Corporate governance, other information about the Bank and its management

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Corporate governance

Board of Directors and management

Board of Directors

During the first half of 2018, the Bank Board of Directors held 11 plenary meetings. During this period there were also 29 meetings of Board committees and 2 Board member workshops.

On June 5, 2018, Ms. Osnat Ronen resigned her office as Board member.

On July 2, 2018, Mr. Gideon Siterman announced early termination of his office by a few days and resigned his office as External Board member.

On June 25, 2018, Mr. Yossi Shachak resigned his office as member of the Remuneration Committee.

After the resignation of Mr. Gideon Siterman, the Bank has only one Board member who is an External Board member pursuant to the Companies Law and is also an Independent Board member, as this term is defined in the Supervisor of Banks' Proper Conduct of Banking Business Directive 301.

Note also that in addition to the External Board member pursuant to the Companies Law as noted above, the Bank also has two External Board members pursuant to directives of the Supervisor of Banks who are also classified as Independent Board members.

On July 23, 2018, the Bank announced it would convene an extraordinary General Meeting of shareholders with an agenda including the appointment of an External Board member. For more information see Immediate Report dated July 23, 2018, reference 2018-01-069643 and amended Immediate Report dated July 24, 2018, reference 2018-01-069973.

Members of Bank management and senior officers

In the first half of 2018 there were no changes to members of Bank management and senior officers.

Internal Auditor

Details of internal audit within the Group, including the professional standards applied by internal audit, the annual and multi-annual work plan and considerations in its determination, extent of employment of the Internal Auditor and his team and the manner in which reports are submitted with regard to findings of the Internal Auditor have been included in chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" of the 2017 annual report. No material changes occurred in these details during the reported period.

Transactions with controlling shareholders and related parties

Transactions with affiliated persons were executed in the ordinary course of business, at market terms and under terms similar to those of transactions effected with unrelated entities.

Controlling shareholders

Below are developments compared to the 2017 financial statements:

Ofer Group

On March 18, 2018, the Bank received notice from Ofer Investments Ltd. and from Ofer Bros. Holdings (1989) Ltd. with regard to agreement on principles of a separation outline, due to provisions of the Competition Enhancement and Concentration Reduction Act, 2013.

The outline principles are designed to separate control of the significant financial entity (the Bank) from control of the significant non-banking entity (Meliseron Ltd. / Ofer Investments Ltd.) among shareholders in Ofer Group ("the outline"). Note that this outline is not a binding agreement and is merely designed to serve as basis for preparation of a detailed agreement.

For more information about agreed principles for the separation outline at Ofer Group, with due consideration to provisions of the Competition Enhancement and Concentration Reduction Act, 2013, see the Immediate Report by the Bank dated March 18, 2018 (reference: 2018-01-020733).

On August 15, 2018, the Governor of the Bank of Israel, Ms. Karnit Flug, signed an amendment to the permit for holding control and means of control over the Bank, amending the permit issued on January 15, 2013. According to this amendment to the permit, the permit dated January 15, 2013, issued to the estate of Mr. Juli Ofer RIP which is managed by the estate administrators will be terminated, the estate would be removed from the list of permit holders and Ms. Liora Ofer would be listed as holder of Ofer Holdings shares held by Juli Ofer RIP, previously held by the estate administrators. For more information (including a condition for the amendment to the permit), see the Bank's Immediate Report dated August 23, 2018 (reference: 2018-01-078451).

Human Resources

Developments in labor relations

For more information about an economic arbitration between the Bank and the Mizrahi Tefahot Employees' Union, see Note 22.A.6. to the 2017 financial statements. Management believes, based on the opinion of legal counsel, that exposure with respect to this arbitration cannot be estimated.

Legislation and Supervisory Regulation of Bank Group Operations

Laws and regulations

European Union Markets in Financial Instruments Directive (MIFID 2)

European regulation applicable to European countries, became effective on January 3, 2018. The objective of this regulation is to create uniform directives in Europe, so as to increase trading transparency, market efficiency and investor protection in the European market. This regulation is not directly applicable to the Bank in Israel, but given the Bank's global operations and many interfaces with the European market, the Bank has been requested to arrange its contractual relations with European counterparts.

Credit Data Act, 2016

On April 12, 2016, the Credit Data Act was published and would become effective on October 12, 2018, unless postponed (but not later than April 12, 2020).

The act reforms the market for credit data service. When this act would become effective, the Credit Data Service Act, 2002 would be rescinded.

This act is relevant for the Bank, both due to the Bank being an "information source", required to provide credit data for Bank clients to a central information repository at the Bank of Israel and due to the Bank being a "credit data user", authorized to receive credit data from the credit bureaus.

In conformity with the Act, an information repository is being created at the Bank of Israel. A credit bureau would receive information from this repository and a credit provider may request a credit report, credit indication (definitive recommendation on whether to extend credit) and monitoring (monitoring of changes to the borrower's standing over the loan term) from the credit bureau. In order to obtain information, the credit provider must obtain explicit consent from the borrower (to obtain an indication, it is sufficient to inform the borrower). A client may ask the Bank of Israel to exclude their credit data from the repository or not to provide such data for compiling a credit report.

Over the preparation period for application of the Act (from publishing of the Act through its effective start date), the Bank provides information about clients to the repository being created, as instructed from time to time by the Bank of Israel.

Application of the Act is not expected to have any material impact on the Bank's financial statements.

Financial Services Supervision Act (Regulated Financial Services), 2016

The Act became effective on June 1, 2017. The Act is designed to govern the non-banking credit market, to generate fair, transparent competition in this area, which had been gray and exposed in part - and to allow consumers to have confidence in non-banking credit providers.

According to the Act, as from June 1, 2017 it is not permitted to engage in Israel in "extending credit" (which is very widely defined) without a valid license, contingent on minimum capital, verification of good standing and supervision by the Supervisor of Capital Market, Insurance and Savings. As from October 1, 2018 (or sooner - should the AML Ordinance be enacted for financial service providers in financial assets), it would no longer be allowed to engage in "provision of service in financial assets" in Israel without a proper license. This prohibition would not apply to financial institutions, which are subject to licensing pursuant to other legislation. The Bank may refuse account management to anyone required by law to hold a license who would fail to present such license. Currently, Bank clients that provide discounting and lending services are subject to licensing pursuant to this Act and the Bank has contacted the relevant clients, requiring them to present their license or, alternatively, to certify that they do not extend credit.

On February 1, 2018, Amendment 4 to the Act became effective, stipulating that operation of a "credit brokerage system" constitutes a "financial service". Therefore, as from the effective start date of this Amendment, it would no longer be possible to engage in operation of a credit brokerage system in Israel without an appropriate license. The Amendment stipulates, *inter alia*, that the license holder must manage lender and borrower funds transferred to the license holder in a separate trust account in favor of the lenders, with one of the entities listed in the Act, including with a banking corporation. The Bank is studying the Amendment and is preparing for its implementation.

Application of this Act has no impact on the Bank's financial statements.

Restructuring of the Stock Exchange

On April 6, 2017, the Securities Law (Amendment No. 63), 2017 was officially published, concerning restructuring of the Stock Exchange.

The Law puts in place the legal infrastructure for separation of ownership of the Tel Aviv Stock Exchange and the rights of Stock Exchange members to use its services, while removing the existing requirement for the Stock Exchange to distribute its earnings. It also stipulates restrictions on holding of shares of the Stock Exchange, requiring Stock Exchange members and banking corporations other than Stock Exchange members to sell any means of control they hold in excess of 5%. The Law further stipulates arrangements for allocation of share capital of the Stock Exchange among members thereof and sale of holdings in excess of 5%. In conformity with the Act, on June 29, 2017 the Stock Exchange filed a request to convene a General Meeting of Stock Exchange members, in order to approve an arrangement on changes to the Stock Exchange structure in conformity with Section 350 of the Companies Law (hereinafter: "the Arrangement"). In the proposed Arrangement, bylaws of the clearinghouses were amended so that clearinghouse members would not take part in its management and objections were made to the proposed text. The Court approved the motion to convene a General Meeting and ordered that should agreement be reached on the change to wording of a proposed resolution on amendment of the clearinghouse Bylaws, no further Court hearing would be required. Consequently, provisions with regard to amendment of clearinghouse Bylaws were revised to include claim and audit proceedings and have been approved by the Stock Exchange Audit Committee and Board of Directives (hereinafter: “the Amendment”). On August 10, the Arrangement was approved, as amended, by the General Meeting of Stock Exchange members; on August 16, a motion was filed with the Tel Aviv District Court for approval of the Agreement pursuant to Section 350 of the Corporate Act. On September 7, 2017, the Court approved the arrangement for changing the stock exchange structure.

On September 18, 2017, the Bank received a letter from the Tel Aviv Stock Exchange, containing a notice of share allotment to the Bank and registration of the Bank in the Stock Exchange's register of shareholders.

On December 28, 2017, the Tel Aviv Stock Exchange Ltd. ("Stock Exchange Company") contacted the Bank, which holds 6,640,416 shares or 6.640417% of the Stock Exchange share capital, as shareholder of the Stock Exchange, seeking proposals to acquire the shares held by the Bank. This solicitation was addressed to Stock Exchange members, whereby shareholders wishing to sell their shares in the Stock Exchange Company ("Offering Shareholder") are requested to issue an offer to the Stock Exchange Company for sale and transfer of Stock Exchange Company shares held thereby, at such terms and conditions as stated in the solicitation. According to the solicitation, the price for shares offered for sale was set at NIS five hundred (500) million divided by the total number of allotted shares of the Stock Exchange Company, multiplied by the number of shares offered for sale by the Offering Shareholder. On January 18, 2018, the Bank accepted the Stock Exchange’s offer to sell part (1.7%) of the Stock Exchange shares held by the Bank, such that after the sale, the Bank would hold 4,900,000 shares, or 4.9% of the Stock Exchange share capital. The expected consideration for these shares amounts to NIS 8.7 million. On April 16, 2018. the Bank was informed by the stock exchange member that the Bank's aforementioned proposed sale of shares has been accepted. According to this notice, the shares would be sold and transferred to one or to multiple buyers ("the Buyer"). The consideration payable to the Bank would be higher than indicated in the offer but, in conformity with provisions of the Securities Act on this matter, the difference between the consideration paid and the price indicated in the offer would be transferred to the stock exchange member. Closing of the transaction is contingent on obtaining regulatory approvals and closing is scheduled for June 19, 2018 ("the Effective Date"). Should the approvals not be obtained or the closing not take place by the Effective Date, the transaction would be terminated unless otherwise agreed by the Buyer, the Stock Exchange and the Bank.

On June 12, 2018, the Stock Exchange contacted the Bank, seeking to delay the effective date to August 31, 2018, with all other terms and conditions of the transaction remaining unchanged; the Bank agreed to this request by the Stock Exchange.

On August 27, 2018 the Bank received notice from the Stock Exchange, whereby the closing of the transaction for sale of Stock Exchange shares took place and the proceeds for the shares, amounting to NIS 8.7 million, were deposited into the Bank's account.

The Non-banking Loans Arrangement Law (Amendment 5), 2017

On August 6, 2017, the Law, known as the "Fair Credit Law", was published.

The law applies to credit extended to individuals from banking corporations, settlement providers, insurers and management companies.

The Law provides a uniform maximum interest rate for all lending entities and applies to:

- Loans in NIS: The Bank of Israel interest rate plus 15%.
- Loans in foreign currency: One-year LIBOR interest rate plus 15%.
- Arrears interest: Maximum interest rate multiplied by 1.2.

In the third year after implementation of the Law, the Finance Minister will examine the average interest rate for credit extended by banks and will be authorized to reduce the maximum borrowing cost.

The following were excluded from the scope of the uniform maximum interest rate:

- Short-term loans (up to 3 months) - capped at a maximum of 5% over the maximum interest rate.
- Transactions involving discounting a note for business (non-personal) use.
- Loans subject to an interest rate decree, pursuant to the Interest Law (such as arrears interest for housing loans or CPI-linked loans).

The provisions of the Law would apply only to new loans. The effective start date of the Law is November 6, 2018.

The Bank is preparing to implement the Act. Application of the Act is not expected to have any material impact on the Bank's financial statements.

Reduction of Cash Usage Act, 2018

On March 18, 2018, the Reduction of Cash Usage Act, 2018 was made public.

The Act is designed to reduce the use of cash in transactions - by both payer and payee.

The Act also governs payment by check. The Act stipulates certain restrictions on the use of cash and checks.

The Act will become effective on January 1, 2019, except for certain sections effective as from July 1, 2019.

Pursuant to the Act, the Supervisor of Banks may impose monetary sanctions on banking corporations that pay a check in breach of any of the restrictions applicable to such check pursuant to Addendum II.

The Supervision of Banks may start imposing sanctions as from July 1, 2019.

The Bank is preparing to implement the Act.

Insolvency and Financial Rehabilitation Act, 2018

The Insolvency and Financial Rehabilitation Act, 2018 (hereinafter: "the Act") was officially published on March 15, 2018. The Act shall be effective 18 months after publication.

The Act provides a codification of insolvency laws and comprehensively encompasses all insolvency laws for individuals and corporations, eliminating the old ordinances and arrangements provided for in the Companies Law.

The Act has three major goals:

- Financial rehabilitation of the debtor. Regard credit default and insolvency as a financial mishap, rather than a moral flaw.
- Increase in debt percentage to be repaid to creditors.
- Increase certainty and stability of the Law, through shorter proceedings and reduced bureaucratic burden.

The Act stipulates changes to various matters, such as: Threshold for launch of insolvency proceedings, duration of insolvency proceedings, linkage and interest, floating lien, mutual debt offsetting, the position of a financing provider for operations of a company under stay of proceedings, liability of Board members and managers and negotiations of debt re-structuring.

The Bank believes that the Act would affect the extension of credit and the repayment rate upon default. The Bank is preparing to implement provisions of the Act.

Prevention of Proliferation and Financing of Weapons of Mass Destruction, 2018

The Act was made public on March 11, 2018 and became effective as from said date. The Act is designed to prevent proliferation and financing of weapons of mass destruction, including by way of sanctions imposed by the Security Council on entities involved in proliferation, financing or assisting the proliferation and financing of weapons of mass destruction. New violations were specified, which are also violations of the AML Act.

The Act imposes duties and prohibitions on banks as well and imposes criminal sanctions for violation thereof. The duties include: prohibition of any economic transactions with any proclaimed or affiliated entity (as these terms are defined in the Act) and mandatory reporting of any such activity discovered. The Act imposes personal liability on officers of the company, including the officer responsible for implementation of AML duties, who is also tasked with implementation of the Act. The Bank applies the Act.

Economic Plan Act (Legislation Amendments to Implement Economic Policy for 2019 Budget Year), 2018

On March 22, 2018, the Act was made public, including multiple legislative amendments. These include amendment of the Banking Act (Customer Service), 1981. The amendment to the Act involves client transition from one bank to another, and would become effective on March 22, 2021 unless postponed (two allowed six-month postponements).

According to the amendment to the Act, should a client (individual or corporation of the type specified in regulations by the Governor of the Bank of Israel) wish to transition to another bank, the client's original bank and the receiving bank shall take all required actions to allow the client to transition their financial activity to the receiving bank through an online, convenient, reliable, secure process at no cost to the client for such transfer of their financial activity, within seven business days or by another date specified by the Governor of the Bank of Israel with consent of the Minister of Finance.

Transitional provision (for the period from publication of the amendment to the Act through its effective start date): Should a client ask to close their account with their bank, the bank shall not rescind, merely due to the closing request, any benefits and discounts to which the client was eligible in managing their account, sooner than prescribed in an agreement between the bank and the client and, unless otherwise stipulated, for at least three months.

Application of the amendment to the Act is not expected to have any material impact on the Bank's financial statements.

Anti-Trust Rules (Class exemption for syndicated loan arrangements) (Interim directive), 2018

On May 9, 2018, the Anti-Trust Supervisor issued the following rules, which exempt any syndicated loan arrangement one of the parties to which is a banking corporation, institutional investor or settlement provider, as defined in the rules, or similar entities incorporated outside Israel, from the requirement to obtain approval of the arrangement by the Anti-Trust Court, upon fulfilling various conditions, including the following: The syndication agent approached other lenders with prior written consent of the borrower; the borrower may negotiate with the other lenders the terms and conditions of credit in the syndicated loan, other than through the syndication agent; one of the following conditions has been fulfilled: There is at least one potential syndication agent that is not party to the arrangement; all potential syndication agents are party to the arrangement but unless they all participate, the borrower may not obtain credit terms similar to those offered in the arrangement; all potential syndication agents are party to the arrangement but the aggregate share of lenders who are potential syndication agents is less than 20%; one of the following conditions has been fulfilled: The arrangement includes up to one major lender (defined as a lender whose share of credit extended to the business sector in Israel exceeds 20%); the arrangement includes more than one major lender, but up to one major lender serves as syndication agent, and unless they all participate, the borrower may not obtain credit terms similar to those offered in the arrangement; the arrangement includes more than one major lender, but the syndication agent is not a major lender and the aggregate share of major lenders is less than 20%; the syndicated loan arrangement is not essentially designed to reduce or avoid competition; the syndicated loan arrangement includes no restrictions that are not required for realizing the essence thereof.

The rules are effective for three years after publication.

Note that the rules rescind the letter by the Anti-Trust Supervisor dated December 28, 2017, to managers of banking corporations and institutional investors, about consortium arrangements and about the Anti-Trust Supervisor not enforcing provisions of the Anti-Trust Act, 1988 on any credit consortium that complies with conditions listed in the letter, including documentation of all meetings and contacts between the parties to the arrangement prior to joining and reporting of such documentation to the Anti-Trust Supervisor at the end of every year.

Publication by the Anti-Trust Authority - transition to daily credit card settlement

In April 2018, the Anti-Trust Authority announced that credit card companies would be required to transition to daily credit card settlement as from July 2021. This is in conjunction with conditions for approval of the restrictive agreement for cross-settlement between credit card companies.

Application of this requirement is not expected to have any material impact on the Bank's financial statements.

Supervisor of Banks

Circulars and Public Reporting Regulations

Debt collection proceedings

On February 1, 2017, the Bank of Israel issued Proper Banking Conduct Directive 450 "Debt collection proceedings", designed to govern the actions to be taken in order to increase fairness and transparency in debt collection from clients who fail to repay their loan on time and when handling debt collection prior to and during any legal proceedings. The effective start date of this directive is one year after its issue date. The Bank applies the directive as from February 1, 2018.

Prohibition of money laundering

On January 1, 2018, Proper Banking Conduct Directive 411 "AML and Terror Financing Risk Management" became effective, which integrates supervisory circulars and letters on this matter issued since the most recent extensive revision of this directive. The directive was expanded and compiled as a risks management directive, including identification, assessment and operative mitigation steps. The key amendments to the directive include: Explanation of the risk-based approach, clarification of definitions, expanded description of the roles of corporate governance functions, details of items on which the bank is to rely when preparing the risk assessment and details of the information database to be gathered by the bank from internal and external sources in order to formulate the risk assessment. The Bank is applying this directive.

Reduced cross commission in deferred and immediate charge transactions using credit cards

On February 25, 2018, the Bank of Israel issued an outline designed to reduce the cross commission in deferred charge transactions using charge cards by 30%, from 0.7% of transaction amount today, to 0.5% in January 2023. This change will take place in 5 stages: First in January 2019 (0.6%); second in January 2020 (0.575%); third in January 2021 (0.55%); fourth in January 2022 (0.525%); and final in January 2023.

The Bank of Israel also decided to reduce the cross commission for immediate charge transactions using credit cards, from 0.3% to 0.25% in January 2023. This change will take place in 2 stages: First in January 2021 (0.275%) and second in January 2023.

Application of the reduced commission is not expected to have any material impact on the Bank's financial statements.

Capital measurement and adequacy

On March 15, 2018, the Supervisor of Banks issued a circular revising Proper Banking Conduct Directive 203 "Measurement and capital adequacy - Credit risk" with regard to risk weighting of loans with LTV ratio higher than 60%.

The circular stipulated that loans with LTV ratio higher than 60% would be assigned a 60% risk weighting, compared to 75% prior to this revision.

The revision is designed to provide relief to young couples and second home buyers who purchase apartments with a high LTV ratio.

The revision is effective as from the circular issue date. The Bank is applying this directive.

Application of this directive reduces risk assets due to origination of new housing loans with LTV ratio higher than 60%, originated as from the circular issue date.

Banking corporation operations with clients who are regulated financial service providers and offering coordinators

On April 15, 2018, the Bank of Israel issued a circular designed to specify guidelines to allow banking corporations to provide service and manage risk associated with their operations with regulated financial entities (entities supervised by the Capital Market Authority, in conformity with the Supervision Act). This is further to the Financial Services Supervision Act (Regulated Financial Services), 2016 which is designed to provide for comprehensive and coherent regulation, in as much as possible, of the entire financial services market and entities operating in this market.

In conformity with the circular, the Bank must specify policy and procedures for opening and management of accounts for regulated financial entities so as to reflect, *inter alia*, a risk-based approach.

The Bank is preparing to implement the circular.

Application of this circular has no effect on the Bank's financial statements.

Management of cyber risk in the supply chain

In April 2018, the Bank of Israel issued Proper Banking Conduct Directive 363 "Management of cyber risk in the supply chain", designed to clarify the bank's responsibility for maintaining secure work procedures with material external suppliers and the bank's obligations to appropriately manage cyber risk in operations of such suppliers in their premises, in bank premises and in bank - supplier interfaces. Key provisions of the directive shall become effective 6 months after its publication.

The Bank is preparing to implement this directive.

Application of this directive has no effect on the Bank's financial statements.

Transactions to acquire debtor debt from commercial clients

On May 28, 2018, the Bank of Israel issued a letter about transactions to acquire debtor debt from commercial clients, which lists highlights and bank commitment to map and to manage the risk due to each debt acquisition transaction and to address aspects of credit management, financial reporting and compliance arising from terms and conditions of such transaction. The Bank is required to conduct a comprehensive Internal Audit with regard to appropriate handling and must provide the audit report to the Supervisor no later than the end of June 2019. The Bank is preparing to implement the directive.

Application of the directive is not expected to impact the Bank's financial statements.

Debit cards

On July 2, 2018, the Bank of Israel issued an update circular to Proper Banking Conduct Directive 470 concerning "Debit cards". According to this circular, as from February 1, 2019, banks would transfer to the debit card issuer operator any funds with respect to transactions in cards issued by it on the date when the operator is required to transfer these funds to the settlement provider, regardless of the client debit date or the identity of the settlement provider. It was further stipulated that new operating agreements between issuer and operator, or similar agreements materially amended and signed by January 2022, would be sent to the Supervisor.

The Bank is preparing to implement the circular.

Application of this circular has no material impact on the Bank's financial statements.

Restrictions on indebtedness of borrower and borrower group

On August 1, 2018, the Bank of Israel issued an update to Proper Banking Conduct Directive 313. In conformity with this update, the exposure of a banking corporation to any "borrower group - credit card issuer", net of the amounts allowed by the directive, may not exceed 15% of the banking corporation's capital, similar to the restriction applicable to "borrower group - banking".

Moreover, the indebtedness of any "borrower group - credit card issuer" shall be included in the aggregate restriction for major borrowers (borrowers whose indebtedness exceeds 10% of the banking corporation's capital. Furthermore, the exception for indebtedness of any "group of borrowers - banking" to a credit card company with regard to the aggregate restriction for major borrowers has been eliminated.

For five years after the publication date of the update to this directive, indebtedness of any "group of borrowers - banking to a credit card company" shall not be subject to the restriction for "group of borrowers - banking" and shall be excluded from the aggregate restriction for major borrowers. All other updates to the directive are effective as from the issue date of the directive.

Application of the update has no material impact on the financial statements.

Bank's credit rating

On January 21, 2018, S&P GLOBAL RATINGS MAALOT LTD (hereinafter: "Ma'alot") confirmed the Bank's issuer rating of ilAAA with a Stable rating outlook.
The rating of subordinated notes issued by Tefahot Issuance is one rank below the issuer rating, i.e. rated ilAA+. These subordinated notes qualify as Tier II capital under transitional provisions of Basel III.
The Bank's subordinated capital notes, which qualify as Tier II equity in conformity with transitional provisions of Basel III, are rated ilA+.
The contingent subordinated notes with contractual loss-absorption provisions (CoCo), which qualify as Tier II equity in conformity with provisions of Basel III, are rated ilAA- with Stable rating outlook.
On September 10, 2017, Midroog Ltd. (created in partnership with Moody's International, which owns a 51% equity stake) (hereinafter: "Midroog") issued an initial rating of the Bank. Long-term deposits and senior debt of the Bank wererated Aaa.il / Stable outlook. Subordinated notes (Lower Tier II capital) were rated Aa1.il / Stable outlook and subordinated capital notes (Upper Tier II capital) were rated Aa2.il / Stable outlook.
contingent subordinated notes with contractual loss-absorption provisions (CoCo), which qualify as Tier II equity in conformity with provisions of Basel III, are rated ilAa3 with Stable rating outlook.

On June 30, 2015, Moody's rating agency confirmed the Bank's long-term deposit rating at A2 and raised the outlook from Negative to Stable.

Operating segments

For more information about supervisory operating segments, see chapter "Corporate Governance, Audit, Other Information about the Bank and Management thereof" of the 2017 financial statements.

Addendums to condensed quarterly financial statements

Addendum I - Interest Revenue and Expense Rates - of the Bank and its Subsidiaries[(1)]

Reported amounts (NIS in millions)

A. Average balances and interest rates - assets

	For the three months ended June 30, 2018 Average balance[(2)]	For the three months ended June 30, 2018 Interest revenues	For the three months ended June 30, 2018 Revenues rate In %	For the three months ended June 30, 2017 Average balance[(2)]	For the three months ended June 30, 2017 Interest revenues	For the three months ended June 30, 2017 Revenues rate In %
Interest-bearing assets						
Loans to the public[(3)]						
In Israel	180,016	[(7)]2,113	4.78	169,975	[(7)]1,817	4.34
Outside of Israel	3,313	51	6.30	2,979	37	5.06
Total	183,329	2,164	4.81	172,954	1,854	4.36
Loans to the Government						
In Israel	194	1	2.08	196	1	2.06
Outside of Israel	298	5	6.88	128	2	6.40
Total	492	6	4.97	324	3	3.76
Deposits with banks						
In Israel	1,139	1	0.35	721	-	-
Outside of Israel	252	1	1.60	347	2	2.33
Total	1,391	2	0.58	1,068	2	0.75
Deposits with central banks						
In Israel	36,901	8	0.09	36,368	8	0.09
Outside of Israel	2,891	13	1.81	3,671	9	0.98
Total	39,792	21	0.21	40,039	17	0.17
Securities loaned or purchased in resale agreements						
In Israel	40	-	-	66	-	-
Outside of Israel	-	-	-	-	-	-
Total	40	-	-	66	-	-
Debentures held to maturity and available for sale[(4)]						
In Israel	8,499	38	1.80	10,383	34	1.32
Outside of Israel	854	5	2.36	1,045	4	1.54
Total	9,353	43	1.85	11,428	38	1.34
Debentures held for trading[(5)]						
In Israel	50	1	8.24	127	1	3.19
Outside of Israel	-	-	-	-	-	-
Total	50	1	8.24	127	1	3.19
Total interest-bearing assets	234,447	2,237	3.87	226,006	1,915	3.43
Receivables for credit card operations	3,421			3,273		
Other non-interest bearing assets[(6)]	5,253			6,257		
Total assets	243,121			235,536		
Total interest-bearing assets attributable to operations outside of Israel	7,608	75	4.00	8,170	54	2.67

See remarks below.

Interest Revenues and Expenses Rates - of the Bank and its Subsidiaries[1] - Continued

Reported amounts (NIS in millions)

A. Average balances and interest rates - assets

	For the six months ended June 30, 2018 Average balance[2]	For the six months ended June 30, 2018 Interest revenues	For the six months ended June 30, 2018 Revenues rate In %	For the six months ended June 30, 2017 Average balance[2]	For the six months ended June 30, 2017 Interest revenues	For the six months ended June 30, 2017 Revenues rate In %
Interest-bearing assets						
Loans to the public[3]						
In Israel	178,493	[7]3,444	3.90	168,563	[7]3,082	3.69
Outside of Israel	3,251	95	5.93	3,029	73	4.88
Total	181,744	3,539	3.93	171,592	3,155	3.71
Loans to the Government						
In Israel	198	2	2.03	191	2	2.11
Outside of Israel	277	8	5.86	131	4	6.20
Total	475	10	4.25	322	6	3.76
Deposits with banks						
In Israel	958	2	0.42	790	2	0.51
Outside of Israel	270	1	0.74	346	3	1.74
Total	1,228	3	0.49	1,136	5	0.88
Deposits with central banks						
In Israel	37,496	15	0.08	35,105	16	0.09
Outside of Israel	2,880	24	1.67	4,068	18	0.89
Total	40,376	39	0.19	39,173	34	0.17
Securities loaned or purchased in resale agreements						
In Israel	61	-	-	71	-	-
Outside of Israel	-	-	-	-	-	-
Total	61	-	-	71	-	-
Debentures held to maturity and available for sale[4]						
In Israel	7,704	84	2.19	9,358	61	1.31
Outside of Israel	870	10	2.31	1,062	8	1.51
Total	8,574	94	2.20	10,420	69	1.33
Debentures held for trading[5]						
In Israel	532	1	0.38	683	2	0.59
Outside of Israel	-	-	-	-	-	-
Total	532	1	0.38	683	2	0.59
Total interest-bearing assets	232,990	3,686	3.19	223,397	3,271	2.95
Receivables for credit card operations	3,401			3,132		
Other non-interest bearing assets[6]	3,061			5,612		
Total assets	239,452			232,141		
Total interest-bearing assets attributable to operations outside of Israel	7,548	138	3.69	8,636	106	2.47

Interest Revenues and Expenses Rates - of the Bank and its Subsidiaries(1) - continued

Reported amounts (NIS in millions)

A. Average balances and interest rates - liabilities and equity

	For the three months ended June 30, 2018 Average balance(2)	For the three months ended June 30, 2018 Interest revenues	For the three months ended June 30, 2018 Revenues rate In %	For the three months ended June 30, 2017 Average balance(2)	For the three months ended June 30, 2017 Interest revenues	For the three months ended June 30, 2017 Revenues rate In %
Interest-bearing liabilities						
Deposits from the public						
In Israel						
On-call	21,604	18	0.33	13,952	4	0.11
Term deposits	115,410	479	1.67	122,114	435	1.43
Outside of Israel						
On-call	601	-	-	563	-	-
Term deposits	4,717	19	1.62	4,311	10	0.93
Total	142,332	516	1.46	140,940	449	1.28
Deposits from the Government						
In Israel	50	-	-	55	-	-
Outside of Israel	-	-	-	-	-	-
Total	50	-	-	55	-	-
Deposits from banks						
In Israel	1,262	2	0.64	1,477	3	0.81
Outside of Israel	2	-	-	-	-	-
Total	1,264	2	0.63	1,477	3	0.81
Securities loaned or sold in conjunction with repurchase agreements						
In Israel	-	-	-	-	-	-
Outside of Israel	-	-	-	-	-	-
Total	-	-	-	-	-	-
Debentures and subordinated notes						
In Israel	30,077	373	5.05	28,627	289	4.10
Outside of Israel	-	-	-	-	-	-
Total	30,077	373	5.05	28,627	289	4.10
Other liabilities						
In Israel	49	1	8.42	88	1	4.62
Outside of Israel	-	-	-	-	-	-
Total	49	1	8.42	88	1	4.62
Total interest-bearing liabilities	173,772	892	2.07	171,187	742	1.75
Non-interest bearing deposits from the public	44,855			40,066		
Payables for credit card transactions	3,421			3,273		
Other non-interest bearing liabilities(8)	6,456			7,191		
Total liabilities	228,504			221,717		
Total equity resources	14,617			13,819		
Total liabilities and equity resources	243,121			235,536		
Interest margin			1.80			1.69
Net return(9) on interest-bearing assets						
In Israel	226,839	1,289	2.29	217,836	1,129	2.09
Outside of Israel	7,608	56	2.98	8,170	44	2.17
Total	234,447	1,345	2.31	226,006	1,173	2.09
Total interest-bearing liabilities attributable to operations outside of Israel	5,320	19	1.44	4,874	10	0.82

See remarks below.

Interest Revenues and Expenses Rates - of the Bank and its Subsidiaries[1] - continued

Reported amounts (NIS in millions)

A. Average balances and interest rates - liabilities and equity

	For the six months ended June 30, 2018 Average balance[2]	For the six months ended June 30, 2018 Interest revenues	For the six months ended June 30, 2018 Revenues rate In %	For the six months ended June 30, 2017 Average balance[2]	For the six months ended June 30, 2017 Interest revenues	For the six months ended June 30, 2017 Revenues rate In %
Interest-bearing liabilities						
Deposits from the public						
In Israel						
On-call	21,799	21	0.19	15,613	2	0.03
Term deposits	113,991	748	1.32	118,484	654	1.11
Outside of Israel						
On-call	568	-	-	607	-	-
Term deposits	4,724	35	1.49	4,507	20	0.89
Total	141,082	804	1.14	139,211	676	0.97
Deposits from the Government						
In Israel	51	-	-	53	-	-
Outside of Israel	-	-	-	-	-	-
Total	51	-	-	53	-	-
Deposits from banks						
In Israel	1,283	4	0.62	1,509	6	0.80
Outside of Israel	1	-	-	3	-	-
Total	1,284	4	0.62	1,512	6	0.80
Securities loaned or sold in conjunction with repurchase agreements						
In Israel	-	-	-	-	-	-
Outside of Israel	-	-	-	-	-	-
Total	-	-	-	-	-	-
Debentures and subordinated notes						
In Israel	30,095	451	3.02	27,798	387	2.80
Outside of Israel	-	-	-	-	-	-
Total	30,095	451	3.02	27,798	387	2.80
Other liabilities						
In Israel	74	1	2.72	105	2	3.85
Outside of Israel	-	-	-	-	-	-
Total	74	1	2.72	105	2	3.85
Total interest-bearing liabilities	172,586	1,260	1.47	168,679	1,071	1.27
Non-interest bearing deposits from the public	44,846			40,432		
Payables for credit card transactions	3,401			3,132		
Other non-interest bearing liabilities[8]	5,672			6,255		
Total liabilities	226,505			218,498		
Total equity resources	12,947			13,643		
Total liabilities and equity resources	239,452			232,141		
Interest margin			1.72			1.68
Net return[9] on interest-bearing assets						
In Israel	225,442	2,323	2.07	214,761	2,114	1.98
Outside of Israel	7,548	103	2.75	8,636	86	2.00
Total	232,990	2,426	2.09	223,397	2,200	1.98
Total interest-bearing liabilities attributable to operations outside of Israel	5,293	35	1.33	5,117	20	0.78

Interest Revenues and Expenses Rates - of the Bank and its Subsidiaries[1] - continued

Reported amounts (NIS in millions)

B. Average balances and interest rates - additional information about interest-bearing assets and liabilities attributed to operations in Israel

	For the three months ended June 30, 2018 Average balance[2]	For the three months ended June 30, 2018 Interest expenses (revenues)	For the three months ended June 30, 2018 Expense (revenue) rate In %	For the three months ended June 30, 2017 Average balance[2]	For the three months ended June 30, 2017 Interest expenses (revenues)	For the three months ended June 30, 2017 Expense (revenue) rate In %
Israeli currency - non-linked						
Total interest-bearing assets	161,041	1,084	2.72	154,436	999	2.61
Total interest-bearing liabilities	116,327	(218)	(0.75)	109,855	(188)	(0.68)
Interest margin			1.97			1.93
Israeli currency - linked to the CPI						
Total interest-bearing assets	52,169	977	7.70	50,826	784	6.31
Total interest-bearing liabilities	35,765	(574)	(6.58)	38,565	(494)	(5.23)
Interest margin			1.12			1.08
Foreign currency (including Israeli currency linked to foreign currency)						
Total interest-bearing assets	13,629	101	3.00	12,574	78	2.50
Total interest-bearing liabilities	16,360	(81)	(2.00)	17,893	(50)	(1.12)
Interest margin			1.00			1.38
Total - operations in Israel						
Total interest-bearing assets	226,839	2,162	3.87	217,836	1,861	3.46
Total interest-bearing liabilities	168,452	(873)	(2.09)	166,313	(732)	(1.77)
Interest margin			1.78			1.69

See remarks below.

Interest Revenues and Expenses Rates - of the Bank and its Subsidiaries[1] - continued

Reported amounts (NIS in millions)

B. Average balances and interest rates - additional information about interest-bearing assets and liabilities attributed to operations in Israel

	For the six months ended June 30, 2018 Average balance[2]	For the six months ended June 30, 2018 Interest expenses (revenues)	For the six months ended June 30, 2018 Expense (revenue) rate In %	For the six months ended June 30, 2017 Average balance[2]	For the six months ended June 30, 2017 Interest expenses (revenues)	For the six months ended June 30, 2017 Expense (revenue) rate In %
Israeli currency - non-linked						
Total interest-bearing assets	160,512	2,149	2.70	152,070	1,982	2.62
Total interest-bearing liabilities	115,283	(438)	(0.76)	107,351	(347)	(0.65)
Interest margin			1.94			1.97
Israeli currency - linked to the CPI						
Total interest-bearing assets	51,972	1,195	4.65	50,419	1,024	4.10
Total interest-bearing liabilities	36,060	(638)	(3.57)	38,577	(614)	(3.21)
Interest margin			1.08			0.89
Foreign currency (including Israeli currency linked to foreign currency)						
Total interest-bearing assets	12,958	204	3.17	12,272	159	2.61
Total interest-bearing liabilities	15,950	(149)	(1.88)	17,634	(90)	(1.02)
Interest margin			1.29			1.59
Total - operations in Israel						
Total interest-bearing assets	225,442	3,548	3.17	214,761	3,165	2.97
Total interest-bearing liabilities	167,293	(1,225)	(1.47)	163,562	(1,051)	(1.29)
Interest margin			1.70			1.68

Interest Revenues and Expenses Rates - of the Bank and its Subsidiaries[1] - continued

Reported amounts (NIS in millions)

C. Analysis of change in interest revenues and expenses

	For the three months ended June 30, 2018 compared to the three months ended June 30, 2017 Increase (decrease) due to change[10] Quantity	For the three months ended June 30, 2018 compared to the three months ended June 30, 2017 Increase (decrease) due to change[10] Price	For the three months ended June 30, 2018 compared to the three months ended June 30, 2017 Increase (decrease) due to change[10] Net change	For the six months ended June 30, 2018 - compared to the six months ended June 30, 2017 Increase (decrease) due to change[10] Quantity	For the six months ended June 30, 2018 - compared to the six months ended June 30, 2017 Increase (decrease) due to change[10] Price	For the six months ended June 30, 2018 - compared to the six months ended June 30, 2017 Increase (decrease) due to change[10] Net change
Interest-bearing assets						
Loans to the public						
In Israel	118	178	296	192	170	362
Outside of Israel	5	9	14	6	16	22
Total	123	187	310	198	186	384
Other interest-bearing assets						
In Israel	(1)	6	5	2	19	21
Outside of Israel	(5)	12	7	(13)	23	10
Total	(6)	18	12	(11)	42	31
Total interest revenues	117	205	322	187	228	415
Interest-bearing liabilities						
Deposits from the public						
In Israel	3	55	58	10	103	113
Outside of Israel	2	7	9	1	14	15
Total	5	62	67	11	117	128
Other interest-bearing liabilities						
In Israel	14	69	83	29	32	61
Outside of Israel	-	-	-	-	-	-
Total	14	69	83	29	32	61
Total interest expenses	19	131	150	40	149	189

(1) Information in these tables is after effect of hedging I derivative instruments.
(2) Based on balances at start of the months (in Israeli currency, non-linked segment - based on daily balances).
(3) Before deduction of average balance sheet balance of provisions for credit losses. Includes impaired debt not accruing interest revenues.
(4) From (to) the average balance of debentures available for sale, for the three-month periods ended June 30, 2018 and June 30, 2017, and for the six-month periods ended June 30, 2018 and June 30, 2017, we deducted (added) the average balance of unrealized gains (losses) from adjustment to fair value of debentures available for sale, included in equity under Cumulative Other Comprehensive Income, under "Adjustments with respect to presentation of securities available for sale at fair value", amounting to NIS (96) million, NIS (16) million, NIS (70) million and NIS (25) million, respectively.
(5) From the average balance of debentures held for trading, for the three-month periods ended June 30, 2018 and June 30, 2017, and for the six-month periods ended June 30, 2018 and June 30, 2017, we deducted (added) the average balance of unrealized gains from adjustment to fair value of debentures held for trading amounting to NIS (3) million, NIS (2) million, NIS (2) million and NIS (1) million, respectively.
(6) Includes derivative instruments, other non-interest bearing assets, net of provision for credit losses.
(7) Commissions amounting to NIS 64 million, NIS 45 million, NIS 127 million and NIS 105 million were included in interest revenues for the three-month periods ended June 30, 2018 and June 30, 2017 and for the six-month periods ended June 30, 2018 and June 30, 2017, respectively.
(8) Includes derivative instruments.
(9) Net return - net interest revenues divided into total interest-bearing assets.
(10) The change attributed to change in quantity was calculated by multiplying the new price by the change in quantity. The change attributed to change in price was calculated by multiplying the old quantity by the change in price.

Glossary and index of terms included on the financial statements

Below is a summary of terms included on the financial statements:

1. Terms with regard to risks management at the Bank and to capital adequacy

B	**Basel - Basel II / Basel III** - Framework for assessment of capital adequacy and risk management, issued by the Basel Committee on Bank Supervision.
C	**CVA** - Credit Valuation Adjustment - CVA is the component of the fair value of a derivative, which accounts for the credit risk of the counter-party to the transaction. CVA risk is the risk of loss due to mark-to-market with respect to expected counter-party risk for OTC derivatives. This means - loss due to impairment of fair value of derivatives, due to an increase in counter-party credit risk (such as: lower rating). **Counter-party credit risk** - The risk that the other party to a transaction would be in default before final settlement of cash flows in the transaction.
E	**EVE - Economic Value of Equity** - The economic value approach to analysis and estimation of the effect of changes in interest rates on the fair value of assets, liabilities and off-balance sheet positions of the Bank.
I	**ICAAP -** Internal Capital Adequacy Assessment Process by the Bank. This process includes, *inter alia*, setting capital targets, capital planning processes and review of capital status under various stress scenarios. This process is part of Pillar 2 of the Basel II directive.
L	**Loan To Value Ratio (LTV)** - The ratio between the approved facility when extended and the asset value.
M	**Minimum capital ratio** - This ratio reflects the minimum supervisory capital requirements which the Bank is required to maintain in conformity with Proper Banking Conduct Directive 201.
S	**Standard approach -** An approach used to calculate the required capital with respect to credit risk, market risk or operational risk. Calculation of capital allocation is based on a formula, which is based on supervisory assessment components which have been specified by the Supervisor of Banks. **Supervisory capital (total capital)** - Supervisory capital consists of two tiers: Tier I capital, which includes Tier I shareholders' equity and additional Tier I capital. Tier II equity: As defined in Proper Banking Conduct Directive 202 "Measurement and capital adequacy - supervisory capital". **Subordinated notes** - Notes whose rights are subordinated to claims by other Bank creditors, except for other obligations of the same type. **Stress tests** - A title for various methods used to assess the financial standing of a banking corporation under a n extreme scenario.
P	**Pillar 2** - The second pillar of the Basel II project, refers to the Supervisory Review Process. This part consists of the following basic principles: - The Bank shall conduct the ICAAP process, as defined above. - The Supervisor shall conduct a process to assess the ICAAP process conducted by the Bank, to review the Bank's capacity to monitor and achieve supervisory capital ratios. - The Bank is expected to operate above the specified minimum capital ratios. **Pillar 3** - The third pillar of the Basel II project, designed to promote market discipline by developing a set of disclosure requirements, which would allow market participants to assess the capital, risk exposure and risk assessment processes - and use these to assess the Bank's capital adequacy.
R	**Risks document -** A document which concisely presents the Bank's risk profile, in order to allow the Board of Directors to monitor action taken by management and to ensure that such action is in line with the risk appetite and with the risks management framework approved by the Board of Directors. The Risks Document is compiled and presented to the Board of Directors quarterly. **Risk assets** - These consist of credit risk, operational risk and market risk, calculated using the standard approach as stated in Proper Banking Conduct Directives 201-211.
V	**VAR** - A model used to estimate overall exposure to diverse market risk factors. The VaR (Value at Risk) obtained by the model is a statistical estimate of the maximum expected loss for the Bank due to materialization of market risks factors in a given time period at a pre-determined statistical confidence level.

2. Terms with regard to banking and finance

A

Active market - A market where transactions involving an asset or liability take place regularly and in sufficient volume, so as to regularly provide information about pricing of assets and liabilities.

Average effective duration - The average term to maturity of debentures. Measured in years, by weighting principal and interest payments for the debenture over its term to final maturity. The average effective duration of a debenture reflects the financial instrument's sensitivity to changes in interest rates. Average effective duration is calculated as the ratio between the weighted average debenture payouts to its price.

D

Derivatives - A financial instrument or contract whose value changes in response to changes in the price of the underlying asset (a financial instrument, physical asset, index, credit rating or other underlying asset), requires a small or minimal initial investment, compared to other contract types, and is expected to be settled on a future date.

Debentures - Securities which are obligations by the issuer to pay to the debenture holder the principal issued plus interest, on specified dates or upon realization of a specified condition.

Debt whose collection is contingent on collateral - Impaired debt whose repayment is expected through realization of collateral provided to secure such debt.

Debt under restructuring - Problematic debt under restructuring is defined as debt for which, for economic or legal reasons related to financial difficulties of the debtor, the Bank has made a concession by way of modification to terms and conditions of the debt, designed to make it easier for the debtor to make cash payments in the near term (reduction or postponement of cash payments due from the debtor), or by way of receiving other assets as debt repayment (in whole or in part).

Debt under special supervision - Debt under special supervision is debt with potential weaknesses, which require special attention by Bank management. Should these weaknesses not be addressed, the likelihood of debt repayment may deteriorate.

F

Financial instrument - A contract that creates a financial asset for one entity and a financial liability or capital instrument for another entity.

I

Indebtedness - On- and off-balance sheet credit, as defined in Proper Banking Conduct Directive 313.

Inferior debt - Inferior debt is debt insufficiently secured by collateral or by debtor repayment capacity, and for which the Bank may incur a loss if faults are not corrected, including debt over NIS 700 thousand which is 60-89 days in arrears.

Impaired debt - Debt is classified as impaired when its principal or interest is in arrears over 90 days, unless the debt is well secured and is in collection proceedings. Further, any debt whose terms and conditions have been changed in conjunction with restructuring of problematic debt would be classified as impaired debt, unless prior to and following such restructuring, a provision for credit losses by extent of arrears was made with respect to the debt pursuant to the appendix to Proper Banking Conduct Directive 314 on problematic debt in housing loans.

OTC - Over the Counter - Transaction involving financial instruments which is conducted over the counter and not on a stock exchange.

Off-balance sheet credit - Contracting for providing credit and guarantees (excluding derivative instruments).

Problematic debt - Debt classified under one of the following negative classifications: special supervision, inferior or impaired.

Recorded debt balance - The debt balance, including recognized accrued interest, premium or discount yet to be amortized, net deferred commissions or net deferred costs charged to the debt balance and yet to amortized, net of the debt amount subject to accounting write-off.

Syndication - A loan extended jointly by a group of lenders.

3. Terms with regard to regulatory directives

E

EMIR - European Market Infrastructure Regulation - EU regulations adopted in order to increase stability, transparency and efficiency of derivative markets.

FATCA - Foreign Accounts Tax Compliance Act - The US Foreign Accounts Tax Compliance Act stipulates mandatory reporting to the US tax authority (IRS) of accounts held by US persons with foreign financial institutions (outside the USA).

LCR - Liquidity Coverage Ratio is defines as the ratio of High Quality Liquid Assets and net cash outflow for the next 30 days, under a stress scenario. This ratio is a benchmark for the Bank's capacity to fulfill its liquidity needs for the coming month.

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