

Translation of Immediate Report

Bank Leumi le-Israel B.M.

Registration No. 520018078
Securities of the Corporation are listed on The Tel Aviv Stock Exchange
Abbreviated Name: Leumi
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7 July 2015
Reference: 2015-01-067953

To: Israel Securities Authority (www.isa.gov.il)
The Tel Aviv Stock Exchange (www.tase.co.il)

Immediate Report

Nature of Event: End of Tenure - Chief Risk Officer

See the attached annex.

Date and time at which the corporation first became aware of the matter being the subject of the report: 7 July 2015 Time: 15:00.

Note: English translations of Immediate Reports of Bank Leumi are for convenience purposes only. In the case of any discrepancy between the English translation and the Hebrew original, the Hebrew will prevail.
The original Hebrew version is available on the distribution website of the Israel Securities Authority:

<http://www.magna.isa.gov.il/>

Name of Electronic Reporter: David Raoul Sackstein, Position: Advocate, General Secretary
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7 July 2015

To

Tel Aviv Stock Exchange
Ahuzat Bayit Street 2
Tel Aviv 6525216

To

Israel Securities Authority
Kanfei Nesharim Street 22
Jerusalem 95464

Dear Sir or Madam:

Re: **Non-substantive update of the terms of employment for the Chief Risk Officer in light of the end of her tenure**

Pursuant to the Bank's Immediate Report dated 11 June 2015 (Reference No. 2015-01-046185), regarding the notice given by Dr. Hedva Ber to the Bank's Board of Directors concerning her intention to end her tenure as the Chief Risk Officer of the Bank and of the management company, in light of the decision reached by the Governor of the Bank of Israel to appoint her to serve as the Supervisor of Banks; and pursuant to the Immediate Report dated 5 July 2015, regarding the end of Dr. Ber's tenure at the Bank, the Bank hereby announces the resolutions of the Compensation Committee and of the Bank's Board of Directors to update the terms of Dr. Ber's employment, in a non-substantive manner, as described below:

1. Manner in which decisions were reached

- 1.1 The Board of Directors' Compensation Committee deliberated and adopted a resolution on 1 July 2015, pursuant to section 272(d) of the Companies Law, 5759-1999, and the Board of Directors itself deliberated and approved a resolution on 7 July 2015, as provided in Section 301 of the Proper Banking Management Divisions.
- 1.2 Background information that was presented to the said Bank organs prior to the adoption of the Resolution included, *inter alia*: (a) Dr. Ber's current terms of employment; (b) the Remuneration Policy for the Bank's corporate officers; (c) legal opinions regarding the matter provided to the Committee by external legal advisers; and (d) an economic opinion regarding the matter, provided by an external economic expert.

2. The background for the resolutions adopted by the Compensation Committee and by the Board of Directors

- 2.1 The Remuneration Policy for the Bank's corporate officers establishes the fixed remuneration and the variable remuneration to which corporate officers at the Bank are entitled. Accordingly, the Remuneration Policy provides that the Bank's corporate officers will be entitled to a variable annual bonus once the threshold conditions established in the Remuneration Policy are satisfied, with the amount of the bonus being determined according to the parameters and conditions established in the policy.
- 2.2 According to the Remuneration Policy, and after the publication of the Bank's financial results for 2013, it was determined that the Bank's corporate officers, including Ms. Ber,

would be entitled to a variable annual bonus with respect to that year. It should be noted that with respect to 2014, the Bank's corporate officers, including Ms. Ber, would not be entitled to such a variable annual bonus.¹

- 2.3 Pursuant to the Remuneration Policy, half of the amount of the variable annual bonus for 2013 was paid in cash to the Bank's corporate officers, including to Dr. Ber, shortly after the reporting of the Bank's financial results for 2013. The second half was given to the corporate officers (and to Dr. Ber) through blocked performance share units (PSU's) that were allocated to these corporate officers close to the above-mentioned date.

For a description of the said allocation, see the Bank's Immediate Report regarding the private offering, dated 31 March 2014 (Reference No. 2014-01-030870) (the "Private Offering Report"). For additional details regarding the Remuneration Policy, see the Private Offering Report to which the Remuneration Policy was attached as Appendix A (above and below, the "Remuneration Policy").

- 2.4 Pursuant to the provisions of the Remuneration Policy, the PSU units mature into Bank shares over the course of three years, in three equal tranches - if the conditions established in the Remuneration Policy for their maturity are satisfied. These conditions depend on the Bank's results for each one of the calendar years preceding the maturity date of the relevant tranche of the PSU units. For a description of the conditions for the maturity of the PSU units into shares on the maturity dates, see the Private Offering Report and the Remuneration Policy.
- 2.5 Pursuant to the above, PSU units were allocated to Ms. Ber in an amount reflecting 50% of the variable annual bonus for 2013, with the first tranche of the above-mentioned PSU units maturing into shares one year after the allocation, and those shares being blocked for an additional year. (The first tranche was comprised of one third of the PSU units that were allocated to her.) The balance of the PSU units that have not yet matured and are expected to mature in two equal tranches, shortly after the date of the publication of the Bank's annual reports for 2015 and 2016, respectively, subject to the satisfaction of the said conditions for their maturity.
- 2.6 It is clarified that pursuant to the provisions of the Bank's Remuneration Policy, a corporate officer's voluntary resignation from the Bank does not undo or cancel the officer's entitlement to the release of the remainder of a variable annual bonus which had already been awarded and the release of which had been delayed.

¹ We note, in order to provide a complete picture, that regarding the variable annual bonus for 2015, Ms. Ber notified the Bank that she was waiving her right to such a variable annual bonus in advance, if she were entitled to such a bonus. She did this in order to prevent a conflict of interest with her new position, since the receipt of the said variable annual bonus depends on the Bank's results in 2015. We nevertheless note that the Bank's corporate officers who hold audit and control positions are entitled to a fixed annual bonus of a single monthly **portion** (as described in the remuneration policy). Ms. Ber is therefore entitled to receive the proportionate share of the above-mentioned fixed annual bonus, taking note of the number of months in which she actually worked at the Bank during 2015 (about half a year.)

- 2.7 Under the unique circumstances of Ms. Ber's departure from the Bank, and taking note of the position which Ms. Ber will be holding as the Supervisor of Banks at the Bank of Israel, and in order to prevent any concern regarding a conflict of interest with her position, Dr. Ber may not continue to hold shares in the Bank (or shares in any other Bank) and/or continue to be entitled to payments from the Bank which are dependent on the Bank's results for the years 2015 and 2016. We note, regarding this matter, that according to the conflict of interest prevention arrangement established for Dr. Ber, she may not continue to hold bank shares, including shares in the Bank.
- 2.8 It is also noted that in order to prevent a suspicion of a conflict of interest, Dr. Ber announced that she was waiving, in advance, the proportionate part of the variable annual bonus for 2015. The part that she waived is that part to which, according to the remuneration program, she is entitled in proportion to the part of 2015 during which she was employed at 2015.

3. The Resolution of the Compensation Committee and of the Board of Directors

- 3.1 The Compensation Committee and the Board of Directors decided that despite Dr. Ber's entitlement to the deferred part of the variable annual bonus for 2013, as described above, and which was already given to Dr. Ber at the beginning of 2014 and which should be released from the blocking period in 2015 and 2015 (8,909 blocked regular shares in the Bank and 17,819 PSU units, as described in section 2.5 above) a single payment will be paid to Dr. Ber, close to the time of the conclusion of the employment relationship between the parties, as described below.
- 3.2 The payment that Dr. Ber will receive as stated will be at the current economic value (**reduced** value) of the deferred bonus for 2013, pursuant to the outline that was formulated and presented to the Compensation Committee and the Board of Directors by the external economic expert ("the Outline"). According to this Outline, the current economic value was determined after a reduction, in an amount that reflects an overall economic calculation a discount expressing both the uncertainty as to whether the conditions for maturity of the PSU units will be satisfied and a discount expressing the fact of the actual early payment. As a result, it was determined that the total discount would be at the rate of 21% of the value of the deferred remuneration (before the reduction). The amount that will be released after the discount is approximately NIS 347,000. It should be noted that Dr. Ber will pay any taxes resulting from the approved change. This outline was adopted by the Compensation Committee and the Board of Directors - **in order for Ms. Ber not to receive any benefit that would appear to be involved in the early payment** of the said deferred part of the bonus.

4. The reasoning of the Compensation Committee and of the Board of Directors

- 4.1 In reaching their decision, the Compensation Committee and the Board of Directors took into consideration, *inter alia*, the principles of the Outline formulated on the basis of the external economic expert, and the fact that there is nothing in the said Outline that grants Ms. Ber any financial benefit in comparison to the existing contractual terms and/or in

comparison to the contractual terms for the other corporate officers at the Bank who are entitled to an annual bonus for 2013. As stated above, the payment that Ms. Ber received instead of the deferred part of the annual bonus for will reflect a reduction, on the basis of an external economic opinion, reflecting both the probability of the Bank's satisfying the conditions for the maturation of the deferred portions that had not yet matured, and in light of the early actual payment of the deferred part. Taking note of the above, the members of the Committee and of the Board of Directors, after holding a deliberation regarding the matter and in light of the legal and economic opinions presented to them, found that the proposed step did not create either a benefit or a loss for Ms. Ber from a financial perspective, in relation to her current terms of employment, and which [thus] constitutes a non-substantive change in the composition of her existing remuneration, as established in the Bank's Remuneration Policy.

- 4.2 The resolution was adopted by the Compensation Committee and the Board of Directors, in light of the function that Ms. Ber will be carrying out as the Supervisor of Banks at the Bank of Israel. This position will not allow Ms. Ber to continue to have any connection, financial or other, with the Bank. As stated, the Bank of Israel's internal directive prohibits a Bank of Israel employee from holding any bank shares. Against this background, the Compensation Committee and the Board of Directors believed that to the extent possible, they should take a course of action that does not discriminate against Ms. Ber and does not deny her entitlement to the bonus which had already been formulated pursuant to the Bank's Remuneration Policy and the Bank's results for 2013, for the payment of a variable bonus with respect to 2013.
- 4.3 The Compensation Committee also took into consideration the fact that Dr. Ber had, on her own initiative, announced that she was waiving her entitlement to the proportionate share of the variable bonus for 2015. She announced this waiver despite the fact that according to the remuneration plan she was entitled to a proportionate part of the bonus that will be determined for 2015, based on the portion of the year 2015 during which she was employed.
- 4.4 The members of the Compensation Committee and of the Board of Directors also considered, in reaching their decision, the special circumstances of Ms. Ber's resignation, and noted that this was an exceptional incident, which will not repeat itself, and which therefore does not have any broad impact and does not constitute and cannot constitute a precedent with respect to other corporate officers at the Bank who may resign from their positions at the Bank to take other positions. The absence of any possibility of her continuing to hold shares or PSU units in the Bank is a unique problem and inherent to the position of being the Supervisor of Banks, as the Supervisor is an official who is meant to supervise the Bank and the banking system as a whole. This situation does not arise with respect to other positions. Thus, the Compensation Committee and the Board of Directors believed that the harm done to the purpose of the arrangement for the deferral of the variable remuneration payments which is established in the Remuneration Policy would be marginal and of only limited scope.

- 4.5 When, during 2013, decisions were reached and actions taken by the Bank's corporate officers were approved, the corporate officers who served in the Bank that year, including Ms. Ber, knew that the annual bonus for that year would also be examined, partially, in light of the realization of the risks involved in those decisions and actions, over the course of the following three years, in accordance with the mechanism that had been established in the Remuneration Policy. In this sense, the members of the Compensation Committee and of the Board of Directors believed that the Outline did not do any retroactive harm to the incentives that motivated the said corporate officers, including Ms. Ber, in the year 2013. In light of this as well, and taking into consideration the scope of the Outline and its limited application (this is an Outline which affects only the date of payment of the deferred portions, which relates to a bonus for only one year, and to only a single corporate officer among the 15 corporate officers who received an annual bonus for the year 2013), the Compensation Committee and the Board of Directors determined that given the circumstances, no harm was done to the objective of the deferral arrangement for the payment of the variable remuneration which is established in the Remuneration Policy, and to the extent that such harm is done, it is marginal and only of limited scope.
- 4.6 The Compensation Committee and the Board of Directors, in reaching their decisions, took into consideration, *inter alia*, various guidelines issued by the Bank Supervision Department for the purpose of implementing section 301A of the Proper Banking Management Directive, according to which the Bank Supervision Department recognized that there were cases which would involve elements that supersede the interest that forms the basis of the deferral arrangement and of the policy of spreading out the payment of the variable remuneration.

Sincerely,

Bank Leumi Le'Israel Ltd.

By: Dani Cohen, Head of the Human Resources Division

Hanan Friedman, Legal Adviser