

**UPDATE OF CHAPTER A (DESCRIPTION OF COMPANY OPERATIONS)¹
OF THE PERIODIC REPORT FOR 2007 ("THE PERIODIC REPORT")
OF "BEZEQ" – THE ISRAEL TELECOMMUNICATIONS CORP. LTD. (HEREINAFTER: "the Company")**

In this report, which contains an update of the chapter regarding the description of the Company's business in the 2007 periodic report, the Company has included forward-looking information, as defined in the Securities Law 5728-1968 (hereinafter: the "Securities Law") with respect to both itself and the market. Such information includes forecasts, goals, appraisals and assessments which apply to future events or matters the occurrence of which are not certain and are not within the Corporation's control. Forward-looking information in this report will usually be identified specifically, or by employing statements such as "the Company expects", "the Company estimates", "it is the Company's intention", and similar statements.

Forward-looking information is not a proven fact and is based only on the Corporation's subjective assessment, which relies on its assumptions based, *inter alia*, on a general analysis of the information available at the time of drafting of this report, including public announcements, research and surveys, which contain no undertakings as to the correctness or completeness of the information contained therein, and whose correctness has not been independently corrected by the Corporation. The Corporation's assessments vary from time to time in accordance with the circumstances.

In addition, the occurrence or non-occurrence of the forward-looking information will be affected by factors that cannot be assessed in advance, and which are not within the Corporation's control Corporation, including the risk factors that characterize its operations as set out in this report, and additionally, developments in the general environment, and external factors and the regulation that affects the Corporation's operations, as set out in this report.

1. Description of General Development of Group Operations

Section 1.1 – Group Activity and Description of its Business Development

A. The Worldwide Economic Crisis

During the current quarter, subsequent to the worldwide economic crisis, global markets have entered a slowdown and credit choke. It is assumed that this situation will continue to be felt throughout 2009 and possibly worse, with a shift from growth to recession. A significant slowdown and decline of business operations and key economic parameters are also expected in the local market. The Corporation assumes that this crisis may have a negative impact on its operations, but cannot at this stage estimate the scope of such impact on the Group's operation

This information includes forward looking information based on internal estimates of the Company. The actual results may be materially different from the foregoing estimates if changes take place in any of the factors taken into account for this assessment.

B. Gronau Committee Report

On March 12, 2008, the Gronau Committee, appointed by the Minister of Communications to formulate detailed recommendations regarding policy and rules of competition in the field of communications in Israel (the "Gronau Committee"), published its Report. Following are the principal summary recommendations:

Fixed-Line Sector

1. To act to develop the wholesale market in the fixed-line sector, centered around the local loop unbundling (hereinafter - "LLU") obligation. In this context, the owners of the universal infrastructure are required to sell services wholesale and lease access segments to competitors. For reasons of technological applicability, at this stage the local loop unbundling obligation will only apply to the Company.

¹ The update is pursuant to Article 39A of the Securities Regulations (Periodic and Immediate Reports), 5730-1970, and includes material changes or innovations that have occurred in the corporation in any matter which must be described in the Periodic Report. The update relates to the Company's periodic report for 2007 and relates to the section numbers in Chapter A (Description of Company Operations) in such periodic report.

2. Within 15 months of the date of adoption of the recommendation by the Minister of Communications, the regulating body will publish maximum tariffs for the leasing of access segments and other services sold on the wholesale market (bitstream access services, resale, etc.) and the conditions for provision of such services. Such tariffs and conditions are to be determined subsequent to hearing the positions of the entities operating in the segment.
3. To grant a permit to the Company's subsidiaries to supply non-degradable service packages², including Bezeq Fixed-Line telephony and broadband services and IPTV, after implementation of the arrangement set out in section 1 above. On that date, the subsidiaries of the Company shall also be entitled to receive special licenses for the supply of domestic carrier services that are not VOB.
4. So long as the Bezeq Group's market share is greater than 60%, supervision of the Company's tariffs shall continue in the format of fixing binding tariffs (fix); various restrictions (as set out in the recommendations) shall be set with respect to approval of alternative tariff bundles for the Company; with respect to supervised tariffs - up until the middle of 2009, cost-based tariffs will be prescribed for call completion on the fixed-line network; with respect to non-supervised tariffs, "loyalty discounts" will be prohibited so long as the Company is a monopoly: PRI lines - if there is no significant change in market share, the prices of these will come under supervision.
5. The structural separation in the Company is to remain so long as there are only two companies with nationally deployed fixed line infrastructure. Likewise, if the Minister of Communications finds, within a reasonable time of implementation of the local loop unbundling arrangement (no longer than two years), that the Company's actions are preventing expansion of competition in the domestic communications market, the recommendation is that he will exercise his powers under section 4(d2)(3) of the Communications Law regarding structural separation between operation of the infrastructure and operation of services at the Company.

Cellular Sector

It is necessary to accelerate the regulation processes required for the entry of virtual carriers, to accelerate the WiMAX tender in order to strengthen competition in the mobile sector and additionally, during 2009, to check the cost of call completion on mobile networks and to amend the tariff accordingly.

International Call Sector

International call tariffs via mobile telephones to be prescribed by the international calling company, and that company will make payments to the cellular company at the tariff determined in the Interconnect Regulations for call completion on mobile networks. Furthermore, new players controlled by the cellular companies shall be permitted entry into the international call sector.

Multi-Channel Television

1. Setting up of a "narrow basic channel package", including 5-10 channels (open channels and channels of special social or cultural value), with the possibility that the regulating body might determine the price of the package.
2. Enforcement of structural separation between Hot Broadcasts and Hot Telecom in the framework of their licenses, in accordance with the existing format in place in the Company.

General

Consumer Issues - The OECD recommendations are a guiding framework for handling consumer issues. It shall be prohibited to change fixed tariffs in a contract with customers during the contract term, the term of contracts shall be limited to 18-24 months and the prevention of transfer due to the tying of purchase of a handset to purchase of services will be removed.

Royalties - adoption of the position taken by the Carol Committee regarding the gradual reduction of the rate of royalties payable by licensees, up to cancellation of such royalties in the future. If there is a reduction of taxes during 2008-2012, the royalties will be cancelled. It is proper that cancellation of the royalties accompany a parallel reduction in tariffs.

On August 13, 2008, the Minister of Communications announced his decision to adopt the Committee's recommendations, subject to changes and points of emphasis, which will become the

² For which there is no obligation for any service included in such packages to be purchased individually under similar terms as provided in the service package.

Ministry's guiding policy for the upcoming years. The Minister's decision clarifies the regulatory situation to a certain extent. Hereunder, please find the principal changes and points of emphasis:

Structure Changes in the Fixed Line Sector

According to the decision of the Minister of Communications, the Ministry of Communications will commence work on preparing the regulatory and pricing infrastructure required to establish a wholesale market, including arrangements for separation into segments (LLU). Nonetheless, in order to provide an incentive for the Company to implement the wholesale market arrangements as quickly as possible, the Company will be allowed to present the Ministry with a commercial agreement for the provision of wholesale services with any communications operator that is not a subsidiary of the Company.

The Minister agrees with the Committee regarding the importance of the fixed telephone infrastructure. Therefore, as long as the Minister thinks that it is appropriate to create incentives for the Company, which will advance rapid, universal deployment of the next generation network (NGN), he will work to do so.

Tariff Flexibility for Bezeq – Alternative Service Packages

In order to streamline the process for approving alternate payment packages and provide a higher level of certainty for the Company, the Minister decided to change the mechanism for approving alternate payment packages, such that the Company will not need to wait until the explicit approval of two Ministers is received but rather it will be able to offer a package 45 days subsequent to the detailed request being filed at the Ministry of Communications unless the Minister of Communications or the Minister of Finance informs it of their objection to the request. It should be noted that the Minister adopted the Committee's recommendation that as long as the Bezeq Group's market share is greater than 60%, regulation of the Company tariffs will continue in accordance with the current format of setting obligatory ("fix") tariffs. Regarding alternative payment packages, the maximum permitted discount rate will increase as the Group's market share for fixed telephony decreases (it will remain 15% as long as the market share is greater than 85%; 25% as long as the market share is between 75% and 85%; and 40% when the market share is between 60% and 75%).

Competition in the Mobile Field

The Minister instructed the CEO of the Ministry of Communications to work towards advancing a licensing policy for virtual operators (MVNO).

Multi-Channel Television Sector – Basic Package of Channels

The Minister decided to conduct a more comprehensive examination of all aspects of the broadcast field. Therefore, he announced that in the near future, it is his intention to appoint a committee to provide recommendations regarding policy and terms of competition in the multi-channel and commercial television sector. It is noted that the Minister of Communications appointed an inter-ministerial committee to regulate the commercial television sector and subsequently, on October 12, 2008 the committee announced a hearing to be replied by December 1, 2008.

Structural Separation in the HOT Group

According to the decision of the Minister of Communications, the Ministry of Communications will work in order to ensure that the companies in the Hot Group comply with the rules of structural separation established in their licenses, with the exception of the possibility available to the companies, of marketing packages of services that include services offered by the companies, on a regular basis as is currently permitted by their licenses, contrary to the committee's decision, which was that the terms of separation in the form applied to the Company, should be enforced.

The guidelines for structural separation must make it possible to implement the recommendations regarding the wholesale markets in general and its prices in particular.

International Call Sector – Entrance of Players Controlled by Mobile Companies to the International Call Sector

The Minister is of the opinion that the recommendations of the Committee regarding setting fees for outgoing international calls using a mobile network in the framework of the interconnect regulations should be advanced.

The Company is examining the decisions of the Minister and is unable to assess, at this stage, what their precise impact will be on its business results and those of its subsidiaries.

See also updates to sections 3.7, 4.1.2 and 5.1.3.5 below.

Section 1.1.4 - Holdings of the Company

The following are details of the current rate of holdings of the Company, fully diluted, assuming the exercise of all of the options actually allocated to employees of the Company as of September 30, 2008 and November 23, 2008 (as set out in the Periodic Report for 2007 and in the update to section 1.3.2 below, including the allocation to the Chairman of the Board of Directors, made on June 1, 2008), and subsequent to the exercise of Ap. Sab. Ar.'s option to purchase approximately 10.66% of the State's shares in the Company (see update to section 1.3 hereunder):.

Shareholders	Holdings		
	As of 30.9.08	As of 23.11.08	Fully diluted
Ap.Sb.Ar	40.66%	40.66%	38.65%
State of Israel	4.95%	4.70%	0.96%
Zeevi Group	17.75%	17.75%	16.87%
Public	36.64%	36.89%	43.52%

Section 1.1.5A – Mergers and Acquisitions – DBS

The hearing of an appeal filed by the Company in the Antitrust Court, against the decision of the Antitrust Commissioner to object to the Company's merger with DBS, is at the closing stage.

Section 1.1.6 - Realizations

With respect to the satellite communication operations - on March 26, 2008, an agreement regarding the sale of the Company's satellite communications operations ("Inmarsat" and "Bezeq Sat") and assets relating to such operations, including the satellite communications site at the Ella Valley, was executed between the Company and RRsat Global Communications Network Ltd., a company registered in Israel whose shares are traded on NASDAQ in the USA for consideration in the NIS amount equivalent to US \$ 15 million plus VAT, subject to price adjustments. Conclusion of the transaction was subject, *inter alia*, to the regulatory consent of the Ministry of Defense, the Ministry of Communications and the Antitrust Commissioner and on November 4, 2008 the transaction was completed subsequent to the fulfillment of all the conditions required for its conclusion, including receipt of the regulatory consent. With respect to this transaction, the Company will record in its financial statements for the period ending December 31, 2008, capital gains of NIS 50 million (gross before tax).

Section 1.3 – Investments in the Corporation's Equity and Transactions in its Shares

Section 1.3.1 – Exercise of Ap. Sab. Ar option

On September 25, 2008, Ap.Sab.Ar acquired 277,697,862 ordinary shares of the Company from the State, by way of fully exercising the option granted to Ap.Sab.Ar by virtue of the purchase agreement for the controlling interest in the Company between Ap.Sab.Ar and the State of Israel signed on October 11, 2005. The consideration for the option exercise is NIS 1.08 billion. Per Ap.Sab.Ar's request, the holder of the acquired shares is registered in the name of the trust company (Romema Trust Ltd.).

As a result of the exercise of options as aforesaid, Ap.Sab.Ar's holding in the Company has increased to 40.66% (38.64% fully diluted) and the State's holding declined as a result to 4.95% (0.96% fully diluted) and from that date on, the State ceased to be an interested party in the Company

Section 1.3.2 - Employee Share Option Plans

Under the share option plan for senior managers and employees of the Group of November 2007 for the allocation of up to 65,000,000 options, since the date of publication of the 2007 periodic report and as at September 30, 2008, the date of the publication of this report, 21,450,000 additional options have been allotted (including the allotment of 9,000,000 options to the Chairman of the Board of Directors of the Company and 4,250,000 options to the CEO of DBS) such that as of the date of this update, a net total (less options that have been forfeited) of 57,650,000 options have been allotted through the plan (57,750,000 options as at September 30, 2008).

Section 1.4 – Payment of Dividends

On April 28, 2008, a cash dividend for a total amount of NIS 679 million was distributed to the Company shareholders, representing, as at the date of the distribution NIS 0.260648 per share, this having been approved by the General Meeting of shareholders of the Company on April 3, 2008.

On October 29, 2008, a cash dividend was distributed to the Company's shareholders in a total amount of NIS 835 million, representing, as at the date of the distribution NIS 0.3205318 per share, subsequent to the approval by the General Meeting of shareholders of the Company on September 28, 2008.

Section 1.5 - Financial Information regarding the Group's Areas of Operations

Section 1.5.3 - Principal Results and Operational Data

A. Bezeq Fixed-Line (operations of the Company as domestic carrier)

	Q3 2008	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q 2 2007	Q1 2007
Revenues (NIS millions)	1,388	1,354	1,408	1,453	1,425	1,393	1,442
Operating Profit (NIS millions)	422	428	368	340	327	243	369
Depreciation and amortization (NIS millions)	214	211	218	232	236	236	237
EBITDA (NIS millions)	636	639	586	572	563	479	606
Payments for investments in property, plant and equipment and intangible assets (NIS millions) ¹	156	132	158	141	149	101	113
Proceeds received from sale of property, plant and equipment (NIS millions) ¹	12	25	60	23	16	96	18
Number of active subscriber lines at the end of the period (thousands)	2,645	2,681	2,712	2,761	2,767	2,778	2,798
Average monthly revenue per line (NIS) ²	84.3	81.8	83.9	86.1	85.9	85.4	88.5
Number of outgoing call minutes used (millions) ³	3,425	3,346	3,511	3,653	3,760	3,654	3,802
Number of incoming call minutes used (millions) ⁴	1,708	1,655	1,673	1,661	1,651	1,553	1,545
Number of ADSL subscribers at the end of the period (thousands)	994	982	970	963	942	924	912
Average monthly revenue per ADSL subscriber (NIS) ⁵	67.3	66.5	68.3	68.6	63.5	62.1	61.4

1 Data for Q1 2008 were updated retroactively, in order to reflect the timing of payments of investments in property, plant and equipment and receipts from sale of property, plant and equipment.

2 Not including revenues from transmission and data communications services, internet services, services to communications providers, and other contractor work. In this item, insignificant adjustments were made to prior quarters in order to present nominal, non-standardized figures.

3 Outgoing calls were updated retroactively to exclude the number of direct dial internet calls and the calls of Bezeq's operational lines.

4 Incoming calls were updated retroactively to include the number of international calls.

5 The average monthly revenue for ADSL subscribers was updated retroactively to include revenue from equipment.

B. Telephone

Telephone	Q3 2008	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	1,214	1,188	1,173	1,182	1,203	1,152	1,147
Operating Profit (NIS millions)	293	266	215	133	219	240	213
Depreciation and amortization (NIS millions)	129	130	129	126	121	115	117
EBITDA (NIS millions)	422	396	344	259	340	355	330
Net profit (NIS millions)	211	180	163	104	154	173	154
Cash flows from current operations (NIS millions)	386	351	264	252	392	246	359
Payments for investments in property, plant and equipment and intangible assets (NIS millions)	350	182	103	120	81	117	63
Proceeds received from sale of property, plant and equipment (NIS millions)	-	1	1	3	-	-	2
Number of subscribers at end of period (thousands)	2,698	2,636	2,595	2,622	2,560	2,513	2,478
Average minutes of use per subscriber (MOU) per month	359	358	355	358	363	350	344
Average monthly revenue per subscriber (NIS) (ARPU)	129	128	126	130	135	129	132
Number of 3G subscribers at end of period (thousands)	1,068	977	867	749	607	471	358
Revenues from value added services and content, as a percentage of total cellular service revenues	16.2%	15.5%	15.0%	13.6%	12.8%	12.5%	12.0%

C. Bezeq International

	Q3 2008	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	329	326	314	334	326	321	323
Operating Profit (NIS millions)	59	63	54	46	54	53	51
Depreciation and amortization (NIS millions)	20	20	20	21	21	22	23
EBITDA (NIS millions)	79	83	74	67	75	75	74
Net profit (NIS millions)	44	47	41	38	39	39	37
Cash flow from current operations (NIS millions)	42	51	8	30	34	32	(1)
Payments for investments in property, plant and equipment and intangible assets (NIS millions)*	33	31	28	36	29	18	8
Proceeds received from sale of property, plant and equipment (NIS millions)	-	-	-	2	2	-	-

* This item also includes long-term investments in assets.

D. DBS

	Q3 2008	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	375	380	381	347	360	354	354
Operating Profit (NIS millions)	52	43	26	4	(4)	31	25
Depreciation and amortization (NIS millions)	59	60	65	70	66	69	68
EBITDA (NIS millions)	111	103	91	74	62	100	93
Net profit (loss) (NIS millions)	(82)	(99)	(66)	(75)	70	(65)	(48)
Cash flows from current operations (NIS millions)	97	32	84	76	53	25	93
Payments for investments in property, plant and equipment and intangible assets* (NIS millions)	56	40	79	81	84	45	45
Number of subscribers (end of period, in thousands)	556	551	549	549	545	543	542
Average monthly revenue per subscriber (NIS).	226	230	231	212	220	218	218

* This item also includes investments in the cost of acquisition of subscribers

2. Fixed-Line Domestic Communications – “Bezeq” – The Israel Telecommunications Corp. Limited (“the Company”)

Section 2.1 – General information on areas of operation

Section 2.1.2 – Limitations set by legislation and standards and special restrictions

Recently, on June 1, 2008, the Company's tariffs change. The interconnect charges to the Company were reduced, effective June 11, 2008.

Section 2.1.3 - Changes in volume of activity and profitability in the area

For changes in the volume of activity and profitability in this area, see update to section 1.5.3(a) above.

Section 2.1.5 – Technological changes that are necessary to significantly impact on the area of activity

Subsection A – Regarding the adaptation of company infrastructure to high broadband, see the updates to sections 2.6.7 and 2.7.2, below, regarding NGN.

Section 2.1.9 – Technological changes Competitive environment and changes therein

With respect to the competitive factors in this sector and the Company's flexibility see update of section 2.6.1 and section 2.16.2 with respect to the decline in the Company's market share in the mobile phone (private sector) sector to below 85% and possible benefits to the Company due to it.

Section 2.2 – Products and Services

Section 2.2.2 - Telephony

On April 7, 2008, a draft amendment to the license and service file of the toll free service (1-800) was received from the Ministry of Communications. The significance of the amendment is, inter alia, that the Company's 1-800 subscribers will pay the cellular companies a higher tariff for calls made to them from the cellular network. On May 6, 2008, the Company sent its comments on the aforementioned amendment.

In respect of the Company's request to the Antitrust Commission for an exemption from a cartel arrangement to an arrangement with the cellular operators and fixed domestic licensees for information services – on August 13, 2008, the Commissioner decided to grant a conditional exemption as a response to the Company's request.

Section 2.2.3 – Internet Access Services

For changes in the number of ADSL subscribers, and the average monthly revenue per ADSL subscriber, see the update to the table in section 1.5.3(a) above.

With respect to broadband access services via internet service providers without purchasing a basic telephone service (ADSL only) - the Company commenced provision of this service on May 15, 2008.

Section 2.2.5B - Satellite Services and Broadcasting

See update to section 1.1.6 above with respect to the agreement for sale of the Company's satellite communications operations.

Section 2.3 - Breakdown of Revenues and Profitability of Products and Services

For updates of data regarding the breakdown of the Company's revenues based on products and services, see Note 11B in the financial statements of the Company for the period ended on September 30, 2008.

Section 2.6 – Competition

For an update regarding publication of the recommendations of the Gronau Committee, see the update to section 1.1 above.

Partner Ltd. recently announced its intention of expanding its operations in the internet (ISP), fixed-line telephony (VOB) and content at the customer's home. If Partner does expand its operations, as aforesaid, this will increase the competition in these sectors.

Section 2.6.1

With respect to the Company's petition to the High Court of Justice with respect to the application to enforce the requirement of structural separation on HOT, on July 15, 2008, the Court decided that the petition will be corrected according to the Company's request, that a hearing will be set and the respondents will submit their responses prior to the hearing.

Regarding the policy for providing VOB services – on August 12, 2008, the Company applied to the Ministry and requested, for the sake of good order, to make an addition to the Services Addendum to the Company's license for broadband telephone service, if it reaches a market share of 85%. It is noted that according to the Ministry of Communications' announcement on August 25, 2008, the

Company's market share has declined, in terms of normative revenues, as at June 2008, in the fixed-line telephony sector (private sector) to below 85%. In addition, according to the announcement of the Ministry of Communications on November 11, 2008, as at August 2008 the Company's market share is 83.8% in the residential sector and 89.2% in the business sector.

Section 2.6.6A - Numbering and Number Portability

As of the end of September 2008, approximately 165,000 thousand lines have switched from the Company to competing companies (of which 47,000 in the third quarter) and approximately 16,000 lines switched to the Company from the competitors (of which 8,000 in the third quarter).

On April 9, 2008, the Ministry of Communications gave notice to the Company and to other communications providers that it was considering amending the numbering plan and prescribing that with respect to the entitlement to number portability a "subscriber" would be deemed to include an NEP licensee to whom telephone numbers have been allocated and who pays for use thereof, and the end user will not be entitled to port such a number. On May 7, 2008, the Company submitted its comments to this amendment, claiming that it would amount to confiscation of the end user's right to decide whether to port the number or not. Despite this, on September 1, 2008 the numbering plan, as stated in the Ministry's announcement above, was amended. Nonetheless, the Ministry noted in an accompanying document that it intends to examine regulating the relationship between the end user and the NEP license holders, in whose name the telephone numbers are registered, so that the number portability regulation will also be applicable to the end users

On May 4, 2008, the Company received an Administrative Directive from the Ministry of Communications to the effect that a customer which has been allotted an abbreviated business dialing number (asterisk plus four digits) may port such a number.

Section 2.6.6.b – Other Potential Competitive Infrastructures

Regarding the hearing on the subject of the policy for allocating frequencies for wireless broadband access networks (WiMAX) – on July 30, 2008, the Ministry of Communications announced an additional hearing in which changes were made to the previous hearing. In this context, the Ministry announced that it is examining the possibility of amending the Communications Regulations (Telecommunications and Broadcast) (Frequencies for Wireless Access Devices) 5762-2002 which lists the devices that are exempt from permits pursuant to Chapter 5 of the Planning and Construction Law, so that it includes the 2.5 GHz and 3.7 GHz frequency ranges. On September 1, 2008 the Company filed its responses for the hearing and reiterated its claim that the Company should be allocated national deployment frequencies at 30 MHz bandwidth and in the 2.5 GHz frequency range and at least in the 3.5 GHz frequency range, and that no maximum limit should be set for the bandwidth allocated to the Company. Furthermore, with respect to the matter of unbundling over the wireless network, should the method be introduced, the Company explained that it is not clear if this can be done at all and in any case, the responsibility should be applicable to all the operators. At the same time as an overall policy is being drawn up, negotiations are underway between the Company and the Ministry of Communication with respect to the allocation of alternative frequencies for the Company in return for vacating frequencies that the Company currently uses to provide services to the radio systems subscribers, as required by the Ministry of Communications (see update to section 2.16.8 below).

Section 2.6.7 – the Company's preparations for managing increased competition

Sub-section (i) regarding examination of the deployment of uniform infrastructure for the transmission of communications services – further to the decision of the Board of Directors of the Company to begin detailed planning of an NGN (Next Generation Network) ("the **project**"), on June 26, 2008, the Board of the Directors of the Company decided to promote the project. In 2008, detailed plans will be made for the project, two areas will be set up as operational pilots and soft switches will be purchased. The project will be conducted in a modular fashion and the Company will examine regularly and at each stage, the feasibility of continuing the project, and the requirement to update the project's outline. The content, pace of implementation and amounts to be invested in the project will be determined annually, as part of the Company's annual budget. In addition to the purchase approved on June 26, 2008, the Board of Directors approved, on July 31, 2008, the purchase of management systems and other equipment required for deployment of the new system. In this respect, see also the update to section 2.7.2, below, and note 3(e) to the financial statements for the period ending September 30, 2008.

Section 2.7 – Fixed assets and Installations

Section 2.7.2 – Domestic, fixed-line communications infrastructure

NGN Network – The Company believes that the requirements of future communications services in the State of Israel, as in the entire world, will require increasing larger broad bands and an advanced IP platform. In order to provide a response to these needs, the Company intends to gradually establish, commencing in late 2008, an NGN network based on the core of the IP network and bringing fiber optic infrastructure to street switching cabinets (the topology of the network is referred to as “fiber to the curb” – FTTC). With this network, it is possible to supply broadband technology up to 50 Mbit/s in the download channel and innovative added-value services. In addition, the NGN network will allow the Company to make the network more efficient. The project for establishing the new network will be implemented gradually with the pace of the deployment being tested annually. In this respect, see also the update of section 2.6.7, above, and note 3(e) to the financial statements for the period ending September 30, 2008.

The information in this section includes forward-looking information based on the Company’s assessments. The actual results are likely to be significantly different from these estimations, when attention is paid to the changes that will occur in technology and in the communications market.

Section 2.7.4 – Land

Subsection d – In Q1 2008, the Company did not sell any real estate assets. During Q2 2008, the Company sold three real estate assets with a total area of approximately 40,500 sq. meters of land and approximately 7,800 sq. meters of building for a total of NIS 22 million. In Q3 2008, the Company did not sell any real estate assets.

Section 2.9 – Human Resources

Section 2.9.1 - Organizational structure and position of employees based on organizational structure

- A. With respect to the organizational structure - the CFO and the VP Strategy and Business Development report only to the CEO.
- B. In May 2008, execution of the amendment to the new collective agreement regarding advancing the completion of implementation of the organizational structure, and regarding advancing dates of retirement and changes in the mix of retirees under the new collective agreement before the end of 2008, was completed.
- C. On October 2, 2008 the Company's board of directors resolved to approve the resignation of 135 employees during the course of 2009, at a cost of NIS 100 million, in accordance with the terms of the collective agreement of December 2006.

Section 2.9.2 – Personnel according to employment framework

During the first nine months of 2008, the number of employees of the Company fell from 7,614 employees at December 31, 2007, to 7,417 as at September 30, 2008 (a net reduction of 197 employees) as a result of retirements from the Company (in parallel with the recruitment of employees required, such as sales representatives)

It is noted that, as at September 30, 2008 all the 975 employees who are supposed to terminate their employment at the Company between 2006-2008 under early retirement tracks or increased severance pay tracks, under the collective agreement of December 5, 2006 (see section 2.17.4(f) of the Periodic Report for 2007), had retired.

Section 2.9.6 – Employee remuneration schemes

Section 2.9.6.3 - for the allotment of options to senior managers and employees of the Group, including to the Chairman of the Board of Directors, see update to section 1.3.2 above.

Section 2.9.7 – Company officers and senior executives

On April 17, 2008, the Board of Directors of the Company, after receiving the approvals of the Remunerations Committee and the Audit Committee of the Board of Directors, approved the conditions of employment of the Chairman of the Board of Directors as set out in the immediate report of the Company published on April 18, 2008. The conditions of employment of the Chairman of the Board of Directors were approved by the general meeting of shareholders of the Company on June 1, 2008 and on September 28, 2008.

Section 2.13 – Finance

Section 2.13.4 - Credit received after December 31, 2007

Commencing June 2008, the Company on occasion takes short-term, on-call loans, generally for insignificant amounts. As of the date of this update, the company does not have any such loans.

Section 2.13.6 – Credit Rating

On May 21, 2008, the Midroog Rating Company (“Midroog”) gave notice that it had returned the Company’s rating (which is Aa1) from negative to stable in light of the improvement in the Company’s financial results, and the continued presentation of a strong financial profile, compensation for erosion in the fixed line communications segment via operations in the other segments and very low rates of financing despite the distribution of all of the net profit as dividend, after transfer of the controlling stake in the Company.

On August 12, 2008, Standard & Poor’s (“S&P”) gave notice that it is changing the Company’s rating outlook (which is BBB+) from “negative” to “stable,” on the basis of its re-examination of its operating performance and the leverage within the company. In its announcement, S&P noted that the company’s rating relies, *inter alia*, on the Company’s leadership as the national communications operator, its operational efficiency, the range of services it offers in the communications market and its adequate financial profile. It is noted that on October 7, 2008, S&P confirmed the validity of this rating and this, *inter alia*, following examination of the anticipated impact of the exercise of the purchase option (10.66%) executed by Ap.Sb.Ar. (see update of Section 1.3.1). On August 25, 2008, S&P Maalot announced that it was raising the Company’s debt rating from AA to AA+ with a stable forecast. In its announcement it noted that the raised rating is based primarily on the Group’s improved performance and operational effectiveness, the stability of the Company’s managerial structure and the changes to the structure of the business risks as a result of the change in the mix of the Group’s revenues. It is noted that on October 13, 2008, Standard & Poor’s Maalot confirmed the validity of this rating and this, *inter alia*, following examination of the anticipated impact of the exercise of the purchase option (10.66%) executed by Ap.Sb.Ar. (see update of Section 1.3.1).

Section 2.13.7 – Assessment of funds raising in the coming year (2008) and sources of financing

In the Company’s assessment, the Company is likely, from time to time, to raise loans from banks and/or other credit providers to bridge gaps in cash flow as may arise, if at all, from time to time.

Section 2.15 – Environmental Protection

Following termination of the strike at the Ministry of the Environment, the process of obtaining operating permits was completed for most of the communications and broadcasting facilities.

Section 2.16 – Limitation and Regulation of Company Activities

Section 2.16.1 – Supervision of the Company’s tariffs

Sub-section (a) (regarding the update of the Company’s tariffs) – on March 20, 2008, a letter was received from the Ministry of Communications under which the next update (on June 1, 2008) would be based on the existing tariff outline prescribed by the Gronau Committee in 2003, in accordance with the formula set out in the Communications Regulations regarding calculation and linkage of payments for telecommunications services (the “Calculations Regulations”). According to the letter, after and to the effect that the Gronau Committee’s recommendations are adopted regarding policy and rules of competition in the communications market, the path will be laid for the work of a commission to prescribe new tariff arrangements for the coming years. On June 1, 2008, the Company’s tariffs were reduced in accordance with a formula fixed in the Calculation Regulations, at the average rate of approximately 2%, except for the fixed fee for a telephone line that was updated in accordance with the increase in the Cost-of-Living index (3.4%). The interconnect tariffs currently paid to domestic carriers by licensees were reduced by an average of approximately 2%, effective June 11, 2008. With respect to the update of the Company’s tariffs, see also the update regarding publication of the recommendations of the Gronau Committee in section 1.1 above.

Section 2.16.2 – The Company’s general license

On July 3, 2008, the Company received a draft amendment of the Company’s license and the licenses of its subsidiary companies Pelephone, Bezeq International and D.B.S. regarding the marketing of joint packages of services. On July 27, 2008, the Company submitted its position to the Ministry of Communications, stating that the amendment of the licenses represents an intensification of regulation

in comparison to the policy document of the Minister of Communications dated March 31, 2004, which is supposed to reflect relief for the Company, and it would be desirable to allow a model for marketing of joint packages of services that represents relief for the Company now that its market share has decreased to 85% or less, together with ministerial supervision using more moderate measures than those proposed in the draft amendment to the license. Regarding the positions of the subsidiary companies on this matter, see the updates to sections 3.18.3.1, 4.1.2 and 5.6.5, below.

According to the Ministry of Communications announcement on August 25, 2008, the Company's market share declined, in terms of normative revenues, as at June 2008, in the fixed-line telephony sector (private sector) to below 85%. In addition, according to the announcement of the Ministry of Communications on November 11, 2008, as of August 2008 the said market share is 83.8% in the residential sector and 89.2% in the business sector.

Regarding the main points of the general license – subsection c regarding tariffs – on April 14, 2008, the Company's license was amended so as to permit it to require a subscriber to pay using a direct debit or a credit card, except for a private subscriber who does not have a bank account. It should be noted that the Economics Committee of the Knesset discussed a proposal to amend the Consumer Protection Law, by which a communications business would not be permitted to make a transaction conditional on payment using a direct debit or credit card. If the law is amended according to this proposal, the Company will be unable, despite the amendment to its license, to require a private subscriber to pay using a direct debit or credit card.

Main points of the general license – subsection 11 (miscellaneous issues) – on May 17, 2008, the Ministry published a hearing regarding its policies and amendment of the operators' licenses regarding fair disclosure on telephone bills. In this context, it is examining imposing new requirements on the operators regarding details and computation of bills. It should be noted that approximately three years ago, the licenses were amended so that a standard was adopted for telephone bills. The Company submitted its position on the matter on July 20, 2008, stating, *inter alia*, that there is no justification, neither from the consumers' perspective nor from an ethical perspective, to make changes in the Company's telephone bills. This would also be harmful to some of the Company's customers while being of no benefit to others. In its position, the Company claimed that since the demands being considered would require very extensive development and resources to implement and because of the technical issues involved, it would be worthwhile, before a decision is made, to discuss the matter with the Company.

On October 28, 2008, the Ministry of Communications approved Company's cessation of the services relating to the satellite communications operations and its overall license, and the fourth addendum to the Telecommunications Order (Telecommunications and Broadcasts) (Determination of Essential Service Provided By Bezeq The Israel Telecommunication Corp., Limited), 5757-1997 was amended accordingly (see update to section 1.1.6 above)

Section 2.16.5 - Immunities

On May 19, 2008, the Company received a letter, dated May 18, 2008, from the Ministry of Communications, addressed to communications licensees, stating that the Ministry of Communications is of the opinion that following the adoption of the Civil Wrongs Ordinance Amendment (No. 10) Law, 5765-2005, under which the restrictions on the State's liability in tort were reduced, there might be grounds to consider reducing the existing immunity arrangement granted to general licensees and special general licensees. The licensees were requested to submit their positions to the Ministry of Communications by June 18, 2008. On July 31, 2008, the Company submitted its position to the Ministry of Communications stating that the said Amendment 10 does not change any of the arrangements regarding liability for torts to an extent that justifies reducing the existing immunity arrangement and assigning responsibility to the communications companies. Additionally, expansion of responsibility means placing a heavy burden on communications companies, including the Company, because of the potential extent of the indirect damages and the dimensions of the possible suits.

Section 2.16.7 - Antitrust laws

Subsection h. with respect to the Antitrust Commissioner's ruling that the Company had abused its market status in handling an interconnection fault between the Company's network and that of HOT, against the backdrop of labor disruptions by the Company's employees - on March 16, 2008, the Company filed an appeal against the Commissioner's ruling. In this regard, see also Note 6C(1) to the financial statements of the Company for the period ended September 30, 2008.

Section 2.16.8 – Telegraph Regulations

Regarding the Company's use of radio frequencies – on October 25, 2007, the Ministry of Communications notified the Company that it is considering ordering it to cease using neighborhood radio and rural radio systems and the frequencies allocated to it for the purposes for which they are being used, amongst others, in order to provide its services in areas where an infrastructure of telephone lines does not exist. On December 25, 2007, the Company submitted its response in which it clarified that the Ministry must allocate alternative frequencies and that the Ministry's requirement would create difficulties for the Company and requires extensive deployment and operations that would entail significant expenses. Furthermore, the Company noted that it would be required, within a period of two years, to transfer subscribers from the existing systems to new systems and demanded that the State bear the cost of the migration from the systems that the Company would be required to evacuate. Since then the Company has been negotiating with the Ministry of Communications with respect to the allocation of alternative frequencies for those frequencies that the Company is required to vacate.

Section 2.16.9 - Proposed Legislation to Amend the Consumer Protection Law and the Communication Law

During April 2008, an amendment of the Consumer Protection Law regarding fixed transactions was approved by the Knesset (the "Amendment"). Under the Amendment, dealers will be required to inform consumers of the date of termination of a fixed transaction prior to termination of such, and of the conditions that will apply after the date of termination. In addition, dealers will be required to obtain the positive consent of the consumer to continue with the contract beyond the fixed period. If positive consent is not obtained, the consumer will be disconnected from the service to which the fixed transaction applied, apart from basic telephone services as defined in the Communications Law (voice services). This Amendment will come into force as of 2009. The Company's hearing regarding the amendment to the Company's license and those of other licensees in this regard, proposed by the Ministry of Communications, is also continuing. In this context, the Ministry of Communications announced on October 29, 2008 that with regard to the hearing with respect to setting a uniform tariff for the commitment period, the Ministry decided to amend only the licenses of general licensees for providing cellular services in a way that will obligate a uniform tariff as aforesaid. This amendment becomes valid as of December 31, 2008. Furthermore, the Knesset approve an amendment to the Consumer Protection Law regarding disconnection from ongoing services (effective October 2008) allowing a private subscriber to disconnect from ongoing service by using mail, electronic mail or telephone. In addition, the Knesset approved the amendment to the Consumer Protection Law (effective September 2008) which imposes, in certain circumstances, fines if a technician is late and an amendment to the Communications Laws regarding junk mail (effective November 2008), according to which requires, among other provisions, as a general rule, a subscriber's explicit permission to receive advertising by way of electronic mail, facsimile, automatic dialing systems and SMS.

The Company is implementing the arrangements which took effect and is preparing to implement the other amendments.

Section 2.16.11 – Erection of communications installations – NOP 36

On April 17, 2008, the Company submitted its objections to the proposed wording of the National Communications Outline plan NOP/36A regarding small broadcast installations, and the National Communications Outline Plan NOP/36B regarding large broadcast installations. In summary, the objections are that the plans, as currently worded, particularly with respect to the changes in definitions of small and large broadcast installations, give rise to practical difficulties which might prevent the Company from providing the public with some of the varied services that it provides, and that it is required by law to provide.

Establishing communications facilities in the territories

On July 29, 2008, the Company received notification that in June 2008 National Master Plan 56, which regulates construction and licensing of communications facilities in the territories, took effect. The plan includes transition instructions for facilities that were constructed prior to 1984 and for existing facilities. The Company is examining the subject and, as of the date this report, it is not able to evaluate the expected ramifications.

Section 2.17 – Significant Agreements

With respect to section 2.17.4(f) – the new collective agreement of December 5, 2006 – regarding the amendment to the agreement, see update to section 2.9.1 above.

Section 2.17.5 – Management Agreement

On September 28,, 2008, the general meeting of the shareholders of the Company approved (subsequent to approval by the Audit Committee and the Board of Directors) the extension of the relationship and management contract with AP. SB. AR. Cayman L.P., a company related to Ap.Sb.Ar., for a period of three additional years commencing January 1, 2009, through December 31, 2011, according to the conditions of the original agreement..

Section 2.18 – Legal proceedings

For updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2008.

Section 2.19 – Goals and Business Strategy

Section 2.19.2 - Summary of Strategy and Directions for the Future

Regarding the Company's network – see sections 2.6.7 and 2.7.2, above, on the subject of NGN.

Section 2.21 – Risk Factors

During the current quarter, subsequent to the worldwide economic crisis, global markets have entered a slowdown and credit choke. It is assumed that this situation will continue to be felt throughout 2009 and possibly worse, with a shift from growth to recession. A significant slowdown and decline of business operations and key economic parameters are also expected in the local market. The Company assumes that this crisis may have a negative impact on its operations, inter alia, as a result of the harm to the Company's revenues and difficulties in selling its real estate properties.

This information includes forward looking information based on internal estimates of the Company. The actual results may be materially different from the foregoing estimates if changes take place in any of the factors taken into account for this assessment.

3. Cellular – Pelephone Communications Ltd. (“Pelephone”)

Section 3.2.1 – Services

At the end of March 2008, the Ministry of Communications published a document of a public hearing regarding the policy of regulating the provision of telephone trading services via a public telecommunications network. Telephone trading services including voice and visual information services, entertainment services, dating services, etc., provided to subscribers via terminal equipment connected to a network. It is important to note that the field of telephone trading services is a significant source of income in the content world of Pelephone and the other cellular carriers. Following the proposed regulation, the Regulator is seeking to dramatically change the conduct of the telephone trading services sector, in a way that it is also likely to harm Pelephone's revenues in this area. The Ministry of Communications has asked all relevant persons operating in the field of telephone trading for responses to the aforesaid hearing. Pelephone submitted its position in this regard, in which it, among others, requested that the Ministry of Communications hold frontal discussions on the subject of the hearing prior to making any decisions. During August 2008, the Ministry of Communication called for frontal discussions on the issue in hand opposite all the cellular providers and part of the content providers. During the aforesaid discussion, Pelephone presented its opinion on this matter to the Ministry's representatives. The Ministry has not yet set down its final policy on this matter.

Section 3.6 – Marketing, distribution and service

In September 2008, Pelephone signed an agreement with Super Pharm, who up until now has marketed Partner phones, to market its phones as of January 2009. Subsequently, Pelephone's distribution will be significantly expanded.

Section 3.7 – Competition

For an update regarding publication of the recommendations of the Gronau Committee, see the update to section 1.1 above.

On August 13, 2008, Minister of Communications published a document regarding adoption of the recommendations of the Gronau Committee. Following are the main points that relate to Pelephone:

1. The Minister instructed the CEO of the Ministry of Communications to work to promote the licensing of virtual operators (MVNO) while making it possible for the relevant parties to express their opinion on the subject to the Ministry of Communications. In the event that within a period of six months from the date that a virtual operator applies to a mobile operator, the parties do not reach an agreement regarding the provision of virtual services, the Minister will examine the reasons for this and, subsequent to a hearing with the relevant parties, consider issuing instructions on the matter in accordance with his authority.
2. It is the intention of the Minister to promote a change in the tariff structure for outgoing international calls using the mobile network, in the context of interconnect regulations so that the international carrier will determine the tariffs for these calls and, in the context of its accounting with the mobile operators, the international operator will transfer only interconnect charges to the mobile operator. A hearing with the relevant parties is to be held regarding the implementation of his policy.

According to the Minister's position, international licenses should not be issued to existing mobile operators, at this stage.

Regarding Section 3.7.2

Recently the Minister of Communications expressed his position according to which he intends to promote the issuance of MVNO licenses in the near future. The Minister stated that the Ministry would examine a variety of possibilities for granting MVNO licenses, ranging from a reseller model to full operation. Furthermore, in September 2008, as part of the Government's discussions with respect to the Budget Law and Settlements Law for 2009, a decision was made that the Minister of Communications shall complete all the procedures required for granting MVNO licenses by April 1, 2009. Similarly, according to media releases, the Ministry of Communications intends announcing a hearing by the end of 2008 for the cellular operators with respect to the granting of MVNO licenses.

During the Government's discussions on the Budget Law for 2009, further decisions were taken with respect to the communication sector and the cellular sector in particular, inter alia, following the Gronau Committee recommendations.

1. The cellular roaming tariffs will be examined by a government inter-ministerial team. The team will submit its recommendations regarding the options for lowering the roaming tariffs by the end of 2008. Similarly, the Ministry of Communications, together with other relevant government ministries, will act to apply the European regulations on roaming tariffs by February 28, 2009.
2. An inter-ministerial team from the Ministry of Communications and the Finance Ministry will examine the option of reducing the interlinking tariffs. The team will submit its recommendations by March 31, 2009 (to the best of Pelephone's knowledge, the format for the team has not yet been formulated).
3. The Ministry of Communications will examine the option of the allocation of frequencies for the establishment of an additional communication network by a new operator which will enter the communications market. This examination will be completed until the end of 2008.

Section 3.7.4

At the end of July 2008, the Ministry of communications published its policies regarding the allocation of frequencies, inter alia, regarding the 2.5 GHz frequency range. This frequency range is intended to serve the WiMAX technology in fixed-line telephony as well as 4G technology in the cellular sector. According to the proposed policies, the aforesaid frequencies will be allocated in two separate tenders: The first will take place by the end of 2008 and in its context; frequencies will be allocated to new operators as first priority and to Mirs as second priority (to establish a network with WiMAX technology). The second tender will take place as of mid 2011, after vacating another band of frequencies in the above frequency ranges, and other cellular operators may also participate in this tender. Pelephone submitted its response to the aforesaid policy document and in this context, expressed its objection to Mirs's priority in the first tender and demanded government undertaking to vacate additional frequencies prior to the second tender in order to ensure the natural development path of fourth generation cellular technology.

Section 3.10 – Intangible Assets

Regarding Section 3.10.2 – Right to use frequencies

During 2008, Pelephone requested the Ministry of Communications to execute the allocation of frequencies in the 2100 MHz range. In order to execute this right, Pelephone is required to pay approximately NIS 181 million in respect of retroactive licensing and frequency fees from the day it won the tender for the frequencies through the day that it executed its right for allocation of the frequencies. During September 2008, Pelephone paid the said amount for the completion of the allocation of frequencies by the Ministry of Communication.

Section 3.15.6 – Credit Rating

On October 28, 2008, Maalot announced the affirmation of the rating of Pelephone's debentures (AA minus).

Section 3.17 – Environment

Regarding Section 3.17.1

On July 17, 2008, a petition was filed on behalf of The Forum for Sane Cellular Consumption and the Israel Union for Environmental Defense with the High Court of Justice requesting an order nisi against the Minister for Environmental Protection, the Minister of Communications and others because of an alleged failure to reach an agreement on the wording of regulations by virtue of sections 25(a)(2) and 25(a)(5) of the Non-ionizing Radiation Law, 5766-2006, despite the obligation stated in the law to issue the said regulations by January 1, 2007. Furthermore, a declaration was requested that until these regulations are issued no construction permits or operating permit would be issued for sources of radiation intended for cellular communications. Simultaneously, a request was also filed for an interim order not to issue construction permits or operating permits for sources of radiation intended for cellular communications until a ruling is made on the petition.

Section 3.18 – Restriction and Control of Pelephone's Actions

Section 3.18.1.4 – the Consumer Protection law

During the month of April 2008, an amendment of the Consumer Protection Law regarding fixed transactions was approved by the Knesset. In this regard, see section 2.16.9 above. Pelephone is examining significance of implementing this regulation and is preparing to implement it.

Section 3.18.3 – Pelephone's license

Regarding subsection 3.18.3.1(e), during June 2008, the Ministry of Communications published a hearing regarding proper disclosure on telephone bills. During this hearing, a variety of changes in the structure of the invoice were proposed. The hearing was based on the recommendations of the Subcommittee of the Knesset Economics Committee and recommendations of the professional committee of the Ministry of Communications regarding the structure of the invoice, which completed its work recently. Pelephone submitted its position to the Ministry of Communications. Implementation of the recommendations as proposed will require Pelephone to make appropriate operational arrangements.

Regarding subsection 3.18.3.1(f) – during the month of March 2008, the Ministry of Communications made a decision to implement the amendment of the MRT licenses under which the maximum obligation term for customers who are not business customers would be reduced to 18 months, and the carriers would be required to offer customers a reasonable no-obligation alternative. This resolution was passed following a hearing into this matter. Implementation of the amendment commenced on April 22, 2008.

Section 3.18.3.1(g) – during the first quarter of 2008, Pelephone submitted its response to a hearing regarding fixed-term transactions, with respect to the policy format presented. However, on April 14, a request was received from the Ministry of Communications for responses to a further hearing in this regard, under which the Ministry of Communications proposed a new ruling to the effect that a fixed tariff would apply during the obligation period, i.e., as different from the previous hearing: the current amendment proposes that during the obligation period, it will not be possible to amend tariffs. Pelephone submitted its response to the Ministry.

On October 30, 2008 the Ministry of Communications published its final amendment for the cellular licenses which states that as of December 31, 2008 in communication contracts with new subscriptions for plans which include a commitment period, the operators will be obligated to set the

service prices in advance and may not update them until the end of the commitment period. Without derogating from the aforesaid, the operators may lower the preset prices during the commitment period. Pelephone is preparing to implement the license amendment.

In September 2008, the Ministry of Communications published an amendment to the cellular operator's licenses regarding the following matters

- 1) Termination of service to a dormant subscriber – pursuant to this amendment, the operator is entitled to terminate service to a subscriber who does not make use of the cellular service for a period of 12 months. The termination of the service will be made possible after the operator gives notice to the subscriber regarding its intention to terminate the service, in the format as set forth in the said license amendment. A subscriber requesting that the service not be terminated despite being a "dormant subscriber" will not be disconnected by the operator, unless no use is made of the cellular service for a period of 36 months.
- 2) Blocking end equipment in the event of loss / theft – according to this amendment, the cellular operators are obligated to maintain a joint store of end devices which were reported lost or stolen and ensure that these devices are blocked from any use immediately upon receipt of the loss / theft report.

Following are additional changes that are being considered by the Ministry of Communications:

- 1) Further to the hearing held on the subject during July 2008, the Ministry of Communications published a legal opinion stating that it is prohibited to make the purchase of a Third Generation (3G) instrument conditional on the purchase of 3G services. According to this opinion, customers must be offered an economically effective alternative for purchasing a 3G instrument without a package of 3G services.
- 2) According to the policy document of the Ministry of Communications from 2004, the Company will be permitted to market joint packages of services with its subsidiary companies when its market share for fixed telephony services drops to 85% as the Company's market share approaches 85% (in the mean time, the Company's market share in the private sector has dropped to below 85%, see update to section 2.6.1 above). The Ministry of Communications recently announced the hearing including the proposed amendments to Pelephone's license. According to the proposed amendment, the Company and Pelephone will be permitted to market combined packages (for fixed and mobile telephony) but only subsequent to approval being received from the Minister of Communications for marketing the package, on the condition that the package will be completely broken up, meaning that each component of the package will also be offered to customers, at the same price, outside of the package, and on the condition that can be proved that similar packages are available in the market. Pelephone submitted its response to the hearing, in which it expressed its objection to the proposed change.

Section 3.18.3.3 – License for Building Sites

On May 1, 2008, the Attorney General expressed his position regarding wireless access devices and stated that he accepts the opinion that the exemption, according to its wording and purpose, also applies to wireless communications devices for cellular communications and that the exemption represents the balance that the legislator created between the various interests. Despite this, and because of changes and developments in the law and the factual reality, the Attorney General asked that an inter-ministerial committee re-examine the significance and ramifications of continued application of the exemption for cellular devices, the purpose of developing an updated position regarding a worthy justification for the exemption for cellular telephone devices, by the end of 2008.

On May 22, 2008, Tel Aviv District Court, sitting as a Court of Appeals, handed down a ruling regarding the issue of wireless access devices. The main points of its determination were as follows:

- a. The exemption from a building permit does not apply to access devices operating in a cellular network that were constructed on the roofs of buildings.
- b. Wireless access devices, as defined by law, are fixed devices.
- c. The antenna is not included the definition of an exception to the requirement for a building permit for an "internal change in an apartment."

Pelephone disagrees with the District Court's ruling and on June 10, 2008, it filed a request for permission to appeal to the Supreme Court.

On July 21, 2008, the Union of Local Authorities in Israel and others filed a petition with the High Court requesting an order nisi instructing the Attorney General to appear and explain, *inter alia*, why the enforcement guidelines he issued to municipal prosecutors stating that charges are not be filed and

administrative demolition orders are not to be issued for the construction and operation of the cellular access devices without a permit should not be cancelled. Furthermore, the High Court was asked to determine, *inter alia*, that the position of the Attorney General (in a document dated May 1, 2008) suffers from an extreme lack of reasonableness. Furthermore, a request was made for an interim order to the Attorney General instructing him to defer or suspend the validity of the enforcement guidelines or, alternately, to forbid the construction of cellular access devices without a building permit, until the court meets and rules on the petition.

It is hereby clarified that Pelephone continues to construct wireless access devices. If Pelephone's position is rejected by the courts, in whole or in part, it will have an adverse impact on the possibility of deploying sites, the pace of deployment, etc. In the event that it is necessary to cease the operation of access devices, there will also be damage to service in the areas where these devices operate.

Section 3.21 – Legal proceedings

For updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2008.

Section 3.24.1 – Macro-economic risk factors

During the current quarter, subsequent to the worldwide economic crisis, global markets have entered a slowdown and credit choke. This situation is expected to continue to be felt throughout 2009 and possibly beyond, and there may be a shift from growth to recession. In the local market the slow down is also expected to be significant, as is a decline of the central economic parameters. This decline is liable to have negative impact on the results of the Pelephone's operations in 2009.

Impacts which could derive from the changes in the economic climate are, among others:

1. Decline in recruiting new subscribers, churn / silencing of existing subscribers.
2. Decrease in revenues resulting from the decline in use, price erosion and reduction in the number of users of additional services.
3. Changes to the exchange rate which will impact the profitability of the sale of end equipment and financing costs.
4. Inflationary changes.

This information includes forward looking information based on internal estimates of the Pelephone. The actual results may be materially different from the foregoing estimates if changes take place in any of the factors taken into account for this assessment.

4. International Communications, Internet Services and NEP – Bezeq International Ltd. (“Bezeq International”)

Section 4.1.2 – Statutory and Standards Limitations on Bezeq International

On March 12, 2008, a report was published by the Committee to Formulate Detailed Recommendations on Policy and Rules of Competition in the field of Communications in Israel headed by Prof. Reuven Gronau. *Inter alia*, the report includes recommendations regarding the areas of operations of Bezeq International, which, if adopted by the Ministry of Communications in setting its policy, will affect the management of Bezeq International's business. Additionally, the Committee recommended: that a permit be given to the subsidiaries of the Company to supply unbundled service packages, including the Company's telephony and broadband services, after implementation of the local loop unbundling arrangement (see update to section 1.1 above); that on such date, the subsidiaries shall be granted special domestic carrier licenses for the provision of domestic carrier services that are not VOB; and that the entry of new players controlled by the mobile telephony companies shall be permitted into the international call sector, after the method of prescription of tariffs for international calls via mobile handsets is changed so that the international call tariff is set by the international calling company, which will pay the cellular carrier in accordance with the tariff set out in the Interconnect Regulations for call completion.

For an update regarding publication of the recommendations of the Gronau Committee, see also update to section 1.1 above.

On August 13, 2008, the Minister of Communications published his decision regarding setting policy and competition guidelines in the field of communications in Israel, on the basis of the conclusions of

the Gronau Commission, which were published in March 2008. In the estimation of Bezeq International, the decisions of the Minister will not have an impact on its business operations in the near future and, in any case, it is currently unable to assess their possible long-term impact since the implementation of changes in its field of activity require, according to the Minister's decision, completion of an extended process of preparing regulatory infrastructure, whose nature is uncertain at this time, as well as the creation of new market arrangements, for which it is unclear when and if they will exist.

On July 3, 2008, Bezeq International received a letter from the Director-General of the Ministry of Communications on the subject of the amendment to its general license regarding the sale of packages of services that include both its services and the services of the Company, to which drafts of the amendment to the licenses of Bezeq International and the Company were appended. In the response written to the said letter and during the hearing on this matter that was held in the Ministry of Communications on July 30, 2008, Bezeq International notified the Ministry of Communications of its objections to the proposed wording of the amendment to its general license because, on one hand, the amendment will not alleviate the limitations that currently apply to it and the Company as regards the sale of joint packages of service and, on the other hand, the proposed amendment could change its current situation for the worse and discriminate against it in comparison to its competitors.

Section 4.6 – Competition

During September 2008, Partner Communications Ltd. ("Partner") announced its intention to begin providing internet access services and IP based content and telephony services. Thus, Partner will join, as a competitor, the markets in which Bezeq International operates. Bezeq International's management expects that this act of Partner is expected to impact the operations of Bezeq International and its business results, and however, at the present time Bezeq International is unable to estimate the extent of this impact on its results. Bezeq International is preparing and adjusting its work plans to its assessments in this regard.

Section 4.9 – Intangible Assets

On March 23, 2008, Bezeq International signed an agreement with Gil A.R. Telecom Systems ("Gil A.R.") under which Bezeq International acquired all of the operations of Gil A.R. relating to the sale, leasing and service of communications products and switches manufactured by Avaya Office.

Section 4.14 - Investments

As at September 30, 2008, Bezeq International held 34.25% (32.42% under full dilution) of the share capital of Walla! Communications Ltd.

Section 4.19 – Legal proceedings

With respect to section 4.19.2 of the Periodic Report of the Company for 2007, regarding the claim filed against Bezeq International and against two other international carriers on grounds of breach of patent for a pre-paid telephone system by persons claiming to be the inventors and owners of such patent, the Court accepted the parties request to defer the dates set in the proceedings in order to enable them to conclude the out of the court compromise negotiations conducted between them.

For further updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2008.

Section 4.21 – Risk Factors

During the current quarter, subsequent to the worldwide economic crisis, global markets have entered a slowdown and credit choke. The impact of this situation is expected to continue to be felt throughout 2009 and possibly beyond, and there may be a shift from growth to recession. In the local market the slow down is also expected to be significant, as is the decline of business operations and of the central economic parameters. Bezeq International's management expects that these events may impact the operations of Bezeq International and its business results, and at the present time Bezeq International is unable to estimate the extent of this impact on its results. However, Bezeq International is preparing and adjusting its work schedules in this regard.

This information includes forward looking information based on internal estimates of the Company. The actual results may be materially different from the foregoing estimates if changes take place in any of the factors taken into account for this assessment.

5. Multi-channel Television – D.B.S. Satellite Services (1998) Ltd. (“DBS”)

Section 5.1.3 – Developments in markets in the area of operations

Section 5.1.3.3 – the private bill regarding the inclusion of two designated channels and the education television channel in the DTT system was approved in a preliminary reading by the Knesset Plenum. A number of private bills dealing with the addition of other channels to the cluster of channels intended for broadcast via the DTT system were also submitted to the Knesset and to the best of DBS's knowledge they are currently in the initial processes of enactment. To the best of DBS's knowledge, the Second Authority for Television has chosen the winner of the tender that it published for the supply of broadcasting equipment which will serve for the establishment of the distribution system. In DBS's estimate, the distribution system will begin operation only in the second quarter of 2009.

Section 5.1.3.5 – in March 2008, the Minister of Communications published the recommendations of the Gronau Committee. The recommendations deal with the areas of telephony, internet and multi-channel broadcasts. Among other recommendations, the Committee recommended requiring multi-channel broadcasting companies to offer their subscribers a narrow channel package containing 5-10 channels, having the characteristics set out in the recommendations. The Committee also recommended not to remove the structural separation applying to the Company at this stage, due to its status in the field of fixed-line telephony, and recommended that subsidiaries of the Company, including DBS, not be allowed to supply “service packages” including the Company's services (including IPTV services) until its other recommendations regarding infrastructure and the Company's services are implemented. DBS expressed its opposition to and reservations regarding the recommendations to the Minister of Communications.

For an update regarding publication of the recommendations of the Gronau Committee and the decisions of the Minister, see also the update to section 1.1 above.

In August 2008, the Government decided, inter alia, that the Communications Law will be amended as such that as of March 1, 2011 DBS and the cable companies will be obligated to allow any subscriber to connect to a basic package including Channel 1, Channel 33, Channel 2, Channel 10 and the Knesset Channel (in this section - "the Basic Package") against payment for the connection to the broadcasting center, which will be calculated on the basis of subscriber connection costs plus reasonable profit; to allow any subscriber to purchase any other broadcast whereby the tariff for the acquisition of several broadcasts shall not be set in a manner that will be conditional as aforesaid; to set a price that will be paid by the owners of the channels in the basic package to the cable companies and to DBS for transferring their broadcasts and this on the basis of usage cost plus reasonable profit; DBS and the cable companies will be entitled to broadcast commercials as of April 1, 2010 when the Commission will establish rules with respect to maximum broadcast time for the various types of channels for a period of three years, which will enable the gradual broadcast of commercials; an order will be legislated with respect to the broadcast of joint channels in the format set forth in section 6(20)1 of the Law, which will expire. In addition, the Government decided to instruct the Commission to examine cancellation of the restrictions applicable to the special license holders for cable broadcasts that do not exist for DBS and the cable companies and the establishment of an inter-ministerial committee headed by a representative of the Ministry of Communications to examine the method of arrangements in the commercial television broadcast sector.

In September 2008 the inter-ministerial committee was established, headed by the CEO of the Ministry of Communications and in October 2008, the committee announced a hearing which included a series of questions regarding the probability of granting additional licenses, including method of distribution to the public and their terms and conditions. DBS has not yet submitted its responses with regard to this hearing.

On October 29, 2008, the Government published the Settlements in the State Economy (Legislative Amendments for Achieving Budget Goals and Economic Policies for Fiscal Year 2009) Bill 5768-2008, which anchored the aforesaid principles of the Government decision in legislature. In DBS's estimation, it is possible that the dissolution of the Knesset for the purpose of elections to be held on February 14, will defer the legislature until the first session of the Knesset following the elections.

In June 2008, the Council published a hearing regarding a new policy relating to broadcast of sports on multi-channel television, effective January 2009. According to the hearing, the Council's intention is to expand the protection of content broadcast on the basic sports channel (Channel 5) and the channel known as Channel 5+ and to impose limitations on the broadcast of live sporting events on the pay sports channels. Furthermore, according to the hearing, the imposition of an obligation to broadcast certain sporting events using the PPV method for a defined payment is being considered. In July 2008, DBS submitted its response, in which it objected to implementation of the policy discussed

at the hearing. In October 2008, the Commission announced that it intended to reduce a number of aspects of the restrictions presented in the above hearing, and accordingly requested DBS's opinion with regard to two options for regulating the sport broadcast market, which in principle is the imposition of restrictions on the pay-for sports channels produced by the Sport Channel Ltd., and extension of the obligations applicable to Channels 5 and 5+ which are included in the basic package and in the sports package, respectively. DBS clarified its opinion in this matter, according to which he objects to any expansion of the regulation on the matter of the sports channels or the imposition of additional restrictions.

In September 2008, the Commission announced a hearing with respect to granting of special license to broadcast a movie and series channel on DBS and the cable companies. According to the hearing, the Commission is considering that the actual granting of the aforesaid license and its terms and conditions, whatever they may be, will limit the ownership of such organization to a number of special licenses and obligating the holders of more than one special license to invest in original productions. DBS objected to the actual hearing with regard to granting new licenses before the issue of transfer fees which will be paid by the special license holders is settled. Furthermore, DBS submitted its responses to the hearing, according to which the granting of special licenses to broadcast movie and series channels should not be permitted or the restriction regarding the maximum number of licenses granted to a single organization should be changed. DBS also requested to equate the obligation to pay license holders royalties as aforesaid, to its obligations and to obligate an organization holding more than one license with a higher obligation to produce original productions than that imposed on DBS.

Section 5.6 – Competition

Entry of a cellular company to the multi-channel television sector:

To the best of DBS's knowledge, Partner Ltd, a cellular operator in Israel, is planning to soon launch a new venture which will include, inter alia, entering the ISP service sector, the VoIP service sector and the content and broadcasts (particularly VOD) sector. Apparently, the provision of these services will initially be via the PC and later via the television screen with end equipment that will also allow reception of channels distributed by means of DTT.

To the best of DBS's knowledge, Celcom Israel Ltd, which is also a cellular operator in Israel, is going to be a partner in a joint venture which will launch a television venture and will offer customers VOD services over the television screen and broadcasts transferred over the internet. This service will be enabled with end equipment which, apparently, will also allow viewing of channels which are distributed by means of DTT.

In September 2008, DBS demanded from the Ministry of Communications to stop all activities of the aforesaid cellular companies taken prior to the matter being examined by the Ministry and until after equality policies with respect to all multi-channel television broadcasts are set. Subsequent to this request, the Ministry announced that it will request clarifications from the cellular companies with respect to their activities in the multi-channel television sector and requested that their response in this matter be given by October 23, 2008.

In October 2008, DBS demanded that the Cable and Satellite Commission proceed and caution the said cellular companies (and any other player wishing to operate in the multi-channel broadcast market) that some extent of supervision will be applicable to them and that the same restrictions and obligations that apply to the multi-channel platforms will also be applicable on them. The Minister of Communication and the Commission Chairman have not yet responded to these demands

Section 5.6.5 – Principal methods for coping with competition

Section 5.6.5(g) – “package of services” – as of April 2008, DBS has ceased marketing a package of services to its subscribers containing broadcasts and high-speed internet connection infrastructure, and has commenced selling the Company's promotions of high-speed internet connection infrastructure such that subscriber contracts regarding such infrastructure are performed with the Company only. DBS has the option of contracting with a subscriber directly and transferring compensation from the subscriber to the Company.

On July 3, 2008, DBS received a letter from the Ministry of Communications stating that the Ministry is considering an amendment to the Company's license as a supplementary amendment to the amendment of the DBS license that would make it possible to offer a package of services according to the following principles:

The package of services will be unbundled so that it will be possible to purchase each of the services offered in the package of services separately for the same price it is offered in the package, a package of services may not be offered if it is not also offered by the cable companies, marketing of the package of services must be approved by prior request by DBS to the Ministry of Communications. These instructions relate to any service offered by DBS together with services from the Company.

In its response to the letter dated July 27, 2008, DBS objected to the proposed amendment to its license. In its response, DBS also claimed that offering the possibility of offering an unbundled package of services does not provide a true response to the package of services offered by its competitor and that the amendments must apply to marketing of the Company's telephony services only and not to other services, such as internet infrastructure services. Furthermore, DBS claims that it is necessary to change the supervisory mechanism for offering and services so that it is not obliged to receive prior permission from the Ministry of Communications but rather required only to notify it and that offering packages of services should not be limited to offering services of the Company similar to those offered by the cable companies.

Section 5.7.1 – Rental for buildings

In November 2008 DBS signed an agreement to extend the rental contract for its main offices, according to which the original rental period will be extended to October 31, 2014, with DBS having an option to extend the contract by a further five years, and this with a price increase of 5%. Furthermore, the rented space was enlarged and is 8,335 sq. m with additional parking spaces. DBS also extended its rental contract for the additional 1,994 sq.m rented from another party, until July 2010. DBS came to an understanding with regard to increasing the rented space in Neshet to 1,612 sq. m and extending the rental period until May 2011. Furthermore, DBS has rented, as of September 2008 until October 1, 2009, 1,100 sq. m space in Beer Sheva for the purpose of operating a service center. DBS has an option to extend the rental period of the service center for periods and at terms to be decided by the parties.

Section 5.8.1 - Licenses

In October 2008, the Ministry of Communication extended the validity of DBS's special license for providing uplink/downlink services to other communication licensees until October 2013.

Section 5.10.4 – Employee Compensation Plans

For further information regarding the allocation of Company options to the CEO of DBS see Note 8 to the Company's financial statements for the period ended September 30, 2008. Furthermore, in September 2008, the annual grant plan for the CEO of DBS became effective for 2009 – 2010, based on the rate for meeting of certain goals as defined in the plan, subsequent to receiving the consent of the Antitrust Commissioner and the approval of DBS institutes.

Section 5.13 – Finance

Section 5.13.6 –at September 30, 2008, DBS is in compliance with the financial stipulations under the financing agreement.

Section 5.13.8 – since debentures (series A) that were issued by DBS were not registered for trading until July 31, 2008, they will begin bearing annual interest at the rate of 8.4% from that date.

Furthermore, in August 2008, Maalot announced its validation of the BBB- / stable outlook rating for the debentures.

Section 5.15.1 – Subordination of Activity to Specific Laws

During April 2008, the Knesset approved an amendment to the Consumer Protection Law regarding group transactions. On this matter see the update to section 2.16.9, above.

In October 2008, the Ministry of Communications informed DBS that due to the fact that Bank Leumi Ltd (in this section: "Bank Leumi") is part of the consortium of banks in whose favor some of the DBS shareholders attached the DBS share capital held by them on the one hand and on the other hand Bank Leumi's holding in on the other hand as part of the share capital of Keshet Broadcasting Ltd., the concession holder in accordance with the Second Authority for Television and Radio, 5750-1990. As of October 31, 2008 on which the transfer provisions set forth in the Regulations for the granting of a license expired with respect to a parallel holding as aforesaid at a rate exceeding 25% of the concession holder's equity, and one of the qualifying restrictions set forth in the Regulations for granting licenses, in the opinion of the Ministry of Communication, will be applicable with regard to

DBS. The permission to surpass expiry of the transfer provision as aforesaid, was given to DBS by Bank Leumi and by the Ministry of Communication, due to the formulated of a memorandum of agreement between them, according to which the Ministry of Communication will not take any action against DBS for its forgoing position, subject to the splitting of the attachment deeds of the attached DBS shares, so that only the appropriate portion of DBS shares attached to all the banks will be attached in favor of Bank Leumi and subject to compliance with other obligations on the part of Bank Leumi, during the defined period.

Section 5.16.2 – Space segment lease agreements

Second space agreement – on April 28, 2008, the Amos 3 satellite, to be operated by HLL and intended as a downstream satellite for Amos 1 and Amos 2, was successfully launched. In July 2008, its positioning in space was completed. Commencing June 30, 2008, DBS ceased using the satellite Amos 1 and it now uses the satellites Amos 2 and Amos 3 for its satellite segments.

On July 15, 2008, DBS and HLL signed an amendment to the second space agreement stating, *inter alia*, that DBS will lease 13 space segments from HLL, instead of 14 and DBS will cease leasing the 13th segment until another agreement is made between the parties, according to the mechanism stated in the agreement. Furthermore, a mechanism for back-up was set up using satellite Amos 3 in the event that space segments are not available on satellite Amos 2.

Section 5.16.4 – Agreement for Telephony Service Center

As of January 1, 2009, DBS intends to independently operate the service center which to date was operated by Bezeq On-line Ltd., in Beersheva.

Section 5.17 – Joint Venture agreements

Section 5.17.1 – as set out in the update to section 5.6.5(g), this joint venture has ended.

Section 5.18 – Legal Proceedings

Regarding the claim against Pace and the counterclaim (section 5.18.1): on July 3, 2008, the registrar rejected the respondent's request to erase the suit, while determining that the nominal amount in the statement of claim is the maximum amount that DBS may receive if it wins the suit, including the amount of value added tax for which it was required to pay a fee. Similarly, the request of DBS to grant an order correcting the statement of defense and the statement of countersuit submitted by the respondent was rejected. A pretrial hearing was set for December 16, 2008.

The class action claim regarding the sports channel (section 5.18.6): on May 29, 2008, DBS, in cooperation with the cable company, submitted a summary of its claims regarding the primary appeal and also a summary of its claims regarding the counter-appeal. On June 23, 2008, appellants submitted summaries of their responses to the primary appeal and a summary of their response to the counter-appeal. On July 9, 2008, D.B.S., in cooperation with the cable company, filed summaries of their response to the counter-appeal. A court date for the hearing the appeal and counter-appeal has been set for June 17, 2009.

Re the deficit demand from the Customs Department (Section 5.18.7): In April 2008, the Taxation Authority stated that there is nothing preventing the VAT in the cash invoice from being paid by DBS, which shall be entitled to deduct the input tax contained therein. Therefore, DBS paid the value added tax. In July 2008, the parties signed a compromise agreement that brings to an end the dispute over the demand for deficit taxes, subject to the payment of approximately NIS 1.5 million by DBS.

For further updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2008.

Section 5.21.1.2 – Macro Risks

During the current quarter, subsequent to the worldwide economic crisis, global markets have entered a slowdown and credit choke. The impact of this situation is expected to continue to be felt throughout 2009 and possibly beyond, and there may be a shift from growth to recession. In the local market the slow down is also expected to be significant, as is the decline of business operations and of the central economic parameters. The anticipated economic slowdown is expected, *inter alia*, to lead to a decrease in the number of DBS subscribers, decrease in DBS revenues and to harm the results of its operations. Furthermore, if the economic slowdown leads to harming the operations or termination of the operations of significant suppliers, it is possible that this will have a negative impact on DBS's operations.

This information includes forward looking information based on internal estimates of the Company. The actual results may be materially different from the foregoing estimates if changes take place in any of the factors taken into account for this assessment.

Section 5.21.3 – Special risks to DBS

Section 5.21.3.5 - as set out in the update to section 5.16.2 above, commencing July 2008, DBS ceased using the Amos 1 satellite and it now uses the Amos 2 and Amos 3 satellites.

Section 5.21.3.6 as stated above, commencing July 2008 HLL is the only owner of rights with whom DBS has a contract for leasing space segments.

November 24, 2008

Date

Bezeq – The Israel Telecommunication Corp. Ltd.

Names and titles of signatories:

Shlomo Rodav – Chairman of the Board

Avi Gabbay, CEO