenced on the instructions of the ISA chairman, and is completed when the investigation file is sent to the office of the district attorney with a recommendation to file an indictment or to close the file. The decision to indict rests with the district attorney.

Investigation Cases Forwarded to the District Attorney's Office, 2006–2010

Type of Offense	2006	2007	2008	2009	2010	Total
Securities Fraud	7	3	4	3	3	20
Use of Inside Information	1	3	6	4	4	18
Inclusion of Misleading Information	3	3	4	4	3	17
Delinquent Filing and Non-Filing		3	1			4
Offenses by a stock exchange member employee or by a licensed investment portfolio manager		1				1
Offenses under the Mutual Funds Law		1			1	2
Offenses under the Penal Code		1	1	2	2	6
Fraudulent acquisition			1		1	2
Total	**11**	**15**	**17**	**13**	**14**	**70**

Source: ISA

Investor complaints

The ISA employs a person full time to deal with inquiries and complaints from the public. This person is for dealing with all complaints and public inquiries about securities market issues.

Inquiries from the public include inquiries from individuals active in the capital market, such as investors, portfolio managers or investment advisors, attorneys representing individuals and/or reporting corporations, individuals who have been harmed or who wish to report irregularities or problems in the capital market as a whole, or in one of its sectors, external entities such as government bodies. In other cases various individuals and entities refer questions and inquiries to the ISA, such as media representatives.

The number of inquiries from the public processed by the ISA has more than doubled over the past five years:

2006	2007	2008	2009	2010
459	460	529	663	1,027

Source: ISA annual reports

The website of the ISA includes a platform enabling persons to send complaints to the ISA regarding suspicious capital market activity and possible violations of the law.

Evidence of ISA's use of its compliance monitoring powers

The Corporate Finance Department and the Investment Department prepare annual work and target inspection plans. At the end of the year, each department checks if it attained its targets.

Corporate finance

The ISA conduct full, partial and minimal[5] reviews of prospectuses lodged by issuers in the capital market. In 2010, 145 applications for permits to publish prospectuses were reviewed under full or partial procedures and 70 applications under the brief review procedure. In the period from January to November 2011, the ISA received 161 prospectuses, and subjected about half of them to full review. All IPO prospectuses are subject to full review.

In 2010, round 160 audits were conducted on reporting companies, using both outsourced service providers and an ad hoc team comprised of ISA employees. Issues covered by these reviews included:

corporate governance;
valuation of real estate assets'; and
material items in the financial statements (such as inventories, investment property, recognition of income, etc.).

Mutual fund activity

In 2010 the ISA Investment Department conducted on-site inspections on six mutual fund managers. Among the matters focused on in these audits were:

[5] A minimal review focuses only on compliance with formal requirements and does not involve analysis of the contents.

	control procedures; the management and control of investments; and revaluation of securities. In addition, fund managers were required to report to the ISA regarding the application of recommendations issued following audits conducted in 2009. Cross-sectional (thematic) desk-based audits were also conducted. These included: an audit of all fund managers focused on investment management and the use of centralized securities allocation accounts to divide the securities bought and sold by the fund manager between the funds under its management. Following the analysis of the audit results, the department issued a staff bulletin to fund managers and trustees regarding the ISA's position on a number of issues arising from the audit; an audit of disparities in the collection of management and trustee fees. Following the findings of this industry-wide audit, the department issued a staff bulletin regarding its position on the provisions governing the calculation of fund manager and trustee fees and subsequently issued an ordinance under Section 97(b) of the Mutual Fund Law on this matter; and an audit of executive compensation of investment managers and senior officers in mutual fund management firms. The Department received 269 prospectuses in 2010, of which 422 were amended following ISA intervention. *ETN issuers* In 2010, the ISA audited three ETN issuers. Two of these audits examined risk management and corporate governance issues employed by the ETN vendors, while a third focused on the operations of the financial group in which the ETN issuer operates. ISA staff examined analytic and decision-making processes, risk management, the relationships between the companies and their trustees, and the conduct of these trustees. It also scrutinized the group's deposits in foreign bank accounts. The companies provided information and documentation to the ISA. *Investment advisers and marketers* During 2010, two types of audits were conducted on investment advisors and marketing agents: seven field audits and five correspondence cross-sectional audits on various issues. Two of these cross-sectional audits relied on data analysis derived from ISA IT systems, and did not directly engage the investment houses subject to audit; and Thirty-six in-depth audits focusing on specific issues of the Investment Advice Law were conducted on licensed investment houses and in the investment advice departments of banking corporations. Of these audits, 22 were conducted by way of correspondence, in which the audited entities were requested to provide documentation. Two were conducted through data analysis derived from IT systems, without directly engaging the audited companies. Following the audits, the department sends letters detailing the defects uncovered during the audit and the measures needed to correct and improve these defects. The Investment Department subsequently follows up on the implementation of these measures. *Portfolio managers* During 2010, six in-depth company audits were conducted in portfolio managers regarding the control environment and compliance with the Law. Eight portfolio management company audits were completed covering especially compliance with the manager obligations to its clients, including know-your-client and suitability rules.

The Investment Department also conducted audits on portfolio management companies that are also stock exchange members. The audits examined compliance with the Money Laundering Prohibition ordinance, including:

the "know-your-client" requirements;
verification of identifying details;
specification of controlling shareholders and beneficiaries;
identification in person requirements;
the safekeeping of identifying documents;
regular and special reporting to the Money Laundering Prohibition Authority; and
whether computerized databases containing identity information are being maintained.

ISA internal controller

ISA has an internal controller of the ISA responsible (among other things) for ascertaining that the ISA fulfills its inspection responsibilities and addresses unusual market activity. This work is designed to identify deficiencies and improve the work of the ISA. The internal controller sets out his findings in audit reports submitted to the ISA audit committee. The controller verifies the ISA's department's performance against their work plan and provides recommendations and suggestions.

Evidence of the ISA's addressing unusual market activity

As described above, the ISA operates a market surveillance and data analysis system using BI technology. The system detects activity that indicates that a possible violation of regulations has occurred, and then sends notification alerts to the appropriate ISA supervisor.

In 2010, following investigations performed by the ISA, 13 indictments were filed by the Tel Aviv District Attorney's Office (Taxation and Economics Department) primarily relating to market abuse, use of inside information, and misleading disclosure.

Total Indictments Filed
(Fraud, Inside Information, Market Abuse, Investment Advice Law, and Penal Code)

2006	2007	2008	2009	2010
7	4	8	14	13

Requirements for supervisory and compliance systems

Criteria for Recognition of an Internal Enforcement Program in the Securities and Asset Management Field

In August 2011, the ISA published Criteria for Recognition of an Internal Enforcement Program in the Securities and Asset Management Field. This project was initiated following the enactment of the administrative enforcement reform and the imposition of supervisory liability on chief executive officers (CEOs).

The ISA has designed criteria for the recognition of an internal enforcement program as a defense claim against potential enforcement procedures, relevant to all issuers and ISA-regulated entities.

An internal enforcement program is a voluntary mechanism adopted and implemented by a corporation on an ongoing basis, designed to ensure the corporation and its units are comply with the provisions of the Securities Law, the Mutual Fund Law, and the Investment Advice Law.

The ISA does not intend to inspect the adoption of these corporate programs on an ongoing basis, but will do so in the event of suspected violations. The enforcement program must be effective in the sense that its existence leads to internalization of the law and the development of a compliance culture. Written procedures are not regarded as sufficient and must be backed by effective practical implementation. In exercising its discretion with regard to its legal enforcement powers, the ISA may

	credit a company implementing an effective enforcement program or individuals within that company. Eight basic criteria set out the principles that will be considered by the ISA in its assessment of an effective enforcement program, including board accountability for the formulation, adoption and implementation of the enforcement program. *Compliance programs for nonbank TASE members* TASE rules require nonbank stock exchange members to appoint a compliance officer to ensure compliance with the laws and regulations to which they are subject, including the Securities Law and TASE rules and regulations. The compliance officer must have a relevant academic degree and the qualifications, know-how, and experience befitting the position and its responsibilities. The compliance officer must act in accordance with a work plan approved annually by the TASE member's audit committee and board. This plan must include a definition of the compliance officer's responsibilities and powers; details of the laws and TASE rules that the compliance officer must consider in the course of their duties; the tools and means made available to the member's employees and managers to support compliance; the sanctions that can be imposed on managers and employees; and the format and frequency of reports the compliance officer must send to the member's CEO, audit committee, and board of directors. The compliance officer is responsible for the integration of procedures among the member's employees, as well as for implementation. The compliance officer is responsible for routinely monitoring the rectification of any defects found. *Internal controls on periodic disclosure in financial statements ("Israeli SOX")* The Securities Law Regulations (Periodic and Immediate Statements)—1970 require a reporting corporation to evaluate the effectiveness of its internal controls on the disclosure of the financial statements (ISOX procedures). Under the regulations, a reporting corporation must attach declarations of the CEO and of the chief financial officer (CFO) of the corporation to its financial statements attesting to the accuracy of the statements, as well as a report of the board and the management of the corporation as to the effectiveness of the internal controls on the reporting and disclosure of the financial statements. ISOX procedures relate only to the financial statements of the corporation and do not apply to immediate reports. *Duty of licensed corporations to set working procedures* Under a directive issued by the ISA pursuant to Section 28(b) of the Investment Advice Law (the Directive to Licensed Corporations Concerning the Duty to Determine Work Procedures for their Operation and Management under the Investment Advice Law (IA Internal Procedures Directive)), a licensed corporation must determine procedures, which ensure compliance with the law and regulations and act in accordance with these procedures. Procedures must cover the implementation of the provisions of the relevant laws and the establishment of standard operating procedures, training programs, and internal enforcement. *Power of ISA to issue directives to fund managers* Section 97(b) of the Mutual Funds Law authorizes the ISA to issue directives to assure the efficiency of internal control procedures, the internal enforcement program, and their sound operation, including ordinances regarding the mandatory appointment of officers in charge of the abovementioned procedures and program. *ISA monitoring of compliance procedures* The ISA monitors the execution of compliance procedures in supervised entities as part of its processes when inspecting a regulated entity.

	In making discretionary decisions on compliance and enforcement matters, the ISA may take into account effective compliance systems and programs maintained by regulated entities. ISA tests whether an internal enforcement program is an effective one and is integrated at all organizational levels. The corporation must ensure that the controlling shareholders, the board of directors, the executives, employees, and relevant service providers are familiar with and committed to the program. Factors to be considered include: confirmation by the relevant parties that they have read the procedures, that the provisions of these procedures are clear to them, and that they are committed to compliance to them; the holding of training sessions and the delivery of information to the relevant parties; the provision of information on an ongoing basis regarding these procedures, and their implementation; and the initiation of internal surveys among the relevant parties checking the degree of their familiarity with internal enforcement procedures and the extent to which these procedures relate to daily operations. **Supervision of employees** Section 52LLL of the Securities Law makes the CEO of a licensed corporation and a partner (excluding limited partner) in a licensed partnership responsible for supervising and requires them to undertake all reasonable measures to prevent violations by a corporation or a partnership or by an employee. The CEO and partner are held accountable and subject to enforcement measures for violations by the licensee (section 52LLL (c) of the Securities Law). If a corporation adopts a proper and effective internal compliance program, which includes sufficient procedures to prevent the violation and appoint a compliance officer, the CEO or partner is considered to fulfill this obligation. In the Criteria for Recognition of an Internal Enforcement Program in the Securities and Asset Management Field (see above) , one of the principles considered by the ISA when evaluating internal enforcement programs is the proper handling and analysis of defects and violations. **Enforcement program** *Enforcement activity based on annual work plans* The Intelligence and Investigation Department, the Department of Administrative Enforcement (which has recently begun to operate following the enactment of administrative enforcement) and the District Attorney's Office for Securities Matters are the ISA's designated enforcement units whose activities are coordinated on a yearly basis. Another designated enforcement division is the Department of Supervision of Secondary Market, which is responsible for stock watch activities. All enforcement departments of the ISA submit their annual work plans to the ISA chairman and are required to demonstrate coordination with the other enforcements departments as well as fulfillment of their targets. *Professional staff* The ISA professional staff includes lawyers, accountants and economists. Many senior level staff members have prior enforcement experience as investigators or prosecutors. Professional enforcement staff receives training, as applicable to their scope of activities. Each department has an internal legal advisor, which specializes in the activities of the department (in addition to the ISA General Legal Counsel).

	Funding Each department of the ISA annually defines its financial requirements, including those pertaining to enforcement activity. The ISA plans its enforcement budget based on anticipated and unexpected enforcement expenses, including expert opinions, investigation activities abroad, the production of special investigation documents (such as telephone records), forensic experts, advisors, and computerized systems. *Powers* The comprehensive enforcement powers of the ISA are detailed in under principles 8 and 9. The ISA has a proven track record in enforcement, and there is good evidence that it has been active and effective in the use of its investigative and enforcement powers.
Assessment	Fully implemented
Comments	The ISA takes a planned and systematic approach to monitoring compliance by regulated entities. There is good evidence of the use of its inspection and surveillance powers, and market participants confirm that its supervision activities are intense and effective in deterring misconduct. The ISA has sophisticated technology to help it detect misconduct. The ISA has a good record in enforcing the regime. The ISA has a proven track record in enforcement, and there is good evidence that it has been active and effective in the use of its investigative and enforcement powers.
Principles for Cooperation in Regulation	
Principle 11.	**The regulator should have authority to share both public and non-public information with domestic and foreign counterparts.**
Description	**Domestic information sharing and cooperation** Section 13 of the Securities Law gives the chairman of the ISA's broad discretion to share information with any third party. This enables the ISA disclose information to other ministries, agencies, the tax authority, and the Knesset. The ISA can share information about matters of investigation and enforcement; rulings pertaining to permits, licensing and approvals; surveillance, market conditions and events; client identification, regulated entities, and TASE-listed companies. ISA must disclose information in response to a court order in criminal, civil or administrative procedures and is obligated to disclose information to the attorney-general upon request solely for the purposes of a criminal trial. Section 3 of the Basic Law- State Comptroller also gives the state comptroller the right to demand information from an audited entity, which includes the ISA. This broad power to share information is supported by a number of arrangements with other regulatory agencies and law enforcement bodies. These arrangements include: *MOU Between Financial Regulators* To facilitate cooperation and the exchange of information between the financial market regulators, the supervisor of banks, the Israel Securities Authority and the commissioner of the Capital Markets Division have signed an MOU on cooperation and exchange of information. The stated objectives of the MOU include advancing and coordinating the efficient, fair, and uniform supervision of the Israeli financial system; strengthening the stability, transparency, and fairness of Israeli financial markets; and advancing the implementation of best supervisory practices commonly accepted around the world.

	Under the MOU, the supervisors agree to share information at their disposal that may be required by the other supervisors, providing that this does not impinge upon the supervisory or investigative process. They also agree to respect nondisclosure of information to third parties, without the consent of the regulator from which the information was obtained. *Cross membership of regulatory bodies* The ISA chairman is a member of the advisory board of the Bank Supervision Department and an ISA representative sits on the BOI' National Committee for Payments and Settlements. Representatives of BOI and the MOF sit on the ISA plenum. *Joint committees and task forces* These are often formed to address specific issues. Examples include the Bachar Committee on structural reform of the capital market; the committee on the concentrated competitive structure of Israel's economy; the interagency committee on regulating securities custody; the securitization committee; the committee on establishing REPO transactions; and the committee which enabled the introduction of REITs to the Israeli capital market. *Law enforcement agencies committees* In 2006, the Israeli cabinet adopted a policy of combining the resources of all relevant professional agencies to wage a concerted war on serious and organized crime and the government decided to consolidate collaboration between all the state authorities engaged in law enforcement. Three forums were established under this initiative, in all of which the ISA plays an active role, a Policy Coordination Team (A high-level team charged with outlining policy for combating serious crime and organized crime); a Permanent Committee (headed by the Police Investigations and Intelligence Department, responsible for directing and coordinating activity for combating serious and organized crime); and a Combined Intelligence Task Force (responsible for the exchange of intelligence information and investigations). *External approval* The ISA is authorized to share information with other domestic authorities without external approval. **International information sharing and cooperation** The ISA is a full signatory to the IOSCO Multilateral Memorandum of Understanding (hereafter IOSCO MMOU). It also has bilateral cooperation agreements with some 19 foreign securities commissions, the latest signed in March 2011 with the China Securities Regulatory Commission. Most cases of assistance with a foreign authority have involved the U.S. Securities Exchange Commission, with which the ISA has had an MOU since 1996. Chapter 9B of the Securities Law (Sections 54K1–54K9) enables the ISA to cooperate and provide assistance to foreign securities authorities with which it has signed an MOU. This Chpater enables the ISA to provide assistance for the purposes of administering and implementing, "securities laws" which are defined in s54K1(a) to include all laws administered by the ISA. Once an MOU is signed, nonpublic information may be released by the ISA to a foreign authority, subject to the following conditions set out in Section 54K2 of the Securities Law: the foreign authority must submit a formal request for assistance; the subject of the request pertains to a possible securities violation under a law for which the foreign authority is charged with implementing and enforcing; and the request complies with provisions of Chapter 9B of the Securities Law and of the MOU. Under Section 54K1, assistance is defined as including the provision of information and documents, conducting a search and/or seizure of documents, conducting investigations, and the delivery of

	information and documents for the purposes of administering and implementing securities laws in a foreign country. Section 54k5(c) allows the ISA chairman to refuse a request if he or she suspects abuse of the process, that is that the information requested is likely to be used for purposes other than those stated in the request or the MOU. Foreign authorities are requested to declare in the request that any information or document transferred pursuant to the request is to be used solely for the purpose it is delivered, as stipulated by Regulation 2(3) of the Securities Regulations (Co-operation with a Foreign Authority), 2000. To date, the ISA has not refused a request for assistance under its MOU agreements. On receiving a request for assistance, the ISA can exercise its authority to demand information and documents, obtain warrants for search and seizure, and conduct investigations. The Securities Law authorizes the ISA to transfer the requested information or document to the foreign authority. Requests for cooperation with agencies with which the ISA has not entered an MOU are handled through the State Attorney's Office under the Law for Legal Assistance Between States—1998. *External approval* Section 54K5 of the Securities Law empowers the ISA to transfer information and documents to foreign counterparts without external approval. This is subject to two exceptions: no nonpublic document relating the business of a banking institution or of an insurer may be transferred to a foreign authority other than with the consent of the supervisor of banks or the insurance commissioner, as applicable; and the attorney general is entitled to deny cooperation with a foreign authority if it deems that the measures undertaken pursuant to a request for assistance are potentially harmful to the sovereignty of the State of Israel, to its security, to a vital interest, to the public interest, or to a pending investigation. **Unsolicited information** The ISA is authorized to disclose information to other ministries, agencies, and authorities at the discretion of the chairman of the ISA. The Law does not limit the issues and information that can be transferred. This authorization also extends to foreign authorities. As a signatory to the IOSCO MMOU, Israel is committed to Article 13 and provides unsolicited information to other authorities. For example, more than 60 Israeli companies are cross-listed on foreign exchanges and the ISA may share information at its disposal with the securities regulator responsible for supervision of the exchange on which these securities are listed. **No requirement for breach of domestic laws** Under Section 54K2 of the Securities Law, assistance may be provided regardless of whether a similar or parallel Israeli law exists, provided that the subject of the request constitutes an alleged violation of the securities laws implemented and enforced by the requesting foreign authority. If the assistance rendered to the foreign authority entails the exercise of ISA search, seizure and arrest powers, one exception applies. Under Section 54K4(a) of the Securities Law, these powers can only be employed if the violation referred to in the request could possibly be the subject of a criminal investigation in Israel. **Bank account information** The ISA is a signatory to the IOSCO MMOU and fully complies with its provisions. In 2010, the ISA

	provided assistance and transferred information and records under Article 7(b)(ii) of the IOSCO MMOU to foreign authorities in six different cases.
Assessment	Fully implemented
Comments	
Principle 12.	**Regulators should establish information sharing mechanisms that set out when and how they will share both public and nonpublic information with their domestic and foreign counterparts.**
Description	**Power to enter into information sharing agreements** *Domestic authorities* By its constituting legislation, the ISA is a corporation, competent for every obligation, right or legal act (section 8 of the Securities Law). Section 2 of the Securities Law states that the function of the ISA is to protect the interests of the public investing in securities, as provided in the Law. These provisions mean that the ISA has the power to enter into agreements with other domestic authorities, for the purpose of protecting the interest of the public investing in securities, including information-sharing agreements. *Foreign counterparts* Chapter 9B of the Securities Law enables the ISA to execute MOUs signed with foreign authorities, subject to certain conditions set out in the Law. An MOU is defined in section 54K1(a) of the Securities Law as an agreement concerning cooperation in the administration and enforcement of securities laws. Entering into an agreement with foreign entities requires the authorization of the ministry of foreign affairs, the ministry of justice and the cabinet, for each agreement. The minister of finance submits each agreement, on behalf of the ISA, to the cabinet for approval, and therefore, in practice, his authorization is required as well. In practice, the ISA usually has not encountered difficulties in receiving such authorizations, and is a party to 19 such agreements. **Information sharing mechanisms** The ISA is a full signatory of the IOSCO Multilateral Memorandum of Understanding, which enables information sharing to facilitate detection, deterrence, licensing and surveillance. Under the MMOU, the ISA exchanges information with foreign counterparts on a regular basis. In addition, the ISA has signed 19 information-sharing agreements. The ISA has used its arrangements with foreign authorities under these MOUs to obtain information for the detection of cross-border misconduct and for assisting in the licensing and surveillance. The ISA has also, within the framework of the IOSCO Emerging Markets Committee Working Group 4, designated an online portal to serve as a gateway to useful information for financial regulators, organized in a user-friendly manner that can increase the effectiveness of interagency cooperation and information sharing. The ISA website includes links to information on matters relevant to fit and proper assessments, and is intended to expand the sources of public information available to IOSCO members. In October 2011, the ISA signed a new MOU with the US Public Company Accounting Oversight Board (PCAOB) for cooperation and the exchange of confidential information related to the oversight of auditors and auditing firms subject to the regulatory jurisdictions of both the PCAOB and the ISA. **Confidentiality** All information provided to the ISA by foreign authorities must be kept confidential by its employees

<table>
<tr><td></td><td>under Sections 13 and 56E of the Securities Law. Other than as required by law, the chairman will not disclose information obtained from a foreign authority to a third party without the consent of that foreign authority.

The only cases where transfer of information is compelled by law are to the attorney-general (for purposes of a criminal trial only) and to a competent court. To date, the ISA has never been called upon by the attorney-general to disclose information received from foreign counterparts. With regards to disclosure to the court, in the process of obtaining court orders, the ISA does disclose the information received from a foreign authority, when acting on the foreign authority's behalf. However, in relevant cases, the ISA can ask the court to preserve the confidentiality of the information.

Section 53(b) of the Securities Law provides the contraventions of the confidentiality provisions are punishable by imprisonment for a term of one year or a fine. Violation of confidentiality is also considered a disciplinary breach, and as such, may lead to disciplinary measures against the offender (including dismissal).

Section 54K9(a) of the Securities Law stipulates that, notwithstanding the provision of any law, the ISA may refuse to provide a third party with information or documentation that was submitted to it by a foreign authority or was received, gathered, or produced pursuant to a request by that authority. This includes the document containing a request for assistance. The sole exception to this is cases in where a request for information was submitted by the attorney-general for purposes of a criminal trial or by the court.

ISA safeguards on confidentiality are not limited to information received but information delivered to foreign authorities as well. All agreements between the ISA and foreign authorities contain confidentiality clauses which uphold ISA obligations regarding confidentiality.

ISA practice

In practice, the ISA shares information with both domestic and foreign regulators.
Most requests for assistance submitted to the ISA are done so under the IOSCO MMOU, to which the ISA has been a signatory since 2006. Since 2006 there has been a marked increase in the number of requests for assistance:

Requests for Assistance Submitted, 2005–2010

<table>
<tr><th></th><th>To ISA</th><th>From ISA</th></tr>
<tr><td>2005</td><td>2</td><td>8</td></tr>
<tr><td>2006</td><td>14</td><td>2</td></tr>
<tr><td>2007</td><td>15</td><td>-</td></tr>
<tr><td>2008</td><td>18</td><td>1</td></tr>
<tr><td>2009</td><td>22</td><td>5</td></tr>
<tr><td>2010</td><td>17</td><td>8</td></tr>
</table>
</td></tr>
<tr><td>Assessment</td><td>Fully implemented.</td></tr>
<tr><td>Comments</td><td></td></tr>
<tr><td>Principle 13.</td><td>The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers.</td></tr>
<tr><td>Description</td><td>Assistance to foreign regulators—records

The ISA is empowered to provide assistance to a foreign authority and to use its investigatory powers on its behalf. Section 54K4 of the Securities Law provides the ISA with the authority to assist a foreign authority, and to use its information gathering powers and its investigative powers to</td></tr>
</table>

	provide assistance to a foreign authority. Relevant information can be shared with a foreign authority subject to the provision of a formal request for assistance under the IOSCO MMOU or another relevant agreement. Sections 56A and 56B of the Securities Law define the power of the ISA to demand from any person any information or document pertaining to corporations which are subject to the Securities Law or Mutual Funds Law, including bank account and brokerage records necessary to reconstruct securities transactions. The BI surveillance system used by the ISA contains almost all information needed to reconstruct securities transactions, including the account numbers (but not names of account holders) relevant to a given transaction. So much of the information is already held by the ISA. Requests for such information are handled in accordance with procedures set out in an internal manual dealing with the handling of requests for assistance from foreign counterparts. **Assistance to foreign regulators—compliance with laws and regulations** Chapter 9B of the Law (and specifically sections 54K1 and 54K2 of the Law) enables the ISA to provide information and documents to foreign authorities in response to requests for assistance under an MOU signed with a foreign counterpart. All matters relating to insider dealing and market abuse, the issue and offer for sale of securities and derivatives and associated reporting requirements, market intermediaries (including broker dealers, investment and licensed trading advisers, managed funds, markets and exchanges, and clearing and settlement facilities pertain to the administration and enforcement of securities laws. Therefore the ISA can provide information on all these matters. The ISA is empowered by the Securities Law to comply with the provisions of the MMOU and regularly provides assistance regarding the matters referenced in the question. **No requirement for independent interest** The ISA may provide assistance to a foreign authority regardless of whether: a specific Israeli law exists in parallel (Section 54K2 of the Securities Law); and the ISA has an independent interest in the matter, provided that the subject of the request may constitute a breach of the securities laws of the requesting foreign authority. If the assistance rendered the foreign authority entails the exercise of ISA search, seizure, and arrest powers, one exception applies. Under Section 54K4(a) of the Securities Law, these powers can only be employed if the violation referred to in the request could possibly be the subject of a criminal investigation in Israel. In addition, section 7(c) to the IOSCO MMOU provides that assistance will not be denied based on the fact that the type of conduct under investigation is not necessarily a violation of the laws and regulations of the requested authority. **Information on regulatory processes** The ISA can provide information about regulatory processes, such as licensing and audit procedures, about reporting companies, and regulated entities under its jurisdiction. For other financial institutions, most licensing procedures are outlined in laws and regulations and hence are public information. **Assistance to foreign regulators** *Documents and statements* Section 56A of the Securities Law defines the power of the ISA to demand information and documents. The chairman of the ISA or a person authorized in writing by the chairman may demand

	from any person any information or document pertaining to corporations which are subject to the Securities Law or the Joint Investment Law, including any report, register, account, certificate or any other document pertaining to their business. This authority can be used to secure the execution of the laws mentioned, or when suspicion of a violation arises, and can also be used in order to provide assistance to foreign regulators. If an MOU has been signed and a formal request for assistance is made to the ISA, the ISA can use its powers to compel the production of information and the giving of testimony (sections 56A and 56C of the Securities Law) on behalf of a foreign authority. Under the Israeli Law a false statement to the ISA may be prosecuted as an attempt to obstruct justice. *Court orders* The ISA has power to offer assistance to foreign regulators in obtaining court orders a follows: if a suspicion has arisen regarding the commission of a securities offense, an investigator may petition a magistrate court judge to issue a warrant allowing the investigator to enter any place and to carry out a search of that location; and an investigator may also ask a magistrate court judge for a temporary warrant for the seizure of property related to the offense and for instructions regarding how to dispose of such property. These warrants remain in force for a period of one year from the date issued unless indicated otherwise. Their duration may be extended subject to certain conditions. ISA assistance of this kind can be offered to foreign authorities only if the subject matter of the request could be the subject of a criminal investigation in Israel. **Financial conglomerates** *Group structure* The ISA's supervision of the financial institutions in its jurisdiction (mutual fund managers and trustees, portfolio management companies and ETN issuers) is based on activity rather than group. With that limitation, the information resources and tools at the ISA's disposal allow reconstruction of Israel's securities service conglomerates. This includes providing information that is publicly available and information from the ISA's centralized intelligence system which, through cross-referencing from multiple sources of information, can uncover business links on both the corporate level and individual stakeholder level. Information of this kind can be provided to a foreign authority under the IOSCO MMOU and the bilateral MOUs to which the ISA is party. *Capital requirements* The capital requirements applicable to ISA-regulated financial companies are readily attainable public information. Similarly, the capital requirements for TASE members are set out in publicly available TASE rules and regulations. *Cross investments in company groups* Provisions in the Mutual Funds and Investment Advice Law prohibit or restrict the activities of mutual fund managers and portfolio management companies. A portfolio manager may make proprietary investments in select group affiliates, as permitted by the legislation. ETN issuers must follow a passive investment strategy. Investments made by mutual fund managers which may entail conflicts of interest are subject to board approval and the scrutiny of the fund trustee. For all practical purposes, therefore, investment in group companies is largely localized to the proprietary investments of a parent holding company and can be easily monitored. *Intra group and group wide exposures* The ISA does not monitor intra-group or group-wide exposures. Procurement of this type of

	information, which at this time is private in nature, would be likely to require the use of ISA investigatory powers, and hence be subject to a formal request for assistance and suspicion of wrong-doing. *Relationships with shareholders* Publicly traded conglomerate companies are subject to the disclosure requirements that apply to all public companies. They include reporting of all market and OTC transactions conducted by principal shareholders (5 percent + shareholders) as well as extensive immediate reports regarding related party transactions, including the board and special majority shareholder approval process surrounding these transactions. For privately held companies, acquisition of this information would likely require a formal request for assistance on the part of the foreign authority. *Management responsibility and governance* Information about corporate governance requirements of regulated entities, including management accountability and controls, is public information which can be easily provided to foreign authorities
Assessment	Fully implemented.
Comments	
Principles for Issuers	
Principle 14.	There should be full, accurate, and timely disclosure of financial results and other information that is material to investors' decisions.
Description	**Disclosure requirements** The Securities Law and related regulations set out a detailed and comprehensive disclosure and reporting regime for issuers whose securities are offered to the public in Israel. The regime includes requirements for: a prospectus for public offerings of both equity and debt issues; annual reports; quarterly reports; and material event disclosures ("immediate reports"). All disclosures and reports are filed electronically through the ISA's MAGNA regulatory filing system and are made available to the public through a separate distribution site. The ISA is responsible for monitoring compliance with these disclosures obligations and enforcing disclosure and reporting requirements. *Public offerings of securities* Section 15 of the Securities Law prohibits the offer and sale of securities to the public other than under a prospectus which has been approved by the ISA. Exclusions from the definition of "the public" are set out in section 15A and Schedule 1, and include offers made exclusively to qualified investors and offers made to less than 35 offerees. Detailed content requirements for a prospectus are set out in the Securities Law Regulations (Details, Structure and Form of Prospectus and Draft Prospectus)—1969 (the Prospectus Regulations). These regulations require a prospectus to contain detailed information about: the offer of securities; the securities and capital of the issuer; the use of the proceeds from the offered securities; description of the issuer;

	the issuer's subsidiaries and associated companies; the issuer's principal shareholders and senior corporate officers; financial statements; and additional details, including a lawyer's opinion; an accountant's opinion on the audited financial statements; consents of any person providing a professional opinion; and material valuations (where relevant);expenses and commissions relating to the offer; and any allocation of securities made for noncash consideration in the previous two years. Since 2005, shelf regulation is available for issuers who offer securities on a number of occasions during a two year period. Such offers may be made under a single shelf prospectus. See section 23A of the Securities Law and Securities Regulations (Shelf Registration of Securities) 2005. *Annual reports* Annual reports must be filed within 3 months of the end of the issuer's reporting period. Detailed requirements for the content of these reports are sets out in the Securities Regulations (Annual Financial Statements), 2010. Annual reports must contain: a detailed description of the company and the development of its business activities over the reporting year (29 separate items are to be reported on); board of directors' report on the state of the company; audited financial statements and the auditors opinion on them; additional information about the company;' a report on the effectiveness of internal controls, including whether in the opinion of the directors and management the controls are effective. *Quarterly reports* Quarterly reports must be filed within two months of the close of the relevant quarter. Requirements for the content of these reports are set out in Chapter D of the Securities Regulations (Periodic and Immediate Statements), 5730-1970 (the Reporting Regulations). A quarterly report must contain: interim financial statements for the last quarter and for the year to date prepared in accordance with accepted accounting principles for interim period financial statements (section 40, Reporting Regulations); a board of directors report for the interim period (section 38A); an interim internal controls report; and any significant change in the corporation's business (section 39A). *Material event disclosure* Chapter C of the Reporting Regulations sets out the requirements for the timing and content of immediate reports. An immediate report must be filed about any event or issue with a potential material impact on the corporation, including any event or issue that could have a significant impact on that corporation's securities prices (Reporting Regulations, Section 36). As well as this general obligation, an issuer must make an immediate report in circumstances specified in the Reporting Regulations, sections 31-37a3. These include major corporate events, such as a change in the corporation's issued capital; merger and acquisitions decisions, and so on. Under 30A of the Reporting Regulations, if the ISA becomes aware of information about an event not specified in Chapter C and the ISA considers knowledge about it is important to a reasonable investor considering the purchase or sale of the corporation's securities, the ISA may demand that

	the corporation submit an immediate report about the said event, within a period demanded by the ISA. *Shareholder voting decisions* Section 36B(a) of the Reporting Regulations requires an issuer to make an immediate report relating to the convening of any general meeting. The regulations require disclosure of: the type of the meeting; the date, place and time of the meeting; the agenda; for each item on the agenda, a description of the nature of the matter, stating the main facts required in order to understand properly every matter requiring a vote at the meeting, and it shall provide the text of every draft resolution or a brief description of its main points; the place and times when it is possible to inspect every draft resolution whose full text was not included in the details of the agenda; the type of resolution required for each of the matters on the agenda, if it is not an ordinary resolution; the date for the entitlement of the shareholders to participate and vote at the general meeting; if the agenda of the meeting includes matters on which it is possible to vote proxy, the preconditions for a valid proxy vote; the quorum for holding the meeting; if the agenda of the meeting included a proposal to appoint a person to a directorship in the corporation, details relating to the proposed director.. An immediate report under this regulation must be filed on the day when the date of the meeting and its agenda are decided on. Reports relating to meetings must include position notices and proxy forms that must be filed with the ISA under section 89 of the Companies Law and the regulations. Immediate reports must also be filed relating to the results of meetings, including details about resolutions passed and details of voting for resolutions requiring special majorities. *Listing of securities* The regulatory framework for listing securities is governed by TASE Rules and Regulations. TASE listing rules set out criteria for newly-listed companies and products. Listing criteria are articulated in the Second Part of the TASE Rules. The factors considered are: shareholders' equity after listing; the free float; minimum dispersion requirements; and in most cases, operating history. Specific rules apply to debt offerings, convertible securities offerings, the follow-on offerings of listed companies, ETNs, and dual listings. Special, more flexible, listing rules apply to early stage research and development companies. TASE also imposes free float and shareholders' equity maintenance requirements. If a company does not comply with the maintenance rules, the TASE notifies the company and grants it a six-month grace period to restore compliance. If compliance is not restored, the company may be transferred to a "maintenance list" and eventually be delisted. For example, the public-float rate in a new company (excluding research and development companies) must be no lower than:

When the public float value (in NIS millions) is greater than...	The public float rate (%) must be at least...
20	25.0
30	20.0
40	15.0
50	10.0
200	7.5

Source TASE website

Advertising

Securities can only be offered through an approved prospectus. Through a Staff Legal Bulletin, the ISA has indicated that, during the period in which marketing activities are permitted, the publication of information about offered securities, their price and their rating is prohibited, except for information designed to increase awareness of an open prospectus and which limits the information to the name of the offered security, the fact that that the published information is not an offering and a location where one can examine the prospectus.

Derivative markets

The derivative market in Israel is operated by the TASE, under the By-laws of MAOF Clearing House, Ltd., (MAOFCH) a wholly-owned subsidiary of the TASE. The derivatives are written by the clearing house, which serves as CCP for all derivative transactions.

Section 2 of the Seventh Part of the TASE Rules requires TASE members to make available a derivatives profile for inspection by any client carrying out a derivatives transaction for the first time. The TASE member needs to have the client sign that the Profile was made available to him, and to give the client a copy if requested to do so.

The Profile includes a general description of the conditions and provisions applicable to the derivatives (options and futures), their creation, holding, trading in them, and their exercise and expiration. The appendices include a description of the different kinds of derivatives. Detailed information must be contained in the Profile about terminology, MAOFCH, each derivatives contract, risk factors including market risks, taxation, how trading and clearing and settlement takes place, margin requirements and other matters.

Timeliness of disclosure and reports

Disclosure of information in prospectuses, listing documents, annual and other periodic reports, is of sufficient timeliness to be useful to investors for making their decisions based on such information in a way that allows the investors ample time to react to the new information.

Prospectuses.

The Securities Law requires that orders for offers made under a prospectus cannot only be made after at least five business days following the publication date of the prospectus and within forty five days from the date of publication (section 24 Securities Law; Securities Regulations (Period for Submitting Orders for Securities Offered According to Prospectus) 2005). If a supplement or amended prospectus is published, the date of publication is deemed to be the new date of the prospectus's publication. If information in a prospectus (including a shelf prospectus) changes or becomes outdated during the time an offer is open, an issuer must either publish an amendment to the prospectus as an immediate report, or an amended prospectus. In either case, a subscriber is entitled to cancel their orders and receive full reimbursement (section 26 Securities Law).

The prospectus must include annual financial statements as at a date that is no more than fourteen

	months prior to the date of the prospectus. If the date of the annual financial statements is more than five months earlier than the date of the prospectus, interim financial statements must also be included. (section 56 Prospectus Regulations). A prospectus of a reporting corporation must include either: the financial statements described above; or the financial statements included in its periodic report for the last year ending prior to the date on which the prospectus was submitted, as well as its interim financial statements and information about post-balance sheet date events which were reported after the date of the last periodic report (section 60B, Prospectus Regulations). These statements are signed close to the date of the prospectus. This re-signing requires the company to reconfirm the financial statements close to the date of the prospectus is to ensure (in accordance with the accounting rules) post-balance sheet date events are included in the audited financial statements that appear in the prospectus. When the audited financial statements included in a prospectus are outdated, additional financial statements and comparison data are required. In such cases, the most recent interim financial statements must also be included (section 56, Prospectus Regulations). *Annual and quarterly reports* An issuer's annual report must be submitted within three months of the end of its reporting year and the earlier of: fourteen days or more before the date set for convening the general meeting at which the corporation's financial statements are submitted; and within three days after the external auditor signed its opinion on the corporation's audited financial statements (section 7 Reporting Regulations). The report must include the corporation's annual financial statements as of the date on which the reporting year ended. Issuers' quarterly financial reports must be submitted within two months of the report date, and must be filed within three days of the date on which the corporation's auditor signed the review report relating to the interim financial statements (section 39 Reporting Regulations). *Immediate reports* Immediate reports must be filed: if the corporation first learns of an event before 9:30 on any trading day - no later than 13:00 on that day; if the corporation first learns of an event at another time – no later than 9:30 on the next trading day. Section 30A(B) of the Reporting Regulations. *Shareholders meetings* Reports about the convening of shareholder meetings and the results of them are required to be made as immediate reports. *Related Party Transactions* A company must disclose information about a related party transaction, its terms and the process of its approval, including the convening of the general meeting within fourteen days of the date of its approval by the board of directors. Such disclosure must be submitted to the ISA in a detailed report called a "Transaction Report". In addition, it must notify its shareholders and publish an announcement in at least two newspapers as detailed above and, upon request, must send the transaction report by registered mail to a shareholder.

	The company must file an immediate report about the results of the voting at the meeting within one trading day after a general meeting convened. See sections 2 and 13 Related Party Regulations. The ISA reviews these documents to check the adequacy of the disclosure, especially whether it contains all information for an informed decision on voting and to identify any corporate governance issues (by examining the reasons that led the issuer's board and audit committee to approve the transaction). *Private Placements* If a private placement allocates twenty percent or more of the voting rights in a company before the offering, the company must disclose information on the offering and the convening of a general meeting, if required, within fourteen days of the date of the offering. In addition, the issuer must notify its shareholders and publish an announcement in at least two newspapers and, upon request, send the transaction report by registered mail to shareholders. The company must file an immediate report regarding the results of the voting according to the timeline set for the filing of an immediate report on a material event. Sections 3, 22, 23 Private Placement Regulations. *Tender Offer* A tender offeror must file a specification document, which includes every detail known to it that may be important to a reasonable holder considering a response to a tender thereunder and the specification must not contain a misleading detail. The specification must be given to the ISA, TASE and the target company. No later than the first business day after the date of the specification, the offeror must publish a notice about the filing, in at least two widely distributed Hebrew language daily newspapers appearing in Israel. (Sections 5, 6, 20, Tender Offer Regulations.) The last date for acceptance must be a trading day no earlier than fourteen days from the date of the specification; for a special tender offer the date must be no earlier than twenty-one days, and no later than sixty days. **General disclosure obligation** *Public offerings* The Securities Law includes a specific provision which requires that every detail of importance to a reasonable investor must be included in the prospectus. This provision is in addition to the s the very detailed regulations made under the Securities Law with respect to prospectus disclosure. (Section 16(a), Securities Law) The issue of materiality has been tested in the courts and case law has determined that there must be substantial likelihood that, under all the circumstances, the disclosure of the (omitted) fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information available to the investor about whether to invest. *Immediate Reports* As well as an issuer's obligations to make an immediate report in specified circumstances, the ISA has a general power to require a corporation to file an immediate report regarding a certain event if it is of the opinion that information regarding such event is of importance to a reasonable investor considering a purchase or sale of the corporation's securities. (Section 36(e), Securities Law).

	Measures available to regulator The ISA has explicit power to demand additional information from any issuer, even if it is not an item specifically required by the legislation, if it deems that information to be material (Section 20 of the Securities Law). As well as powers to review and where necessary require correction of disclosure documents and reports, the ISA's powers of information gathering described under Principles 8 and 9 apply if it has a reasonable basis for suspecting a violation of a provisions involving potential criminal or administrative liability. *ISA prospectus review* For prospectus purposes, the ISA rates issuers on a red-amber-green basis and does reviews accordingly. Red lane prospectuses are subject to full review; amber lane prospectuses are subject to a partial review; and green lane prospectuses are subject to minimal review focusing on checking that procedural aspects of an offer are complied with. Issuers likely to be subject to full review normally give the ISA 60 days' notice of a proposed issue, while others give 20 days. All IPO prospectuses are subject to a full review. In the period January to November 2011, the ISA dealt with 161 prospectuses of which around 50 percent were subject to a full review. **Responsibility for information in regulated offer documents** For breaches of the disclosure and reporting obligations of issuers, the ISA has powers to: impose monetary sanctions; conduct administrative proceedings (under the new administrative enforcement legislation); initiate criminal investigations; contribute to the financing of class and derivative actions. Stakeholders can initiate private class and derivative actions, providing civil enforcement of the law. *Monetary Sanctions* Under section 52O of the Securities Law the ISA can impose monetary sanctions on any legal or natural person violating the Securities Law. These sanctions are available for a range of violations, including failures to comply with required disclosures and breaches of reporting obligations. *Administrative enforcement* Offences subject to administrative enforcement are set out in the Seventh Schedule to the Securities Law. They include failures to make timely disclosure or provide information; and breaches of disclosure content requirements, including by making misleading disclosures or omitting material information. *Criminal liability* The violation of some provisions of the Securities Law including disclosure provisions, may subject a person to criminal prosecution. Criminal liability is mainly imposed on the failure to file a full and accurate disclosure, while failure to file on a timely basis generally does not attract criminal liability. Violations that attract criminal sanctions include intentional inclusion of misleading information in a prospectus (Section 53(a)(1)); giving an opinion, report or certificate included or referred to in a prospectus, with prior consent, knowing that it contains misleading information(Section 53(3)); and intentionally causing a report or notice or registration document to contain a misleading item (Section 53(4)).

	Civil Liability The Securities Law imposes third party civil liability for misleading statements in a prospectus and other regulatory filings. Both individual and joint liability to injured parties applies. (Section 34 and 38C, Securities Law). For prospectuses , liability for damages caused by misleading information in a prospectus may attach to signatories to a prospectus (the issuer, a majority of the board and the underwriter if applicable) and anyone who was, on the date the board approved the final wording of the prospectus, a director, general manager or a controlling shareholder are liable for dam. These persons may be liable to anyone who purchased securities or sold them in either primary or secondary markets (section 31 of the Securities Law). In addition, any person who consented to provide an opinion, report, review or certificate included or mentioned in the prospectus bears liability for damages resulting from misleading information in the opinion, report, review or certificate issued by him (section 32). For periodic and current disclosures, the Securities Law establishes liability for misleading information in ongoing regulatory disclosures. Principal shareholders and senior corporate officers must inform the corporation about any information that requires the issuers to disclose in reports or notices submitted to the ISA (Section 37, Securities Law). A corporation, its director, CEO or a controlling shareholder are liable for disclosures in a report, notice or document that the corporation filed pursuant to the Law (Section 38C(1), Securities Law). Parties issuing an opinion, report, review or certification that was included or mentioned, with its consent, in a Report are liable for the content of these documents (Section 38C(2), Securities Law). Civil liability is also established under the Mutual Fund Law for disclosure violations in the prospectuses and filings of mutual funds. **Derogations** *Prospectuses and periodic reports* The ISA has the power to exempt issuers from disclosing any item in a prospectus if it is of the opinion that the preservation of a trade secret justifies the nondisclosure of the item, provided that the item in question is not one which, had it been included in the prospectus, would have deterred a reasonable investor from purchasing the offered securities (Section 19(a)(1), Securities law). It has similar powers with respect to a disclosure required in a periodic or immediate report, (section 36C(a), Securities law). The ISA may also exempt an offeror from disclosing information that is liable to damage the security or economy of the State, or any investigation conducted by the Israel Police or by the ISA (section 19(a)(2), Securities law). The Court may exempt a reporting corporation from disclosing such information in an ongoing report if it is of the opinion that these conditions have been met (Section 36C(b), Securities law). If an exemption has been granted, this must be stated in the prospectus or periodic or current report (as applicable). (Sections 19(c) Securities law, 36C(c) Securities Law, as applicable). In practice, these powers are rarely used. *Immediate report* Section 36 of the Reporting Regulations permits a corporation to delay disclosure regarding a matter or event reportable under the immediate reporting provisions if to disclose it may prevent the completion of an action or transaction to which the corporation is a party or in which it has an interest, or could significantly worsen the terms of such an action or transaction, provided that no information with regard to the event or matter has been made public by the corporation.

	An immediate report disclosing the event and the reason for the delay must be filed once the impediment is removed. *Suspension of trading* If a corporation does not comply with reporting timetable or content requirements, the ISA can suspend trading in the issuer's securities. (Section 38A of the Securities Law.) *Restrictions on trading by persons with superior information* The prohibition against insider trading applies to insiders and third party recipients of inside information. This includes inside information resulting from the issuance and reporting obligations of an issuer. **Cross border matters** The Securities Law includes a special dual listing regime (Chapter 5C of the Securities Law), which recognizes the regulation placed by a foreign authority on the issuer. These provisions provide that companies whose securities are traded on the NASDAQ, the New York Stock Exchange , the NYSE American Stock Exchange, or the London Stock Exchange Main Market Premier Listings, can dual-list their securities on TASE, The right to a dual listing has also been extended to French companies listed on an AMF-regulated markets. Issuers may rely on the same prospectus and regulatory disclosures filed abroad. To date there are round 50 dual listed companies, all having listings on US markets. Since these corporations are regulated by the foreign regulator, the ISA does not exercise its power at the same level of intensity as it does for corporations listed solely on TASE. This approach is based on recognition that the foreign disclosure regimes provide at least the level of protection as Israel's domestic laws. Israel's prospectus disclosure regime has been recognized by ESMA as being valid for prospectus registration under the requirements of the EU Prospective Directive, which incorporates IOSCO standards.
Assessment	Fully implemented
Comments	Though not a matter for formal assessment of this Principle, a comment should be made on underwriting in the Israeli market. Since 2005, shelf regulation is available for issuers who offer securities on a number of occasions during a two year period. Such offers may be made under a single shelf prospectus. See section 23A of the Securities Law and Securities Regulations (Shelf Registration of Securities) 2005. A number of market participants commented that the introduction of the shelf prospectus regime contributed to a decline in underwritten issues and that where an offer is underwritten it is on a "best endeavors" basis only. This means that the there are now fewer offerings where underwriters play an effective gatekeeper role and conduct thorough due diligence. Underwriters must be registered. Only a corporation can be registered and it and its directors are subject to fit and proper assessment that excludes only those who have been convicted of an offence. Under the existing Securities Law, prospectus liability only applies to underwriters if they underwrite in the economic sense. These underwriters have available a due diligence defense. "Best endeavors" underwriters are not liable, for example for misleading statements in a prospectus - that is, under the current law they have less incentive to carry out due diligence in the offering process. *Proposals* Two proposals are in train:

	a. Increase the fit and proper standards for underwriters by making them subject to broader scrutiny at the time of registration. Under the proposal, an underwriting company, its directors and controlling shareholder would be subject to the broader tests that apply for other financial sector intermediaries (under the standards jointly adopted by the ISA, BOI and CMISD). The proposal is at advanced stage and is before the Knesset. An amendment to the Securities Law that would make all underwriters subject to liability for misleading or defective statements in a prospectus, again with a due diligence defense available. This would apply to best endeavors underwriters acting as distributors in the offering process. In addition the amendment will impose a mandatory duty to engage with an underwriter in every offering. Even if the company did not hire a distributor it will be forced to hire at least one underwriter that will undertake the due diligence duty. The amendment will also give the ISA the authority to inspect underwriting services and publish it views as to the quality of the due diligence service. This proposal is at earlier stage: the ISA has done a public consultation and comments closed on 15 November 2011. The next stage is for the ISA to review comments and begin drafting proposed legislation. If the second proposal becomes law, the ISA plans to conduct reviews of the underwriters' due diligence processes and publish the high level results of these reviews. The second proposal will create strong incentives (under threat of liability) for all underwriters to undertake thorough due diligence. This seems to be why it is not a popular proposal.
Principle 15.	**Holders of securities in a company should be treated in a fair and equitable manner.**
Description	**Rights and equitable treatment of shareholders** A range of provisions in the Companies Law and the Securities law are aimed at ensuring the rights and equitable treatment of holders of shares that are listed for trading on a stock exchange, or have been offered to the public pursuant to a prospectus. Some provisions also apply to holders of bonds in "bond companies" (that is, companies whose bonds are listed for trading on a stock exchange, or have been offered to the public pursuant to a prospectus as defined in the Securities Law, and are held by the public). *Voting* Section 46B of the Securities Law requires a company whose shares are listed for trading to have capital consisting of one class of shares only, conferring equal voting on a one share one vote basis. *Elections of directors* Directors are appointed by the annual general meeting, unless otherwise stated in a company's by-laws (section 59 of the Companies Law). Public companies must have at least two external (outside) directors (section 239 of the Companies Law). A special majority provision applies for the appointment of external directors. The nomination of external directors requires the support of a majority of shareholders who are neither controlling shareholders nor related to them. (Section 275 of the Companies Law). These arrangements are designed to minimize the influence controlling shareholders[6] have on the appointment of external directors.

[6] A controlling shareholder is a person who holds twenty-five percent or more of the voting rights in the general meeting of the company if there is no other person who holds more than fifty percent of the voting rights in the company – section 268 of the Companies Law.

	Fundamental corporate changes An amendment of the company's by-laws must be approved by a general meeting of shareholders. (Sections 20 and 57 of the Companies Law). *Changes to the registered share capital* The general meeting has the power to increase or decrease registered share capital, subject to the provisions of the law. The company may not stipulate alternative provisions regarding this matter (Sections 57-58). *Related party transactions* Some 45 percent of the equity in Israeli public companies is held by "principal shareholders" – shareholders who hold more than 5 percent or more of the equity. In practice many companies have controlling shareholders who own more than 25 percent of equity. This makes related party transactions a significant issue both for institutional and retail shareholders, and for the regulatory regime. Considerable efforts have been made to ensure that transactions involving a controlling shareholder and a public company do not detract from rights of minority shareholders. Chapters 5 and 6 of the Companies Law deal with related party transactions. These are transactions between a company and a controlling shareholder or an office holder of the company or transactions in which a controlling person or an officer has a personal interest. Related party transactions with controlling shareholders in public companies require the approval of the audit committee, the board of directors and the general meeting. Special majority provisions require that one of the following holds: the majority voting in favor of the transaction must include a majority of the votes of the shareholders who do not have a personal interest in the approval of the transaction and are present and voting at the meeting; the total number of opposing votes does not exceed 2 percent of the total voting rights in the company. (Section 275). Related party transactions with controlling shareholders in bond companies require the approval of the company's audit committee and board. *Notice of general meeting* Section 2 of the Companies Regulations (Notification of a General Meeting and a Class Meeting in a Public Company) – 2000 provides that a notice of the convening of the meeting is to be published 21 days prior to the date of the general meeting. The notice must be published in two widely distributed daily newspapers and on the company's website, if such applicable. In addition, the company is required to notify all shareholders on the company's register of the general meeting at least 21 days prior to the date of the meeting, unless otherwise stated in the company's the by-laws. Where the bylaws state that no notification to the shareholders is required, the notice must be published 14 days prior to the date of the meeting. A notice convening a meeting on the agenda of which are matters requiring the company to enable proxy voting, must be published 35 days prior to the date of the meeting. (Section 2, 3 of the Companies Regulations (Notification of a General Meeting and a Class Meeting in a Public Company) – 2000). The Securities Law also mandates that companies file an immediate report notifying the public of the meeting and posting its agenda and the resolutions placed before the shareholders. The details that

	must be included in the immediate report are stipulated in Regulation 36b of the Reporting Regulations and include the type of meeting; the date and location; a description of the topics on the agenda; the type of resolution required for each of the matters, etc. *Voting at the general meeting* Public companies must allow remote voting at general meetings (section 87 of the Companies Law). Proxy voting must be available to shareholders as an option where the agenda for a general meeting includes any of the issues listed in Sections 87-89 of the Companies Law, which include the appointment or removal of directors, approval of a merger and approval of related party transactions. Shareholders may request that the company sends position statements to other shareholders of the company regarding these issues. Prior to the opening of a securities account, TASE members must inquire of each shareholder about how he wishes to receive ballot papers and position statements, with regard to all the securities in the account. They must also distribute ballot papers to their clients prior to the meeting. The Companies Law Regulations (Proxy Voting and Position Statement)- 2005 (hereinafter: Proxy Regulations) specify the format and manner the proxy ballot must take. *Ownership registration and the transfer of shares:* A company must keep a register of shareholders. A public company must keep a register of principal shareholders in addition to the standard register of shareholders. These registers are open to the public for inspection. (Companies Law, sections 127 to 130) A company whose shares are listed solely on a stock exchange in Israel must register a nominee company in its shareholders registry as the owner of record. The nominee company holds and administers securities or other assets as the registered owner on behalf of the beneficial owner. A nominee company is not considered a shareholder and the shares registered in its name are beneficially owned by those who are entitled to them. (Section 132 of the Companies Law). The Companies Law states that a shareholder who is registered in the shareholders register is entitled to receive a certificate from the company certifying the shareholder's ownership of their share. The law also states that a nominee company is entitled to receive a certificate from the company attesting to the number of shares and type of shares registered in its name in the shareholders register (Section 178). A shareholder in a public company who wishes to vote at a general meeting has an unconditional right to receive confirmation of share ownership from the stock exchange member through whom his share is held (Companies Law Regulations (Proof of Securities Ownership for Purposes of Voting at General Meetings) -2000, Section 1). *Receipt of dividends:* Under the Companies Law, every shareholder is entitled to receive a dividend, in accordance with the rights attached to each share if a resolution about dividend distribution has been passed. The shareholders who are entitled to dividends are those holding shares on the date of the resolution or on a later date as prescribed in the resolution. (Sections 190 and 306). **Takeover bids and changes of control** In general, Israeli law restricts the acquisition of shares if, as a result the purchaser becomes entitled to 25 percent or 45 percent share of issued shares (provided no other shareholder in the company holds these amounts). Such acquisitions are regulated as takeovers or other changes of control.

	In practice, takeovers (involving the creation of a new controlling shareholder) are less common than transactions that involve taking a company private. For example, in 2010 there were 2 takeovers (8 in 2009), and 18 going-private transactions (31 in 2009). *"Special" Tender Offers* By section 328 of the Companies Law, a purchase of shares in a public company that result in a person becoming the holder of a control block of more than 25 percent of voting rights (if there is no such holder in the company) requires the purchaser to make a tender offer in accordance with the provisions of Chapter 2 of Part VIII of the Companies Law. These offers are "special tender offers". The same applies to purchases that increase the purchaser's holdings above forty-five percent of the voting rights in the company (if there is no other person holding more than one-half of the voting rights). A special tender offer must be made to all shareholders, who can give notice as to their consent or objection to the offer. A special tender offer can only be accepted by a majority of the votes of those shareholders who give notice. When votes are counted, the votes cast by a holder of control in the offeror or a holder of a controlling block, are excluded. Where a special tender offer has been accepted, offerees who did not given notice of their position, or who had objected to it, have the option of accepting the offer, no more than four days following the last day of acceptance (section 331). *Taking a Company Private* Shareholders seeking to hold interest of more than 90 percent must undertake a "full tender" offer to acquire the remaining outstanding shares. If after the tender, the holdings of the shareholders who rejected the offer is less than five percent of the issued share capital and more than half of the shareholders who have no personal interest in the offer have accepted it, all the shares tendered in the offer must be transferred to the acquiring company, which becomes a private company. (Sections 336, 337 and 339of the Companies Law). Under Section 56(d)(1) of the Securities Law, all tenders relating to listed companies , including "ordinary" tender offers[7] initiated voluntarily by the offeror, are subject to the filing of a tender specifications document and must provide shareholders equal opportunity to sell their holdings at the offering price. See Securities Law Regulations (Purchase Offer)-2000 (the Tender Offer Regulations) *Private Placements* Private placements which result in the creation of a new controlling shareholder of the company are permitted only if a shareholders meeting has given its approved. (Section 328(b)(1) of the Companies Law.) *Mergers* Where all a target company's assets and liabilities are transferred to an acquiring company and as a result of which the target company is liquidated, the Companies Law provides that the merger requires the approval of the board of directors and of the general meeting of each of the merging companies (section 320 Companies Law). Notwithstanding the required approval of a merger by the general meeting, voting rights belonging to the other merging company or to an entity holding at least twenty five percent of the controlling

[7] An ordinary tender offer is a public offer made to equity holders which is not a special tender offer or a full tender**.**

	shares in that company are not taken into account if a majority of all the other shareholders opposes the merger (Section 320(c)). Mergers with a controlling shareholder or a company controlled by it, or in which the controlling shareholder has a personal interest, are also subject to a special resolution (section 275). *Holding the company and its directors responsible in case of violations of law* Directors owe a duty of care (section 252 of the Companies Law) and a duty of trust (section 254) to the company, and are required to act in good faith and for the company's benefit. Under these duties a director must refrain from any act involving a conflict of interest and must disclose to the company all the relevant information which he or she has obtained as a result of his position within the company. Breaches of fiduciary duties are civilly enforceable. Private and class action suits against the corporation or against the directors for such breaches are possible. Similarly derivative actions taken on behalf of the company against an offender is possible. The ISA is authorized to provide financial assistance for class and derivative actions. If a violation involves disclosure requirements under the Securities Law, the company and its directors may be liable under civil law to stakeholders (section 31 of the Securities Law, with respect to a prospectus and section 38 with respect to other disclosures). Directors and senior management are exposed to administrative or criminal prosecution for direct or indirect violations of disclosure requirements. Section 53(e) of the Securities Law states that where an offence is committed by a corporation, the directors and the general manager of the corporation are criminally liable as well, unless they can establish defenses provided in the law. In Israel, a criminal ruling may serve as evidence in a civil action, and therefore may facilitate shareholders in enforcing their rights under the Companies Law. *Bankruptcy or insolvency of the company* Section 350 states that where a compromise or debt restructuring arrangement is proposed between a company and its creditors or shareholders, or between a company and any particular class of creditors or shareholders, the company, a creditor, a shareholder or the liquidator (if there is one) can apply to the court to order the convening of a meeting of debt or shareholders. If the majority of the persons present and voting at the meeting, collectively holding 75 percent of the value represented at the vote, agree to the compromise or arrangement, and the court approves it, a compromise or arrangement is binding on the company and all the creditors, shareholders or any class of them (as the case may be), and on the liquidator. A settlement under section 350 of the Companies Law requires that an immediate report be submitted by the Company to the ISA, including details on the main points of the restructuring program, the grant of an order suspending proceedings or an order transferring assets, as applicable, the appointment of a corporate official by the court, and the powers held by the appointed party; a decision concerning the convening of creditors' or shareholders' meetings, and the results of the meeting, and the court's rulings. (Section 31H of the Reporting Regulations).] **Disclosure to shareholders** *Investment decision* Section 16 of the Securities Law requires a prospectus to contain every detail of importance to a reasonable investor considering the purchase of the securities offered therein. Section 36 of the Securities Law and regulations under it establish the reporting requirement for public companies. In particular, Section 36 of the Reporting Regulations is a general requirement to

	file an "immediate report" with respect to any event or matter which could have a significant impact on the corporation or which could significantly affect the price of the corporation's securities. *Voting decisions,* Under Reporting Regulation 36B, when a shareholders meeting is convened, the corporation must submit an immediate report containing details of the meeting and its agenda. **Changes of corporate control transactions** With regards to tender offers, the offeror must provide shareholders with all the information it has available which could influence the shareholder's decision about the proposed offer (Regulation 9 of Tender Offer Regulations). The Tender Offer Regulations specify the time shareholders are given in which to consider proposals relating to a takeover bid and submit acceptance notices. Under Regulation 6, the last acceptance date must be no earlier than 14 days and no later than 60 days from the date of the filing of the tender specification document. In the case of a special tender offer, the last acceptance date is fixed no earlier than 21 days and no later than 60 days from this date. The Tender Offer Regulations set out a detailed a list of disclosure requirements with which an offeror company must comply. On the basis of the information given to them, Shareholders have adequate information to enable them to assess the merits of the proposal. In general, the offeror must provide shareholders with all the information it has available which could influence the shareholder's decision with regards to the offer proposed (Regulation 9). In tender offers, an offer must be made to all shareholders on equal terms. The purchase offer can only be accepted through a member of the stock exchange, which ensures the execution of the offeror's undertakings. (Regulation 5). If a special tender offer is made, the board of the target company must provide its opinion on the offer. If they cannot provide an opinion, then this must be stated together with an explanation as to why they were unable to do so. If any of members of the board of directors have any personal interests arising from the special tender offer, this must be disclosed (section 329 of the Companies Law). Actions by an officer of a target company to frustrate an existing or anticipated special tender offer, or to reduce the chances of its being accepted, make him or her liable to the offeror and the offerees for any damage resulting from his/her actions, unless he or she acted in good faith and had reasonable grounds for presuming that the actions done were for the good of the company. However, an officer may negotiate with an offeror to improve the conditions of the offer, and may negotiate with others to make a counter-offer. (Section 330 of the Companies Law). The Tender Offer Regulations also impose specific responsibilities on directors in circumstances where a special tender offer is made (regulation 21). A merger requires the approval of the general meeting of each of the merging companies. Notwithstanding the required approval of a merger by the general meeting, voting rights of the other merging company or to a person holding at least 25 percent of the shares in it are not taken into account if a majority of all the other shareholders opposes the merger (Section 320(c) of the Companies Law). *Debt restructuring* For debt restructuring compromises or arrangements, section 350 of the Companies Law is designed to safeguard the fair and equal treatment of shareholders and bondholders, particularly minority stakeholders. Any compromise or debt restructuring arrangement between a company and its creditors or

	shareholders binds the company and all the creditors, shareholders and the liquidator only if the majority of the shareholders present and voting at the meeting, collectively holding 75 percent of the value represented at the vote, agree to the compromise or arrangement. Information about the meeting must meet the standards described above. The vote is held in several groups according to the classes of securities in questions. Shareholders and debtholders may also be separated into difference classes if conflicting interests exist, and may also be separated to difference classes due to conflicting interests. An arrangement is also subject to court approval. **Substantial holdings of voting securities** Disclosure requirements about substantial beneficial ownership relate to "principal shareholders" as defined in Section 1 of the Securities Law: a person holding 5 percent or more of the issued share capital of the corporation or of the voting power therein, a person entitled to appoint one or more of the directors of the corporation or its general manager; a corporation in which such a person holds 25 percent or more of its issued share capital or of the voting rights, or is entitled to appoint at least 25 percent of its directors. The CEO and board members, regardless of their shareholdings. To enable the company to fulfill its disclosure obligations, principal shareholders must notify the company about the event that triggered its status as a principal shareholder, current changes in holdings, and the fact that the person ceased to be a principal shareholder (section 37 of the Securities Law). Under the Securities Law Regulations (Details, Structure and Form of Prospectus and Draft Prospectus) - 1969 (the Prospectus Regulations), companies must disclose in their prospectuses the amount of shares that each principal shareholder holds in the issuer and the nominal value of shares in the issuer that it has agreed to purchase or that the issuer has agreed to sell to it. (Regulation 28). The Reporting Regulations set out the disclosure requirements triggered by transactions involving principal shareholders: Under Regulation 33(c), the corporation must file, once a week, a report containing details of the principal shareholders and of their holdings in the corporation's securities (a status report) as of the end of the last trading day of the previous week. This applies only in cases in which there is a change in these holdings since the previous status report. The status report must include specified information for each principal shareholder. In their annual reports, companies must provide details of the shares and convertible shares held by each principal shareholder in the company, including the name of each principal shareholder; the percentage of the corporation's shares and of each class of the corporation's convertible securities held by principal shareholders; and the nominal value of shares in the company that the shareholder agreed to purchase or that the company agreed to sell to it. Details must be provided about the shares and convertible securities that each principal shareholder holds in each subsidiary or affiliate of the corporation on the date of the report or on a date as close to that date as possible (Reporting Regulation 24). If a change has occurred in the holdings of a principal shareholder, an immediate report must be filed, providing details of the (Regulation 33(a)). If two or more persons hold securities under a collaborative agreement (whether written or oral), they are deemed to jointly hold the securities. Under Section 1 of the Securities Law, all disclosure requirements apply to these persons.

	The main tool which assures compliance and enforcement of the principal shareholder disclosure requirement is the legal duty of the principal shareholder to inform the company of the fact that he/ she/it has reached the applicable threshold, and of any changes in his/her/its holdings thereafter (Section 37 of the Securities Law). The failure to report such information to the company bears administrative and criminal liability (chapter 8c and Section 53 of the Securities Law respectively). A company who failed to disclose principal shareholders related disclosure is also exposed to administrative and criminal liability. **Holdings of voting securities by directors and senior management** Under section 24(e) of the Reporting Regulations, the corporation and any of its senior officers who hold the corporation' securities are deemed to be principal shareholders and are therefore subject to the requirements described above. Section 55 to the Prospectus Regulations also provides that details of shares and options that a principal shareholder or a senior corporate officer holds in the issuer, in any subsidiary or in any related company, be disclosed to the best ability of the issuer or his directors. **Cross border** In general, a company incorporated outside of Israel is not subject to the Israeli Companies Law. Foreign companies whose securities are offered to the public in Israel are subject to the provisions of the Companies Law and regulations listed in the Fourth Schedule of the Securities Law. These include provisions pertaining to: general meetings; chairman of the board and CEO; audit committee; internal auditor; the right of a shareholder to inspect and receive information; class and derivative actions; external directors; duties of corporate officers; related-party transactions; and tender offers. The ISA can exempt the corporation from all or part of such provisions and regulations if it is convinced that a foreign law applicable to the company sufficiently ensures the interests of the investing public in Israel. The ISA must inform the company of such an exemption (if it applies) when issuing the permit to publish the prospectus - section 39A of the Securities Law. As part of its authority to demand any information relevant to a reasonable investor, the ISA requires foreign issuers, to submit a comparison between the Israeli law requirements and the foreign law requirements, in relevant matters such as rules of incorporation; purchase of own shares; dividends distribution; rights of shareholders and so on in their prospectus. Under Section 61 of the Securities Prospectus Regulations, the ISA requires foreign issuers to submit opinions of an Israeli and foreign attorney confirming that the rights attached to the securities being offered are described accurately, that the issuer has the authority to issue the securities in the manner in which they are being offered, and other relevant legal matters. *Dual-listing regime* Dual listed entities can make offers and list on TASE under the foreign prospectus and a registration document. The prospectus is filed with the ISA but is neither vetted nor approved by it.

	If the ISA requests it, the foreign company must submit an explanation to the ISA about any detail, information or document pertaining to an item included in its registration document. The ISA may make enquiries with the relevant regulator responsible for supervising the company without referring to the company itself. It may also order the company to submit an immediate report amending the registration document (Section 35X). For the purpose of meeting the Israeli disclosure requirements, the Securities Law permits dual listed companies to comply to foreign ongoing disclosure requirements as well. Accordingly, the company is subject to a single set of disclosure requirements which satisfy the regulation in both markets. The key requirement is that the same securities are traded on both the foreign exchange and the Israeli exchange.
Assessment	Fully implemented.
Comments	
Principle 16.	**Accounting and auditing standards should be of a high and internationally acceptable quality.**
Description	**Audited financial statements** Section 56 of the Prospectus Regulations provides that a prospectus for an initial public offering should include annual financial statements of the issuer, which have been properly audited and prepared. Section 9 of the Reporting Regulations provides that annuals report must include audited annual financial statements by an independent outside auditor. The reports should also include the opinion of the auditor regarding the audited financial statements. Section 43 of the Securities Law also provides that if all or most of the proceeds from an offer of securities are designated for investment in a company that is or will become a subsidiary, the subsidiary's last audited financial statements must be included. Financial statements must be prepared in accordance with IFRS and therefore must include: a balance sheet or statement of financial position a statement of the results of operations a statement of cash flow a statement of changes in ownership equity or comparable information included elsewhere in the audited financial statements or footnotes. Financial statements are comprehensive, understandable by investors (to the extent compliance with IFRS requirements permits this); and comparable if more than one accounting period is presented. Financial statements are filed electronically in xBRL, in a standard format that makes them accessible, including to non-Hebrew speakers. *Review of compliance with accounting standards* The ISA reviews financial statement to ensure compliance with accounting standards. Around 160 companies financial statements are reviewed each year and more than 50 companies are subject to a more intensive review. The ISA aims to review all issuing companies over a four year cycle. Of the 40 professional staff in the Corporate Finance Department, round 30 have accountancy qualifications. Where the ISA disputes the accounting treatment in a financial statement, this commonly leads to a restatement by the issuer. The results of the ISA's enforcement activities with respect to financial statements are published.

	The ISA participates in the IOSCO Forum for the Implementation and Enforcement of IFRS. **Accounting standards** Since January 1, 2008, Israeli listed corporations are obligated to prepare their financial statements in accordance with IFRS. This obligation was set by the Israel Accounting Standards Board (IsASB), which published Accounting Standard 29 in July 2006, mandating the adoption of IFRS by January 2008 for all corporations that are subject to the Securities Law – 1968. This obligation was later incorporated into the Securities Regulations (Annual Financial Reports) 2010. Israel decided to adopt IFRS in full without any carve–outs and without undergoing an endorsement process prior to accepting new standards or interpretations published by the International Accounting Standard Board (IASB). When IFRS was made mandatory for public companies in 2008, banks and insurance companies were exempt from immediate transition. Over time, the Commissioner of Capital Market Division, adopted the IFRS with regards to insurance companies. However, accounting rules for banking institutions are set by the Supervisor of Banks. These standards are unique, and based on a combination of US GAAP, IFRS and standards set by the Supervisor of Banks. **Auditing standards** The Israeli Law does not define the term "properly audited". However, Section 24 of the CPA Law Regulations (Mode of Performance)-1973 (the CPA Conduct Regulations) provides that acting according to any standard or directive established by the Institute of Certified Public Accountants in Israel (ICPAS) is considered as acting according to an accepted auditing standards, unless proven otherwise. In practice, responsibility for developing and setting auditing standards rests with a non-government professional body, the ICPAS. It does so through a Committee for Auditing Standards and Auditing Procedures and its Professional Council. The standards deal with issues such as auditor's report, risk assessment, internal control, audit fair value measurement, audit materiality, audit evidence, and documentation. The auditing standards are published on the ICPAS website. In addition, they are published in printed editions, which include the auditing standards as well as interpretations and clarifications relating to these standards. The ICPAS is progressively translating and adopting the international ISA standards, but this process is not yet complete so full congruence with international standards has not yet been achieved. To address inefficiencies in the current regulatory framework, the ISA is working to establish an independent, non-profit statutory body to exercise regular oversight of the development and implementation of auditing standards, auditor independence, and ethical conduct. The proposed body would register accounting firms and keep a central register. Firms not included in the register may not audit or take part in the audit of reporting corporations set auditing standards carry out inspections and investigations, and enforce compliance by the imposition of sanctions be responsible for supervising accounting firms that carry out auditing of reporting corporations and oversee the audit process applied carry out reviews and to transfer any information it discovers in the auditing of financial statements to the ISA that relates to criminal violations of the law, or to the auditor's freedom of occupation. **Auditor independence** The Companies Law requires that all companies incorporated in Israel appoint an external auditor,

	who must be directly and indirectly independent from the company (Sections 154 and 160). Under section 10 of the Certified Public Accountants Law- 1955 (the CPA Law) CPAs are prohibited from engaging in any activity which may engender conflicts of interest between their activities as an auditor and their other activities, or which may impair their independence as auditors. Auditor must be directly and indirectly independent of the audited entity, and must maintain independence during their professional work (Section 2 of the CPA Conduct Regulations). The CPA Law Regulations (Conflict of Interests and Impairment of Independence Resulting from Outside Activity)- 2008 (the Auditor Independence Regulations) specify circumstances in which an auditor is presumed to be involved in a conflict of interest situation (a presumption which may be contradicted) as well as the disclosure requirements imposed on auditors. An auditor acting contrary to these regulations may be subject to disciplinary sanctions imposed by the Auditors Council (as defined in the CPA Law). The CPA Law and Regulations apply to all auditors, including but not limited to auditors providing services to reporting companies. The Auditor Independence Regulations supplement and do not derogate from any other law or regulation. In addition to the abovementioned regulation that applies to all auditors, there is a specific set of rules which relate to the independence and conflicts of interest among auditors of reporting companies. Israeli Securities Law and its regulations require that annual and quarterly financial statements must be audited or reviewed (respectively) by an independent auditor. Section 9 of the Reporting Regulations requires that financial statements be duly audited in accordance with the law. By virtue of the requirements in section 9, the ISA has the power to examine whether accountants meet auditing standards and may disqualify financial statements if the auditing process does not meet proper auditing practice. In cases where the ISA finds that financial statements are not properly audited, it can require these statements to be re-submitted and re-audited either by the same or by a different auditor. The ISA directly addressed the issue of auditor independence in a decision issued in August 1992 (the ISA Independence Guidelines), which clarifies its position and expectations. These guidelines were issued prior to the 2008 Auditor Independence Regulations, and were issued because, at that time, section 2 of the CPA Conduct Regulations did not specify what auditor independence actually entailed. The Independence Guidelines state that an external auditor must not be directly or indirectly dependent on the audited entity and must maintain strict independence when auditing financial statements that are submitted to the ISA. Auditor independence must be evident not only in practice but also in appearance. Financial statements which do not comply with the required standards of independence are not considered to have been audited in accordance with the law and are treated by the ISA as non-compliant with the requirements in the Securities Law and its regulations. If after one month from the time the company fails to submit duly audited financial statements, trading in the company's securities is suspended. The ISA has issued clarifications regarding the ISA Independence Guidelines. Two sets of norms (the CPA Law Regulations and the ISA Independence Guidelines) apply to the auditors of reporting companies, inconsistencies may arise. In such cases, the stricter provisions prevail, as they reflect higher standards of independence. Auditor independence is addressed both from the standpoint of corporate governance and from the standpoint of regulation of the accounting industry. A breach in auditor independence can serve as ground for ISA rejection of a public company's regulatory filings. **Use of unaudited financial statements** Interim (quarterly) financial statements must be prepared and presented in accordance with IFRS

	requirements. The need not be audited, though they must be accompanied by an audit review. (Companies Law, Section 154). **Oversight, interpretation and independence** The ICPAS publishes clarifications and interpretations of the standards. Interpretations (as well as the standards) are published on the ICPAS website and in printed editions. Prior to the issuance of a new standard, the ICPAS transfers the text of the proposed standard for ISA comments and disseminates an exposure draft for public comments on its website. The comments are examined by the ICPAS and integrated into the standard insofar as necessary. ISA's comments are usually accepted. The ICPAS is an independent body not directly supervised by the ISA. Nonetheless, in relevant circumstances, where the ISA identifies material deficiencies, it may intervene, usually by requesting that ICPAS seek a joint relevant solution. Such intervention has occurred in the past, in the case of an audit standard relating to "reliance on the opinion of other auditors". In accordance with ISA's initiative, and following joint discussions, ICPAS published a clarification to the relevant standard.
Assessment	Fully implemented
Comments	The current arrangements meet the standards of this Principle. It should be noted, however that the audit standard setting process, and the supervision of auditors may not fully comply with the new IOSCO standards (see also Appendix 1).
Principles for Collective Investment Schemes	
Principle 17.	**The regulatory system should set standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme.**
Description	In Israel, collective investment schemes are referred to as mutual funds or managed funds. Investment in mutual funds accounts for approximately 6.2 percent of the public's total savings (Bank of Israel 2010 Annual Report). Although the legislative framework provides for closed end funds, there are none currently operating in the Israeli market. Proposals are currently being developed to bring the regulation of exchange traded notes (ETNs) under the Mutual Funds Law, rather than (as currently) the Securities Law. Issuers of ETNs will be subject to a more extensive regulatory regime analogous to that applying to fund managers. It is anticipated these regulations will be completed in 2012**.** The proposed regulation will also make some changes to the law as it applies to mutual funds generally. **Regulatory framework - authorization** The basic definition of a mutual fund is set out in section 2 of the Mutual Funds Law. A mutual fund subject to the Mutual Fund Law and related regulations is an arrangement or scheme that meets the following conditions: it is an arrangement the purpose of which is a joint investment in securities and joint profit-making from the holding of such securities and from any transaction involving them and is not regulated by any other law; the number of participants (unit holders) exceeds fifty or there was an offer to the public of the fund units. Under Israeli law, each fund must have a fund manager and a trustee. The fund manager plays the main role in managing, but the trustee has responsibility for overseeing the actions of the fund manager and its mandated activities go beyond mere holding of fund assets in trust for unit holders. The trustee's role in supervising the fund manager is set out in s78 of the Mutual Fund Law.

	Marketing a CIS The marketing and distribution to investors of fund units may only be carried out by a licensed investment adviser or marketer, or a licensed portfolio manager. A CIS operator is prohibited from marketing or distributing units of its own (or any other) funds. *Operating a CIS* The two entities involved in the overall management of a fund, the fund manager and the trustee, are each required to be authorized by the ISA. See section 13(a) of the Mutual Fund Law (fund managers) and section 9(a) (trustees). The Mutual Funds Law (section 13(a)(1)) states that the sole occupation of a fund manager must be fund management. It may not engage in other activities and therefore may not hold an investment adviser or portfolio manager license. **Eligibility criteria** The Mutual Fund Law sets out eligibility standards for both fund managers and trustees. *Fit and proper test (reliability)* Fund managers and trustees are subject to fit and proper criteria in the form of a "reliability" test. Under sections 9(a1) (trustees) and s13(a1) (fund managers) of the Mutual Fund Law, the ISA may refuse to issue a license if it has concerns about the reliability of an applicant company, its controlling shareholders[8], a corporate officer or (in the case of fund managers) a person who will participate in decision making in relation to a fund managed by the applicant. The ISA has published a detail list of what will amount to a concern about reliability (List of Circumstances for Evaluating a Deficiency in the Fitness of Entities Supervised by the Authority). See also sections 9A and 23B1 of the Mutual Fund Law. The ISA, the Bank of Israel Supervision of Banks Department and the Ministry of Finance Capital Market, Insurance, and Savings Division in December 2010 published criteria that each of the regulators will use in examining reliability, to ensure a uniform application of this test across the regulated financial sector. As it is required to do by section 23D(b) of the Mutual Fund Law, ISA is currently consulting on proposed additional guidance about the circumstances to be taken into account in assessing reliability of entities supervised by ISA. Controlling shareholders of mutual fund management companies must also be ISA approved under the Mutual Funds Law and the standards of reliability also apply to them (section 23B). *Fund managers* In addition to criteria relating to reliability, applicants for a funds manager's license must meet criteria relating to competence and financial capacity. *Competence*: Requirements regarding competence of key staff are set out in the Joint Investment Trust (Equity and Insurance of the Fund Manager and Trustee and Criteria for Suitability of Directors and Members of the Investment Committee) Regulations, -1995 (MF Equity, Insurance and Suitability Regulations).

[8] A shareholder of a fund manager is a controlling shareholder if a fund manager if they hold of more than 30 percent of the company – section 23B(a).

	For fund managers, at least one third of the Board and two thirds of the investment committee must have "professional experience" in the investment field. An individual has relevant professional experience if they have worked in at least one of the following: the management of investment portfolios; the provision of investment advice (as defined in the Investment Advice Law); the analysis of investment portfolios; or the analysis of investments. In certain circumstances, educational qualifications may replace the professional expertise or may be combined with it. *Financial capacity*: Financial capacity is determined by a combination of capital requirements and insurance requirements (Mutual Funds Law, Sections 9(a)(2) and (3) and 13(a)(2)). Minimum equity requirements for a fund manager are set out in the Managed Funds Equity, Insurance and Suitability Regulations. The amount was originally set (in 1995) at NIS 500,000 linked to the CPI. The current amount is NIS 900,000. Insurance requirements for fund managers are set out in the MF Equity, Insurance and Suitability Regulations. Professional liability insurance must be taken out as well as insurance against breach of trust by staff and by those taking part in the decision making process regarding fund management. The Mutual Fund Law permits fund managers to substitute insurance with bank guarantees (issued in favor of the unit holders), short term cash deposits or State of Israel bonds. (Equity, Insurance and Suitability Regulations Sections 7 and 8). *Powers and duties*: The powers and duties of the operator are set out in detail in the Mutual Fund Law and regulations, but they are not assessed as part of the initial licensing process or criteria for eligibility *Internal management procedures*: The ISA does not have the power to assess an applicant's systems and processes at the time of assessing the application. Proposed amendments to the Mutual Fund law will permit the ISA to assess an applicant's systems and processes at the time the application for a license is being assessed, and require a trustee to demonstrate they have the means to supervise fund manager activity effectively at the time of an application for a license. However, the trustee must ascertain that a fund manager is compliant at all times, including when commencing operations for the first time, and this assessment includes control systems, operations and procedures, and a prospectus for a new fund offered by a fund manager requires disclosure of internal systems and controls. In practice, the ISA examines the internal systems and controls of applicants for authorization as a trustee at the time of the application. *Trustees* Section 9(a) of the Mutual Fund Law sets out the criteria to be met by applicants for authorization as a trustee. To qualify for authorization , an applicant must: Be one of the following: a banking corporation within the meaning of this term in the Banking Law, excluding a joint service company; an insurer, as defined in the Insurance Business (Control) Law, 1981; a company whose main occupation is carrying out trust functions; [9]

[9] Currently there are 6 authorized trustees, 3 subsidiaries of banks and 3 specialist trust companies.

	Have equity, in addition to the equity required by law because of its other occupations, in an amount not less than an amount prescribed by the Minister of Finance in regulations. The current equity requirement is NIS 900,000, but will be increased as part of the amendments to the Mutual Fund Law; Have insurance, a bank guarantee, a deposit or securities in the amounts, percentages and subject to conditions prescribed by the Minister of Finance. Minimum equity requirements and required insurance arrangements for trustees are set out in the MF Equity, Insurance and Suitability Regulations, and are the same as those for fund managers. **International cooperation** The way the Israeli market is structured at this time means that the need for international cooperation is not relevant to licensing decisions. The initial approval of an Israeli mutual fund or manager does not take into account the potential need for international cooperation. In practice Israeli funds are not marketed or distributed abroad. Currently it is also not possible to "passport" a foreign fund into Israel based on the adequacy of the relevant foreign regulation or any other reason. Any foreign fund must comply with all Israeli regulation before it may be distributed in Israel. The ISA has extensive international co-operations agreements described under Principle 11-13 which could be used if the need arose in the domestic market. **Sanctions for non–compliance** ISA has available a range of sanctions for non-compliance with the requirements of the managed funds legislation it administers. Unlicensed operation of a mutual fund is a serious offense that exposes the offender to both administrative and criminal liability (Mutual Funds Law section 124(a)(1) and (2)). Violations of obligations under the Mutual Fund Law are subject to three levels of sanction: For the least serious offences, there is a system of fixed fines which, in the case of fund managers and trustees, are linked to the value of assets managed or in trust. Offences where sanctions that can be imposed by the new Administrative Enforcement Committee (AEC), which is yet to commence operations. The fines that may be imposed by the committee are at the committee's discretion but are capped (maximum fines are NIS 25,000 for a regular employee who is not a company officer; NIS 1,000,000 for any other individual; NIS 5,000,000 for a corporation). A wide range of other sanctions may be imposed by the AEC (described under Principles 8 and 9). The deterrence effect of these sanctions is enhanced by section 120B of the Mutual Fund Law which prohibits indemnity against sanctions imposed by the AEC (and voids any insurance that does exist). The section also prohibits a corporation and its controlling shareholder from indemnifying any other party such as a company officer or employee against such a sanction, and making void any such provision. Criminal sanctions apply to a range of violations of the Mutual Fund Law. The violations to which these sanctions apply are listed in section 124. The maximum prison sentence is one year, rising to five years if the court finds there was an intention to mislead investors. **Supervision and ongoing monitoring** *Responsibility and powers of regulator* The ISA has sole responsibility for licensing fund managers and authorizing trustees and the controlling shareholders of fund managers and for ensuring regulated entities comply with their obligations under the Mutual Fund Law and related regulations. This includes ensuring that

	regulated entities continue to comply with eligibility criteria Section 97 of the Mutual Fund Law makes fund managers and trustees subject to the supervision of the ISA and empowers the ISA to issue directives regarding their conduct. These directives are enforceable and a violation may result in administrative sanctions. Sections 97 and 97A of the Mutual Fund Law give the ISA powers to investigate suspected breaches, including by demanding information and documents, and to carry out inspections and on-site audits of fund managers and trustees. The ISA may (and does) also appoint third parties (typically auditing firms) to do this on its behalf. Remedial actions available directly to the ISA (without recourse to the AEC or the courts) are fixed fines and the power to revoke, or apply conditions to, a license or authorization. A license or authorization may be revoked or have conditions applied to it if the fund manager or trustee no longer complies with any one of the conditions under which it was granted or if circumstances have arisen which indicate a defect in the reliability or trustworthiness of the entity in question, its principal shareholders or its company officers (Mutual Fund Law, sections 10A and 15) Violations for which fines may be imposed directly by the ISA are listed in the First Schedule to the Mutual Fund Law. An operator is also subject are those that may be imposed by the AEC. For AEC matters, the ISA carries out the investigation and brings the case to the AEC. Sanctions available to the AEC include: financial sanctions; an order to make a payment to any party injured by the operator's violation; an order to take remedial action to correct the violation and prevent its repetition (the AEC can order the operator to deposit a bank guarantee against full compliance with the order); prohibiting an individual from serving as a senior company officer in an ISA-regulated entity; revocation or suspension of a license, authorization or permit. A suspension of longer than one year and a revocation requires court approval. Criminal sanctions can only be imposed by a court. *Ongoing monitoring* A member of the Investments Department reviews all periodic, ongoing and immediate reports submitted to the ISA under the Mutual Fund Law and regulations. Reports relating to specific matters (for example, change of ownership of a fund manager) are reviewed by designated ISA staff members. All reports are made through MAGNA, the ISA's automated regulatory filing system, using a specific form that has a specific form number. The system sends a notice to the staff member responsible for a certain issue whenever a form with that number is loaded onto MAGNA. The Investments Department has an annual work plan of inspections and audits on both fund managers and trustees. These are carried out in accordance with an internal procedure on audits of fund managers and intermediaries, the Procedure for Field Audits of Investments Intermediaries. In 2006 an amendment was made to the Mutual Funds Law that authorizes the ISA to contract third-party auditors. In the years 2007-2010, a total of 26 in-depth audits of mutual fund operators were conducted with the aid of external auditors. During 2010, the Investments Department and external auditors appointed by the ISA carried out 6 field audits of mutual fund managers (out of a total of 27 funds managers. The audits focused on the control environment, management and control of investments and the valuation of securities. Fund managers were also required to report to the ISA regarding the application of recommendations issued following audits conducted in 2009. Cross-sectional (thematic) audits are also carried out, examining an issue across all fund managers.

	For example, a major cross-sectional, desk-base, audit was carried out in 2010, focusing on investments management and the use of centralized accounts to divide the securities bought and sold by the fund manager between the funds under its management. Following analysis of the audit results, in August 2010 the Department issued a staff bulletin to fund managers and trustees on a number of issues related to the findings of the audit Similarly, in February 2011 following another round of cross-sectional audits the ISA published its feedback and instructions on fund managers' internal procedures and controls. This dealt with issues relating to fund managers' governance, internal controls and operational activities (including protection of fund assets and the valuation of units). The Investment Department also undertook a cross-sectional audit of all fund managers on the issue of executive compensation in mutual fund management firms. *Fund trustees*: The Investments Department carried out inspections and audits of fund trustees. In 2010 these focused on internal systems, audit of fund assets, and trustee responses to breaches by fund managers. A cross-sectional audit on disparities in the collection of fees covered both management and trustee fees and the resulting ISA directives apply to both fund managers and trustees. *Investigations* In its regulation of mutual funds, the ISA uses its general investigative powers described under Principle 9. Investigative activities (as opposed to supervisory inspections and audits) are triggered by suspicion that a violation of the Mutual Fund Law or its regulations has occurred. The ISA gathers intelligence, including by questioning fund manager or trustee staff and demanding documents. At the end of the intelligence gathering phase, the ISA reaches a decision as to whether there is sufficient prima facie evidence to open a formal investigation. Intelligence gathering is typically be triggered by complaints received from investors, discoveries made during routine inspections and audits, unusual trading activity detected through the ISA's monitoring of the secondary market and from information in the media. For further details, see under Principles 9 and 10. **Reporting and record keeping requirements** Fund managers are subject to extensive reporting requirements mainly set out in the Joint Investment Trust Regulations (Reports) 5754-1994 (MF Reporting Regulations), though some are contained in the Mutual Fund Law itself. The MF Reporting Regulations require all material changes in directors, management (including the internal auditor), organization or by-laws to be notified by an immediate report. An immediate report is also required about the indictment or conviction of management personnel, controlling shareholders, or the trustee (see sections 8, 12-13, 14 and 16-17). Notice of changes to the by-laws is not specifically required, but where an amendment is made or confirmed by a resolution of the general meeting of unit holders, this must be reported under the requirement to disclose details of all general meeting resolutions (section 20V of the Reporting Regulations). Responsibilities for maintaining records of the operations of a mutual fund are set out in section 129 of the Mutual Fund Law. A fund manager must maintain details relating to the fund, to the assets held by it, the transactions carried out on its behalf, and the decisions made with regard to its management. These must be stored for at least seven years. Both computerized and paper records must be kept.

Conflicts of interest

The Mutual Fund Law deals with conflicts of interest in three main ways:

prohibitions or restrictions on activity;
matters that must receive prior consideration and board approval; and
disclosure requirements.

The approach used depends on the circumstances of the conflict or potential conflict.

This approach is used for conflicts of interest between a fund and its operators or their associates or connected parties; and for conflicts that may adversely affect the interests of investors.

The main prohibitions and restrictions on activity are:

Receiving benefits

Section 81 of the Mutual Funds Law provides that a fund manager may not receive any benefit with regard to fund management, except for the management fees stipulated in the fund agreement and the prospectus and remuneration for certain related services and for accommodation that may be received from a person controlling the fund manager.

Controlling shareholders, directors, members of committees and employees are prohibited from receiving any benefit with regard to the management of the fund except from the fund manager.

The trustee may not receive any benefit with regard to fulfilling its duties as trustee of the fund, except for the remuneration set out in the fund agreement and the prospectus, which must be paid out of fund assets.

Brokerage agreements

Section 69 of the Mutual Fund Law prohibits a fund manager from entering into a contract with a broker or dealer involving the payment of commissions to the broker or dealer paid out of the fund assets unless the contract is put out for tender. The fund manager's board of directors and the trustee must approve the tender process and the outcome of the tender must be approved by the fund manager's audit committee and board. The rules are more flexible for brokerage services in foreign securities.

Once a tender has been conducted, the fund manager may enter into contracts with a broker or a dealer who is affiliated with the fund manager or the fund trustee, so long as the contract is no less favorable than that of the successful tenderer and the fund manager's audit committee and board have given their approval after considering the interests of the unit holders. There is also a volume limitation - the service provided by the related party cannot reach more than 40 percent of the total value of commission paid for all transactions (no more than 20 percent for a firm related to the fund manager and no more than 20 percent for a firm related to the trustee)

The Joint Investment Trust Rules (Holding of a Tender and Determination of Relationship of a Trading Company with a Fund Manager) 2011 come into force in December 2011 and contain a requirement that the fund manager must base its broker tender decision on the commission prices offered by the broker in a way that best serves the interests of the unit holders of all the funds it manages.

Distribution commissions

In the Israeli market distributors must be licensed advisers, marketers or portfolio managers. Section 42(d) of the Mutual Fund Law provides that distributors must not receive commission-based incentives to direct investors to the units of funds managed by particular fund managers. The law requires a distributor to charge the same commission for issue, redemption and custody to all fund

	managers it deals with. In addition section 82 prohibits any other payment or any other benefit with regard to the purchase of unit. Distributors are mostly employees of banks. *Fund manager – trustee affiliation* Under section 9(d) of the Mutual Fund Law, a company may not act as trustee for a fund is it (or a director, manager or employee of it) is affiliated by ownership to the fund manager. A company is prohibited from acting as trustee if it or a person that controls it has a permanent substantial business relation or a direct or indirect professional connection with the fund manager or a person that controls the fund manager, or a corporation controlled by such a person. *Related party transactions* Section 67 of the Mutual Fund Law prohibits the purchase or sale of securities and financial instruments for a fund either in off-exchange transactions or in on a pre-arranged trade on the stock exchange from or to one of the following: fund managers; fund trustees; a person having control of one of the above; a person holding ten percent or more of the issued share capital of one of the above; a company controlled by one of the above; a director, employee or staff member of the fund manager, the trustee, a company controlled by one of these, a company in which one of these is a principal shareholder or an employee. The same prohibition applies to the purchase or sale of non-traded assets (Mutual Fund Law, Section 67). *Other conflicts* Sections 18(6) and 18(7) of the Mutual Fund Law, require other transactions that may involve a conflict of interest (as defined by regulations or deemed as such by the fund trustee) to be approved by the board of directors. For this purpose the term "conflict of interest" is defined as a conflict between the interest of the unit holders and the interest of one or more of the following: the holders of units in another fund managed by the fund manager, the fund manager, a principal shareholder in the fund manager or a company controlled by such a principal shareholder. The trustee has an ongoing role in determining which material transactions or types of transactions may involve a conflict of interest and referring them to the fund manager's board for consideration and approval (section 78(b) of the Mutual Fund Law). Section 20AA of the MF Reporting Regulations requires a fund manager to submit a report to the ISA detailing all off-exchange and OTC transactions entered into by the fund manager on the 1st and 15th of every month. The report must specify any transaction requiring board approval because of a potential conflict of interest and must disclose whether the external director(s) participating in board deliberations supported or objected to the transaction. **Conduct of business rules** The Mutual Fund Law requires fund managers and trustees: to carry out their duties and exercise their powers only in the best interests of the unit holders (Mutual Fund Law, section 74); in carrying out their duties and exercising their powers, to act carefully, faithfully and diligently (section 75); and to take reasonable measures to protect the assets of the fund and all rights attaching to them (section 75 (b)).

	There are no express legislative requirements in the Mutual Fund Law or regulations with respect to best execution or churning. It should be noted that only one securities exchange operates in Israel at this time, and the Mutual Fund Law and related regulations restrict investments in foreign securities to securities traded on regulated markets. So best execution issues do not arise in practice. Churning would be likely to result in a breach of the manager's general fiduciary duty. To ensure appropriate trading and timely allocation of transactions, a fund manager's board must prescribe internal procedures governing decision-making process about the fund's investments, internal review of investment management and unbiased management of the various funds under a fund manager's control (section 18(8) of the Mutual Fund Law). Section 3B of the MF Conflict of Interest Regulations restricts fund managers from subscribing for securities in an offering in which the underwriter has a connection with the fund manager. **Delegation** In practice, a fund manager may delegate some of its functions, notably day-to-day trading and investment decisions, but it may not delegate liability for them. Section 86 of the Mutual Fund Law provides that a trustee or fund manager may not delegate their powers or transfer their obligations under this Law, but that the employment of a person by a trustee or a fund manager shall not be deemed a delegation of powers or a transfer of obligations, and shall not derogate from the employer's liability to the unit holders. An ISA Staff Law Bulletin sets out the ISA's position on the employment of external investment managers by a fund manager and their supervision), and states that the persons to whom functions have been delegated are to be treated as being employed or engaged by the fund manager. Management of a fund's investments may only be transferred to an external body that is itself licensed by the ISA as a portfolio manager (Mutual Fund Law section 13(c)(1)). *Responsibility* The fund manager remains fully responsible for all actions of the transferred functions. This is emphasized in an ISA SLB that sets out the ISA's position on the use of external fund managers and their supervision. The SLB provides a non-exhaustive list of steps that a fund manager must take before contracting with an external investment manager, including by requiring that fund managers have written procedures regarding the appointment and ongoing supervision of delegated functions. These procedures must require a detailed due diligence process for appointment, and ongoing supervision and periodic checks by the fund manager, and reporting by the external manager. *Termination* The Mutual Fund Law and the SLB do not specifically refer to termination of the agreement with the external investment manager (apart from the disclosure requirements described below). Responsibility for the actions of the external investment manager remains with the fund manager which is expected to ensure that its contract with the external investment manager permits immediate termination if necessary. *Disclosure and reporting* Both engagement of an external investment manager and its termination must be reported to the ISA and also published in at least two widely circulated daily newspapers. Detailed disclosure requirements include the name of the fund, name of the external investment manager and its controlling shareholders, the date the management begins, the part of the portfolio or type of assets the external investment manager will manage, the scope of the discretion given to the external

	investment manager in making investment decisions as well as various other details (MF Reporting Regulation section 20A). The report must contain the following statement: "The employment of a portfolio manager does not detract from the responsibility of the fund manager towards the holders of the units." The report must be submitted at least two days before the date of the commencement of employment. Termination of the employment must also be reported to the ISA and published in at least two widely circulated daily newspapers. If the termination of the engagement involved circumstances in which the holders of the units have a special interest, the circumstances must be described. In addition, a prospectus of a fund for which an external investment manager is engaged, must give full details of the arrangement and the external manager. The requirements are set out in the MF Prospectus Regulations. The fact that the fund is managed by an external investment manager must be written in bold writing on the cover of the prospectus (MF Prospectus Regulations section 7(11)).
Assessment	Partially implemented
Comments	Overall compliance with this Principle is strong. The regulatory regime is sound and comprehensive, and the ISA actively monitors compliance with the obligations of fund managers and trustees. The fact that the ISA does not have the power to assess the adequacy of the internal management procedures as part of its assessment a fund manager's application for authorization affects the assessment of this Principle. Proposed amendments to the Mutual Fund law will permit the ISA to assess an applicant's systems and processes at the time the application for a license is being assessed. The assessor welcomes the proposal to address the gap in the regulatory regime.
Principle 18.	**The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.**
Description	**Legal form/investors' rights** The Mutual Fund Law specifies the form that managed funds must take in Israel. Mutual funds are not independent legal entities, but are based on a fund agreement between the fund manager and the trustee. Matters which must be included in the fund agreement are specified in section 5(a) of the Mutual Fund Law. All fund assets and cash must be held in the name of the trustee for the sole benefit of the unit holders. The fund manager carries out transactions in the fund assets by way of a power of attorney granted to it by the trustee. The fund manager cannot pledge or otherwise encumber the fund assets except for the purpose of carrying out a transaction for the fund and then only in accordance with the regulations (section 76 of the Mutual Fund Law). This applies to both open and closed-ended funds. (The Mutual Fund Law provides for both types of mutual fund, but there are currently no closed-end funds operating in Israel.) The term of office of the trustee under the fund agreement may not be less than three years. If the trustee's term of office is extended, the extension must not be for less than two years (Mutual Fund Law, section 9(e)). The trustee may only voluntarily resign during its term if a court approves. In an application to the court both the fund manager and the ISA must be heard (Mutual Fund Law section 11(a) (3)). The Mutual Fund Law emphasizes the role played by fund manager's board of directors. The requirements regarding external and independent directors that apply to publicly listed companies apply to fund managers (Mutual Fund Law section 16). The key obligations and responsibilities of the fund manager and trustee are specified in Chapter 7 of the Mutual Fund Law (sections 74 to 87).

	The trustee is a representative of the unit holders, and plays a significant role in control of mutual fund operations. The basic duties of trustees are set out in Section 78 of the Mutual Fund Law and include: supervision of the fund manager's implementation of the Mutual Fund Law, of the fund agreement and of the undertakings stipulated in each prospectus; verification that the fund manager maintains proper decision making procedures and an internal control system, which ensures proper management of the fund's books; ensuring that the management of each fund is in accordance with the fund manager's internal procedures prescribed by its board of directors. keeping the fund manager's employees informed about the provisions of the Mutual Fund Law. The trustee also determines the materiality of certain transactions or types of transactions or whether they engender potential conflicts of interest. If so designated by the trustee, these transactions are subject to consideration and approval by the fund manager's board of directors. Section 78(b). The trustee is empowered to demand and receive from the fund manager any document and information it requires in order to carry out its function. If it discovers defects in the management of a fund, it must instruct the fund manager in writing to correct them and set a time limit for this being done. The trustee's roles includes assessing and approving all external directors of the fund manager (Mutual Fund Law section 16(a1)). *Disclosure* The form of a managed fund and the rights of unit holders are established by the legislation and are therefore publicly available. The fund agreement must be filed with the ISA and is made publicly available through the ISA's on-line regulatory filing system, MAGNA. Fund managers and trustees are bound by the requirements of the legislation and the terms of the fund agreement, and both parties can only exercise discretions in accordance with the terms of the legislation and the funds agreement. **Responsibility for monitoring compliance with form and structure requirements** As the sole regulator of funds management, ISA is responsible for ensuring compliance by both fund managers and trustees with their obligations under the legislation. The trustee is responsible for ensuring that the fund manager complies with its obligations under the fund agreement. **Changes to investor rights** An act by the fund manager or trustee that changes investor rights must be publicly reported both to the online public reporting systems of the ISA (MAGNA) and the TASE (MAYA) and in some cases also disclosed in at least two widely circulated daily newspapers. Such an act requires an immediate report as an act or event that may be important to an investor considering the purchase, redemption or sale of units (section 20AB of the MF Reporting Regulations). The MF Reporting Regulations list a number of acts of events which may affect investor rights. These are set out in the following table, with the relevant section number in the MF Reporting Regulations and the prior notice that must be given and whether notice must also be publicized in at least two widely circulated daily newspapers:

Act or event	Section no.	Timing	Also newspapers
Transfer of fund to management by another fund manager	20C	2 days prior	Yes
Change of trustees	20D	Immediate	Yes
Change of investment policy	20E	2 days prior	Yes
Change in remuneration of fund manager or trustee	20F	2 days prior	Yes
Change in commissions on transactions	20H	Immediate	No
Change in the appointed time for offers/redemptions of units	20I	2 days prior	No
Change in payment distribution policy	20J	2 days prior	Yes
Non-performance of payment	20L	2 days prior	Yes
Error in unit and redemption prices	20Q	Immediate	Yes

All immediate reports must be submitted no later than the end of the first business day following the day on which the mutual fund operator became aware of the act or event. Some events require a minimum prior notice period, usually of two days.

The Chairman of the ISA may order that such a report be published in a newspaper.

This reporting method described above applies to all reports required under the MF Reporting Regulations unless the regulations specifically state that the particular report is to be made only to the ISA. In that case, the report is not sent to MAYA nor is it accessible to the public on MAGNA.

Separation of assets/safekeeping

All fund assets must be held in the trustees name for the benefit of the unit holders and the trustee must segregate them from all other assets (Mutual Fund Law section 76). The assets of each fund must be segregated from the trustee's own assets and from the assets of other funds held by the trustee, including other funds of the same fund manager.

Section 76(a) of the Mutual Fund Law requires that where an asset is not traded on TASE (and therefore is not deposited in a securities account with a custodian and subject to the normal protections of the law), this asset must be registered in the trustee's name.

The trustee empowers the fund manager to trade in fund assets though a power of attorney, and subject to the limitations on that power set out in section 76.

Books and records

A fund manager is required to maintain the fund’s books in such a way that they include all the information relating to the fund including:

assets held by the fund;
transactions carried out for the fund; and
decisions made with regard to its management.

The fund's records must be preserved for at least seven years (Mutual Fund Law, section 129).

Audit

The trustee is required, in consultation with the fund manager, to appoint an external auditor (section 99 of the Mutual Fund Law). The appointment must be approved by a general meeting of unit

	holders within three months. If the external auditor becomes aware of a material, continued or recurring breach of the Mutual Fund Law or of the fund agreement by the fund manager it must report the matter to the trustee, the fund manager and the ISA (section 99(b)). The auditor is responsible for auditing the annual financial statements of each fund managed by the fund manager. The requirements for the audit are set out in very detailed terms in Joint Investment Trust (Financial Statements of a Fund) Regulations-2009 (MF Financial Statements Regulations). **Winding up** The circumstances in which a fund may be wound up and the procedures that apply are set out in Sections 103 – 110 of the Mutual Fund Law. A fund may be wound up fall into two basic circumstances: where a court intervention is not required (for example, because a limited life fund has reached the reached its end date or because a special resolution has been adopted to wind up the fund in accordance with provisions in the fund agreement (Mutual Fund Law, Section 103)); or as a result of an application to the court (for example if the ISA is of the opinion that the best interests of the unit holders require the winding up of the fund in which case the ISA may submit a petition for winding-up to the Court (Mutual Fund Law, Section 104)). The Mutual Fund Law sets out the requirements for a winding up, and these include rules for: appointing the liquidator and determining the liquidator's remuneration; giving public notice of the winding up; commencing the winding up; the duties of the trustee and fund manager during the winding up; liquidating fund assets and distribution of cash to the unit holders; and completing the winding up. Section 105 permits the fund manager to act as the liquidator of fund unless the winding up occurs on the application of the ISA. In that case the trustee is appointed liquidator, unless the court has reason to appoint another liquidator (who must be suitably qualified and experienced).
Assessment	Fully implemented
Comments	
Principle 19.	**Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme.**
Description	**Disclosure to investors** *Prospectus disclosure* Offers of units to the public (including units or shares of a foreign fund) must be made in a prospectus that has been approved by the ISA (section 25(a) of the Mutual Fund Law). Section 26 of the Mutual Funds Law requires a prospectus for a fund to include all items required by the MF Prospectus Regulations and any other item that may be important to a reasonable investor who is considering the purchase of the units offered. As well as detail required by the MF Prospectus Regulations, the ISA has a broad power to require that additional information be included in a prospectus if it believes that, given the circumstances, it is important for a reasonable investor considering the purchase of the units being offered (section

	27 of the Mutual Fund Law). This includes but is not limited to: reports or opinions of experts and others; new financial statements and auditor opinion, if the ISA believes that those submitted were not prepared in accordance with accounting principles or do not accurately reflect the state of the fund manager or a related company. Section 2 of the MF Prospectus Regulations sets out format requirements, including a requirement in Section 2(h) that a prospectus must be set out in a clear manner, easy to read, written in as simple and lucid manner as possible with its pages numbered. The MF Prospectus Regulations set out a list of disclosure requirements that must be placed on the prospectus cover (which may be several pages long). This makes the "cover" function as a key information document. The ISA may also instruct the fund manager to transfer particular details or information included in the prospectus from one place to another, to present information in a different manner or to remove it entirely from the prospectus. If the ISA requires additional information beyond that required in the MF Prospectus Regulations, that information must be included in the section of the prospectus dealing with the same or related matter and all headings must be bold. Mutual Fund prospectuses are comprised of two parts. Part A provides information about the specific fund, while Part B provides information about the fund manager and trustee. Detailed disclosure requirements for each part are specified in the MF Prospectus Regulations. The prospectus must be dated within the 15 days following approval by the ISA (Mutual Fund Law section 31(a)). The Prospectus Regulations state that no provision of the law or regulation need be included in the prospectus unless specifically required by regulation (section 2(e)). The fund agreement between fund manager and trustee is publicly available on the ISA reporting site (MAGNA) and provides detail about the rights and duties of the fund manager and the trustee, and about the relationship between them. The fund prospectus is not generally required to contain a section setting out the general rights of unit holders, since disclosure about them is available from other sources. The prospectus must, however, contain: a section explaining how units may be purchased and redeemed - this is a prescribed text which must be used in the prospectus (MF Prospectus Regulations section 41); a section on general meetings of unit holders explaining how they are convened, how the unit holder may take part in voting and how the unit holder may receive information on agenda items prior to the meeting in order to reach a decision on how to vote (section 44). Part B of the prospectus deals with the fund manager and the trustee and contains extensive information on both, including detailed information about the holders of key management and compliance positions, and fund manager and trustee shareholders. Basic information about the manager and trustee must be on the cover of Part A of the prospectus. Detailed disclosure requirements to be contained in Part B about the fund manager, trustee and their principals are set out in sections 24 to 36 of the MF Prospectus Regulations. The Joint Investment Trust (Purchase and Sale Prices of a Fund's Assets and Value of a Fund's Assets) Regulations, -1995 mandate a detailed methodology to be used for asset valuation and need not be repeated in the prospectus.

	Where asset valuation based on market prices is not possible and the fund manager's board is required to instruct the fund manager how it must be calculated, the MF Reporting Regulations require disclosure in an immediate report. Procedures for the purchase and redemption of units must be included in the prospectus using a prescribed text (MF Prospectus Regulation section 41). The pricing of all units is published by TASE and is available on many websites (for example, those of domestic banks). The cover of Part A of the prospectus must include a notice to investors stating that it is advisable to monitor changes to unit prices (MF Prospectus Regulations section 7(2)(b)). The audited financial statements of each fund must be filed on the ISA's MAGNA regulatory filing website but are not included in a prospectus or follow-on prospectus. The prospectus itself must contain a notice that the financial statements are available on MAGNA and must also state the document reference on MAGNA so they are easily accessible (MF Prospectus Regulations section 19). The prospectus must identify any custodians used in Israel or abroad and, if a custodian holds an interest in the fund manager or trustee, this must be disclosed. The investment policy of each fund must be described on the cover of the prospectus (MF Prospectus Regulations section 7(8)). This disclosure is based largely on the categorization of the fund that is required under the characterizations of funds rules set out in the Joint Investment Trust (Classification of Funds for Publications Purposes) Regulations – 2007, but also includes some additional disclosures in certain circumstances. In practice, ISA has required all funds to have, as part of the name of the fund, a designation based on a matrix-style classification that captures the fund's investment policy, including for example exposure to shares and foreign currency. In a follow-on prospectus, any changes made to the investment policies of a fund during the last year must also be disclosed (in addition to an immediate report at the time the change is made) (MF Prospectus Regulations section 10). Risks inherent in investment objectives must be included on the prospectus cover under a separate bold heading. This section must list the risks inherent in the fund's investment policy, the method of managing the fund, the kind of assets the fund intends to hold and the markets in which the fund invests (MF Prospectus Regulations section 7(19)). Disclosure about the appointment of external investment advisers is required in both Parts A and B of the prospectus, and details must be provided. Disclosures must be made in both on the cover of Part A of the prospectus (MF Prospectus Regulations section 7(11)) and Part B of the prospectus (section 30). There must be disclosure about external service providers, such as foreign agents (MF Prospectus Regulations section 31(3)). The external auditor and the fund manager's independent counsel must also be identified (sections 31(4) and (5)). The annual remuneration payable to the fund manager and the trustee must be set out on the prospectus cover (MF Prospectus Regulations section 7(9) and (10)) and in Part A of the prospectus (sections 11(2)(a) and (b)). A follow-on prospectus must list the actual amounts paid from the fund for the remuneration of the fund manager and trustee, and transaction charges and taxes (MF Prospectus Regulations S.11(2)(e)). A follow-on prospectus must also detail any changes to the remuneration paid to fund manager or trustee during the previous year (MF Prospectus Regulations sections 10(2)(d) and (e)). Part B of the prospectus must disclose the rates of distribution fees paid according to fund type under distribution agreements the fund manager has entered into. Distribution fees are paid by the fund manager and may not be paid for from fund assets.

	The fund manager is permitted to impose an additional fee upon unit holders for transaction costs incurred in purchase or redemption (Mutual Fund Law section 42(c)). This fee is not included in the fund manager's regular remuneration and is relatively unusual in the Israeli market. However, if charged it must be disclosed on the cover of the prospectus (MF Prospectus Regulations (s7(12)(a)(2)). *Periodic and immediate reports* The approach described above for prospectuses is used by the Mutual Funds Law for periodic and immediate reports. Section 72(a) of the Mutual Funds Law empowers the Minister of Finance to prescribe reports and their contents. Section 72(b) empowers the ISA to demand additional reports from fund managers or trustees, if in the opinion of the ISA, the additional information would be important to a reasonable investor considering buying or redeeming a unit. *Suitability* There is no requirement for the prospectus to state what types of investors the fund may be suitable for. This is because fund managers are not permitted to give advice of any kind and do not deal directly with the client. Potential investors in mutual funds deal with either advisers (many of whom are employed by the banks) or marketers. The prospectus does contain information about risk which can be used by a potential investor or an adviser to assess the fund's suitability for a particular client. **Regulator's powers** Since an offer of units to the public may only be made under a prospectus the publication of which has been approved by the ISA, the ISA may hold back an initial offering of securities until it is satisfied that all material information has been appropriately disclosed (Mutual Fund Law, Section 29(b)). Once units have been issued and the offering is ongoing, improper, inadequate or misleading disclosures are primarily dealt with as a matter to be disclosed and corrected, and do not automatically constitute grounds for the suspension of fund activity. Under section 34 of the Mutual Funds Law a fund manager must submit a report on MAGNA and to TASE and publish a notice in at least two widely circulated daily newspapers immediately upon becoming aware of a misleading item in a prospectus. If the ISA becomes aware of a misleading item, which has not been corrected by the fund manager, it has power to order the fund manager to file public reports and place a notice in the press (section 72(b) to the Mutual Fund Law). The filing of such a report or notice does not in any way detract from the fund manager's liability for the misleading item. Nor does it limit the ISA's power to pursue disciplinary or criminal proceedings against the fund manager. Section 48(a)(c) of the Mutual Fund Law also authorizes the ISA Chairman to suspend an offering when he or she believes that the failure to order the suspension may harm the interests of unit holders. If misleading information in a prospectus is, in the opinion of the Chairman, so significant as to render the continuation of the offering unsafe until corrected, he or she can intervene. In practice the exercise of this authority is extremely rare. The ISA can also intervene in an offering where a director of the fund manager is opposed to the publication of the prospectus or has refused to sign it and has brought the matter to the attention of the ISA in writing. In this situation, the ISA may impose a ten-day delay (Mutual Fund Law, Section 30(f) cross referencing Sections 22 (e) and (f) of the Securities Law). ISA reviews prospectuses using a risk based approach to determine which require intensive review. In 2010, 1,269 permits to publish prospectuses were granted, 126 of which were for prospectuses of mutual funds offering their units to the public for the first time. 422 of these prospectuses were amended following comments on them by the ISA.

	Advertising Section 73 of the Mutual Fund Law sets out the conditions which apply to the publication by a fund manager of any material relating to a fund other than in a prospectus or other regulatory reports and notices. The Mutual Fund Law regulates the content that may be included in advertising and other materials. The trustee of the fund must approve publication of these materials prior to their release and ensure that their publication complies with the rules articulated in section 73 of the Mutual Funds Law, including rules about: how a fund's past performance is stated; the absence of misleading items; limitations on references to funds not managed by the fund manager; Information and notices that must be included in these publications and the format in which data must be presented. The ISA is authorized to instruct fund managers to correct any publication that it believes contains a misleading content (section 73(d)). The Joint Investment Trust (Calculation of Yield) Regulations, 1995) set out detailed requirements on the presentation of data on fund performance in promotional materials. **Reports** Each mutual fund prospectus remains valid for a period of twelve months from the date appearing on its cover (section 32(a)(1) of Mutual Fund Law). To continue offering units in existing funds after the end of the twelve-month period, the fund manager must submit a new prospectus to the ISA following exactly the same procedures and subject to the same law and regulations. This "follow-on" prospectus must be correct as of the new date of submission and so must be fully updated to reflect changes over the previous year. As well as this follow-on prospectus, the fund manager must provide either a declaration that no material changes relative to the previous years' prospectus have occurred or alternatively, a report providing a list of the changes that have been made, referencing the page numbers in the new prospectus and a referral to the periodic or immediate report in which the matter in questions was originally disclosed during the year. This procedure applies to both Part A and Part B of the prospectus (Processing Procedures Pertaining to Publication Permit of a Trust Fund Prospectus section 6 (a) (2) and 12(a)). If significant changes occur during the year, an immediate report is required, but there is no requirement for a supplementary or replacement prospectus. **Reporting** The periodic reports that a fund manager or trustee must submit are set out in the MF Reporting Regulations. There are two types of periodic reports, the annual report and the monthly report (sections 22A and 21 of the MF Reporting Regulations). In most cases, the annual report is the follow-on prospectus described in the response to the previous question. By updating Parts A and B of its prospectuses the fund manager provides full disclosure of its activities and current status. This is in addition to any immediate reports that may have been published during the year. If a follow on prospectus is not produced, an annual report in the form of and complying with prospectus disclosure rules must nonetheless be made (section 22A of the MF Reporting Regulations. The monthly report, due on the 15th of each month, provides data as of the last trading day of the

	previous month on the assets of each fund, its liabilities, its receipts and expenses. An addendum to the MF Reporting Regulations provides the template for the format and manner of reporting all the required information. These reports remain available to the public for forty five days from the day on which they are submitted to the ISA. **Accounting standards** Regulation 2(b) of the MF Financial Statements Regulations requires financial statements of regulated funds to be prepared in accordance with Israel GAAP and to be duly audited. For managed funds, implementation of IFRS has been postponed until 2016, with a review to take place in 2014.
Assessment	Fully implemented
Comments	
Principle 20.	**Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme.**
Description	**Asset valuation** *Requirement for valuation* Section 43 of the Mutual Funds Law requires a fund manager to calculate the purchase price and the sale price of fund assets in accordance with the fund's net asset value (NAV). The MF Asset Valuation Regulations provide detailed standards for the valuations of each category of assets that mutual funds are permitted to hold, and a description of how the value of each asset must be calculated. *Principles for valuation* The MF Asset Valuation Regulations require that the "purchase price" and the "sale price" of fund assets be calculated. The purchase price is the NAV plus purchase costs and the sale price is the NAV less sale costs. Purchase and sale costs means costs that would be incurred in the purchase or sale of the assets had the transaction taken place on the day on which the calculation is made (section 3 of the MF Asset Valuation Regulations). Generally speaking NAV is calculated using the closing prices of the securities on the exchanges on which they trade. *Timing* The net asset value of fund assets must be calculated at the end of each trading day. For funds where the purchase and redemption prices are calculated twice daily, the net asset value must also be calculated twice (section 2 of the MF Asset Valuation Regulations). *Where market prices are not available* If a market price is not available, the MF Asset Valuation Regulations place the responsibility upon the fund manager's board, which must provide instructions as to how asset value is calculated. Section 14B outlines the requirements for such board instructions: the instructions must state the factors that must be taken into account in determining the value of the asset; the instructions must have been approved by the trustee after the trustee has verified that they are suitable for this purpose in the relevant circumstances; once every three months the board must review its instructions and either adjust them or confirm them; board instructions must be articulated in writing and delivered to the CEO of the Fund Manager together with the trustee's approval.

	In addition, any valuation made under board instructions that precipitates a change of more than two-tenths of a percent in the redemption price of the fund's units must be made public in an immediate report. This report must disclose the reason the asset valuation was referred to the board of directors, and the percentage change in the value of the particular asset and the percentage change in the net asset value of the fund resulting from valuation according to board instructions. *Independent audit* An audit of the value of assets held in a fund is carried out as part of the preparation of year-end financial statements. There is no separate requirement for audit of valuations made during the course of the year, except insofar as one occurs as part of the sampling carried out during the audit of the financial statements. **Pricing and redemption of interests** *Requirement* Section 42 of the Mutual Funds Law sets out the basic regulatory requirements relating to the pricing of units and the charging of loans that managers would receive. On the first day of the initial offering of a fund, the price is the nominal price and thereafter the price for buying units is the purchase price (as described above) divided by the number of the fund's units and the price for selling is the sale price (as described above) divided by the number of the fund's units. At any other time, the price of a unit is the current net asset value of the fund's assets divided by the number of units in the fund (section 42(a)(2) and section 43. Section 42 of the Mutual Fund Law sets out other regulatory requirements relating to pricing including: the right of the fund manager to add an additional percentage amount to the purchase price or deduct this from the redemption price ("a surcharge") which will be part of the fund manager's remuneration and not added to the fund's account; a prohibition against a distributor adjusting its purchase, redemption and custody charges depending upon the identity of the fund manager. The ISA checks net asset values on a daily basis. The check is conducted by comparing the net asset value of each fund to a benchmark fund that the ISA creates and tracks for each fund type (shares, bonds, sector, country etc). Each benchmark portfolio is designed to provide an indication of the rate of return funds of the same type should be showing.[10] Fund managers must submit a Rate of Return (ROR) Report to the ISA on a daily basis for each of its funds. If the previous day's performance of a fund varies significantly from the results of the relevant benchmark fund, this may indicate an error in calculation of the net asset value or that the fund manager has purchased assets for the fund that do not comply with the fund's stated investment policy. These potential problems are flagged by the ISA system and forwarded to the relevant ISA staff member for further examination. *Disclosure* The Joint Investment Trust (Publication of the Unit Price and Redemption Price in an Open Fund

[10] ISA computerized systems make the calculations based on data which fund managers are obliged to publish (unit price, redemption price) and on data delivered by the TASE Clearing House (asset value, creations and redemptions.

	and Unit Price and its Value in a Closed Fund) Regulations 5754-1994 require a fund manager to publish the purchase and redemption price of units in an open-ended fund on the TASE price publication system for market closing prices. This is published following the close of business of every trading day. *Pricing errors* Pricing errors are dealt with by the disclosure regime applying to fund managers. The MF Reporting Regulations (sections 20P and 20Q) divides reportable errors into two classes: those that result in the published purchase or redemption prices being off by at least one tenth of a percent and those that result in the published purchase or redemption prices being off by at least two tenths of a percent. In both cases, the error is a reportable event if the fund manager becomes aware of the error within two weeks of the publication of the erroneous price when a correction can be made through the TASE settlement system. The Mutual Fund Law and its regulations do not require the fund manager to compensate unit holders if the error caused them any loss in either case, but in practice fund managers provide compensation. In the case of errors of at least one tenth of a percent, the fund manager is required to report the erroneous and correct prices and to state whether it has corrected, or intends to correct, the error in the accounts of unit holders. The reporting requirements for errors of at least two tenths of a percent are more detailed and include a description of the nature of the error (MF Reporting Regulations s.20P and 20Q). The Mutual Funds Law prohibits a distributor/custodian from charging a unit holder for any expenses incurred in connection with correcting the records maintained by the distributor or custodian following the correction of a pricing error (Mutual Fund Law s.80A). *Suspension/deferral of valuations and redemptions* Generally speaking, a fund manager is under an obligation to redeem units on a daily basis or, in the case of a fixed date fund (as defined in section 47(a) of the Mutual Fund Law), on the dates disclosed in the fund prospectus. Section 48 of the Mutual Fund Law deals with suspensions of the issuance and redemption of units. A suspension may only occur as the result of an act of the Chairman of the ISA. The Chairman may: issue an order suspending the issuance or redemption of units of an open-end fund for a period of not more than three trading days following consultation with the TASE Chairman. This authority may be exercised when trading is not taking place, or if the results of trading have severely impaired the ability of the fund manager to buy or sell securities for a fund or calculate the purchase price and the sale price of the fund's assets. Such an order may be extended by the Chairman of the ISA, with the approval of the Minister of Finance, as long as the grounds for issuing the order persist. approve a written request from the manager of an open-end fund (after approval by the trustee) to suspend redemption of units for a period of not more than three trading days. Such a request from a fund manager is permitted if it or a party providing services to it is undergoing a severe disruption in its normal business and is unable to redeem units. During the suspension period no units may be issued to the public. issue an order suspending the offering and redemption of units of an open-end fund for a period of not more than seven trading days, if he or she believes that the interests of the unit holders warrant this. Such an order may only be issued following consultation with CMISD and after having giving the fund manager and the trustee a proper opportunity to state their positions. The Chairman may extend such an order for additional periods of not more than seven trading days each, up to a limit of

	sixty consecutive days. The Chairman of the ISA must publish a notice regarding the exercise of this authority in at least two widely circulated daily newspapers. In practice, this power has only been used once, for a fund that was exposed to Iceland assets. *Regulatory authority to monitor compliance* The asset valuation rules in the Mutual Fund Law and regulations are backed by the supervisory and enforcement powers of the ISA. The ISA may instruct a fund manager to recalculate or correct asset valuation. It may also demand documentation demonstrating how calculations were made and question fund manager staff. The RoR Report regularly discloses cases in which the daily rate of return of a given fund deviates from the return of ISA's benchmark fund. The ISA examines all such cases and on average makes one to two calls per week to fund managers to discuss unusual returns. *Reporting to regulator and regulator's powers of intervention* A failure to redeem units following receipt of an instruction to do so is classified in the First Schedule to the Mutual Funds Law as an offense for which the sanction (under section 114 of the Mutual Fund Law) of a financial penalty can be imposed directly by the ISA. The failure to redeem offense is included in Part 3 of the First Schedule, rendering an offending fund manager liable to the highest level of fines (as stipulated in the Second Schedule).
Assessment	Fully implemented
Comments	
	Principles for Market Intermediaries
Principle 21.	**Regulation should provide for minimum entry standards for market intermediaries.**
Description	**Regulatory and industry background** Two separate authorization (licensing) regimes apply to intermediaries in the Israeli market: a regime for intermediaries who are portfolio managers, investment advisers or investment marketers (ISA licensees); a regime for broker-dealers who are members of TASE (TASE members). A new regime is also being introduced for the providers of electronic trading platforms. It is expected to be in operation from early in 2012. *Portfolio managers, investment advisers and investment marketers* The activities of these intermediaries are governed by the Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management Law – 1995 (the Investment Advice Law) and the regulation and directives made under it. The categories of licensees to which this regime applies are: *portfolio managers* - entities licensed to manage investment portfolios for clients on a discretionary basis. Portfolio managers can also provide advice and accept client trading instructions. They must be corporate entities. Subsidiaries of banks, including foreign banks, play a significant part in this market. At the end of 2010, there were 164 licensed portfolio management companies, with NIS 242 billion under management, and 1,041 individuals licensed to provide portfolio management services.

	investment advisers - entities and individuals licensed solely to provide advice on all types of investments. The holder of an investment advice license is not permitted execute transactions for a client or to handle clients funds or assets (though they may arrange for execution if, for example, they do so in their capacity as a bank employee). Many investment advisers are employed by banks, which do not require a license issued by the ISA, although the employees who provide advice services to clients must be individually licensed as advisers. At the end of 2010, there were 12 licensed investment advice companies and 3,960 individuals licensed to provide advice services. *investment marketers* - entities and individuals licensed to provide advice to clients about financial products but are classified as marketers because they have a commercial connection with a financial product or product issuer (even if they does not give advice about that product). Licensees in this category are not permitted execute transactions for a client or handle client funds or assets (though they may arrange for execution if, for example, they do so in their capacity as an employee of a TASE member). Many marketers are employees of mutual fund managers or portfolio managers. At the end of 2010, there were 27 companies licensed as investment marketers, and 604 individuals licensed as investment marketers. *Stock exchange members (TASE members)* These intermediaries are subject to the direct supervision of TASE and are not licensed by the ISA. The ISA is responsible for supervising TASE activity, trading and management and ensuring TASE effectively operates as an SRO. The regulatory requirements imposed and supervised by TASE are set out in the TASE rules and regulations. The TASE rules are subject to the approval of the Minister of Finance after consultation with the ISA and the Knesset Finance Committee, and TASE regulations are subject to ISA approval. Under TASE Rules (First Part - Stock Exchange Membership), there are six categories of member: a banking corporation that is a listed company (rule 3) a banking corporation that is not a listed company (rule 4) (In practice, there are no members in this category.) a foreign bank that is not a remote member (rule 4A) for a listed company that is not a banking corporation and that is not a remote member (rule 5) a company that is not a banking corporation or a listed company and that is not a remote member (rule 6) remote member (rule 6A). There are 26 active members of TASE, including 14 bank members supervised by the Bank of Israel (and in the case of two members, also by their foreign home regulator) and 12 non-bank members (one of which is a remote member). The Bank of Israel is also a TASE member. *Electronic trading platforms* The legislation that will require operators of personal account trading platforms to be licensed by the ISA has been enacted but is not yet in force. This is scheduled to take place at the beginning of 2012. There are currently round 10 such platforms active in Israel and a number of smaller entities operating from offshore. They mostly offer clients the opportunity to trade in foreign exchange and commodities contracts, and exotic options. As far as is known none offer trading facilities for securities transactions. The amendment to the Securities Law is set out in Chapter 7-C of the Law, and will require operators and controlling shareholders of regulated platforms to be hold a platform license. By section 44P, the holder of a platform license must not engage in any other occupation other than the management of a trading platform, and may not extend credit to its customers.

	Authorization of licensees *Basic requirement* Portfolio managers, investment advisers and investment marketers must be licensed prior to providing services in Israel (section 2 of the Investment Advice Law). Section 3 creates some exceptions from the licensing requirement, including: where a person manages a corporation's portfolio as part of his function within that corporation (treasury management functions) portfolio management by an attorney or accountant within the framework of their professional duties and where a portfolio manager has been appointed by the courts to manage assets. where a person provides service to no more than five clients where the services are provided to a "qualified" client (defined in the First Schedule to Investment Advice Law to include financial market participants, high worth companies and individuals, and individuals who meet at least two of three specified conditions). In cases c. and d. above, conduct of business rules apply notwithstanding that a person is not required to hold a license (sections 3(a1) and (a2) of the Investment Advice Law). Both individuals and companies must hold a license to provide services. Separate criteria apply to individuals and to companies. The ISA must grant a license to any applicant who meets the relevant criteria (sections 7 and 8 of the Investment Advice Law). The gaps in the regime mentioned under Principle 1 are of particular importance for this Principle. Not all intermediaries that provide, or could provide intermediary services in the Israeli market are required to be licensed. This applies to broker-dealers that are not authorized by virtue of being members of TASE, provided they do not provide advice that would require them to be licensed by the ISA as advisors or marketers. It also applies to those who conduct OTC derivatives activities, including by offering OTC derivatives to retail clients (again, if they do provide advice to retail clients, they need to do so under a license issued by the ISA). (see ISA comments regarding this issue above) *Capital requirement* All types of licenses require applicants that are corporate entities to meet minimum capital requirements (see under Principle 22). *Integrity* Integrity standards apply to all categories of licensee. *Advisers and marketing licenses:* Individuals must not have been convicted of a criminal offence (section 7(a)(3) of the Investment Advice Law). Analogous rules apply to partnerships and to companies. In these cases, employees and partners providing the services that require a license must hold an individual license. *Portfolio management licenses*: The same standards apply to individuals as apply to individual adviser and marketing licenses. Applicants that are companies can only employ licensed individuals in roles that involve portfolio management, investment advising or investment marketing (section 8(b)(2)). The ISA also has a broad power to refuse to grant a license if it is of the opinion that circumstances exist which, in light of the profession's requirements, render the applicant unfit to serve as a licensee; and if the applicant is a corporation, that such circumstances exist with respect to either of the following a party which controls the company applying for a license; or an office holder in either the applicant or a company that controls the licensing applicant. (Section.8(c)).

	Conduct that might be expected to cause the ISA to refuse to grant a license under this general power includes the type of conduct, which if applicable to a licensee, may cause the ISA to revoke or suspend the license. In addition to circumstances specified in the Investment Advice Law, the ISA has published a list of considerations which will be considered in the licensing process. A draft of this list is currently being circulated for public comment. The ISA, the Supervisor of Banks at the Bank of Israel and the Commissioner of the Capital Market Division (Ministry of Finance) have also published 'fit and proper' criteria for those seeking to operate in the regulated area. In practice, the ISA has access to detailed police records that cover not only convictions, but also cases in which a person has been under investigation. *Competence* Competence standards apply to all categories of licensee. Individuals who provide regulated services must: have passed 5 examinations administered by the ISA (and 1 additional examination for portfolio managers); have completed a six month internship (nine months for a portfolio manager) under the supervision of a person with at least 5 years industry experience in the relevant activity. The examinations set by the ISA cover securities law and professional ethics; accounting; statistics and finance; economics; securities and financial instrument analysis; and portfolio management. In some cases exemptions from certain exams may be obtained based on the applicant's education and professional experience. *Internal controls* As part of its broad powers to refuse a license under sections 7(d) and 8(c) of the Investment Advice Law, the ISA has power to consider an applicant’s internal controls and risk management and supervisory systems as part of the licensing process. Ongoing regulatory requirements following licensing require the licensee to have such systems in place, along with written procedures on a range of issues. In practice, the ISA provides training and guidance for all new licensees, and carries out an inspection of all new licensees within a year of their commencing operations. In 2010, 12 training sessions were carried out, emphasizing the licensees' fiduciary duty to act for the benefit of their clients, and stressing the need for internal corporate controls and enforcement. **Authorization of TASE members** For broker-dealer members of TASE, initial and ongoing membership requirements are set out in the TASE Rules and TASE Regulations. Membership requirements are based on objective standards and requirements vary according for each of the six categories of members, though there is significant overlap of requirements across the different categories. Differences between requirements stem largely from the fact that the TASE Rules take into account that some entities (in particular banks) are subject to other licensing requirements and supervision. For example the TASE Rules do not prescribe capital adequacy requirements for banks licensed in Israel, but rely on Bank of Israel supervision of bank capital levels; and disclosure requirements vary between listed companies and non-listed companies. For listed companies, disclosure requirements are less onerous and take account of the fact that information required for non-listed members (such as details of shareholders' identities) is already publicly available for listed companies. A distinction between types of members is made throughout the TASE Rules between bank and non-bank members. This is reflected in numerous differences in authorization requirements and ongoing supervision by TASE, for example in relation to capital requirements, the integrity and

	expertise of officers and senior managers, officers and controlling shareholders, and control and compliance systems. *Capital requirement* All members are subject to initial (and ongoing) capital requirements (see Principle 22). For non-banks, these are set out in the TASE Rules (TASE Rules Part 1 – Membership, s.5(g) and 6(a)). Banks are subject to capital supervision by the banking regulator. See further under Principle 22. *Integrity* An applicant's senior managers and controlling shareholders must all be of good repute and may not have been convicted of a criminal offense involving ignominy (unless the period of prescriptions has expired). Senior managers in this context include directors; the CEO; senior managers; any holder of another office whom the TASE Board of Directors determines is a senior manager for the purpose of the TASE Rules. (See for example, TASE Rules Part 1 – Membership, rule 5.a.) As part of its due diligence process when considering applications, TASE refers to the ISA about senior managers and controlling shareholders. The ISA provides information it holds that may have a bearing on TASE's decision, but does not obtain police checks as it does for its own licensees. Senior managers and controlling shareholder of applicants for TASE membership must not be undischarged bankrupts, and must not have been principal shareholders in a corporation that has been liquidated without paying its debts. (TASE Rules Part 1 – Membership, s.5(a)). *Competence* A majority of the directors of a non-bank applicant for TASE membership must have know-how in the capital market. The CEO and the managers of its securities unit must have know-how and have undergone training in the capital market. At least one of the senior managers must have at least five years' experience in capital markets (TASE Rules Part 1 – Membership, s.5(d)-(f)). *Systems, technology and staff* A non-bank applicant for membership must have the mechanism, means, computer systems and skilled personnel enabling its proper activity on the Stock Exchange and the performance of its duties to its clients, TASE and other members (TASE Rules Part 1 – Membership, section 5(k)). Written policies and internal procedures required for credit control, risk management, compliance and internal audits (TASE Regulations, Chapter IV, 25K-25T). **Authority of Regulator** *ISA licensees* The ISA has the power to refuse licensing if authorization requirements are not met (sections 6 and 7 of the Investment Advice Law). The circumstances in which ISA can suspend or revoke a license are set out in section 10 of the legislation. One is that the criteria for granting the license are no longer being met. Other factors that may cause the ISA to revoke or suspend a license including proven violations and bankruptcy of the licensee. The ISA has administrative powers to revoke licenses for breaches of 'fit and proper' standards. **TASE members** An application for authorization is considered by the TASE Board of Directors. In special

	circumstances the Board may decide not to approve an application even if all the requirements set out in the TASE Rules have been met but such a decision requires a 75 percent majority amongst those directors present for the vote. Such a vote may only be taken after the applicant has been given an opportunity to state its case in writing (TASE Rules Part 1 – Membership, s.8). A decision by TASE to refuse an authorization may be appealed to the Economic Court (section 47 of the Securities Law). TASE has power under the TASE Rules to revoke, suspend or imposes conditions on a member. The powers of the TASE Board to revoke or suspend membership are set out in Chapter VIII of the TASE Rules Part 1 – Membership (Conditions and Procedure for a Member's Suspension and the Revocation of Membership). The Chapter sets out the circumstances in which the TASE Board may revoke or suspend membership, or prohibit a member from certain types of trading activity. Grounds for these actions include the discovery of material flaws in the business processes of a members, failure to continue fulfilling the initial membership requirements and failure to fulfill its obligations to TASE, the TASE clearing houses or other members. TASE can prohibit or restrict the continued engagement of an employee or senior manager in the securities business with a member for a specific period or permanently (TASE Rules, Part 1 – Membership, s.65(e)). This applies to any employee, not only one that is individually licensed by the ISA. *Regulatory oversight of TASE admission process* The Securities Law requires the ISA to supervise TASE on an ongoing basis, including oversight of its compliance with the TASE Rules and TASE Regulation. If the ISA consider that TASE is operating contrary to the provisions of its rules or regulations, the ISA can direct it as to the proper manner of operation (Securities Law, section 51(b)). The ISA is directly involved in the admission of new members. It has the right to send a representative to any meetings of the board of directors and its committees (Securities Law section 51(d)) and in practice attends all TASE board meetings. **Ongoing requirements** *ISA licensees* Chapter E of the Investment Advice Law requires licensees to provide the ISA with periodic and immediate reports. A licensee’s annual report to the ISA must include details of its insurance cover and capital levels. Licensees are required to report immediately to the ISA if any conditions for the granting of the license cease to be met (section 27(c)). Under ISA directives, this section is also the basis of further general reporting requirements, notably the requirement to report within 7 days all changes in the company's senior officers and changes to persons controlling the licensee company. *TASE members* Members are required by the TASE Rules to file financial statements and periodic reports with the TASE, in accordance with the detailed requirements in the TASE Regulations (TASE Rules, Part 1 – Membership, section 20). TASE Regulations require an annual report and three quarterly reports. The content requirements are closely modeled on the periodic reports public companies must file, with some adjustments (mainly additional disclosure requirements) (TASE Regulations Part 1 - Membership, section 25). Remote members must file with TASE all the periodic reports that they are required to file to the competent authority in the relevant home country (section 25A1). A member must also continue to fulfill all the membership criteria on an ongoing basis and report to TASE any breach of the TASE Rules and Regulations or of a resolution of the TASE Board.

	A member must provide immediate written notice to TASE of the appointment or termination of employment of any senior manager (whether initiated by the manager or the member). In the case of termination, the notice must disclose any circumstances that must be brought to TASE's attention or declare that the termination does not involve any such circumstances. **Public disclosure of licensed intermediaries** The ISA website makes publicly available a list of licensees, the type of license and the current status of the license. Section 8(b)(1) of the Investment Advice Law restricts the activities a portfolio manager can engage in to portfolio management, investment advice or marketing, financial planning (retirement) and marketing of retirement savings schemes, the execution of transactions on a stock exchange, and related transactions such as investment in foreign currency deposits and approved savings schemes. Additional information such as senior management and individuals authorized to act on the portfolio manager's behalf are reported to the ISA but are not available to the public. *TASE members* The fact that a company is a TASE member, as well as whether it is a bank or non-bank member, is public knowledge. This information may be obtained from TASE and appears on the TASE website. The TASE Rules do not require a member to make available to the public the names of senior management or any individuals authorized to act in the name of the member. However the name of the CEO and the name of a contact person are available on the database on the TASE website. If the company is public, senior management will have been disclosed by virtue of the disclosure regime for public companies. In practice, most members (whether public or not) do voluntarily provide the names of all or some of their senior management on their websites. The financial statements of a non-bank member must be available for inspection by the public on request at its offices (TASE Rules, Part 1 – Membership, s.20(c)). **Monitoring, investigation and enforcement** *ISA licensees* The annual supervision plan of the Investment Department makes provision for a program of "audits" (reviews and inspections) of licensees. A risk scoring system (on a scale of 0-100) is used to identify licensees who will be the subject of ISA audits. This approach is used for the 40 largest portfolio managers and the 8 largest banks and is combined with assets under management or assets under advice to reach a final risk score. All other licensees are rated according to asset size only. The most critical criterion is the value of assets under management (for portfolio managers) and of assets under advice (for banks). For assets under advice, the figure is based on the clients advised and the size of their portfolios. Both banks and non-banks are included in this assessment. Licensees with a high risk score have a member of the Department's staff assigned to them, and are subject to close attention. The designated staff member meets regularly with the licensee and follows both public and non-public information (including from the ISA's BI system) about the licensee. The strategy with these licensees includes improving the quality of their internal controls and compliance mechanisms. For other licensees, the ISA aims to conduct reviews on a 2 year or 4 year cycle, with more frequent reviews for larger entities. These reviews are usually desk based reviews. The ISA carries out two types of audits: cross-sectional audits examining a particular issue across a number of licensees;

	focused audits examining compliance by a specific licensee with a number of specific regulatory requirements. During 2010, the ISA carried out seven cross-sectional audits and 36 focused audits. Five of the cross-sectional audits were carried out by correspondence with licensees and two by gathering data without direct contact with the licensee. Of the focused audits twelve were conducted in the licensee's premises and 22 by correspondence. The procedures and practices used by the ISA when carrying out onsite audits at licensees is set out in an internal ISA procedure (the Procedure for Field Audits of Investments Intermediaries. If an audit uncovers failings in the practices of the licensees, these are detailed in letters to the licensees with the changes the license is required to implement. These are then followed up as part of the ISA's ongoing supervision. In addition to cross-sectional and focused audits, the ISA conducts audits on compliance with anti-money laundering regulation and enforces compliance by portfolio managers and non-bank TASE members with their reporting obligations. The ISA also carries out investigations of licensees in response to client complaints and suspicions that arise during the course of its ongoing supervisory work. 111 such cases were investigated during 2010. The ISA also meets regularly with employees of licensees that are responsible for compliance and internal enforcement. These meetings include periodic updates and supervision of internal enforcement programs. As part of this ongoing contact, the ISA requires supervised entities to independently review the results of these programs and report their findings to the ISA. *TASE members* TASE's Membership and Surveillance Department is responsible for ongoing monitoring of members. The department prepares an annual work plan setting out its objectives for the coming year, including plans for onsite inspections and proposed matters of focus. This work plan is discussed with staff of the ISA. Key issues such as the management of financial risks, the proper functioning of members' internal accounting and risk management mechanisms and maintenance of capital levels are regular parts of these work plans, although the emphasis may vary from year to year. Other matters will typically include the functioning of internal compliance procedures and internal audit function, segregation of client assets, client agreements, ownership and senior management of the member and, in recent years, inspections arising from the 2008 crisis (such as exposures to foreign financial institutions and to volatile foreign markets, and relations with foreign custodians). In the last year, TASE carried out more than 500 reviews, 75 percent of which were on non-banks TASE members. Areas of focus included: three audits of non-bank member credit and collateral levels and an inspection that securities held as collateral were given the correct weightings in the member's systems; separation between client activity and proprietary dealing; booking transactions abroad in the member's systems; compliance officer reports to the board and senior management; capital adequacy levels, including checks on intangible assets and liquid assets; collateral posted by TASE members to secure clearing house activity; proper use of securities allocation accounts by non-bank members; disaster and contingency planning. In addition, the Department carried out in-depth audits on a range of issues on two non-bank members.

	The findings of these audits must be discussed by the member's audit committee and a report of that discussion is given to TASE. If TASE is not satisfied with the member's response, it returns it to the member with a request that it be reconsidered and acted on. TASE provides monthly reports to the ISA on its supervision activities. The ISA can request a specific issue to be addressed by TASE audit of its members. For example, it did so recently in relation to potential exposure of TASE members to the failed US group, MF. For banks members of TASE, the bank supervision area of the Bank of Israel has a consumer protection unit responsible for supervision of the way that banks deal with their customers, including their securities customers. To carry out this responsibility, the unit responds to complaints from bank customers. From time to time the supervision area includes consumer protection issues in its on-site and offsite supervision of banking groups. The number of complaints from securities customers is a small proportion of the over 8,000 complaints the unit deals with a year (for example, of the 260 complaints received over the last 3 years relating to one large bank, only 13 related to the bank's securities customers). **Investment Advisers** *ISA licensees* Under Israeli law, advisers (who provide independent advice to their clients) and marketers (who provide advice about products with which they or their employers have a connection) are not permitted to deal on behalf of their clients and may not hold client funds or assets. Portfolio managers, investment advisers and marketers are subject to record keeping requirements. The basic requirements are set out in Section 25 of the Investment Advice Law and elaborated in the Investment Advice Law Regulations Governing Engagement in Investment Counseling, Investment Marketing and Investment Portfolio Management (Recording of Transactions and Recording of Counseling Activities), – 2007). Portfolio managers must maintain records of all transactions executed on behalf of a client as well as each instance that they render advice. An adviser or marketer must maintain records of each instance that advice is given. All advisory activity must be recorded irrespective of whether the advice ultimately leads to a transaction. Records must be stored for at least seven years. The regulation sets out comprehensive requirements for the records a portfolio manager must keep of each transaction it carries out. There are currently no specific legislative requirements about the content of disclosures licensees must make to potential clients (except for a requirement for portfolio managers and marketers to disclose to clients any connection they have to financial assets (section 16A of the Investment Advice Law). However, the IA Internal Procedure Directive[11] requires licensees to establish an internal procedure for the way potential clients must be treated. This includes a requirement that the internal procedure specify which information and documents must be presented to potential clients in the course of enlisting new clients. A proposal for the enhancement of ongoing disclosure by portfolio management to their clients and to the ISA is currently under discussion by the Knesset Finance Committee. Proposed regulations under the Investment Advice Law will expand the disclosure to clients (for example quarterly report

[11] The Directive to Licensed Corporations Concerning Duty to Determine Work Procedures for their Operation and Management.

	will include more details than currently required, such as data on the quarterly return of the portfolio). In addition, the proposed regulation sets a format for the report to be applied to all managers to enable comparative analysis between portfolio managers. In practice a written agreement between portfolio manager, adviser or marketer and the client. must set out: the payment and expenses that the client will be charged including the manner in which they will be calculated. disclosure about a conflict of interest when the investment service provider is a portfolio management company affiliated with a financial institution or a marketing agent or when the portfolio manager itself is also engaged in investment marketing. This written agreement must be completed and signed before any services may be provided. *Conflicts of interest* A portfolio manager must not: use a client's funds, securities or financial assets other than for the purpose of executing transactions on the latter's behalf, and in accordance with the agreement entered into with the client and with the power of attorney received from such client; enter into a transaction as counterparty with a client nor receive any benefit from client's assets, unless the client has given consent in advance and in writing to the particular transaction or the particular benefit. Conflicts of interests are dealt with on two levels: full disclosure to the client is required under the Investment Advice Law whenever the licensee becomes aware of any conflict of interest (section 15); a licensee is prohibited under the Investment Advice Law from executing any transaction engendering a potential conflict of interests unless the client has given prior consent in writing or by telephone in a conversation, a record of which the licensee must make and retain (section 15).
Assessment	Not implemented.
Comments	Where the licensing regime applies, it provides a robust framework for assessing minimum standards. The ISA has adequate powers to supervise licensees on an ongoing basis and there is good evidence of its active use of those powers (see also under Principle 10). The rating of not implemented is necessary because of the gaps mentioned in the description (and also under Principle 1). This is a serious shortcoming in the regime, and results in potentially significant capital market activity being unregulated by the securities regime or any other part of the overall regulatory framework. In practice, since much capital market activity is undertaken by licensed banking groups, banking supervision could provide some regulation of these entities. The assessor is not aware of significant problems currently affecting the market as a result of unregulated activity. Nonetheless, this is more than a theoretical question. The absence of a licensing framework for intermediaries of this kind could have serious implications for investor protection and (if unregulated activity grew to a significant size) have the potential to have an impact on overall market stability. The supervisory activities of the TASE do not appear to place strong emphasis on examining compliance with the rules relating to the way non-bank members deal with their customers, focusing more on compliance with capital requirements and on the interaction of members' systems with the TASE's trading and clearing and settlement systems. Supervision by the banking regulator of banking groups' dealings with their securities clients is largely complaint driven and does not involve proactive supervisory techniques. (These issues will be reduced if the ISA is responsible for

	regulating and implementing conduct of business norms on broker dealers, in cooperation with other regulators as needed.)
Principle 22.	**There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.**
Description	**Capital requirement for ISA licensees** All licensees must comply with minimum capital requirements, the details of which are set out in the Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management Regulations (Equity and Insurance) - 2000 (IA Equity and Insurance Regulations). The regulation requires advisers, marketers and portfolio managers to hold capital of NIS 200,000. This sum is adjusted by reference to the CPI and currently stands at NIS 254,000. In this context it should be noted that: investment advisers and marketers only provide advice and do not handle or control client funds or assets; in the case of portfolio managers, the securities comprising the portfolio must always remain in a securities account maintained in the client's name with a TASE member or a bank. Similarly, cash balances are held in the client's bank account or an exchange member's account (TASE members must hold all client funds in a trust account at a bank). At no point in the execution of a transaction do either client assets or client cash cross an account in the name of the portfolio manager. [12] *Insurance* The Investment Advice Law places greater emphasis on liability insurance or equivalent measures than on capital levels. Licensees must take out insurance against liability for negligent actions or omissions in relation to its clients and the malpractice of employees. This insurance may be substituted with bank guarantees or cash or securities deposits. As well as these minimum capital requirements, ISA licensees must maintain a deposit for an amount equal to the difference between the deductible in their insurance policy and 2 percent of their capital (thus, the higher the deductible, the more cash must be held). Apart from these obligations, they are not subject to other capital or liquidity requirements, **Capital requirement for TASE members** Initial and ongoing capital requirements apply to all TASE members. *Bank members* In the case of bank members, the Bank of Israel is responsible for setting capital and liquidity requirements. The only exception to this is the initial capital requirement for MAOFCH membership, which applies to all TASE members and was set at NIS 120 million each for the MAOFCH member and each TASE member that is not a MAOFCH member and receives clearing services from the MAOFCH member.

[12] There is one exception to this rule: a portfolio manager may use a "securities allocation account" (an account in its own name through which it executes orders in the same security for multiple customers). If the portfolio manager buys a security for a number of customers, it may execute a single purchase which is settled in its own account and then allocate a portion of the shares to each of its clients. This process is permitted by law and regulation. However, even in relation to trades executed in this manner, the client is not exposed to portfolio manager insolvency, since the portfolio manager may debit the purchase price from each of the client accounts only upon transfer of the purchased shares to the client.

	Non-bank members TASE recently revised capital and liquidity requirements for its non-bank members. The new model is based on the EU Capital Adequacy Directive and Basel principles. It is designed to reasonably ensure that non-bank TASE members are able with a high degree of certainty to conduct while maintaining the ability to service all short-term liabilities through the timely liquidation of assets at their disposal. TASE capital adequacy requirements permit non-bank members to take on an additional risk only if they either offset that risk by reducing another risk, or by increasing equity. The current capital adequacy regime described below was introduced at TASE earlier in 2011 and members are currently in a transition period to the new regime. Members who on 30th June 2011 were not in compliance with the requirements on capital and net unencumbered liquid assets have until 30th June 2012 to comply. TASE has prescribed two milestones to ensure such members are converging on the new requirements. During the transition period, any member that is not yet complying with the new requirements is prohibited from allowing its current capital level to fall. The initial and ongoing capital requirement is set out in the TASE Regulations, Part 1 – Chapter II, section 5(e). The minimum initial equity capital is set at the higher of : NIS 20.6 million (the rule provides for an amount NIS of 16.5 million linked to the Dec 2000 C.P.I.) or an amount calculated which is the sum of: operating risks; and financial risks. The formulas for calculating operating risk and financial risk are set out in detail in sections 5(c) and 5(d) of the TASE Regulations, Part 1 – Chapter II (pages B5 – B25). Broadly speaking: operating risk is calculated as a function of the value of client assets held and trading volumes, with different weights being assigned to each component of operational risk; financial risk covers risks engendered in the extension of credit to clients; and in proprietary trading activities (including but not limited to derivatives trading, REPO transactions, short sales, underwriting obligations; the holding of other, (i.e., fixed and intangible) assets. After an entity meets the initial minimum equity capital requirement, its capital requirement will vary in line with changes in operating risk and financial risk. The member must continue to meet the minimum equity capital requirement. Capital requirements above this minimum level may be met by equity capital or secondary capital (long-term debt that may not be repaid within the short term, provided that this debt complies with conditions set out in the regulations). The regulations provide sliding scale as to what proportion of debt can be used as secondary capital, with 100 percent of loans for longer than 5 years being recognized, and (from 1 January 2012) 20 percent of 1-2 year loans. There is no limit to the proportion of secondary capital that can be used for this purpose. *Liquidity requirements*: In addition to these capital requirements, non-bank members are required to hold a prescribed amount of net unencumbered liquid assets. The total value of assets that must be so held is calculated as the sum of amounts based on the member's short-term liabilities and long-term liabilities that are callable in the short term, that part of long term loans received by the member that are not recognized as secondary capital, the amount of operating risk, other client-related liabilities and the amount of financial risk (TASE Regulations, Part 1 – Membership s.6). They are also required to have the capacity to examine and ascertain compliance with its capital requirements on a daily basis. A member must maintain net unencumbered liquid assets in an amount of not less than the sum of all the following amounts: the sum of the member’s short term liabilities that are payable in the short term, including long-term loans repayable in the short term; the amount of the part of long term loans that may be recognized as secondary capital but is not

recognized as secondary capital;
the amount of the member's operating risk;
the amount of the financial risk inherent in other credit and guarantees given by the member to its customers;
the amount of the financial risk inherent in the member's own account trading in derivatives, and repo transactions, short selling activity, underwriting activity, and other financial obligations (that is, including the member's off balance sheet liabilities),

Insurance: TASE members are required to carry insurance, which can function as protection against legal risk. The requirements include obligations to carry professional liability insurance. This and other risks that must be insured against are listed in TASE Regulations, Part 1 – Membership, section 6D).

Risk-sensitivity of capital requirements

ISA licensees

Because of the nature of licensees' activities, the protection which it must hold against ongoing risks is focused primarily on insurance.

The level of insurance required to be taken out by advisers and marketers is flat. For individuals it currently stands at NIS 761,000 and for companies at NIS 1,523,000.

For portfolio managers the insurance cover required is sensitive to the value of client assets under management by the portfolio manager for all its clients (see table below)

Value of total managed assets	Minimum insurance required (expressed as a percent of total managed assets)
Not more than NIS 5,167,000	Higher of 9 percent or NIS 1,269,000
NIS95,167,000 to NIS380,667,000	Higher of 5 percent or NIS8,565,000
NIS380,667,000 to NIS761,334,000	Higher of 4 percent or NIS19,033,000
Over NIS761,334,000	Higher of 3 percent or NIS30,453,000

An alternative to this requirement is available: if the company's capital is at least NIS 10 million or if it has deposited a bank guarantee or cash or securities in favor of its clients in the amount of at least NIS 3 million, a portfolio management licensees is entitled to take out insurance of not less than NIS 30 million. This alternative is subject, however, to verification by the portfolio manager's board of directors that the insurance coverage and terms of the policy are sufficient to allow the portfolio manager to meet all its insurance obligations under the Investment Advice Law.

Insurance may be replaced by bank guarantees or asset or cash deposits (bank guarantees and asset or cash deposits referred to as hereinafter "collateral"). The Equity and Insurance Regulations set out the applicable collateral amounts, which are lower than the required insurance coverage.

Advisers and marketers are permitted to replace up to two thirds of the insurance coverage with collateral in an amount equal to one third of the insurance coverage being replaced.

A more complicated formula is used to determine the extent to which portfolio managers can substitute collateral for insurance cover, based on the size of assets under management. As for other licensees, some insurance cover must in all cases be used.

Collateral must be deposited by the portfolio manager in a trust account held by an attorney or CPA. Similarly bank guarantees must be in favor of an attorney or CPA, who will liquidate them on behalf of clients a court ruling or a compromise agreement or arbitration decision that has been given the

	force of a court judgment. *TASE members* The capital requirements described above are risk-sensitive and the amount of capital required, and liquidity requirements, vary according to risk, including market risk, credit risk and operating risk. **Orderly winding down** *ISA licensees* There are no specific capital requirements for ISA licensees that could serve as a buffer and facilitate orderly winding down of a licensee. The insurance and collateral requirements described above are designed to allow the licensee to absorb losses. Regarding disruption to the orderly functioning of the market, since a licensee does not itself hold client assets there is little risk of any serious disruption should a licensee fail. *TASE members* The capital and liquidity requirements described above are designed to create a mechanism to allow a TASE member to absorb losses. If the TASE member is also a member of the TASECH, the participants' risk guaranty fund can be used to ensure trading continuity. **Record keeping and reporting** *ISA licensees* There is no express requirement for licensees to maintain updated records of net capital or exposure levels for the purpose of adjusting capital adequacy. Under its general authority to receive regulatory information from licensees, the ISA is able to require a licensee to disclose its current capital at any time. The same authority applies to insurance and collateral. When the licensee is a corporation, its annual report to the ISA must include an accountant's confirmation regarding the fulfillment of the minimal capital requirements as well as the actual capital level at the preceding year's end. A number of periodic and immediate reports must be provided to the ISA in relation to insurance and collateral. Annual reports must be accompanied by a report from a CPA confirming their accuracy (for company licensees company, the company's auditor must sign the report). A significant deterioration in capital levels must immediately be reported to the ISA if it involves the capital level falling to below the regulatory minimum. (Investment Advice Law, Section 27(c)). *TASE members* Each member is required to carry out a daily examination that it is complying with capital and liquidity requirements. These daily examinations are extremely detailed covering all the elements used to calculate capital requirements. They must be documented in a prescribed format and kept for at least 7 years (TASE Regulations, Part 1 – Membership, s.6B). Non-bank members are required to report to TASE, detailing all aspects of the capital and liquidity requirements set out in the TASE Regulations. Appendix D to the TASE Rules, Part 1 – Membership, contains the templates of the table to be used by each member when providing this information. There are two tables: a summary of the equity levels and changes thereto since the last such report (Appendix D1, pages

	D70-D71); a detailed table in which the member specifies all the figures used in calculating the various component risk factors which determine the capital requirement. The format of the table mirrors closely the requirements set out in the TASE Regulations and contains every figure that is used in the calculation of capital adequacy and shows how this was reached (Appendix D1A, pages D72-D106). The above information must be attached to the annual and three interim reports which are due quarterly. The same level of detail is required for all four periodic reports. The annual report must be filed with TASE within three months of year end and the interim reports within two months of the relevant quarter end. The tables themselves are signed by two of the member's management team. They are attached to the annual or interim financial statements under a prescribed cover letter signed by directors of the member. As long as capital requirements are met there is no reporting requirement in addition to the annual and three interim reports. The TASE may demand at any time to see the daily tables so compiled. A reporting requirement does arise if there is any failure in compliance with capital requirements. This stems from a general requirement to report any breach of TASE Rules and TASE Regulations (TASE Rules, Part 1 – Membership section 16(d)). However, a deterioration in capital levels that does not breach the capital requirements is not required to be reported. **Independent audit** *ISA licensees* The annual financial statements of a corporate licensee must be audited. If the auditor's opinion contains any deviation from the standard auditors' text including reference to any special matter or emphasis it must be provided to the ISA. The ISA may at any time also require a licensee to deliver the financial statements to which the auditor's opinion relates. The IA Equity and Insurance Regulations require that the reports detailing the insurance and collateral held by the company be audited. In the case of a licensee that is an individual, a report by a CPA confirming the reports' accuracy must be attached.] *TASE members* The annual summary of equity levels and changes to them, as well as the annual detailed table showing how capital requirements have been calculated, must be audited by independent auditors. Auditors must supply a separate opinion focusing specifically on this data (TASE Regulations, Part 1 – Membership section 25(a)(4)). A member's annual financial statements must be independently audited and an opinion provided. In addition, the independent auditor must provide certification of the accuracy of the details concerning a member's holdings in companies not traded on an exchange. The prescribed text that independent auditors are required to use in relation to financial statements (Appendix E, page D118) also contains specific declarations in addition to its opinion regarding the financial statements. In the prescribed text the auditor states that, in addition to its audit of the financial statements it has carried out an audit of the member's compliance with TASE Rules and TASE Regulations in the course of which it did not find any failings in a number of areas, some of which are directly relevant to maintenance of the required capital levels and liquid assets. These confirmations by the auditors cover: the member’s accounting system, including the processing of financial and trading entries, confirmation that net unencumbered liquid assets are in fact unencumbered; and proper compliance with the rules on credit, guarantees and collateral, use of customers' cash

	balances and charges over assets and capital. **Monitoring by regulator** *TASE members* The quarterly and annual reports form the basis of TASE reviews of capital levels. It routinely carries out in-depth reviews of these detailed reports including non-bank members' secondary capital. There have been only a small number of cases since 2008 of levels falling below the required levels. In all cases, the members involved were instructed to bring them into line with the requirements which was done without further action being required. There were also a couple of cases in which TASE informed members that the method of calculating their capital levels required adjustment. TASE may impose fines on a member for failing to meet capital requirements, but this is very unusual. **Regulator's powers of intervention** *ISA licensees* The ISA can impose conditions on a license at the time the license is issued. Following initial licensing, the Investment Advice Law authorizes the ISA to revoke or suspend a license (section 10), but it does not specifically state that it may change the terms of the license. It is not the practice of the ISA to alter the conditions of a license once issued. The ISA would be more likely suspend a license if it believes that the licensee's capacity to fulfill its obligations is in jeopardy or when it fails to meet minimum requirements. Since the business models of licensees means that there is very little risk exposure of clients or the market generally to failure of a licensee, suspension or even cancelation of a license does not raise major concerns in terms of financial stability. *TASE members* If a member's capital levels fall below those required by the TASE Rules, the TASE board may take a number of courses of action: prohibit a member, for such period as it decides, from engaging in certain transactions or certain types of transaction in securities, in trading on or off TASE (requires simple majority of board members present); suspend a member from TASE membership for such a period as it prescribes not exceeding six months; (requires 75 percent of board members present); revoke a member's membership (this requires a vote by at least 75 percent of board members present at a meeting). These powers derives from the general power granted the board in relation to any failure to fulfill the requirements set out in Chapters II to IV of the TASE Rules. (TASE Rules, Part 1 – Membership s.75(g), s.76(g) and s.78(f)). If a member's capital deteriorates in a manner which, although it does not fall below minimum requirements, raises concerns, the power of the TASE board to intervene is based on its power to intervene in any situation in which its fears that a member might not perform its obligations or pay its debts. In these circumstances the same three courses of action are available with a simple majority of Board members being sufficient in all three cases (TASE Rules, Part 1 – Membership s.75(d), s.76(d) and s.78(c)). There have been cases of TASE interventions in these circumstances.

	Risks from outside the regulated entity *ISA licensees* The capital framework does not address risks from outside the regulated entity. *TASE members* The TASE capital and liquidity requirements take into consideration not only the activity of the TASE member but also of its securities subsidiaries ("supervised companies"). A supervised company is defined in section 1 is a company in which a non-bank member holds 50 percent or more of the share capital or voting rights, that engages in investment portfolio management, investment consultancy, investment marketing and the execution of transactions for others in securities, including derivatives, whether or not traded on the Stock Exchange. Chapter IX of the TASE Rules, Supervised Companies, sets out the general requirements on this topic, amongst them the capital and net unencumbered liquid asset requirements with which supervised companies must comply (TASE Rules Part 1 – Membership s.85(c)). The details of these requirements are set out in the TASE Membership Regulations (s.11). The capital requirements are broadly similar to those for members with some adjustments. The net unencumbered liquid asset requirements are simply cross-referenced to the member's requirements and are identical. Off-balance sheet risks are taken account of within the calculation of net unencumbered liquid assets. The full value of such risks are included in the capital calculation (TASE Rules Part 1 – Membership s. 5(h)(5)). The term "non-balance sheet liabilities" is defined in section 1 of the TASE Rules to mean liabilities that are not included in the non-bank member's financial statements, including the amount of the financial risk inherent in guarantees provided by the non-bank member in favor of its customers, the amount of the financial risk inherent in liabilities of the non-bank member's customers to the non-bank member by reason of their activity in derivatives and in REPO transactions.
Assessment	Broadly implemented
Comments	The capital requirements imposed on ISA licensees and non-bank TASE members appear adequate for the functions they are designed to perform. The assessor has some concerns about the fact that the TASE rules provide only for quarterly and annual reports on capital levels. Prima facie, this appears to be insufficient to enable TASE to monitor capital levels. However, TASE's level of supervisory engagement with non-bank members means that in practice it will become aware if a member's capital position is deteriorating without needing to rely on the periodic reports. Similarly, for ISA licensees, the obligation to report a decline in capital only occurs when capital has fallen below the required minimum. It would be desirable for there to an early warning point triggered before capital has fallen below the minimum required. The assessor accepts, however, the more limited role capital requirements play for licensees that are not permitted to hold client funds or assets, and notes the role played by the insurance requirements. The capital requirements set for ISA licensees do not address risks from outside the regulated entity. Though this is unlikely to give rise to serious problems given the nature of these licensees' activities, it does not meet the standard set by the IOSCO principles. Due to the specific regulation of licensees, the ISA sees no need to change capital requirements in this respect and impose unnecessary burdens on the industry. The fact that TASE allows member firms to include non-subordinated debt as capital makes its capital rules out of line with those of other jurisdictions. It creates a potential incentive to increase

	longer term leverage (since it counts as regulatory capital) and may undermine the objectives underlying securities regulation capital regimes. Hence, consideration should be given to excluding non-subordinated long-term debt from the definition of capital for this purpose. However, it is recognized that in practice the use of secondary capital is very limited.
Principle 23.	**Market intermediaries should be required to comply with standards for internal organization and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters.**
Description	**ISA licenses** The internal management and supervision of licensees is subject to ISA supervision under s28(a) of the Investment Advice Law. Section 28(b) empowers the ISA to issue instructions relating to the manner in which a licensee, an office holder in a licensee and anyone employed by a licensee must conduct itself. Section 1.1 of the ISA's IA Internal Procedures Directive[13] requires a licensed corporation to establish procedures to ensure compliance with the provisions of the law and the regulations by the corporation, its officer holders and workers, and requires the corporation to act in accordance with these procedures. *Management and organizational structure* In addition to the responsibilities placed on senior managers (see below), a licensed corporation must have a person responsible for supervision of internal procedures and controls. *Internal controls* The IA Internal Procedures Directive contains a non-exhaustive lists of ten areas for which internal procedures must be established. Required procedures include (among other things) ensuring staff are aware of relevant legislative provisions law and required work procedures, are adequately trained and subject to an internal enforcement regime; conflicts of interest; and the handling of client complaints. Each internal procedure must meet detailed standards including operating rules; nomination of the person(s) responsible for its implementation; mechanisms for supervision and inspection to ensure proper implementation; review; and procedures for reviewing and updating. *Senior management responsibility* The responsibility of senior management for ensuring the maintenance of appropriate standards of conduct and adherence to proper procedures by the entire firm is addressed in two ways: under the IA Internal Procedures Directive, each internal procedure must be approved in writing by the CEO and discussed and confirmed by the board of directors. The same applies to each revision of an internal procedure (section1.4); under the provisions of the Investment Advice Law, the CEO carries personal liability for administrative offenses (offenses dealt with by the administrative enforcement process). The same rule applies to partners (other than limited partners) in a licensed partnership (section 30(c) and section 40 of the Investment Advice Law). The CEO and the Board can also be personally liable for criminal violations.

[13] The Directive to Licensed Corporations Concerning the Duty to Determine Work Procedures for their Operation and Management under the Investment Advice Law.

	The CEO and directors of a corporate licensee (and partners in a partnership licensee) are prima facie liable for administrative offenses, whenever the corporation or an employee is found to have committed an administrative offense. It is a defense against either administrative or criminal liability if the a CEO, director or partner can establish either that the offense was committed without their knowledge and they were not in a position in which they should, or could, have known about it; or that they took all reasonable measures in order to prevent the commission of the offense. In August 2011, the ISA published Criteria for Recognition of an Internal Enforcement Program in the Securities Field setting out criteria for the recognition of an internal enforcement program as a defense claim against potential enforcement procedures. *Evaluation of internal controls and risk management* Until November 2011, there was no legal or regulatory requirement that licensees have an independent evaluation of internal control and risk management. New legislation (Corporate Governance for Fund Managers and Portfolio Managers Proposed Law (legislative amendments) of 2011) enacted in November 2011imposes on large portfolio management licensees[14] an obligation to have an evaluation of their internal controls and risk management and their internal enforcement programs. Section 24f(2) of the new law requires boards to approve internal controls and internal enforcement programs; section 24h requires the audit committee to evaluate internal controls find faults and suggest remedies to the board; and section 24i requires the internal auditor to examine the adequacy of procedures for ensuring compliance with the requirements of the law and in particular internal controls. The amendment was approved into law by the Knesset on November 8, 2011 and published on November 16, 2011. The amendment becomes effective six months from its official publication date (i.e., late May 2012). In addition, under the ISA guidelines on effective internal enforcement program a regulated entity, including portfolio management firms, must perform a compliance survey that examines the internal procedures and how they assure the companies compliance with the applicable laws and regulations. This survey should be carried out every 4-5 years (see section 7 of the guidelines). **TASE members** TASE Rules and Regulations set out detailed requirements for the management and supervision of the business of TASE non-bank members. Bank members are not covered by these rules on the grounds that they are subject to appropriate supervision in their capacity as institutions regulated by the banking regulator. *Management and organization structure* Requirements for non-banks members of TASE vary between those members that are publicly traded corporations and those that are privately held corporations. The TASE Rules set out basic corporate governance provisions that apply to privately held non-bank members. These rules bring the corporate governance requirements for private corporations to the standard required for listed corporations generally. They include rules relating to:

[14] Defined as portfolio management companies that have either over 50 clients and client portfolio assets with a total value of over NIS 5 billion, or over 1,000 clients.

	Board structure: a member's board must consist of at least three directors, at least one of whom is an external director (TASE Rules, Part 1 - Membership, section 6(e)). If an external director resigns, the member must provide TASE with a copy of his or her reasoned, written resignation within seven days of receiving it and, at the request of TASE, must provide further details of the circumstances surrounding the resignation. (TASE Rules, Part 1 - Membership, section 6(g)). The chairman must not be the CEO (TASE Rules, Part 1 - Membership, section 6(f)). *Audit committee*: The board must appoint an audit committee from amongst its members. At least one external director must sit on the audit committee. The TASE Rules also apply various restrictions on the qualifications of members of the audit committee (TASE Rules, Part 1 - Membership, section 6(h)). *Internal auditor*: An internal auditor must also be appointed. The TASE Rules have imported the provisions of the Companies Law which apply to public companies for this purpose (TASE Rules, Part 1 - Membership, section 6(i)).TASE Regulations prescribe the subjects to be covered and scope of the internal auditor's duties, the manner of performing these duties and the minimum number of working hours per year allocated to this, the number of hours being proportionate to the equity of the member (TASE Regulations, Part 1 - Membership, s.16A). There must be a clear division of responsibilities and separation of positions between the front office, the back office, the department managing risk, the risk management control function and the internal auditor. *Internal controls* TASE Rules require a member to have a number of specified management positions: *Credit Officer*: Must be directly appointed by the board and may not hold any other position in the member which may create a conflict of interests pertaining to the control of credit and collateral or would otherwise affect the credit control function (TASE Rules, Part 1 Membership, section 5(n)). *Risk Officer*: Must be directly appointed by the board and may not hold any other position except Credit Officer and/or Compliance Officer (and then only subject to further conditions) (TASE Rules, Part 1 Membership, section.5(o)(2)(b)(1)-(4)). The Risk Officer is directly subordinate to the CEO (TASE Rules, Part 1 Membership section.5(o)). *Compliance Officer*: Must be directly appointed by the Board and may not hold any other position in the member company that may create a conflict of interest pertaining to compliance or otherwise affect the compliance function. This position reports directly to the CEO (TASE Rules, Part 1 Membership section.5(p)). A compliance officer cannot be removed from office without his or her consent, unless decided by the member's board of directors, after it has obtained the views of the audit committee and after the compliance officer has been given a reasonable opportunity to state his/her case to the board and the audit committee (TASE Regulations, Part 1 – Membership s.25(r)(d)). The internal auditor is responsible for examining compliance with TASE Rules and the law as well as compliance with internal operating procedures. He or she must also implement the internal audit plan of the member. The accounting system used by the member must permit every entry to be traced to its source and the relevant documentation. The minimum amount of data that the accounting system must contain is prescribed. The accounting system must undergo testing at least once a month. Customer accounts must be updated after the close of trading every day. Correcting entries may not delete the original errors. Procedures for credit control must set out the mechanisms for applying credit limits to customers and ensuring collateral is properly obtained. The member's central system must automatically apply blocking and warning mechanisms and detailed limitations in relation to the extension of credit as set out in section 15 of the TASE Rules, Part 1 - Membership.

	Separate risk control procedures relating to each type of risk to which a member is subject must be applied. The member must set up systems to manage and control risk, define the staff and activities in each case to which the procedures apply, establish detailed operational rules and periodically review the risk controls. The member must also train all staff affected by internal risk controls. Whenever a new activity is taken on by the member it is subjected to a risk analysis which evaluates the exposure it creates and sets out the mechanism by which such risk will be controlled, such as hedging requirements, automatic warnings and segregation of positions. The risk officer must provide monthly reports to the member's board on risk control activity, which include details of unusual incidents, changes in procedures and any breach of standard procedures and how this was addressed (TASE Regulation, Part 1 – Membership s.25N(b)) A non-bank member's compliance plan must be discussed and annually approved by the member's board. The plan must set out the full set of laws, regulation and TASE Rules and Regulations that the Compliance Officer must consider in the course of his or her work and must contain specified detail. To ensure the Compliance Officer is able to fulfill his or her duties, the TASE Regulations require that he or he have access at all times to all the member's divisions and officers, and to all the member's records and information. TASE Rules also require the member's board to set policies and procedures which must then be implemented internally. Specific areas that must be covered include policy and procedures for collateralizing securities portfolios to secure credit or guarantees extended to clients (TASE Rules Part 1 – Membership s.15(f)); investment policy regarding the member's proprietary holdings (TASE Rules Part 1 – Membership s.17B); approval of the extension of credit, receipt of collateral and short sale procedures (TASE Rules Part 1 – Membership s.24D); trading practices and mechanisms for trading in overseas markets (TASE Rules Part 1 – Membership s.24H(a)). All internal procedures and work plans designed to ensure the maintenance of appropriate standards of conduct within the member must be approved by the board and the senior control officers. All internal control activities and events must be reported to the board and the audit committee and senior management. *Senior management responsibility* TASE rules make senior managers and directors responsible for setting policies and receiving reports the compliance officer. This does not, however, extend to strict liability for acts carried out by the member in which a particular senior manager played no part. The TASE Rules clearly state that members are liable for proper implementation of the TASE Rules and the TASE Regulations by its senior management, but does not also state that the senior management, by virtue of their positions, are liable for the failings of the member. *Evaluation of internal controls and risk management* Each TASE member is subject to two types of periodic survey: a risk survey and a compliance survey. These must be carried out by a professional entity with suitable qualifications. The TASE Regulations stipulate that the risk survey may not be carried out by the Risk Officer, there is no requirement that surveys be carried out by external professional entities. *Risk survey*: The risk survey must be carried out at least every three years and must identify, evaluate and quantify the risks engendered in the member's activity as well as examine the manner in which the member manages and controls those risks. The risk survey must be considered by the member's board within 45 days of its conclusion. The member must prepare a report (known as an exposure paper) based on the external risk survey. The exposure paper must include detailed documentation of all risks and the exposure and of the risk management and control mechanisms employed by the member (TASE Rules Part 1 – Membership, s.24K(f) and (g)). Detailed requirements regarding what the risk survey must cover and how it must be utilized by the member

	are set out in TASE Regulations Part 1 – Membership s.25O and 25P. *Compliance survey*: The compliance survey must be designed to ascertain that the member is ready to implement and perform its duties as articulated in the applicable laws, rules and regulations. This also must be discussed by the board within 45 days of completion. The compliance survey must be carried out at least once every four years and, among other things, must serve as the foundation of the member's compliance plan. The compliance survey must be carried out by a suitably qualified professional person but there is no requirement that this be an external entity. (TASE Rules Part 1 – Membership, s.24L(c)). The full requirements regarding the compliance survey are set out in TASE Regulations Part 1 – Membership s.25T. There is no requirement to supply either the risk survey or the compliance survey to TASE. In practice, TASE may demand to see the surveys or the exposure paper or compliance work plan that are based upon them at any time. **Customer protection - ISA licensees** *Investor complaints* A licensed corporation must establish a procedure for handling client complaints. This must address at least: appointment of the person responsible for handling client complaints; determination of the manner of reporting client complaints; specification of the mechanism for handling client complaints, including the drawing up of memoranda, recording the manner in which the complaint is handled, how discussions with the client should be carried out and establishing the timetable for the stages of handling client complaints. (IA Internal Procedures Directive section 2.8) *Client funds and assets* Under Section 22 of the Investment Advice Law, a portfolio manager must segregate client assets from its own assets and those of other clients. It must also create and retain separate records of assets held for each customer. The same rules apply to client funds. The portfolio manager must also segregate the execution of transactions on behalf of clients from proprietary trading and must credit and debit client accounts on the day that transactions are settled. Under Section 23 of the Investment Advice Law, portfolio managers are also prohibited from using client funds or assets other than in strict compliance with their agreement with the client and the power of attorney granted to it by the client. In Israel the portfolio manager operates in the client accounts through a power of attorney. The question of the need to transfer positions or protect client assets in the event of the portfolio manager's insolvency does not arise. Investment advisers and marketers are not authorized to handle client assets or cash. **Customer protection – TASE members** *Investor complaints* TASE members must inquire into written complaints they receive from their customers and retain documents relating to its handling of those complaints (TASE Rules Part 1 – Membership, section 37). In addition, customer complaints are one of the factors which must be taken into account when preparing the annual compliance work plan (TASE Regulations Part 1 – Membership section 25S(d)).

	Client funds and assets A combination of the TASE Rules and the operational structure of the TASE clearing houses provides protection of ownership rights in TASE-traded client securities traded. TASE members are required to maintain separate accounts in their own books for each client and to segregate its own assets from those of its clients. In addition, the TASE Rules require a member to hold client securities in trust for the benefit of its clients. As a result of the trust arrangement, client assets are protected and do not fall into the pool of assets available for distribution to creditors in the event of the member's insolvency. Instead they are remain the property of the member's clients and are not subject to third party claims. Twenty of the 26 TASE members are also TASECH members. Under the provisions of the Clearing House By-laws, Clearing House members are required to maintain separate accounts at the Clearing House for clients and proprietary assets. They may divide client accounts into separate sub-accounts for some or all individual clients if they so choose, subject to certain conditions (By-laws, Part 2, Ch. 4, section 2). Where a TASECH member provides clearing services to a non-clearing TASE member, the TASE member must undertake to comply with all the provisions of the By-laws that apply to it (these provisions are set out in Appendix 3 of the By-laws) and is treated by the Clearing House member like a normal client (By-laws, Part 2, Ch. 1, s.2(a)). The prohibition on the use of customer assets is regarded as implicit in the requirement to segregate all client assets from the member's assets. For example, members may not lend client assets or use them as collateral for their own obligations or those of other clients All positions in securities are cleared and settled through TASECH, and are thus available for transfer within short timeframes. All client transactions must be carried out in the TASE market and be settled to the account at TASECH used by the member. **Client information, know your client and suitability rules – ISA licensees** Section 12 of the Investment Advice Law requires license holders, to the extent possible, to adapt the advice, marketing, and types of transactions they execute for a client in accordance with the client's needs and instructions after clarifying the client's financial position (including the financial instruments it already holds), the goals of the investment and other circumstances relevant to the provision of the service, to the extent that the client agrees to give such information. This requires the licensee to make inquiries of a client about these matters. The requirement only applies to the extent that a client agrees to provide the information. A licensee may provide a service without this information when the client has decided not to provide it. This information must also be set out in the written agreement with the client that must be signed before the provision of services begins (section 13 of the Investment Advice Law). These requirements are expanded on in an ISA Directive, Directive to Licensees in Relation to Ascertaining the needs of the Client, Matching Service to Needs (pursuant to section 12 of the Law and Recording of Details pursuant to section 13 of the Law) New Version, 2010. *Disclosure requirements* Specific disclosure requirements relating to the clients ability to make an informed investment decision apply. An investment adviser and marketer must provide its client with proper disclosure of all matters of material importance in relation to the service he provides and any proposed transaction (section 14(a) of the Investment Advice Law). Where a licensee becomes aware of a conflict between the interests of the licensee and its client,

	full disclosure must be made in writing or by telephone and a full record kept of the disclosure (section 15(a) of the Investment Advice Law). Transactions involving special risks require disclosure to the client. Special risks include short sales and securities lending; and futures, option and structured products. Where a transaction involves any special risk, an adviser or marketer must inform the client of the nature of the risk (Investment Advice Law, Section 18(a)). A portfolio manager may not execute a transaction with a special risk until the client has approved the specific transaction or unless the client has previously approved the specific type of transaction. *Anti- money laundering know-your-client rules* In addition, portfolio managers must comply with the know-your-customer provisions set out in anti-money laundering and prevention of terrorism financial legislation. These are set out in the Anti-money Laundering (Identification, Reporting and Record Keeping Obligations of a Portfolio Manager for the Prevention of Money Laundering and Financing of Terror) Ordinance, 2010. These requirements do not apply to advisers and marketers since they do not handle client assets or cash. **Client information, know your client and suitability rules – TASE members** A TASE member may only provide management or advisory services if it has been separately licensed for that purpose under the Investment Advice Law. That law applies to these services and compliance with it is monitored by the ISA. TASE Rules and TASE Regulations do not deal with the issue of client information; know your client and suitability rules. The Anti-money Laundering (Identification, Reporting and Record Keeping Obligations of an Exchange Member for the Prevention of Money Laundering and Financing of Terror) Order, 2010 applies to TASE members. It follows closely the requirements for portfolio managers and the ISA is directly responsible for monitoring compliance with it. Under TASE rules disclosures that a member must supply to its clients are purely historical in nature (e.g., statements of account and of transactions executed etc.). **Customer access to terms and conditions of services** *ISA licensees* Section 13 of the Investment Advice Law requires a written agreement between a licensee and a client which must be signed prior to the provision of any services. The agreement must set out a client's needs and instructions for providing services of investment advice, investments marketing or management of an investment portfolio. The agreement must include : the client's identifying details and information; the client's needs and instructions as specified in section 12; the wage and reimbursement of expenses for which the client will be charged and the manner in which they will be calculated; a provision which states that the client may cancel the contractual relationship with the licensee at any time; a provision which indicates whether or not advice or marketing services may be provided over the telephone; a provision which states that the client is aware that the duty of confidentiality that is imposed on the licensee is subject to his obligation to provide information as required by law;

	for a licensee who is a stock exchange member, a provision stating that the client is aware that the agreement is subject to a TASE member's duties in accordance with the TASE rules. A portfolio manager's agreement with a client must contain additional information, including: A power of attorney which specifies the scope of the authority and discretion granted to the portfolio manager, including an indication of whether the investment portfolio will be managed as a blind trust or otherwise; Whether the manager will be permitted to obtain credit for the client and the conditions thereof, or the absence of such a possibility. Provisions regarding the types of securities and financial assets which will be included in the investment portfolio and the percentage of each type in relation to the portfolio's value, or a provision indicating that these will be determined at the portfolio manager's discretion; A provision authorizing the manager to purchase securities, options or future contracts at a higher price than the known stock market price at the time of the purchase, as well as the authority to sell them at a lower price than the known market price at the time of the sale, or a provision specifying that the manager has no authority to make such purchase or sales; Regarding a portfolio manager which is a corporation that is affiliated with an institutional body or a marketing agent, and regarding a portfolio manager that is engaged in investment marketing – the agreement shall include the details which are required to be brought to the client's attention pursuant to section 16a(a). *TASE members* Before the provision of any services can take place, a TASE member must complete a written agreement with each client and deliver it to the client. Any amendments to it must also be delivered to the client before they take effect. The TASE Rules set out detailed requirements about the issues to be covered in the client agreement. These include provisions dealing with: commissions, management fees, reimbursement expenses and other financial charges and the method of computing them; telephone orders; the extension of credit to the customers and the terms thereof or the exclusion of such possibility; the holding of securities under the member's control and the management of the customers' cash account; the types of services and financial instruments in respect of which the customer wishes to receive services from the member (TASE Rules, Part 1 – Membership s.29). **Internal compliance monitoring – ISA licensees** The Internal Procedures Directive applies the requirements relating to compliance on a procedure by procedure basis. It does not contain a specific requirement for a dedicated, centralized compliance officer or equivalent function to be established within licensees. Compliance functions may be carried out by persons who also have other responsibilities. (Note that the ISA guidelines on effective internal enforcement programs do require licensees to have a nominated compliance officer as an integral condition to the validity of the program as a defense in administrative proceedings.) It is worth noting that in practice significant part of licensee services are provided by banks (by licensed bank employees in the branch networks) and under banking regulation, compliance officers are required. TASE members who provide portfolio management, advice or marketing services are also required by TASE rules to have a compliance officer. The Internal Procedures Directive requires a licensee to identify in an internal procedure the person or job function within the licensee that is responsible for supervision of the implementation of the procedure; and the person or job function responsible for the actual implementation of the procedure (section1.6(d) and (e)).

	The Directive also requires a licensee to set out in a procedure, the licensee's internal work practices in order to ensure that all applicable statutory provisions are complied with; that changes to the legislation are examined; and that work practices are reviewed in the light of these changes. (Internal Practice Directive section 2.10). The Directive also requires the licensee to establish: A mechanism for mapping out the provisions of the law and the regulations applicable to the licensee. The work practices that will prevent the violation of law and regulation, including follow up on revisions of legislation and regulations. Rules for carrying out audits to inspect the proper implementation of the work practices prescribed by the procedure. The ISA has examined compliance with these requirements across a large spectrum of ISA licensees, and intends to publish the results of this work. **Internal compliance monitoring – TASE members** The requirement for a compliance officer as well as for a credit officer and risk officer are described above. **Statement of account and information on remuneration** *ISA licensees* Section 26 of the Investment Advice Law requires a licensed portfolio manager to provide each client with a statement of account at least once every three months. Items that must be included are as follows: a detailed statement of the composition of the client's portfolio; cash account balances; direct and indirect remuneration and expenses charged by the portfolio manager including any payment to any person controlling the portfolio management company, any company controlled by the portfolio manager and any person controlled by such a company; a list of all transactions executed for the client since the previous statement, upon which transactions involving special risk and transactions involving an extension of credit to the client are marked. A client may at any time request additional details and the portfolio manager must comply so long as the client's demand is not unreasonable. The ISA has issued a directive on this issued a directive, Directive to Portfolio Managers Regarding Proper Disclosure in a Periodic Report to a Client, expanding on the disclosure requirements of licensees. *TASE members* A TASE member must to provide every client with: notice of every transaction executed for the client within ten days of execution if so required by the client; the transaction statement must provide comprehensive information on price, volume, and fees; a monthly transaction report listing all transactions executed in the client's account including a details of each transaction; monthly notice of the securities and financial instruments held for the customer; any debit balances if the client has been extended credit by the member; if the client's account is managed by a portfolio manager (whether the member itself or another

	portfolio manager), a rate-of-return report, unless the other portfolio manager has notified the member that it supplies the client with this report. Institutional investors may waive or alter the reporting requirements in a written agreement in which they declare that they are aware that the alternative arrangements do not comply with TASE requirements (TASE Regulations Part 1 – Membership s.33-34 and TASE Regulations Part 1 – Membership s.27 – 28C). Under TASE rules the original written agreement signed with all clients must set out the method by which the member calculates and deduct commissions and fees. They do not, however, require periodic disclosure of such commissions and fees to clients. **Books and records** *ISA licensees* Section 25 of the Investment Advice Law sets out the recording keeping obligations of licensees. All licensees are required to keep a record of each instance of giving advice or marketing. Such records must be written, computerized or stored as a sound recording. A portfolio manager must maintain full records of every transaction executed for a client (section 25(a). Records must be retained for a period of at least seven years. Details of record keeping requirements are set out in the Investment Services Law and the Regulations Governing Engagement in Investment Counseling, Investment Marketing and Investment Portfolio Management (Recording of Transactions and Recording of Counseling Activities) Regulations, 5768 – 2007. See under Principle 21. Licensees must have a written procedure dealing with record retention. This must cover not only how they are stored but also client confidentiality and information back-up and retrieval. All records must be in a form that allows full supervision by the ISA. The ISA has extensive powers to demand information and documentation from any licensee including the power to enter licensee premises and seize material if necessary. *TASE members* TASE rules require anon-bank member to keep a set of accounts that comprises both a general set of accounts and a set of customer accounts Both accounting systems must: enable every entry to be traced to its sources and the documentation relating to them. enable a visual printout of all the transactions input to the permanent file no later than the day after the input date. enable a printout to be produced at any time specifying the dates of input to the permanent file (TASE Regulations, Part 1 – Membership s.17). The TASE Regulations set out the minimum data that must be stored in the general accounting system and the customer accounting system (TASE Regulations, Part 1 – Membership s.18). All records must be stored for at least seven years. They must be immediately available for six months and thereafter retrievable within two business days, including upon the demand of TASE or another competent authority such as the ISA (TASE Regulations, Part 1 – Membership s.23)

	Appropriate systems of customer protection, risk management and internal and operational controls *ISA licensees* Requirements for licensees to establish internal procedures are set out in the Internal Procedures Directive. The directive requires internal procedures designed to ensure compliance by the licensee with law and regulations. It requires each compliance function to have a function or procedure to have a named person responsible for its implementation and ongoing implementation. It requires a procedure to establish a mechanism for identifying the provisions of the law that apply to the licensee; a mechanism to ensure work practices will be compliant; and rules for carrying out audits or inspections to ensure compliance procedures are effectively implemented. The Investment Advice Law does not have a general requirement for segregation of key duties and functions. An amendment approved in November 2011 introduces additional corporate governance principles for large portfolio management companies. Amongst the corporate governance rules is a prohibition on the CEO or any person that is directly or indirectly subject to the authority of the CEO or any relative of the CEO holding the position of Chairman of the Board of Directors. *TASE members* The main areas of focus of required internal procedures and controls are in relation to credit exposure and collateral, risk, compliance and the internal audit plan. The obligation of a TASE member under the TASE rules is to ensure compliance with all TASE rules and regulations. This includes relating to the conduct of the member in relation to their clients (Chapter 5 of the First Part of the TASE Membership Rules). For example, the TASE Rules require that a member acts loyally for the benefit of its clients and take all reasonable steps to secure its clients' interests. A member is also required to act faithfully and diligently for the benefit of its clients and may not prefer its personal interests over the benefit of its clients nor the interests of one client over another (TASE Rules, Part 1 – Membership, s.25). These requirements must be included in the work plan of the Compliance Officer including in the plan for training of staff but are not the subject of a specific requirement to create internal procedures and controls. **Conflicts of interests** *ISA licensees* The Investment Advice Law and regulation deal with conflicts of interest primarily through disclosure and client consent rather than by a clear requirement to endeavor to avoid them in advance. If a licensee becomes aware of a conflict of interest between either himself or the licensed corporation in which he works and the client, the licensee must notify the client. The licensee must refrain from carrying out any transaction which involves a conflict of interest, unless the client has agreed to it in advance, in writing or by telephone, in a conversation which must be noted by the licensee. (Section 15(a) of the Investment Advice Law) The Internal Procedures Directive requires the licensee to have an internal procedure which establishes the mechanism to be used by the licensee to manage and supervise conflicts of interest when they do arise. One of the issues that must be addressed is how to minimize conflicts of interest. *TASE members* TASE Rules state that a member must not place itself in a position where there is, or might be, a conflict of interest between its client and itself or between its client and a corporation which it controls or in which it is an interested party (TASE Rules, Part 1 – Membership, s.25(d)).

	The mechanism prescribed if conflicts of interests do arise, or the member is aware that they might arise, is one of disclosure and client consent. The member must immediately disclose the conflict of interests to the client, upon becoming aware that it has or might arise and may not perform any act involving that conflict of interest until it has received the written consent of the affected client. If the member follows this procedure, it is not required to decline to act where conflict cannot be avoided. The TASE Rules provide the option of a partial carve out for institutional investors. A member may execute transactions between its own account and the account of its client who is an institutional investor if it has received a general, prior written consent from the institutional investor to execute such transactions. Such consent must be dated within the calendar year in which the transaction is executed and therefore must be renewed annually (TASE Rules, Part 1 – Membership, s.25(d)).
Assessment	Broadly implemented
Comments	The level of compliance with this Principle is generally high. The fact that a requirement for an independent periodic evaluation of internal controls and risk management processes was only enacted in November 2011 is the only issue that leads to a broadly implemented assessment. This is on the basis that the new amendment will not be implemented until May 2012. Similarly, the assessor welcomes the legislative backing introduced to require segregation of the role of chairman and CEO in large portfolio management companies. Consideration should be given to requiring more systematic segregation of functions (for example, between back office and front office functions in large portfolio managers). Under new proposed custody rules currently being finalized by an inter-departmental committee chaired by the ISA, any intermediary that holds client assets or arranges for custody of client assets with third parties will be required to undergo an audit of such services at least annually. This audit will be carried out by the intermediaries' external auditors and will examine compliance with the new custody regulation. The external auditor's opinion will be required to either confirm compliance or detail the failings found.
Principle 24.	**There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.**
Description	**Plans for dealing with failure of regulated firm** *ISA Licensees* Portfolio managers do not hold any funds or assets in their own account but operate client accounts by way of a power of attorney. The potential for investor loss or systemic damage if a portfolio manager fails is therefore limited. The ISA would oversee any failure of a portfolio manager to ensure the winding up of the company was handled in an orderly way. *TASE members* The actions to be taken in the event of a non-bank member's failure are outlined in an ISA internal procedure of the Supervision of Secondary Markets Department entitled Supervision of the Secondary Market – Work Procedures (the Procedure). Section 4.10 of the Procedure deals with a failure of a Clearing House member to settle a trade. Section 5.5 of the Procedure deals with a more general failure of a non-bank member which causes the member to be unable to fulfill its obligations or function as required. The powers available to TASE to restrain conduct and to ensure assets are properly protected in

	such situations exist as part of TASE's general powers as set out in the TASE Rules and the TASE Regulations. The TASE Board has the power to intervene and prohibit a member from engaging in specific transactions or certain types of transaction in securities, on or off the exchange if it fears or suspects a member might not at a future date perform its obligations or pay its debts. Obviously such powers also exist following an actual failure (TASE Rules, Part 1 – Membership s.75(d)). The TASE Board may also suspend a member or revoke its membership on the same grounds. **Early warning systems** The main mechanisms by which TASE would learn in advance of potential defaults by a member are reports that members must provide and the program of audits and inspections that TASE carries out on members. A number of reporting mechanisms provide TASE with some early warning. In particular, each TASE member must calculate its capital requirement on a daily basis and ensure its compliance. In the event that its capital levels fall below the required, it must immediately report this to TASE. This is pursuant to a general requirement upon members to report any breach of TASE Rules (TASE Rules, Part 1 – Membership s.16(d)). Such an immediate report would also apply to a situation in which the net unencumbered liquid assets that a member must hold have fallen below the required level. (Details of member reporting requirements may be found in the response to Principle 22 question 6 above.) Monitoring of members' open positions in exchange traded derivatives is carried out by the MAOF Clearing House on a daily basis (see Principle 29 below). This daily monitoring is based on the daily open positions reports supplied to TASE by the members and may provide early warning of members being dangerously exposed or, for example, struggling to provide collateral. In the event that TASE is aware of a potential failure and is considering the possibility that it may need to realize a member's contribution to the Risk Fund, it must immediately inform the ISA with details of the possible shortfall (Procedure s.4.10.3). **Regulator’s powers to intervene** The ability of the TASE Board to restrict activity is described above. Section 5.5(4) of the procedures prescribes that in the event that a member is unable to continue to supply services to its clients, TASE will assist its management to make arrangements that will permit its clients to continue to trade through other members. The TASE Rules do not contain a provision conferring upon TASE or the ISA a power to appoint or apply to a court to appoint any type of receiver or administrator. Nor does TASE or the ISA have the authority to take possession or control of assets held by a member or by another on a member's behalf. The TASE Rules do not confer upon TASE the authority to demand that a member makes a disclosure of this kind to the public. The MAOF Clearing House maintains a Risk Fund in order to fulfill its obligations as a central counterparty. Clearing House members participate in the fund according to their relative share in trading activity. The Risk Fund’s money is invested in liquid investments, in government bonds and in bank deposits. The value of the Risk Fund is adjusted twice a year in March and September based on historical turnovers. As of March 2011, the size of the Risk Fund was NIS 797 million, of which at least 25 percent was in cash. **Communication and cooperation with other authorities**

	The ISA has signed a MOU with the Bank of Israel relating specifically to cooperation on payments and clearing (see Annex 3). The MOU includes an undertaking to share information that the other requires in order to fulfill its duties and in particular to cooperate and share information in unusual situations or when the holder of the information foresees a potentially serious risk to the proper functioning of the clearing process (s.5).
Assessment	Fully implemented
Comments	
Principles for the Secondary Market	
Principle 25.	**The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.**
Description	**Israel's secondary markets** *TASE markets* TASE is the only stock exchange in Israel. It started operations prior to the enactment of the Securities Law but obtained a license from the Minister of Finance after the enactment of that legislation and became subject to the supervision of the ISA. The TASE operates an order-driven fully computerized system, TACT, and provides a platform for trading in shares, corporate bonds, convertible securities, treasury bills, indices, derivatives, ETNs and mutual funds. The Board of the TASE includes 7 members appointed by members; 5 external directors whose appointment is subject to the approval of the ISA Chairman; one director appointed by the Ministry of Finance; one director appointed by the Commissioner of the Bank of Israel; a chairman who must be an external director and whose appointment is subject to the approval of ISA Chairman; and a general manager appointed by the board. A secondary professional market for trading privately placed securities is conducted on a platform operated by TASE and for which TASE operates as central counterparty. Only institutional investors are able to trade on this platform. Corporate bonds, convertible bonds for which the underlying asset is a TASE-traded share, and commercial paper are traded on this platform, but only non-public securities can be listed on it. Only the issuer can elect to have its securities listed on this market. The issuing company does not have to comply with the capital and dispersion requirements imposed on regular TASE listings. Orders on TACT Institutional are routed through TASE members, who are responsible for ascertaining the end investor's eligibility to trade on the platform. Transactions are cleared by TASECH, which also serves as CCP for them. OTC blocks trading in TASE-listed and institutional securities is cleared by TASECH but TASECH does not act as CCP for these transactions. In 2010, OTC trading by institutional investors amounted to NIS 2.8 billion (total TASE trading volume was NIS 829 billion, of which NIS 236 billion was in equities) and off exchange block trading accounted for 2.3 percent of TASE trading volumes. *Clearing houses* The two clearing houses (TASECH and MAOFCH) are subsidiaries of TASE and operationally integrated with it. TASECH operates as CCP for all exchange and institutional investor platform transactions. For clearing OTC block transactions, it does not operate as CCP. Further details of the operation of the TASE clearing houses and supervision of them is contained in the note on clearing and settlement systems prepared as part of the Israel FSAP.

Alternative trading platforms

In 2010, the Securities Law was amended to establish a licensing and ongoing regulatory regime for alternative trading platforms (ATPs) in Israel, which is geared towards the retail market. Section 44L defines regulated dealer-operated trading platforms as venues where organized, frequent and systematic trading takes place and excludes transactions resulting from direct negotiations between buyers and sellers. The new regime will come into force shortly, when regulations are finalized. There are currently round 10 ATPs operating in Israel, offering mostly foreign exchange and option products, but not competing directly with TASE traded products.

Authorization of exchanges

The requirements for obtaining a license are detailed in section 45 of the Securities Law as follows:

a stock exchange may only be opened or managed after receiving a license from the Minister of Finance, to be issued after consultation with the ISA.
a license can only be given to a company that does not limit the number of its members and:
its memorandum of association restricts its objectives to the management of a stock exchange;
its articles of association ensure that its profits are used exclusively for achieving its objectives and are not distributed amongst its members. Upon liquidation, the balance of its assets is used for purposes as prescribed by the Minister of Finance; (The provisions of this section only apply once two or more licenses are granted)
it has adopted rules as required by section 46 of the Securities Law, and the rules have been approved by the Minister of Finance after consultation with the ISA, and by the Knesset Finance Committee;
it will manage a stock exchange located in a city in which there is not yet a stock exchange.

Under Section 46 to the Securities Law, a stock exchange must establish rules for its fair and orderly management. TASE rules deal with to membership, listing, the obligations of listed companies, suspension of trading and delisting, market data dissemination, and fees for TASE services.

Authorization of TASE Clearing Houses

Clearing houses are not required to be separately licensed, but are subject to ISA supervision under the Securities Law's special regulatory regime for them (see below).

Supervision of exchange markets and exchanges

ISA supervision of TASE

The ISA's authority to supervise stock exchanges is set out in section 51 of the Securities Law. The ISA's authority relates both to the fair and orderly management of an exchange and to fair and orderly trading on its markets.

The ISA Department responsible for supervision of secondary market has internal procedures which describe the supervisory functions and duties of the department. The procedures specify in detail the scope of ISA supervision of TASE and TASE clearing houses and include: supervision procedures; the obligations of ISA staff who attend TASE decision making forums; working meetings with the TASE; the obligation of the department to ensure the existence of annual work plans for TASE to carry out audits of members; backup and emergency recovery of TASE systems; the reporting obligations of the TASE towards the ISA including the ISA review of the annual TASE work plan, the annual report summarizing the implementation of the TASE work plan, and the annual financial statements submitted by the TASE to the ISA regarding its clearing houses, internal audit reports, protocols of the Audit Committee's deliberations and a risk survey.

ISA supervision of TASE clearing houses

Section 50A of the Securities Law establishes the framework for the prudential regulation of clearing houses, including a requirement for delivery-versus-payment (DVP) for all clearing house activity, a

	requirement that a member's liability to the clearing house be prioritized as senior debt and a requirement that assets pledged to secure members' obligations to the clearing house be protected against third-party creditors. Section 50B of the Law outlines the rule-making authority of the clearing houses and requires that clearing houses ensure stability in their operations, employ the means to manage, prevent and reduce the risks associated with clearing and settlement operations, and have contingency back-up facilities to adequately address emergency situations. TASE audits it operations and has recently engaged a full-time risk officer to implement on-going risk management spanning its entire operations. Under the TASECH and MAOF Clearing House By-laws, all clearing house members must be TASE members of long standing. As TASE members, clearing house members are subject to the prudential regulations, including capital, liquidity and insurance requirements imposed on them by the Bank of Israel (bank members) or TASE (non-bank) members. The requirements are described under Principle 22. Section 50C of the Securities Law gives the ISA broad powers of supervision over clearing houses, including a power to require a clearing house to adopt new rules or amend its existing rules. The stated objective of ISA's supervision is to assure their stability and efficient operation as articulated in section 10 of the Payment Systems Law. The ISA requires that TASE conduct a risk management survey of the clearing house at least every five years. An MOU between ISA and the Bank of Israel (which is responsible for the sound performance of the payments systems in Israel and on their efficiency and safety) aims to facilitate the cooperation and the flow of information between the regulators to promote efficient, fair and unified oversight. The MOU clarifies the scope of responsibilities of each entity and establishes a mechanism for cooperation and the information sharing between the two entities. *Surveillance of trading activity by the ISA* The surveillance of trading activity on TASE is conducted directly by the ISA. The ISA conducts stock watch surveillance on the trading activities and operates a market surveillance and data analysis system using Business Intelligence (BI) technology. These activities are described under Principles 8 and 10. **Securities and market participants** *Market products* TASE's listing rules and regulations must be approved by the ISA and contain criteria for newly-listed companies and products. These rules are detailed in the Second Part of the TASE Rules and in the TASE's Trading Guide Regulations to The Second Part of the Rules. For equity securities, the listing criteria include minimum post-listing equity, a free float requirement, a minimum distribution requirement and in some cases (depending on the size of the company or its status as a research and development company), operating history. Specific rules also apply to debt offerings, convertible securities offerings and follow-on offerings of listed companies, as well as special listing rules that apply to early stage research and development companies. If an issuer does not comply with the equity maintenance rules, TASE gives it a six-month grace period to restore compliance. If compliance is not restored, the company may be transferred to a "maintenance list" and eventually be delisted. The ISA examines the terms of proposed new products and the rights and risk they pose for investors, especially focusing on disclosure requirements. For example, when ETNs were initially listed, the ISA was examined each product and introduced special disclosure requirements related to them.

	Members A representative of the ISA participates in discussions by the TASE board about applicants for membership. Among other things, this enables the ISA to monitor the way TASE implements its membership rules. The TASE Membership and Surveillance Department regularly carries out inspections of both banks (on average 9 per year) and non-bank (approximately 35 per year) members. It has full access to non-bank member books and records. In addition, TASE performs 500 to 600 desk audits of its members each year, with round 75 percent being audits of non-bank members. It focuses especially on non-bank members' compliance with capital rules and on the interaction of member's systems with exchange systems. The Securities Law empowers the ISA to impose ongoing conditions on the TASE and its subsidiary clearing houses. The obligation of a stock exchange to establish rules and regulations is specified in sections 46 and 46A of the Securities Law. All TASE regulations are subject to ISA approval. The ISA is authorized to intervene in the management of the TASE if it is of the opinion that its fair and orderly management has been impinged. It has power to require TASE to amend its bylaws (Section 48) or change the manner in which it is operated (section 51). The TASE Membership and Surveillance Department is responsible for the licensing of TASE members and for the supervision of non-bank TASE members. The Bank of Israel is responsible for the supervision of TASE's bank members. Supervision of TASE members is designed to incorporate considerations of financial stability, the mitigation of operational risks and conduct of business. These include: capital requirements, limitations on margin trading, subjects related to fair and orderly trading, and fair practice from the standpoint of consumer protection. The supervision of non-bank members under the TASE Rules and Regulations applies also to non-bank member portfolio management/advisory/marketing subsidiaries, as well as securities dealing subsidiaries. Or a description of the Supervisor of Banks' supervision of bank member of TASE, see under Principle 21. **Fairness of order execution procedures** Trading on TASE is conducted on the Tel-Aviv Continuous Trading System (TACT)**,** an order-driven fully automated system. The TACT trading system is multi-phased, combining auctions at the opening and close of the trading day and continuous trading conducted throughout most of the day. TACT includes the following functions: order routing, transferring orders from one trading phase to the next, price discovery, sending trade confirmations and market queries. Order priority is determined by price and time. Computerized matching minimizes the risk of failure to operate in a fair, accurate and reliable way. The order priority rules are set in the TASE Rules and Regulations. Execution rules are part of the TASE Rules and Regulations subject to regulatory approval and must therefore be disclosed to the regulator prior to their adoption. TASE posts the rules relating to execution on its website, as well as a tutorial relating to them. **Operational information** Market rules and operating procedures are published on the TASE website. Trading data is disseminated in real time over TASE system to all members and subscribers and posted free to the public on the website after a twenty minute delay. The ISA receives all trading information from TASE on real-time basis; it can reconstruct all trading activity at any time.

Assessment	Fully implemented
Comments	
Principle 26.	**There should be ongoing regulatory supervision of exchanges and trading systems, which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.**
Description	**Trading supervision** The ISA directly monitors trading activity on TASE markets using its BI surveillance and data analysis system. This technology detects potential market abuse and other violations of legislative requirements by tracking unusual price movements and the investment activity of principal shareholders and institutional investors (cross-referencing information in other ISA data bases). It also monitors the compliance of mutual funds to restrictions stipulated in the Mutual Funds Law and to stated fund investment policy. Regulatory oversight is implemented as outlined in the ISA Supervision of Secondary Markets Department's Working Procedures. Much of the ISA's oversight focuses on monitoring prudential compliance, but the ISA also examines TASE's overall performance in preserving and promoting market integrity. As described under Principle 7, ISA representatives are observers in the TASE and clearing house decision-making bodies, including the board and audit committees of TASE and its clearing houses. The ISA oversees TASE rulemaking and management and gives its opinion on amendments to TASE Rules and Regulations. The ISA also checks TASE's compliance with its statutory responsibilities by examining the annual TASE work program and monitoring its implementation. This includes monitoring the implementation of the risk management strategy adopted by TASE; internal TASE procedures relating to trading and clearing operations; and the functioning of TASE's contingency backup system. TASE must report to the ISA the results of in-house periodic testing and inform it of any failure in trading and clearance systems and any damage which may result from such failure. Supervision of the clearing houses focuses primarily on capital adequacy and liquidity compliance, but the ISA reviews on a quarterly basis all planned and pending regulatory activity, important events occurring in the quarter under review and key system failures encountered during this period. It also ensures that TASE conducts a corporate governance assessment of its non-bank members once every three years. Through the BI system, the ISA receives all trading information in real time, such as quotes, orders, transactions, limits, and information about block trading. The information available to ISA is more extensive than that available to market participants, because the ISA receives all trading information while market participants only have access to the three best bids and ask prices in the trading book at a given time. Section 56A1 of the Securities Law provides that, to secure the execution of the Securities Law, the ISA chairman (or an ISA employee authorized by the Chairman) may demand any information or document relating to a transaction involving exchange-listed securities from a stock exchange, exchange member, a trading platform licensee or a portfolio manager, including identifying details of the party for whom the transaction was carried out or of the party that instructed them to carry out the transaction. **Approval of market rules** Under Section 45(b)(3) to the Securities Law, the rules adopted by the an exchange require the approval of the Minister of Finance after consultation with the ISA, and by the Knesset Finance Committee. Section 48 applies this to any subsequent changes to the rules. Section 48 also gives the ISA power to require changes to rules, if it considers that this is needed to ensure fair and orderly management of the TASE. It does so by giving notice to TASE. If TASE does not amend the rules, the Minister of Finance may, following an ISA proposal and with the

	approval of the Knesset Finance Committee, amend them by ordinance. The amendment becomes effective on the date designated in the ordinance. The TASE may not alter or revoke an amendment effected in this manner, other than with the consent of the Minister of Finance. In practice these are rare cases and most amendments to rules are coordinated by the ISA and TASE. **Powers of intervention** By section 51 of the Securities Law, if the ISA is of the opinion that the TASE is operating contrary to its rules or regulations, or in a manner that undermines its orderly and fair operation, the ISA can direct TASE as to the proper manner of operation, after first granting the chairman of the TASE board of directors the opportunity to be heard. Under this section, the ISA can also require the TASE to provide information about the operation of the stock market. The section also empowers an ISA representative to attend all general meetings of TASE, and meetings of its board and committees. The Securities Law does not specifically refer to the authority to revoke stock exchange authorization. However, according to Israeli administrative law, the authority of an administrative authority to grant an authorization (such as a license) also includes its authority to withdraw it (Section 15 to the Interpretation Law). Accordingly, the Ministry of Finance has this authority, which, is likely to be exercised only after consultation with the ISA. Given that TASE is the only exchange in Israel, this power is unlikely to be used in practice and most issues are resolved by continual close contact between the ISA and TASE.
Assessment	Fully implemented
Comments	
Principle 27.	**Regulation should promote transparency of trading.**
Description	**Pre-trade and post trade transparency** Trading on TASE is conducted through an order-driven fully computerized system. TASE's TACT is a transparent trading system, and at any time all participants see the same detailed picture of trading in real time. Post trade information is available to the public through a number of channels such as the TASE website (20-minute delay) and Israeli and international data vendors (real-time). All market participants are provided with the same information and any interested party can access the information. At the end of each trading day TASE publishes trading data on its internet site including: data on the securities listed on the exchange, including the name of the security, the number of the security, the closing price and the volume; the trading volume for each individual security; off-floor block transactions; the total volume of transactions in shares and bonds executed on TASE on that day. For derivatives, the following details are published: the name and number of the derivative; closing price; volume in units and NIS; and open interest. The provisions of this section do not apply to the non-public securities traded on the institutional market platform. Non-trade information is made available through TASE’s information dissemination system in real

	time. It includes comprehensive information about securities other than derivatives, including information specific to the opening and closing phases (including theoretical price and volume information); the best three bids and offers prioritized for trading during continuous trading; intraday high and low prices and so on. For derivatives, pre trade information is available about the volume of orders submitted at each of the three bids and asks prices prioritized for implementation, the base price, and pre-arranged transactions (which are marked with a special symbol). TASE also publishes information about calculated indices, trading volumes of all securities; and other market announcements and information Data on trading in the TACT institutional-only market system is made available through the TASE information dissemination system.
Assessment	Fully implemented
Comments	
Principle 28.	**Regulation should be designed to detect and deter manipulation and other unfair trading practices.**
Description	**Prohibition of market abuse** The Israeli regulatory system prohibits insider trading and other forms of market abuse. *Fraud in connection with securities*: Section 54 of the Securities Law defines securities fraud as: inducing or attempting to induce a person to purchase or sell securities by way of a statement, promise or projection - written, oral or otherwise- which the person knew or ought to have known to be false or misleading, or by concealing material facts; fraudulently influencing the price of securities. Regulated entities or securities investors (as defined in the Securities Law) who engage in any of the following commit an administrative offense: giving a person a statement, promise or projection which they ought to have known to be false or misleading, or concealed material facts, and they ought to have known that their actions might induce that person to purchase or sell securities. engaging in wash trades, matching orders or securities price stabilization. *Misleading Information:* Section 53 of the Securities Law prohibits the disclosure of misleading information in public reports and financial statements, and causing the disclosure of misleading information incorporated in a draft prospectus or in a prospectus. These offences carry criminal sanctions. The seventh schedule of the Securities Law sets out the circumstances in which disclosure of misleading information constitutes an administrative violation. *Use of Inside Information***:** Chapter 8A of the Securities Law deals the use of inside information. Under section 52B, a person who does any of the following makes illegal use of inside information: carries out a transaction in a publicly held or traded corporate security (or carries out a transaction in a different security for which the a public company's security serves as an underlying asset) while in possession of inside information or while the company possesses inside information; while in possession of inside information, delivers inside information or an opinion regarding a company's securities (or securities for which the company's securities serve as an underlying asset) to any party which the person delivering the information or opinion knows, or has reasonable grounds to assume, will make use of the inside information.

	Violations of the prohibition against insider trading carry criminal penalties of up to five year imprisonment form primary insiders and two years for secondary insiders; and (in the circumstances set out in the seventh schedule of the Securities Law) administrative sanctions. *Front Running*: There is no single legislative prohibition against front running. It is dealt with in a variety of ways. Section 52I of the Securities Law prohibits employees of stock exchange members from buying or selling securities for their own account except in the course of trading on a stock exchange. They must submit written orders at least one day prior to the purchase or sale. and must hold their securities in an account in their name at the stock exchange member by whom they are employed. Breach of the prohibition can be a criminal offence and in other circumstances an administrative offense. Individuals licensed under the Advice Law are prohibited from holding or purchasing securities listed in Israel or units in Israeli closed-end units for their own account. An individual who is an investment portfolio manager must not manage investment portfolios for a family member or for a corporation of which they or a member of their family is a controlling shareholder (section 4 of the Investment Advice Law). These prohibitions are intended, among other things, to prevent front running. A licensee's fiduciary duty under section 11 of the Law would also to prohibit front running. Violation of section 11 is subject to administrative sanctions. For mutual funds, section 21 to the Mutual Fund Law places limitations on trading by directors and employees of mutual fund managers which are intended among other things to prevent front running. A violation of Section 21 is a criminal violation or an administrative violation, as circumstances warrant. The duty of fund managers to act for the benefit of the unit holders in good faith (sections 74 and 75 of the Mutual Fund Law) would prohibit front running. The ISA can also address front running in criminal cases by using sections of the Penal Code, such as section 415 (fraudulent acquisition), and Section 425 (fraud and breach of trust in a corporation). These provisions have been used for this purpose. A new law on the Prohibition on the Unfair Use of Information on Securities is in preliminary legislative stages. An exposure draft is being circulated for public comment. The proposed law has two objectives: prohibiting front-running by asset managers and their employees. It is designed to establish a unified and comprehensive approach to front running to remedy the current piecemeal regulatory treatment. For example, the proposed law would extend front running restrictions to include additional securities and financial intermediaries, currently not covered under Section 52I; establishing a unified framework regarding limitations on securities holdings and transactions currently stipulated in the Investment Advice and Mutual Fund Laws. *ISA Enforcement Activity* The ISA is responsible for detecting and investigating the market offences described above. Its record is as follows:

Investigated Securities Fraud, Misleading Disclosure, Inside Information and Violation of Broker/Portfolio Manager Restrictions Forwarded to the Investigations and Intelligence Department, 2006-2010

	2006	2007	2008	2009	2010	Total
Securities Fraud	5	1	2	4	4	16
Inside Information	4	3	2	6	2	17
Misleading Disclosures 1/	2	2	5	4	5	18
Violation of Stock exchange member employee and portfolio manager prohibitions	1	1	-	-	-	2
Total	**12**	**7**	**9**	**14**	**11**	**53**

Source: ISA 2010 Annual Report
1/ In prospectuses, financial statements, immediate reports.

Administrative enforcement of these offences will commence in the near future so there are no examples of such actions.

Regulatory approach

The ISA operates a market surveillance and data analysis system using its BI technology. It receives all trading information from TASE online, such as quotes, orders, transactions, limits, which TASE members are party to the transaction and information about off-floor block trading. In the surveillance system, market data is cross-referenced with information on the participant, which, if validated, substantiates suspicions of possible market abuse or insider trading activity. The ISA conducts inspections of regulated entities.

In addition embedded mechanisms in TASE rules and its trading system are designed to prevent or deter market abuse:

Listing Requirements: A company must maintain a minimum free float. Continuous trading does not take place for thinly traded shares, which are traded twice daily, at the opening and closing auction.

Lock Up periods: TASE listing rules require that the shares held by shareholders prior to an IPO, as well as those of investors becoming principal shareholders (including directors and senior executives) by virtue of their subscription to the IPO, be locked up for varying periods of time.

Construction of the TA-25 Index: The decision to place 25 shares in the index (which is the underlying asset for TASE's most heavily traded derivative) and impose weight caps on the constituent shares was meant to reduce opportunities for manipulating constituent share prices, the price of the entire index and hence, the value of options written on it.

Order Handling Rules: Order priority on the TACT system is determined by price and time and priority setting is automated, its accuracy and reliability is guaranteed.

Extraordinary Order Limits: TASE monitors the size of individual orders to identify and prevent the submission of extraordinarily large orders which may affect price movements. Similarly filters have been built into the TACT trading system to filter so-called "unusual" orders for which the price fluctuation limit exceeds 35 percent of the price of the last transaction conducted.

Open Interest Ceilings: To reduce a single participant's ability to influence the market (cornering), TASE imposes a limitation on the open interest market participants may have in options.

	Trading Schedule: The TASE uses random opening/closing times for trading during the different trading phases to break the predictability of the trading schedule and deter the submission of orders that may potentially impact opening and closing prices. *Calculation of Closing Price*: For thinly traded shares, the closing price is calculated as a weighted average of the closing auction price and the prices of the latest transactions during the continuous trading phase. *Regulatory Trading Halts*: When material information about a company or about one of its securities is made public, trading in that security may be halted for a period of 45 minutes to give investors an opportunity to reconsider their orders in the light of the new information. *Sanctions* Depending on the severity and the circumstances of a violation, market abuse offenses can attract either administrative or criminal sanctions. Criminal sanctions include imprisonment or the imposition of fines (calculated as a multiple of the maximum alternative fine set under the Penal Code). Securities fraud, misleading disclosure and the use of inside information by an insider are criminally enforceable offenses, each punishable by a five year prison term or a fine of up to five times the maximum set in the Penal Code for individuals and twenty-five times for corporations. Use of inside information received from an insider by a third party is also a criminally enforceable offense, punishable by a two-year prison term or fine of two times the fine set in the Penal Code for 2-year term offenses, for individuals and 12.5 times for corporations. Part 3 of the Seventh Schedule to the Securities Law describes the circumstances under which misleading disclosure or use of inside information is categorized an administrative offense. . **Cross market supervision** Since TASE is only stock exchange in Israel, there is no domestic cross-market trading. **Foreign linkages** The ISA is a full signatory to the IOSCO MMOU. The ISA has signed MOUs for cooperation with a number of countries and authorities. The Investigations and Intelligence Department of the ISA uses the IOSCO MMOU on an ongoing basis and as of our signing of the MMOU was greatly assisted by foreign authorities, especially by the USA, for the support and completion of investigations.
Assessment	Fully implemented.
Comments	The assessor welcomes the proposal to enact legislation to make the prohibition on front running more comprehensive and coherent.
Principle 29.	**Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.**
Description	**Monitoring of large positions** *Monitoring mechanisms* TASE members' open interest (both their own and their clients') and their credit exposure is monitored at three levels in the TASE Rules: for traded derivatives, open interest and the number of orders placed in derivatives trading are monitored on the MAOF Derivatives Exchange (MAOF); credit exposures are monitored to take account of MAOF open interest as well the other forms of credit; and

	capital requirements take account of credit exposures generally. The TASE requirements dealing with open interest and the use of limits for MAOF trading are contained in Part 3 of the TASE Trading rules and regulations. The Trading Rules limits for MAOF apply to open interests of both client and proprietary trading. In relation to clients, limits apply to a client's overall MAOF trading, its trading in each type of derivative and a client's account together with other accounts to which, the client (or its owner) is linked (TASE Rules, Part 3 – Trading Ch.3, s.7(a)). The requirements for a member to monitor to its client's open interest are set out in Chapter 3, section 7 of the Trading Rules and Chapter 6, section 6 of the Trading Regulations. On opening an account, a client must sign an authorization that permits the member to carry out transactions in the client's account so as to reduce the client's total open position both with the member and with other members. Central monitoring of open interest is carried out by the MAOF Clearing House. Each member must provide a daily report to the MAOF Clearing House of its proprietary open interest and the open interest of each of its clients on a per client basis. The MAOF Clearing House also monitors open interest against collateral on a per member basis in real time throughout the trading day. The online collateral system alerts MAOF Clearing House staff when a non-bank member's collateral falls below the required level. When an alert is triggered the member is informed and must provide additional collateral within either thirty minutes or twenty minutes depending on the circumstances. Such alerts take into account a 15 percent cushion above the collateral calculation and this is done with the mutual guaranty arrangement (Risk Fund) in mind. TASE rules place limit the activities TASE members and their subsidiaries can engage in, including by limiting the provision of credit for margin trading alone. See Chapter 3 Part I of the TASE Rules: The TASE clearing houses are the counterparty to all transactions on the main TASE platform, the platforms for institutional trading, the MTS Israel platform (for trading in government bonds) and MAOF derivatives transactions. Associated exposures are addressed for both the TASECH and MAOFCH clearing houses by their equity capital (which is separate from that of TASE) and by a mutual guaranty (risk) fund for each of the clearing houses The Risk Fund consists of contributions by TASE members of which 25 percent must be in cash and 75 percent on other financial instruments. It provides a source of liquidity to enable the clearing houses to meet their payment obligations; and a source of compensation if a clearing house is forced to sell securities at less than the value it is required to pay for them. The value of the Risk Fund is adjusted twice a year in March and September based on historical turnovers. See also under Principle 7. The MAOFCH employs a collateral (margining) system, which monitors and reacts in real time to the open interest exposure of clearing house members. Members must use the same method to require margins from clients as MAOFCH uses for them. The detailed margin requirements that apply in relation to MAOF trading are set out in Chapter 8 of the MAOF By-laws. Each member must provide a daily report to the MAOF Clearing House of its proprietary open interest and the open interest of each of its clients. The daily reports are transferred as data directly into the MAOF Clearing House system. As well as monitoring open interest and collateral, TASE's Membership and Supervision Department also monitors compliance with the rules limiting the number of orders that may be submitted per trading day. These limits apply at a member level (including all customers except locals) and to clients defined as locals in the TASE Regulations. See TASE Regulations, Part 3 – Trading, Ch. 6, s.5). TASE requires periodic reports from all members in which each client is identified by name as well as by account number and its open position recorded. This data is used to compile a market wide picture of the total number of orders each client submits per day. If TASE observes report that a particular client is especially active, it assigns the client a new unique number that must be used by

	all members through which that client acts. From that point on, it is able to monitor daily those clients on a market wide basis. Currently approximately 100 clients are monitored by TASE in this manner. MAOF Clearing House has power to reduce or close out open MAOF positions of a member or its clients. This power applies to a wide range of situations listed in Chapter 7-B, section 1.1.2 of the MAOF By-laws. To enable it to take remedial action, each member must provide the MAOF Clearing House with an irrevocable power of attorney to act in its name as a condition of membership. The MAOF Clearing House Board is not bound to first call for margin before unwinding or closing out a member's position. It may immediately use these powers if the situation warrants. **Default procedures – transparency and effectiveness** The TASE rules and regulations and MAOF by-laws give a clear picture to market participants of when and how TASE is empowered to intervene when a default occurs or they believe a default may occur. The Securities Law also sets out how the ISA may intervene if required. Similar lists of circumstances in which action may be taken by market authorities are set out in the TASE Rules, Part 1 – Membership and the MAOF By-laws. As well as the circumstances listed above (failure to meet a margin call, failure to fulfill a payment obligation, suspicion that the member is liable not to fulfill a payment obligation) other circumstances related to possible default include: if an administrator is appointed for the member or a receiver is appointed in order liquidate any part of the member's assets; if a petition for liquidation is submitted against the member; if the member's business is substantively reduced or suspended or if the member sells a substantive part of its property; if, without agreement by the MAOF Clearing House, the member assigns any collateral to another creditor; if any debt of a member is accelerated by any other creditor; if a lien is imposed on the collateral deposited in the margin accounts or on any material asset of the member; or if an event that is similar in essence to one of these events occurs. If any of these events occurs, the bodies entitled to take action are the TASE Board of Directors (see Chapter VIII of the TASE Rules, Part 1 – Membership) and the MAOF Clearing House Board of Directors (see Chapter 7-B of the MAOF By-laws). The actions available to the TASE Board of Directors include prohibiting a member, from engaging in certain transactions or certain types of transaction in securities, both on- or off- exchange, and suspending or revoking membership (Chapter VIII of the TASE Rules, Part 1 – Membership). Similar powers are available to the MAOF Board with the addition of its powers to intervene directly to reduce open interest of members described above (MAOF By-laws, Ch.4, s.6,8 and 9 and MAOF By-laws, Ch.7-B, s.1.1).
Assessment	Fully implemented.
Comments	

APPENDIX 1. NEW IOSCO PRINCIPLES

50. **In June 2010, IOSCO reviewed its Principles; 9 new Principles were added and one Principle removed (Principle 6).** IOSCO adopted a revised Methodology in September 2011 covering these new Principles. Assessment of Israel's compliance with IOSCO Principles was against the old Principles and used the old methodology. However, brief discussions were held on the 'state of readiness' to implement the new Principles, using an analysis prepared by the Israeli authorities. A summary of each is below.

Systemic risk monitoring and perimeter of regulation

New Principle 6: The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate.
New Principle 7: The Regulator should have or contribute to a process to review the perimeter of regulation, appropriate to regularly.

51. **The ISA (in conjunction with other agencies) is putting in place processes for analysis of systemic risk.** Measures taken include:

a. Establishment of a forum for cooperation on systemic risk issues. The forum was established at the instigation of the Bank of Israel (BOI) and includes the Governor of the BOI, the ISA Chairman and Commission of Capital Markets (the head of the CMISD). Its mandate is:

   - the formulation of methods, measures and indicators for the timely identification of systemic risks related to the activity of the various financial entities, markets, instruments and the financial system, including an ongoing implementation of these processes for the identification of the said systemic risks;
   - the articulation of measures to manage and minimize systemic risks, and to analyze their impact;
   - definition of the required data and indicators;
   - consideration of alternative courses of action to address crisis situations, and the analysis and assessment of the consequences of these alternatives.

   The forum has begun to meet and will continue to meet regularly.

b. Establishment of an internal ISA taskforce chaired by the ISA's chief economist, to assess systemic risk. This process is still at a preliminary stage. The taskforce includes representatives from all ISA departments, and will be responsible for identifying and managing risks that may result in systemic risk. It will develop extensive databases to facilitate research and analysis functions. It is developing potential indicators of systemic risk in securities markets. The ISA plays an active role in the IOSCO Technical Committee's working group on systemic risk.

52. **As well as using these formal mechanisms, the ISA has been active in using the intelligence it receives through its regulatory activities to monitor and identify areas of**

emerging risk in the marketplace, or weaknesses in the regulatory regime. Recent examples of where it has detected issues and acted to deal with them include:

a. actions to increase bondholder protection during the financial crisis;
b. establishment of a specialized economic department within the Tel-Aviv District Court for securities and corporate law litigation (the Economic Court);
c. the ISA administrative enforcement mechanisms reform;
d. proposals for regulation of securities custody;
e. new regulation of dealer trading platforms;
f. regulation of ETNs;
g. proposals to establishment an auditor oversight body; and
h. initiating underwriting reforms.

Conflicts of interest

New Principle 8: The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed.

53. **The management of conflicts of interest is a major issue in Israeli regulation.** Corporate ownership in Israel tends to be highly concentrated, and the primary 'agency problem' the regulatory system has had to contend with is that of controlling vs. minority shareholders. In the financial sector, until the Bachar reforms, Israel operated under a universal banking system, which meant commercial and investment banking, as well as asset management activities, took place under a single roof. For this reason, the control of conflicts of interest permeates virtually all facets of corporate and securities law, including corporate governance requirements, disclosure requirements and the conduct of business rules governing ISA-supervised entities. A significant portion of ISA regulatory action is focused on the prevention (if possible), disclosure and management of conflicts of interest and misalignment of incentives.

54. **Details about how conflicts are addressed in the regulatory regime are set out in the formal assessment**, under Principles 14-15 (issuers), 17-20 (collective investment schemes) and Principles 21-24 (intermediaries). As described there, there are numerous prescriptive rules designed to minimize conflict, and where it exists, to ensure that it is managed and appropriately disclosed.

55. **To date, securitization has not played any significant role in the Israeli market** so the particular problems associated with the securitization process have not arisen to any significant degree.

Auditor oversight

New Principle 19: Auditors should be subject to adequate levels of oversight Principle 20: Auditors should be independent of the issuing entity that they audit.
Principle 21: Audit standards should be of a high and internationally acceptable quality

56. **The new Principles expand on Principle 16, accounting and auditing standards, and encapsulate some of the detailed work IOSCO has done on oversight of auditors and auditor independence.** The assessment found full compliance with Principle 16 and this means the elements of the new Principles are largely in place.

57. **There are, however, various proposals to introduce new regulatory arrangements for regulation of the audit profession**. To address perceived inefficiencies in the current regulatory framework, the ISA favors the establishment of an independent body to exercise regular oversight of the development and implementation of auditing standards, auditor independence, and ethical conduct.[15] The main task of this new body will be to supervise accounting firms which audit reporting corporations (including foreign reporting corporations and dual listings under Chapter 5C of the Securities Law) and with overseeing the audit process applied to such corporations. The ISA proposes regulating the formation of this oversight board through the amendment of the Securities Law by way of introduction of a new, self- contained chapter of the Law.

58. **The main ISA proposals are**:

a. **Establishment of an independent oversight body.** The proposed body will be an independent, non-profit statutory organization. It will be comprised of three Commissioners appointed by the ISA in consultation with the Governor of the Bank of Israel. Only one of three will be (or has been in the past) a certified public accountant. The proposal includes limitations with respect to the qualifications, appointment, removal and replacement of Commissioners as well as limitations in cases of potential or existing conflicts of interest. The Chairman of the oversight body will be accountable for its actions and responsible for ensuring implementation of its decisions. The board will establish its own procedures for meetings and decisions will be passed with a simple majority. It will, however, be subject to ISA supervision.

   The oversight body will have the authority to perform audits and inspections of auditing firms and will be the sole authority in setting auditing standards for reporting companies. It will be granted investigatory and certain enforcement powers, including the imposition of monetary sanctions. It will also be authorized to apply to the ISA regarding the employment of its administrative enforcement powers. The oversight body will be authorized to cooperate with equivalent foreign bodies, subject to certain conditions.

b. **Auditing standards and reporting**. The oversight body will formulate standards and rules, and give guidance on, all matters relating to auditing that firms are required to carry out, including rules on auditing standards, professional ethics, independence,

[15] Alternative proposals have been made by others.

quality control, the rights and obligations of accountants when performing their professional duties. The accounting firms included in the register will be required to submit reports or notices to the oversight body, as deemed necessary by it.

c. **Quality Assurance Reviews.** The oversight board will oversee and review the auditing work performed by audit firms, their employees and partners. It will issue quality assurance reviews of its findings and will provide them to the reviewed accounting firm and to the ISA Chairman. Select information from the reports will be made available the public after three months, unless circumstances warrant the confidentiality of the report.

d. **Enforcement.** The oversight Body will be empowered with enforcement authority. It will be authorized to take the following measures against any transgressing firm, partner or employee:
   i. to require all or part of the firm's partners or employees to undergo additional professional training;
   ii. to impose fines on firms, partners and employees found in breach of the rules.
   iii. to demand that the breaching party take certain actions to correct the breach and prevent its repetition. The Oversight Body may demand the deposit of collateral to secure these obligations and to liquidate the said collateral if the obligations are not met.

   If the oversight body decides that administrative or criminal prosecution as set out under the Securities Law is warranted; it will forward the relevant information to the ISA Chairman, who has the authority to conduct an inquiry or investigation and launch administrative or criminal proceedings against the company.

   If the oversight board imposes any of the above sanctions, it must immediately disclose this to the ISA Chairman and to the Auditors Council and must publish a public report on its website (which may be delayed at its discretion upon the request of the accounting firm.)

The ISA is currently seeking approval from the relevant Ministry to proceed to public consultation on these proposals.

Credit rating agencies

New Principle 22: Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision

59. **Two credit rating agencies (CRAs) are currently active in the Israeli market:** Standard & Poors Maalot (wholly owned by S&P) and Midroog Ltd (in which Moody's has a 51 percent ownership stake).

60. **The active credit rating agencies are currently authorized by the CMISD under the rules set by it.** A company applying to receive approval as a rating agency must file a written application to the Commissioner and if approved must:

a. engage only in the rating of corporate debt, unless it receives the Commissioner's advance written approval to engage in another activity. In deciding whether to give such approval, the Commissioner considers whether the additional activity is liable to create conflicts of interest with the credit rating activities of the company;
b. operate under a know-how, guidance and support agreement with a recognized foreign credit rating agency for a period of at least five years.

Under this regime, other rules set out in circulars issued by the CMISD apply, including rules about ownership, liquid asset requirements, confidentiality, publication of ratings, governance, and the methodology used for rating (including use of a ratings committee).

61. **A new legislative proposal is being developed that would bring regulation and enforcement of rating agency activity under the authority of the ISA**. The proposal covers transparency, independence, conflicts of interest and accountability issues and be similar in intent, scope and implementation to regulation in Europe and the US. An exposure draft was published in June 2010 and is currently undergoing revision in response to comments solicited from the public. It is scheduled for submission to the Cabinet's Legislative Committee in the coming months. It is proposed that the new legislation and accompanying regulations will cover:

a. definition of the terms, "credit rating" and "credit rating agency";
b. registration requirements (including with regards to equity and insurance);
c. restrictions on the conduct of business. For example, the law may require that the company engages solely in rating and in additional activities which do not engender conflicts of interest;
d. ISA supervision of credit rating agencies;
e. the handling of conflicts of interest;
f. the obligation of a credit rating agency to act independently and solely according to professional considerations;
g. mandatory internal controls and professional qualifications of personnel;
h. equal treatment of rated entities;
i. consistent, systematic and unbiased methodology;
j. reliance on professional considerations.
k. disclosure requirements, including rules regarding disclosure to customers and to the public. The objective of these rules is to ensure that external entities have access to this information in order to monitor the reliability of a rating and to understand its limitations. These rules may relate, *inter alia*, to the method of disclosure and its content

62. **It may be noted that two class actions suit have been filed**, with ISA backing, against a group including Standard & Poor's Maalot rating agency, in relation to the collapse of Lehman Brothers

Analysts

New Principle 23*: *Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.

63. **The current regulation of analytical research services is based on the concept that an analytical report expresses a position and often a recommendation regarding a certain investment, and taken to be investment advice under the definition of the Investment Advice Law.** Therefore, and subject to the exceptions stipulated in the Law, analysts are required to be licensed and are subject to most of the legal obligations set out in the Law. Exceptions from the licensing requirement are specified in the Law and include investment advice through the media and the provision of investment advice, investment marketing or investment portfolio management services to qualified clients (in general the definition refers to institutional and other sophisticated investors).

64. **Non-licensed analysts are subject to some provisions of the Investment Advice Law**, including

a. fiduciary duties- the duty to act in the benefit of the client (Section 11(a));
b. the prohibition of preferential treatment- prohibiting analysts from preferring their own holdings or those of an entity affiliated with the corporation in which they work or are a partner (Section 16(A));
c. the prohibition on incentives- prohibiting the analyst from receiving any direct or indirect benefit in connection with the investment advice rendered, other than the fees and reimbursement of expenses from the client (Section 17).
d. duty of care- the duty to act with care and with an adequate level of skill and to employ all reasonable measures to secure the client's interests (Section 20).

65. **In 2007, the ISA issued a detailed ordinance under section 28(b) of the Investment Advice Law on disclosure obligations relating to analysts' reports.** It mandates disclosure of any conflicts of interest (both on the part of the person preparing a research report and the person's employer. The ISA has also required corporate licensees to set working procedures that ensure compliance with the legislation and regulations by the corporation, its officers and employees.

66. **Consideration is currently being given to amending the Investment Advice Law to create a set of new regulations specifically tailored to the analytical services industry**. The proposed amendment defines the term "general investment advice", as investment advice that is not deemed to be tailored investment advice, and excludes any advice involving personal communication between the advisor and the person advised. Imposing licensing or registration with the ISA as a requirement is under consideration.

Hedge funds

Principle 28: Regulation should ensure that hedge funds and/or hedge fund managers/advisers are subject to appropriate oversight.

67. **There is no special regime for hedge funds in Israel but the Mutual Funds Law recognizes them as a possible investment category for mutual funds.**

68. **In practice, mutual funds do not invest in hedge funds.** Only "special funds" can invest in hedge funds. A special fund is defined in section 1 of the Mutual Funds Law as a closed-end fund whose fund agreement stipulates that it will be a special fund. Hedge funds are also defined very broadly by the mutual fund regulations.[16] To date, no special funds exist and all other funds are prohibited to invest in hedge funds. Therefore, in practice, no mutual fund investments are held in hedge funds, and investment in hedge funds in Israel is confined to pension funds, provident funds and insurers.

[16] See section 1 of Joint Investment Trust (Assets that may be Bought and Held by a Fund and their Maximum Amounts) Regulations, 5755-1994