May 21, 2008

"Bezeq" The Israel Telecommunication Corp. Limited

Quarterly Report for the period ending 31.3.08

Update of Chapter A (Description of Company Operations) of the Periodic Report for 2007

Directors' Report on the State of the Company's Affairs for the period ended March 31, 2008

Condensed Interim Consolidated Financial Statements as at March 31, 2008

Update of Chapter A (Description of Company Operations) of the Periodic Report for 2007

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 from the periodic report for 2007, 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, targets, appraisals and assessments which apply to future events or matters the realization of which is not certain and is not under 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 assesses", "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, based, inter alia, on a general analysis of the information available at the time of drafting of this report, including public announcements, studies and surveys, and they contain no undertakings as to the correctness or completeness of the information contained therein, and the Corporation does not independently check the correctness thereof. The Company's assessments vary from time to time in accordance with the circumstances.

In addition, the realization and/or otherwise of the forward-looking information will be affected by factors that cannot be assessed in advance, and which are not within the control of the Corporation, including the risk factors that are characteristic of its operations as set out in this report, and 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

On March 12, 2008, the Gronau Commission 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 Commission") published its Report. The following are the principal recommendations, in summary:

Fixed-Line Sector

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

2. It is proposed that 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 to be prescribed after 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 packages, 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

[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 2006 [sic] and relates to the section numbers in Chapter A (Description of Company Operations) in such periodic report.

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 axes (line cluster) - 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 (not more 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.

<u>Cellular Sector</u>

The regulation processes required for the entry of virtual carriers, and the WiMAX tender to be accelerated, competition in the mobile sector to be strengthened and the cost of call completion on mobile networks to be checked in 2009, and the tariff amended accordingly.

<u>International Call Sector</u>

International call tariffs via mobile telephones to be prescribed by the international calling company, and paid to the cellular company at the tariff set out 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.

<u>Multi-Channel Television</u>

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 set the price of the package, and enforcement of structural separation between Hot Broadcasts and Hot Telecom in their licenses, in accordance with the format in place in the Company.

<u>General</u>

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 transition obstruction flowing from 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 desirable that cancellation of the royalties accompany a parallel reduction in tariffs.

The Minister of Communications has not yet adopted the recommendations, in whole or in part.

If all of the recommendations contained in the Report are adopted and implemented as drafted, this is expected to cause a substantial adverse effect on the business results of the Company and of its subsidiaries. However, the Company is unable to assess what the Minister's decision might be, or when it might be passed.

See also updates to sections 3.7, 4.1.2 and 5.1.1 below.

<u>Section 1.1.4 - Holdings of the Company</u>

The following are details of the current rate of holdings of the Company, fully diluted, under the presumption of exercise of all of the options actually allocated to employees of the Company as at the date of publication of this report (as set out in the Periodic Report for 2007 and in the update to section 1.3.2 below, with the exception of the allocation to the chairman of the board of directors, which has not yet been completed), and under the presumption of exercise of Ap. Sab. Ar.'s option to purchase approximately 10.66% of the State's shares in the Company:

Shareholders	Percentage holdings as at 15.5.08	Percentage holdings (fully diluted)
Ap. Sab. Ar.	30.00%	38.81%
State of Israel	15.68%	0.97%
Zeevi Group	17.75%	16.95%
The Public	36.57%	43.27%

Section 1.1.5A – Mergers and Acquisitions – DBS

During the hearing of an appeal filed by the Company against the decision of the Antitrust Commissioner to object to the Company's merger with DBS, the Antitrust Tribunal proposed that the parties try to reach an agreement regarding approval of the merger subject to conditions.

Section 1.1.6 - Realizations

With respect to satellite 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. Under the agreement, the operations are to be sold in consideration for the total NIS equivalent of the sum of US $ 15 million (at the representative rate on the date of payment) plus VAT, subject to price adjustments as a result of various stipulations and changes that might occur, if at all, to the operations during the period up until the date of completion of the transaction. Completion of the transaction is subject, inter alia, to the regulatory consents of the Ministry of Defense, the Ministry of Communications and the Antitrust Commissioner. If the deal is completed at the maximum price as aforesaid, then the Company is expected to record a capital profit in respect of it, subject to changes in the representative rate of the dollar, of approximately NIS 49 million (before tax)[2].

Section 1.3 – Investments in Equity and Stock Transactions

Section 1.3.2 - Employee Option Schemes

Under the option scheme for directors and senior employees of the Group of November 2007 for the allocation of up to 65,000,000 options, since the date of publication of the periodic report for 2007, 5,600,000 additional options have been allotted such that as at the date of this update, a total of 45,700,000 options have been allotted under the scheme. Likewise, the board of directors of the Company approved the allotment of 9,000,000 options to the chairman of the board of directors of the Company, in accordance with the private offering report of the Company published on April 18, 2008. The allotment to the chairman of the board of directors requires the approval of the general meeting of shareholders, which has been convened for June 1, 2008.

Section 1.4 – Payment of Dividends

On April 28, 2008, a cash dividend was paid to the shareholders of the Company in the total sum of NIS 679 million, constituting, as at the date of the distribution NIS 0.260648 per share, having been approved by the general meeting of shareholders of the Company on April 3, 2008.

[2] Based on an exchange rate of NIS 3.5 – USD 1.00.

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

Section 1.5.3 - Principal Results and Operations Figures

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

	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	1,408	1,453	1,425	1,393	1,442
Operating Profit (NIS millions)	368	340	327	243	369
Depreciation and amortization (NIS millions)	218	233	236	235	237
Operating profit before depreciation and amortization (EBITDA) (NIS millions)	586	573	563	478	606
Investments in plant & equipment and intangibles (in NIS millions)	124	141	149	101	113
Proceeds of sale of plant & equipment (in NIS millions)	0	23	16	96	18
Number of active subscriber lines as at the end of the period (thousands)	2,713	2,761	2,767	2,778	2,797
Average monthly income per line (NIS)*.	84.9	85.8	85.6	85.1	88.3
No. of outgoing use minutes (millions)	3,594	3,738	3,849	3,753	3,914
No. of incoming use minutes (millions)	1,182	1,164	1,149	1,069	1,045
Number of ADSL subscribers as at the end of the period (thousands)	970	963	942	924	912
Average monthly revenue per ADSL subscriber (NIS).	58.1	58.1	58.5	58.1	57.4

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

B. Pelephone

Pelephone	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	1,173	1,182	1,203	1,152	1,147
Operating Profit (NIS millions)	215	133	219	240	213
Depreciation and amortization	129	125	121	115	117
Operating profit before depreciation and amortization (EBITDA) (NIS millions)	343	258	340	355	330
Net profit	163	104	154	173	154
Cash flow from current operations	264	252	392	246	359
Investments in plant & equipment and intangibles	103	120	81	117	63
Proceeds of sale of plant & equipment	1	3	-	-	2
Number of subscribers at end of period (thousands)	2,595	2,622	2,560	2,513	2,478
Average use minutes per subscriber (MOU) per month	355	358	363	350	344
Average monthly revenue per subscriber (NIS) (ARPU)	126	130	135	129	132
Number of 3G subscribers at end of period (thousands)	867	749	607	471	358
% revenues from value added services and content, of revenues from cellular services	15.0%	13.6%	12.8%	12.5%	12.0%

C. Bezeq International

	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	314	333	326	322	323
Operating Profit (NIS millions)	55	45	54	54	51
Depreciation and amortization (NIS millions)	20	21	21	22	23
Operating profit before depreciation and amortization (EBITDA) (NIS millions)	75	66	75	76	74
Net profit (NIS millions)	42	38	39	39	36
Cash flow from current operations (NIS millions)	8	30	34	32	(1)
Investments in plant & equipment and intangibles (in NIS millions)*	28	36	29	18	8
Proceeds of sale of plant & equipment (in NIS millions)	-	2	2	-	-

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

A. DBS

	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	381	349	360	354	354
Operating Profit (NIS millions)	27	5	(4)	31	24
Depreciation and amortization (NIS millions)	65	70	66	69	68
Net profit (loss) (NIS millions)	(65)	(73)	70	(65)	(48)
Cash flow from current operations (NIS millions)	84	76	56	25	93
Investments in plant & equipment and intangibles* (in NIS millions)	79	81	84	45	45
Proceeds of sale of plant & equipment (in NIS millions)	0	-	-	-	-
Number of subscribers (as at the end of the period, thousands)	549	549	545	543	542
Average monthly revenue per subscriber (NIS).	231	212	220	218	218

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

Section 1.7 – General Environment and Affect of External Factors on Group Operations

The transaction for the purchase of 15% of the share capital of HOT by Netvision, reported by Discount Investments, if and to the extent concluded, might strengthen the position of the IDB Group and of HOT as a communications group in competition with the Group.

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

Section 2.1 – General information on areas of operation

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

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

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 free call (1-800) service 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 this amendment to the Ministry of Communications.

Section 2.2.3 – Internet access services

For changes during the first quarter of 2008 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 began providing 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 12B to the financial statements of the Company for the period ended on March 31, 2008.

Section 2.6 – Competition

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

Section 2.6.1 – Telephony

With respect to the Company's petition to the High Court of Justice with respect to the application to enforce the structural separation obligation on HOT, on April 28, 2008, the Company filed a notice of update to the Court requesting to set a hearing. Under the Company's notice, the Gronau Commission's report contains an unequivocal recommendation that the Ministry of Communications enforce structural separation on HOT, in accordance with the separation format in place at the Company.

Section 2.6.6A - Numbering and Number Portability

As at the end of April 2008, approximately 90,000 thousand lines had ported from the Company, most of them going to HOT.

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 a 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 on this amendment, claiming that it would amount to confiscation of the end user's right to decide whether to port the number or not.

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. The Company is studying the significance of this Directive.

Section 2.6.7 – The Company's preparations for coping with increasing competition

Sub-section (i) regarding examination of the deployment of uniform infrastructure for the transmission of communications services – the board of directors of the Company had approved entry into detailed planning of an NGN (Next Generation Network) project, to complete the purchasing of soft switch installation and to submit a detailed analysis of the project to the board of directors for discussion.

Section 2.9 – Human resources

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

A. With respect to the organizational structure - the VP Finances and the VP Strategy and Business Development report to the CEO alone.

B. In May 2008, execution of the amendment to the new collective agreement regarding the bringing forward of completion of implementation of the organizational structure, and regarding bringing forward dates of retirement and changes in the mix of retirees who are supposed to retire under the new collective agreement before the end of 2008 was concluded.

Section 2.9.2 – Personnel according to employment framework

During the first three months of 2008, the number of employees of the Company fell from 7,614 employees as at December 31, 2007 to 7458 as at March 31, 2008 (a net reduction of 156 employees) as a result of retirements from the Company (contemporaneous with the recruitment of necessary employees such as sales representatives).

Note that out of 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 2006), as at March 31, 2008, 951 employees had retired.

Section 2.9.6 – Employee incentive schemes

Section 2.9.6.3 - for the allotment of options to directors and senior employees of the Group, including 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 consents 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 require the consent of the general meeting of shareholders of the Company, which has been convened for June 1, 2008.

Section 2.13 – Finance

Section 2.13.4 - Credit received after December 31, 2007

The Company has not taken any loans during the report period.

Section 2.13.6 – Credit Rating

On May 21, 2008, the Midroog Rating Company 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 a dividend after the switch in the control core of the Company.

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

In the Company's assessment, the Company might, from time to time, raise short-term 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 operations permits for communications and broadcasting facilities by the Commissioner for Radiation is moving forward.

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 Commission 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"). Under the letter, after and to the effect that the Gronau Commission'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 arrangement for the coming years. On May 11, 2008, the Company received a letter from the Ministry of Communications under which, on June 1, 2008, an annual update of the Company's tariffs is expected to apply in accordance with the recommendations of the Gronau Commission (regarding the Company's tariffs), and that the Minister of Communications intends to make regulations under which the interconnect tariffs currently paid to domestic carriers by an international carrier, cellular licensee or other domestic carrier regarding call completion on a domestic network will be reduced by an average rate of around 2%. With respect to the update of the Company's tariffs, see also the update regarding publication of the recommendations of the Gronau Commission in section 1.1 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 provide their positions to the Ministry of Communications by June 18, 2008. The Company is examining the Ministry's letter in order to formulate its position.

Section 2.16.7 - Antitrust laws

Sub-section 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 7C(1) to the financial statements of the Company for the period ended March 31, 2008.

Section 2.16.9 - Proposed Legislation to Amend 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 (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 is examining the significance of implementation of the Amendment, and is preparing for implementation of it. 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. Furthermore, the Consumer Protection Law regarding disconnection from ongoing services was approved by the Knesset, and the law regarding spam was approved by the Economics Committee of the Knesset, pending second and third readings as was a bill regarding spam and a bill regarding technician visits (the latter with certain reservations by the Government).

Section 2.16.11 – Establishment of communications facilities – National Outline Plan 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.

Section 2.17 – Material agreements

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

Section 2.18 – Legal proceedings

For updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended March 31, 2008.

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 might also 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 by May 29, 2008. Pelephone is formulating its position in this regard.

Section 3.7 – Competition

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

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.

Section 3.18.3.1(f) – Pelephone's license

During the month of March 2008, the Ministry of Communications passed a resolution 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 began on April 22, 2008.

Section 3.18.3.1(g) – Pelephone's license

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 distinct from the previous hearing: the current amendment proposes that during the obligation period, it will not be possible to amend tariffs. Pelephone is studying the significance of this and will formulate its response.

Section 3.21 – Legal proceedings

For updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended March 31, 2008.

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 Commission 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. Thus, the Commission 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 Commission, see also update to section 1.1 above.

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 purchased 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 March 31, 2008, Bezeq International held 34.38% (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, on April 16, 2008, counsel for the plaintiffs filed a notice to the Court in which he gave notice that the settlement negotiations that had been being conducted by the parties had not resulted in any agreement and therefore, the Court is requested to set down a date for pre-trial and dates for the conclusion of discovery proceedings, perusal of documents and responses to interrogatories. As at the date of this report, a ruling has not yet been handed down in the application.

For further updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended March 31, 2008.

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 under first 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.

Section 5.1.3.5 – in March 2008, the Minister of Communications published the recommendations of the Gronau Commission. The recommendations deal with the areas of telephony, internet and multi-channel broadcasts. Among other recommendations, the Commission 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 Commission 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 others of its recommendations regarding infrastructure and the Company’s services are applied.

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

Section 5.15.1 – Specific legal restrictions on operations

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.

Section 5.6.5 – Principal methods for coping with competition

Section 5.6.5(g) – “basket of services” – as of April 2008, DBS has ceased marketing a basket of services to its subscribers containing broadcasts and high-speed internet connection infrastructure, and has commenced selling the Company’s campaigns regarding high-speed internet connection infrastructure such that subscriber contracts regarding such infrastructure are made with the Company only.

Section 5.13 – Finance

Section 5.13.6 – as at March 31, 2008, DBS is in compliance with the financial stipulations under the financing agreement (as amended).

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. According to information provided to DBS by HLL, the procedures for testing and stationing the satellite in the appropriate part of space are expected to end in June 2008. When Amos 1 goes out of service, the leased capacity on Amos 1 is to be transferred to Amos 2 and Amos 3.

The information above regarding the stationing of the Amos 3 satellite is forward-looking information, based, to the best of DBS’s knowledge, on technical and technological parameters relating to the satellite. Therefore, technical faults and other events might postpone or prevent the final stationing of the Amos 3 satellite in space. The transfer of some of DBS’s broadcasts via the Amos 3 satellite is also dependent upon reaching an agreement with HLL. As at the date of this report, a date for commencement of transmission of broadcasts via Amos 3 has yet to be set.

Section 5.17 – Joint Venture agreements

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

Section 5.18 – Legal proceedings

Re the deficit demand from the Customs Department (Section 5.18.7): In April 2008, a response was received from the Legal Department of the Taxation Authority relating only to the VAT charges on the principal in the deficit demand. The Taxation Authority's response 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, despite the fact that the Taxation Authority views Eurocom Communications as the importer of the smart cards. The Taxation Authority's response also states that the aforesaid shall not have implications on Eurocom Communications' obligation for purchase tax imposed upon the smart cards.

For further updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended March 31, 2008.

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, the Amos 3 satellite was launched in April 2008, but its stationing in space has not yet been completed.

21.5.08	
Date	Bezeq – The Israel Telecommunication Corp. Ltd.

Names and titles of signatories:

Shlomo Rodav – Chairman of the Board

Avi Gabbay, CEO

Directors' Report on the State of the Company's Affairs for the period ended March 31, 2008

Chapter B of the Periodic Report

Directors' Report on the State of the Company's Affairs For the quarter ended March 31, 2008

We respectfully present the Directors' Report on the state of affairs of Bezeq - The Israel Telecommunication Corp. Limited (hereinafter: "the Company") and the consolidated Group companies (the Company and the consolidated companies together are hereinafter collectively referred to as "the Group"), for the three-month period ended March 31, 2008 (hereinafter: "the Directors' Report").

The Group operates in four main areas which are reported as business segments in the Company's consolidated reports as follows:

1. **Domestic fixed-line communications**
2. **Cellular**
3. **International communications, internet services and NEP**
4. **Multi-channel television**

The Group has an additional area of operations which is not material to the Group's operations, and which has been included in the financial statements of March 31, 2008 as another business sector, which mainly includes customer call center services and investment in a venture capital fund.

The net earnings in the reporting period amounted to NIS 385 million, the same as the net earnings in the corresponding period in 2007. The net earnings remained the same due to similar results of operations in all the segments. In the domestic fixed-line communications segment and the internet communications, internet services and NEP segment, there was a decrease in income and a decrease in expenses, respectively, and in the cellular and multi-channel television segments there was an increase in income and an increase in expenses, respectively. See below for further details.

1. Financial position

A. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS).

B. The Group's assets on March 31, 2008 amounted to NIS 15.18 billion, compared to NIS 15.69 billion on March 31, 2007. Of these, NIS 5.98 billion (39%) are property, plant and equipment, compared to NIS 6.33 billion (40%) on March 31, 2007.

   The decrease is due to the domestic fixed-line communications segment. There was a decline in total assets in this segment, not including investment in subsidiary companies, compared to the corresponding period last year, in the amount of NIS 1,019 million, mainly due to the sale of financial assets held for trading which was used for distribution of a dividend. In addition, there was a decrease in the depreciated cost of property, plant and equipment resulting from the difference between depreciation expenses and the investment made in the reporting period. The decrease in total assets was offset by an increase in the customer balance mainly due to the late issue of bills to customers and the transition from billing in advance of fixed user fees for telephone lines to retroactive billing.

   In the cellular segment, assets increased from NIS 4.1 billion on March 31, 2007 to NIS 4.42 billion on March 31, 2008. The increase was mainly due to an increase in the cash balances. In addition there was an increase in the customer balances mainly due to the termination of credit card payments. On the other hand, there was a reduction in the tax asset due to the sale of an asset recorded in the past for losses, and a decrease in the depreciated cost of property plant and equipment.

   In the international communications, internet and NEP services segment, there was an increase in total assets compared to March 31, 2007, mainly due to the increase in the customer balance and advance expenses for users rights in capacities that were offset by a reduction in the cash balances used for early payment of loans and tax advance payments.

In the multi-channel television segment, there was an increase in total assets compared to March 31, 2007, which was mainly due to an increase in broadcasting rights and an increase in the net investment balance in property, plant and equipment.

C. The shareholders' equity of the Company on March 31, 2008 amounted to NIS 4.95 billion, representing 33% of the total balance sheet, compared to NIS 4.35 billion on December 31, 2007, which represented 28% of the total balance sheet. The increase in shareholders' equity was mainly due to the Group’s net profit which was partially offset by dividends paid in the amount of NIS 760 million in 2007.

D. Total Group debt on March 31, 2008 amounted to NIS 6.93 billion, compared to NIS 7.83 billion on March 31, 2007. Group debt to financial institutions and debenture holders on March 31, 2008 amounted to NIS 6.54 billion, compared to NIS 7.25 billion on March 31, 2007. The decrease is mainly due to payment of Eurobonds and debentures in the domestic fixed line communications segment in the amount of NIS 1.96 billion and payment of loans and debentures in the cellular segment. In addition, there was early payment of loans in the international communications, internet services and NEP segment.

The decrease was offset mainly by the sale of debentures to institutions in the domestic fixed-line communications segment in the amount of NIS 1.2 billion and issue of debentures in the multi-channel television segment in July 2007 in the amount of NIS 614 million.

The Company’s auditors have highlighted in the financial statements the financial position of DBS. As stated in Note 6, as of March 31, 2008 DBS is in compliance with the financial criteria established for it, after the banks adjusted the stipulations on March 5, 2008 to comply with the budget of DBS. The continuation of the operations of DBS is also conditional on compliance with conditions set for 2008 and/or further relief to be received during the year. The management of DBS believes that the financial resources available to it will be sufficient for its operating needs in the coming period based on the forecasted cash flow approved by the board of directors of DBS.

E. The Group’s cash and other current investment balances on March 31, 2008 amounted to NIS 1.6 billion compared to NIS 1.88 billion on March 31, 2007. The decrease is mainly due to a decrease in the cash balance and the sale of commercially held securities in the domestic fixed-line communications segment, which were used to pay a dividend. In the international communications, internet services and NEP segment, there was a decrease in the cash flow that was used for early payment of loans and advanced tax payments.

The decrease was partially offset by an increase in cash balances in the cellular segment and the positive cash flow from current operations in the principal segments of the Group's operations.

2. Results of operations

A. Principal results

Net earnings attributable to the shareholders of the Company for the first quarter of 2008 amounted to NIS 398 million, compared to net earnings of NIS 399 million in the corresponding quarter last year.

Below are details of the changes in the results of the segments compared to the corresponding quarter last year.

Segment	March 31, 2008 Operating profit NIS millions	March 31, 2007 Operating profit NIS millions
Domestic fixed-line communications	368	369
Cellular	214	213
International communications, internet services and NEP	55	51
Multi-channel television	27	24
Total	664	657

Basic and diluted earnings per share in the first quarter of 2008 and in the corresponding quarter last year amounted to NIS 0.15 per NIS 1.00 par value.

B. Revenue

Group revenue in the first quarter of 2008 amounted to NIS 3.1 billion compared to NIS 3.09 billion in the corresponding quarter last year.

Revenues from domestic fixed-line communications decreased from NIS 1.44 billion in the corresponding quarter last year to NIS 1.41 billion in the reporting quarter (a decrease of 2%). The decrease in the segment's revenues is due to a decrease in interconnect fees to the cellular networks (with a parallel decrease in expenses). An additional decrease is due to a decrease in the number of lines (mainly due to number portability), a reduction in call traffic and a decrease in tariffs in June 2007. The decrease in revenues was moderated mainly by ongoing growth in revenues from high-speed internet service (ADSL) and by an increase in income from data communication services. The Company's auditors continue to highlight the growing competition in the communication sector and the impact of regulation.

Revenues from the cellular segment increased from NIS 1.15 billion in the corresponding quarter last year to NIS 1.17 billion in the reporting quarter. The increase is mainly due to an increase in content revenue and an increase in the number of subscribers, which was partially offset by a decrease in average revenue per subscriber. There was also an increase in revenue from sale of terminal equipment, due to an increase in the number of handsets sold and upgraded.

Revenue in the international communications, internet and NEP services segment amounted to NIS 314 million in the reporting quarter, compared to NIS 323 million in the corresponding quarter last year. In this segment there was a decrease in operations relating to transfer of calls between communication operators around the world. In contrast, there was an increase in revenue from internet broadband service and outgoing calls.

Revenue in the multi-channel television segment increased from NIS 354 million in the corresponding quarter last year to NIS 381 million in the reporting quarter, due to an increase in the number of subscribers and an increase in the average revenue per customer.

C. Depreciation and amortization

The Group's depreciation and amortization expenses decreased from NIS 441 million in the corresponding quarter last year to NIS 429 million in the reporting quarter, mainly due to a decrease in the depreciation expenses in the domestic fixed-line communication segment resulting from full depreciation of property plant and equipment and a decrease in investments in new assets. The decrease was partially offset by an increase in depreciation expenses in the cellular segment as a result of the accelerated depreciation of the 1 X network due to the establishment of a UMTS network.

D. Salaries

The Group's salary expenses increased from NIS 575 million in the corresponding quarter last year to NIS 616 million in the reporting quarter. The increase in salary is due to the expansion of the workforce in preparation for number portability in the cellular segment. The decrease in expenses due to early retirement of employees in the domestic fixed-line communications sector was offset by salary increases in this segment and in the other segments in the Group.

E. General and operating expenses

The Group’s operating and general expenses in the reporting quarter amounted to NIS 1.37 billion, compared to NIS 1.42 billion in the corresponding quarter last year.

In the domestic fixed-line communications segment, operating and general expenses decreased from NIS 533 million in the corresponding quarter last year to NIS 486 million in the reporting quarter. The decrease is mainly due to a reduction in interconnect fees to cellular operators, service and maintenance by subcontractors, building maintenance, and royalty expenses, which were partially offset by an increase in materials and spare parts expenses and by general expenses.

In the cellular segment, general and operating expenses decreased from NIS 668 million in the corresponding quarter last year to NIS 660 million in the reporting quarter. The decrease is mainly due to a decrease in prices of terminal equipment and advertising expenses which was partially offset by an increase resulting from an increase in content expenses and connectivity as well as an increase in revenues.

In the international communications, internet services and NEP segment there was a decrease in general and operating expenses from NIS 189 million in the corresponding quarter last year to NIS 174 million in the reporting quarter. The decrease is mainly due to a reduction in operations relating to call transfers between communication operators around the world alongside a decrease in revenues.

In the multi-channel television segment, general and operating expenses increased from NIS 219 million in the corresponding quarter last year to NIS 239 million in the reporting quarter, due to an increase in content consumption in view of broadcasts of original productions and general expenses.

F. Other operating expenses (income), net

The Group’s other net operating expenses originated mainly from the domestic fixed-line communications segment. These expenses amounted to NIS 21 million in the reporting quarter, compared to income of NIS 7 million in the corresponding quarter last year. This was mainly due to an increase in expenses recorded for provision for severance pay in early retirement and an absence of capital gain.

G. Operating income

The Group's operating income in the reporting quarter amounted to NIS 664 million, compared to NIS 657 million in the corresponding quarter last year, an increase of NIS 7 million. The increase in operating income is due to the changes in the results of the segments described above in the revenue and expenses sections.

H. Financing expenses - net

The Group’s net financing expenses in the reporting quarter amounted to NIS 100 million compared to NIS 58 million in the corresponding quarter last year, an increase of NIS 42 million.

The Group's debt to financial institutions and debenture holders is mainly linked to the CPI and the financing expenses are affected by fluctuations in the Index. In the reporting period there was a rise in the Index, to which the debt balance is linked, compared to the corresponding quarter last year and revaluation of liabilities led to an increase in the Group's financing expenses.

In the domestic fixed line communications segment, there was an increase in net financing expenses compared to the corresponding period. This is mainly due to a decrease in revenues in the capital market and realization of deposits and securities and a decrease in their return. In this segment there is an increase in expenses due to revaluation of CPI-linked liabilities, which was mainly offset by hedging transactions.

In the cellular segment, there was an increase in net financing expenses, mainly due to the reduction in liabilities and the decrease in the dollar exchange rate which was partially offset by the increase in expenses for revaluating CPI-linked liabilities as a result of a rise in the index.

In the multi-channel television segment, net financing expenses in the reporting quarter amounted to NIS 92 million compared to NIS 72 million in the corresponding quarter last year. The increase in the CPI led to an increase in financing expenses due to the revaluation of CPI-linked liabilities and an increase in the Company’s financial debt.

I. Income tax

The Group's tax expenses in the reporting quarter amounted to NIS 180 million, representing approximately 32% of profit before taxes, compared to NIS 214 million in the corresponding quarter last year, representing 36% of pre-tax profit. Most of the decrease in the tax expenses from profit before income taxes is due to a reduction in the tax rate and the cancellation of Income Tax (Taxation Under Conditions of Inflation) Law.

3. Liquidity and sources of financing

Consolidated cash flows generated by operating activities in the reporting quarter amounted to NIS 637 million, compared to NIS 865 million in the corresponding quarter last year, a decrease of NIS 228 million. The decrease in cash flows generated by operating activities is mainly due to an increase in the customer balances, due to the abovementioned reasons, and a decrease in suppliers due to the decrease in the volume of purchases in the cellular segment and international communications, internet services and NEP segment and payments for early retirement.

Cash flows generated by operating activities are one of the sources of financing of the Group's investments, which during the reporting quarter included, inter alia, NIS 307 million invested in the development of communications infrastructures, compared to investments amounting to NIS 177 million in the corresponding quarter last year.

In the reporting period, the Group repaid net debts and paid interest of NIS 313 million, of which NIS 229 million was on account of debentures, NIS 40 million in loans, NIS 56 million in interest payments and NIS 12 million for short-term credit received, compared to payment of net debt and interest payments in the amount of NIS 258 million in the corresponding quarter last year.

In the reporting quarter, cash dividends were not paid compared to NIS 2.1 billion paid in the corresponding quarter last year.

The monthly average short-term credit balance from banks in the reporting quarter amounted to NIS 87 million. The monthly average of long-term liabilities to financial institutions and debenture holders in the reporting quarter amounted to NIS 6,658 million.

The working capital on March 31, 2008 was positive, and amounted to NIS 573 million, compared to negative operating capital on March 31, 2007 which amounted to NIS 2.59 billion, an improvement of NIS 3.2 billion. The increase in the working capital is due to an increase in working capital in all the segments in which the Group operates.

In the domestic fixed-line communications segment there was a decrease of NIS 1.2 billion in the working capital deficit compared to the corresponding quarter of last year. The decrease in deficit is mainly due to a decrease in current liabilities, which is mainly due to repayment of debentures (Eurobonds), a decrease in current provisions related to benefits for employees as well as an increase in customer balance. On the other hand, there was a decrease in investments in commercially held financial assets.

In the multi-channel television segment there was a decrease in deficit mainly due to the classification of bank loans as long-term loans, in view of the compliance with the terms of the financing agreement with the banks.

4. Group involvement in the community and donations

The Group is active in the community through contributions to recognized non-profit organizations that channel funds to education, welfare and other causes, and through development of direct volunteering of employees in the community. In the reporting quarter, the Company started to work with "Matan - Your Way to Give", a non-profit organization that helps donors implement their philanthropic vision. In addition, the Company has become a member of Ma'ale – Business for Social Responsibility, a non-profit membership organization that advocates corporate values. The Group is active in the community through its involvement in social institutions and organizations, such as the education system in underprivileged areas and the confrontation line. In addition, Group employees volunteer in additional and diverse community involvement activities.

During the reporting period the Group donated NIS 214,000. The principal recipients are listed below:

A. In the project "Youth Employment at Bezeq", which has been ongoing for some 14 years, the Company's employees voluntarily mentor underprivileged youth employed at Bezeq with the aim of integrating them into normative life. In addition, Bezeq continues to support the "Dialogue in the Dark" project at the Children's Museum in Holon, and many other activities.

B. Bezeq International is involved in ongoing operations on behalf of underprivileged communities in Petach Tikva, it adopted "lone" soldiers and a combat division and participated in projects for children with special needs.

5. Exposure to and management of market risks

A. Further to the description in the Directors' Report of 2007, hedging transactions against market risks connected to exposure to fluctuations in the exchange rate and the CPI significantly reduced this exposure.

B. The derivative positions report on March 31, 2008 is not significantly different from the report on December 31, 2007.

C. The sensitivity analyses for the fair value and the effect of the change in the market prices on the fair value of on- or off-balance sheet contractual agreements on March 31, 2008, are not substantially different from the December 31, 2007 statement. However, the total fair value of net liabilities that are sensitive to fluctuations in the dollar-shekel exchange rate on December 31, 2007 should amount to NIS 1,148 million. The sensitivity to changes in the dollar interest rate should amount to NIS 622 million, due to the adjusted measuring of communications to space sections, which should amount to NIS 611 million instead of NIS 343 million.

D. The linkage basis report on March 31, 2008 is not substantially different from the report on December 31, 2007.

The surplus financial liabilities on financial assets in or linked to foreign currency on March 31, 2008 amounted to NIS 93 million in the Group. Future currency transactions on March 31, 2008 amounted to NIS 335 million. The purpose of the transactions is also to hedge against off balance-sheet liabilities in or linked to foreign currency.

The surplus liabilities on CPI-linked financial assets on March 31, 2008 amounted to NIS 6,027 million in the Group. As a result of hedging transactions, on March 31, 2008 the net CPI-linked liabilities, which are not defined by forward transactions, amounted to NIS 3,577 million.

6. Critical accounting estimates

The preparation of the financial statements according to international accounting principles requires the management to make estimates and assessments that influence the reported values of assets and liabilities, income and expenses, and disclosure relating to contingent assets and liabilities. Management bases its estimates and assessments on past experience and on additional factors, value appraisals and opinions which it believes are relevant, taking into account the circumstances. The actual results can differ from those assessments based on various assumptions and conditions. Information on the principal matters of uncertainty in critical assessments and judgments in the application of the accounting policy is provided in the annual financial statements. We believe that these assessments and estimates are critical because every change in them and in the assumptions has the potential to materially affect the financial statements.

7. Opinion of process for approving the Company's financial statements

The Board of Directors is responsible for oversight. The Board of Directors appointed a balance sheet committee with the tasks and composition described in the Directors' Report of 2007.

The financial statements were discussed at the balance sheet committee and submitted to the Board of Directors for approval. The following officers attended the board discussion: board members – Shlomo Rodav, Eyal Yaniv, Menachem Inbar, Michael Grabiner, Ran Gottfried, Yoav Rubenstein, Elon Shalev, Kihara R. Kiarie, David Gilboa, Rami Nomkin, Yitzhak Edelman and Yehuda Porat. In addition, the following officers attended: Avi Gabbay – CEO, Alan Gelman – Deputy CEO and CFO, and Bosmat Chelouche – legal consultant. Representatives of Somekh Chaikin also participated in the discussion.

8. Miscellaneous

Events subsequent to the date of the financial statements

A. On January 31, 2008 the general meeting of the Company approved a stock options plan for managers and senior employees in the Company and/or in affiliates. Consequently, 45,700,000 options were allotted. On April 17, 2008 the Board of Directors resolved to allocate an additional separate 9,000,000 options to the Chairman of the Board, in accordance with the plan described in Note 9 to the financial statements.

B. On March 10, 2008 the Company's Board of Directors resolved to recommend, at the general shareholders' meeting, the distribution of a cash dividend to shareholders in the total amount of NIS 679 million (representing NIS 0.26 per share). On April 3, 2008 the General Meeting approved payment of the dividend, which was paid on April 28, 2008.

C. On April 17, 2008 the Company's Board of Directors resolved to partially adopt the recommendations of the committee to examine a corporate governance code (Goshen Committee) as described in the Company's immediate report issued on April 18, 2008.

D. On April 17, 2008 the Company's Board of Directors resolved to approve the employment terms of the Chairman of the Board as described in Note 8 to the financial statements. After examining the separate components of the compensation package and the compensation as a whole, the Board of Directors is of the opinion that the compensation package is appropriate and reasonable under the circumstances, and is in line with the nature of the position, the challenges facing the chairman and the expectations of the board of directors. Comparison with peer companies indicate that the compensation package is within the upper range of compensation packages in the peer companies.

E. On March 31, 2008 the net dollar-linked contractual liabilities (including off-balance sheet liabilities) amounted to NIS 1,028 million. In the period between March 31, 2008 and the date of approval of the financial statements, the dollar exchange rate decreased by 5.4%. The Company estimates that the amount of the exposure does not necessitate deviation from the way the Company currently manages exposure to the dollar.

We thank the managers of the Group companies, its employees and the shareholders.

Shlomo Rodav	Avi Gabbay
Chairman of the Board of Directors	**CEO**

"BEZEQ" THE ISRAEL TELECOMMUNICATION CORP. LIMITED

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

AT MARCH 31, 2008

(UNAUDITED)

The information contained in these financial statements constitutes a translation of the financial statements published by the Company. The Hebrew version was submitted by the Company to the relevant authorities pursuant to Israeli law, and represents the binding version and the only one having legal effect. This translation was prepared for convenience purposes only.

Contents

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The Board of Directors of
"Bezeq" - The Israel Telecommunication Corp. Limited

At your request, we have reviewed the condensed consolidated interim balance sheet of "Bezeq" - The Israel Telecommunication Corp. Limited (hereinafter "Company") at March 31, 2008, as well as the condensed consolidated interim statement of income, the condensed statement of recognised income and expense and the condensed consolidated interim statement of cash flows for the three-month period then ended.

Our review was carried out in accordance with procedures prescribed by the Institute of Certified Public Accountants in Israel. The procedures included, inter alia, reading the said financial statements, reading the minutes of meetings of the shareholders and of the Board of Directors and its committees, as well as making inquiries of persons responsible for financial and accounting matters.

Reports of other auditors were furnished to us which relate to investments in associates in which the Company's investments amount to approximately NIS 39 million at March 31, 2008, and the Company's share in the profits in respect thereof amount to approximately NIS 1.6 million for the three-month period then ended.

As the review is limited in scope and does not constitute an audit in accordance with generally accepted auditing standards, we do not express an opinion on the condensed consolidated interim financial statements.

In the course of our review, including reviewing the reports of other auditors as mentioned above, nothing came to our attention which would indicate the necessity of making material changes to the said interim financial statements in order for them to be in conformity with standard IAS 34 – Interim Financial Reporting and in accordance with the provisions of Section 4 of the Securities Regulations (Periodic and Immediate Reports), 5730-1970.

We draw attention to the uncertainties relating to the following matters, for which the maximum possible exposure is significant:

1. The continuing opening of the communications sector to competition, the changes in the communications market, and the effects of regulation on the Group's financial position and operating results, as described in Note 1.

2. Contingent claims made against the Group of which the exposure cannot yet be assessed or calculated, and other contingencies as described in Notes 7B and 7C.

3. The financial position of a subsidiary. As mentioned in Note 6, as of March 31, 2008, the subsidiary meets the financial criteria set for it, following the amended stipulations in respect of 2008 placed upon it by the banks on March 5, 2008, as adapted to the subsidiary's annual budget. The continuation of the activity of the subsidiary is contingent on, *inter alia*, compliance with the conditions set for 2008 and/or further relief which may be received during the year. In the opinion of the management of the subsidiary, the financial resources at its disposal will be sufficient for the requirements of the subsidiary's operations in the coming year, based on the cash flow projections approved by the board of directors of the subsidiary.

Somekh Chaikin
Certified Public Accountants (Isr.)

May 21, 2008

Condensed Consolidated Interim Balance Sheets as at

	March 31, 2008	March 31, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Assets			
Cash and cash equivalents	**1,283**	1,033	1,203
Investments and loans, including derivatives	**317**	851	389
Trade receivables	**2,480**	2,060*	2,403
Other receivables	**245**	296	247
Inventory	**238**	252	203
Broadcasting rights	**271**	200	243
Current tax assets	**28**	12	11
Assets classified as held for sale	**20**	-	17
Total current assets	**4,882**	4,704	4,716
Trade and other receivables	**562**	489*	535
Investments and loans, including derivatives	**227**	326	233
Property, plant and equipment	**5,981**	6,335	6,064
Intangible assets	**2,495**	2,563	2,526
Deferred and other expenses	**376**	366	367
Investments in associates accounted for by the equity method	**39**	32	37
Deferred tax assets	**623**	871	678
Total non-current assets	**10,303**	10,982	10,440
Total assets	**15,185**	15,686	15,156

	March 31, 2008	March 31, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Liabilities			
Loans and borrowings	**1,032**	3,707	1,913
Trade payables	**1,350**	1,467	1,533
Other payables, including derivatives	**866**	873*	745
Current tax liabilities	**33**	68	57
Deferred income	**19**	36	47
Provisions	**388**	302	392
Employee benefits	**621**	844*	705
Total current liabilities	**4,309**	7,297	5,392
Debentures	**4,242**	2,940	4,420
Obligations to banks	**1,125**	435	307
Loans from others	**140**	172	136
Loans provided by the minority in a subsidiary	**389**	578	375
Employee benefits	**262**	360	261
Deferred income and others	**52**	75	36
Provisions	**58**	53	57
Reserve for deferred taxes	**42**	-	-
Total non-current liabilities	**6,310**	4,613	5,592
Total liabilities	**10,619**	11,910	10,984
Shareholders' equity			
Share capital	**6,132**	6,132	6,132
Reserves	**690**	672	681
Deficit	**(1,870)**	(2,450)	(2,268)
Total equity attributable to shareholders of the Company	**4,952**	4,354	4,545
Minority interest	**(386)**	(578)	(373)
Total shareholders' equity	**4,566**	3,776	4,172
Total shareholders' equity and liabilities	**15,185**	15,686	15,156

Shlomo Rodav	**Avi Gabbay**	**Alan Gelman**
Chairman of the Board	CEO	CFO and Deputy CEO

Date of approval of the financial statements: May 21, 2008.

* See Note3C.

The notes to the interim financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Income

	For the three-month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Revenue (Note 10)	**3,100**	3,089	12,400
Costs and expenses			
Depreciation and amortisation	**429**	441	1,769
Salary	**616**	575	2,375
Operating and general expenses (Note 11)	**1,370**	1,423	5,841
Other operating expenses	**21**	8	188
Other operating income	**-**	(15)	(109)
	2,436	2,432	10,064
Operating income	**664**	657	2,336
Financing costs			
Financing expenses	**161**	162	796
Financing income	**(61)**	(104)	(487)
Net financing costs	**100**	58	309
Profit after financing costs	**564**	599	2,027
Equity in profits of investees accounted by the equity method	**1**	-*	6
Profit before income tax	**565**	599	2,033
Income tax	**180**	214	672
Profit for the period	**385**	385	1,361
Attributable to:			
The shareholders of the Company	**398**	399	1,330
Minority interest	**(13)**	(14)	31
Profit for the period	**385**	385	1,361
Earnings per share			
Basic earnings per share (in NIS)	**0.15**	0.15	0.51
Diluted earnings per share (in NIS)	**0.15**	0.15	0.50

* Less than NIS 500,000.

The notes to the consolidated financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Recognised Income and Expense

	For the three-month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Net change in fair value of financial assets classified as available for sale	**-**	-*	4
Net change in fair value of financial assets classified as available for sale transferred to profit and loss	**(5)**	-	-
Actuarial gains from a defined benefit plan (1)	**-**	-	14
Taxes in respect of income and expenses attributable directly to equity	**1**	-*	(4)
Income and expenses recognised directly to equity	**(4)**	-*	14
Profit for the period	**385**	385	1,361
Total recognised income and expense for the period	**381**	385	1,375
Attributable to:			
The shareholders' of the Company	**394**	399	1,344
Minority interest	**(13)**	(14)	31
Total recognised income and expense for the period	**381**	385	1,375

(1) The Group does not re-examine in each interim reporting period its valuations, assumptions and estimates for the purpose of measuring its provisions in respect of employee benefits, unless there are material changes during the interim period. As a result, there are no actuarial earnings or losses recognised in the reporting period.

* Less than NIS 500,000.

The notes to the consolidated financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Cash Flows

	For the three-month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Cash flows from operating activities			
Net earnings for the period	**385**	385	1,361
Adjustments:			
Depreciation	**351**	376	1,482
Amortisation of intangible assets	**68**	60	270
Amortisation of deferred and other charges	**10**	5	17
Gain from decrease in holdings in associates accounted for by the equity method	**-**	-	1
Equity in earnings of associates accounted for by the equity method	**(1)**	(1)	(6)
Net financing costs	**129**	19*	372
Net capital gain	**(1)**	(17)	(88)
Share-based payment transactions	**13**	-	-
Payments to a former senior officer	**-**	-	6
Income tax expenses	**180**	214	672
Receipts (payment) in respect of clearance of derivative financial instruments, net	**(10)**	5	(9)
Change in inventory	**(37)**	(48)	(6)
Change in trade receivables	**(104)**	(13)	(437)
Change in other receivables	**(53)**	(52)	4
Change in trade payables	**73**	56	(18)
Change in suppliers	**(143)**	33	36
Change in provisions	**(4)**	16	105
Change in broadcasting rights	**(28)**	(31)	(74)
Change in employee benefits	**(83)**	(85)	(300)
Change in deferred and other income	**1**	38	(11)
	746	960	3,377
Interest received	**19**	43	116
Dividend received	**-**	-	3
Income tax paid	**(128)**	(138)	(430)
Net cash from operating activities	**637**	865	3,066
Cash flows from investing activities			
Investment in intangible assets and deferred expenses	**(59)**	(63)	(273)
Proceeds from sale of property, plant and equipment and deferred expenses	**61**	23	177
Proceeds from sale of financial assets held for sale, net	**57**	116	647
Purchase of property, plant and equipment	**(307)**	(177)	(973)
Proceeds from sale of investments and long-term loans	**6**	8	66
Purchase of investments and long-term loans	**-**	-	(8)
Investment in associated company	**(1)**	-	-
Net cash used for investment activity	**(243)**	(93)	(364)

* See Note 3C.

The notes to the consolidated financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Cash Flows (Contd.)

	For the three-month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Cash flows from financing activities			
Proceeds from issue of debentures	**-**	-	1,814
Receipt of loans	**-**	-	50
Repayment of debentures	**(229)**	(82)	(1,927)
Repayment of loans	**(40)**	(69)	(840)
Short-term borrowing, net	**12**	(32)	(37)
Dividend paid	**-**	(2,100)	(2,860)
Interest paid	**(56)**	(75)	(389)
Receipt (payment) for clearance of derivative financial instruments, net	**4**	(12)*	77
Net cash used for financing activities	**(309)**	(2,370)	(4,112)
Net increase (decrease) in cash and cash equivalents	**85**	(1,598)	(1,410)
Cash and cash equivalents at the beginning of the period	**1,203**	2,632	2,632
Effect of fluctuations in the rate of exchange on cash balances	**(5)**	(1)	(19)
Cash and cash equivalents at the end of the period	**1,283**	1,033	1,203

* See Note 3C.

The notes to the consolidated financial statements are an integral part thereof.

Appendix to Condensed Consolidated Interim Statements of Cash Flows

	For the three-month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Appendix of non-cash activities			
Purchase of property, plant and equipment and intangible assets on credit	**103**	186	183
Sale of property, plant and equipment on credit	**67**	162	126

The notes to the consolidated financial statements are an integral part thereof.

NOTE 1 – REPORTING ENTITY

A. Bezeq – The Israel Telecommunication Corp. Ltd. ("the Company") is a company registered in Israel whose shares are traded on the Tel Aviv Stock Exchange. The official address of the Company is 132 Menachem Begin Road, Tel Aviv. The condensed consolidated financial statements of the Company comprise those of the Company and its subsidiaries (together referred to as "the Group"), and the Group's interests in associates. The Group is a principal provider of communications services in Israel (see Note 13 – Segment Reporting).

B. On October 11, 2005, control in the Company was transferred from the State to Ap.Sb.Ar. Holdings Ltd. and the Company ceased to be a government company. The Company was declared a monopoly in the main areas in which it operates. An appeal filed by the Company was pending in the Antitrust Court against the non-revocation of its monopoly status in basic telephony; however, at the suggestion of the court (in view of the time elapsed since it was filed), the Company consented to withdraw the appeal. All the segments of operation of the Group are subject to competition. The activities of the Group are, in general, subject to government regulation and control.

C. The Company is subject to various systems of laws that regulate and limit its business operations, including its tariffs. Arrangements pursuant to Sections 15 and 17 of the Communications Law apply to the Company's tariffs. The Company's controlled service tariffs, which are determined in regulations, are updated according to a linkage formula less an efficiency factor, all as set out in the regulations and based on the recommendations of public committees for examination of the Company's tariffs. In March 2008, the Committee for Examination of the Policy and Principles of Competition in Communications in Israel submitted its recommendations to the Minister of Communications. The Minister has not yet adopted any or all of the recommendations.

It is expected that the intensifying competition, together with all the changes in the communications market, will have an adverse effect on the business results of the Group, an effect that the Group is unable to estimate.

NOTE 2 – BASIS OF PRESENTATION

A. The condensed interim consolidated financial statements were prepared in accordance with the standard IAS 34 – Interim Financial Reporting, and in accordance with the provisions of Chapter 4 of the Securities (Periodic and immediate reports) Regulations, 5730-1970.

B. These financial statements do not include all the information required in complete annual financial statements, and should be reviewed in the context of the annual financial statements of the Company and its subsidiaries at December 31, 2007 and at the year then ended, and their accompanying notes ("the annual financial statements"). The Group states in the notes to the interim financial statements only the material changes that have occurred from the date of the most recent annual financial statements until the date of these interim financial statements.

C. The financial statements were approved by the Board of Directors on May 21, 2008.

NOTE 3 – REPORTING PRINCIPLES AND ACCOUNTING POLICIES

The significant accounting policies applied in these condensed financial statements are consistent with those applied in the annual financial statements for the year ended December 31, 2007, except as stated in this Note.

A. Initial application of accounting standards

Commencing January 1, 2008, the following standards and clarifications of financial reporting standards came into effect:

NOTE 3 – REPORTING PRINCIPLES AND ACCOUNTING POLICIES (CONTD).

A. Initial application of accounting standards (contd.)

(1) Interpretation No. 11 of the International Financial Reporting Interpretations Committee, *IFRS 2 – Group and Treasury Share Transactions*. The interpretation requires that a share-based payment in which the entity receives goods and services in consideration of its equity instruments, be treated as a share-based payment settled by equity instruments, irrespective of how the equity instruments were obtained. The interpretation has not significantly affected the results of Group's activities or its financial position.

(2) Interpretation No. 14 of the International Financial Reporting Interpretations Committee, *IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*. The interpretation clarifies when refunds and reductions in future deposits in future contributions in connection with the assets of a defined benefit plan should be considered available, and provides instruction on the effect of minimum funding requirements on those assets. The interpretation also relates to when a minimum funding requirement establishes an obligation. The interpretation has not significantly affected the results of Group's activities or its financial position.

(3) The Group chose early application of IFRS 2 – *Share-Based Payment – Vesting Terms and Cancellations*. The Standard states that the vesting terms are terms which determine whether the group received the services which entitled the other party to share-based payment, and limits the terms of the service and performance. Terms which are not vesting terms will be reflected in the fair value of the grant on the grant date, where after the grant date the Group will not update the fair value in respect of those terms. In addition, the Standard describes the handling of non-compliance with vesting terms. The early application has not significantly affected the results of Group's activities or its financial position.

B. New standards prior to their application

A number of new standards, amendments to existing standards and interpretations are not yet in force at March 31, 2008 and were therefore not applied in the preparation of these consolidated financial statements. Since the publication of the last annual reports, amendments to IAS 32 – *Financial Instruments: Presentation* and IAS 1 – *Presentation of Financial Statements and Commitments Generated in Liquidation* have been published. These amendments require that certain redeemable financial instruments be classified as equity, as well as commitments generated during liquidation, if a number of criteria are met. In addition, appropriate disclosure is required for redeemable instruments classified as equity. The amendments will apply to annual periods commencing January 1, 2009 or thereafter. The amendments are not expected to have a significant influence on the operations and financial position of the Group.

C. Classified amounts

The condensed consolidated interim financial statements include reclassification of certain amounts in comparison numbers to the relevant items.

NOTE 4 – ESTIMATES

The preparation of interim financial statements requires Management to make judgments and use estimates, assessments and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

The significant estimates applied in these interim statements do not differ significantly from those applied in the annual financial statements.

NOTE 5 – RATES OF CHANGES IN THE CONSUMER PRICE INDEX AND FOREIGN CURRENCY EXCHANGE RATES

The changes that occurred in the consumer price index and in the exchange rates of the US dollar and the euro in the reporting period are as follows:

	Consumer Price Index	Rate of exchange of the US dollar	Rate of exchange of the euro
	%	%	%
For the three month period ended on:			
March 31, 2008	**0.1**	**(7.62)**	**(0.74)**
March 31, 2007	(0.23)	(1.66)	(0.54)
For the year ended December 31, 2007	3.40	(8.97)	1.71

NOTE 6 – GROUP ENTITIES

A detailed description of the Group entities appears in Note 33 to the annual financial statements of the Group at December 31, 2007. Below are the material changes that have occurred in connection with Group entities since the publication of the last annual financial statements.

A. D.B.S. Satellite Services (1998) Ltd.

(1) Since commencing operations, DBS has accumulated considerable losses. Its loss in 2007 amounted to approximately NIS 118 million and the loss in the three-month period ended March 31, 2007, amounted to approximately NIS 65 million. As a result of these losses, its capital deficit and its working capital deficit as at March 31, 2008, amounted to approximately NIS 2,695 million and NIS 513 million, respectively.

(2) The Company's investment in DBS (primarily through shareholders' loans) at the balance sheet date amounts to approximately NIS 1,562 million (without interest and linkage). The balance of the current debt of DBS to the Company and its subsidiaries amounts to approximately NIS 166 million, of which approximately NIS 123 million is owed to the Company. The Company has come to an arrangement with DBS for the collection of a debt balance of approximately NIS 55.6 million that was in arrears. Under the arrangement, the debt will be paid in 60 equal monthly instalments plus interest at prime + 1.5%. At the balance sheet date, the remainder of the debt under the arrangement is approximately NIS 39 million, the balance of the debt to the Company beyond the above arrangement is a current debt balance, for which the agreed terms of payment are the normal credit terms in effect between the Company and its customers. At the date of approval of the financial statements, DBS is not complying with the terms of the arrangement and the credit terms noted above. The Company and its subsidiaries are working to collect the debts of DBS which are in arrears.

(3) During 2005, the banks completed the provision of the entire credit facility to which DBS was entitled under the financing agreements.

The terms of the loans and the credit facility that DBS received from the banks, the balance of which at March 31, 2008 is NIS 974 million, impose various restrictions on DBS that include, *inter alia*, restrictions on the encumbrance or sale of certain assets, a restriction on receipt of credit from other banks without prior approval, a restriction concerning repayment of shareholders' loans, and a requirement for compliance with financial criteria ("the Conditions").

a. DBS requested that the banks revise the stipulations for 2008 to adapt them to its budget. On March 5, 2008 the banks' consent to amend the aforementioned stipulations was received.

b. At March 31, 2008, DBS was in compliance with the financial criteria set for it.

NOTE 6 – GROUP ENTITIES (CONTD.)

A. D.B.S. Satellite Services (1998) Ltd. (contd.)

c. The management of DBS believes that the financial resources at its disposal will be sufficient for the requirements of DBS's operations in the coming year, based on the cash flow projections approved by the board of directors of DBS. If additional resources are required for operational needs in the coming year, DBS will adapt its activities so as to preclude the need for additional resources beyond those available to it.

B. Walla Communications Ltd.

On May 13, 2008, the board of directors of Walla Communication Ltd. (“the investee”) proposed the distribution of a dividend to its shareholders in the amount of NIS 30 million of which the Group’s portion is approximately NIS 10 million. Distribution of the dividend is conditional on the approval of the general meeting of the shareholders, in accordance with the investee’s by-laws.

NOTE 7 – CONTINGENT LIABILITIES

A. Claims

During the normal course of business, legal claims have been filed against the companies in the Group, including applications for certification as class action lawsuits.

In the opinion of the managements of the Group's companies, based, *inter alia*, on legal opinions regarding the probability of success of the claims, including the applications for certification of the class action lawsuits, appropriate provisions amounting to approximately NIS 370 million, where provisions are required, were included in the financial statements to cover the exposure resulting from such claims.

In the opinion of the managements of the Group's companies, the additional exposure (beyond the aforementioned provisions) at March 31, 2008, due to claims filed against the companies in the Group on various matters and the probability of realisation of which is probable, amounts to approximately NIS 12.7 billion, of which approximately NIS 3.4 billion relates to salary-related claims filed by groups of employees or individual employees. The above amounts are before the addition of interest.

Concerning applications for certification as class action lawsuits in respect to which the Group has exposure beyond the aforesaid (since the claims do not state a specific amount), see claims in Note 17A(4), (5), (7) and (20) to the financial statements at December 31, 2007.

For a detailed description of these claims, see Note 17A to the Group's annual financial statements at December 31, 2007. Details of the material changes in the status of the significant contingent liabilities of the Group at December 31, 2007, are provided below:

(1) Further to Note 17A(2)(a) to the financial statements at December 31, 2007, concerning a claim filed by 2,343 retirees who were employees who had been transferred from the Ministry of Communications to the Company at the time of its establishment - on February 12, 2008, the plaintiffs filed the summation of their allegations, after having reduced their claim to the incentive pay component and withdrawn their claim relating to grossing up of tax and to clothing.

Furthermore, the claim from January 2007, filed by another 85 retirees, was consolidated with the above claim.

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

A. Claims (contd.)

(2) Further to Note 17A(8) to the financial statements at December 31, 2007, describing a claim and application for certification as a class action alleging unlawful collection by the Company for high-speed internet surfing – on April 7, 2008 the Company filed an application for leave to appeal the decision of the District Court to certify the claim as a class action in respect of the post-contractual stage of the subscription transaction with the Company and to reject the request to file a class action in respect of the pre-contractual stage of the transaction. The Supreme Court ruled that the application for leave to appeal necessitates a response, and instructed the respondents to respond to it. On May 19, 2008 the response was filed.

(3) Further to Note 17A(19) to the financial statements at December 31, 2007, concerning a claim and application for certification as a class action against the Company (which was later removed from the claim), Bezeq International, the chairman of the board of Bezeq International and the then current CEO of Bezeq International, filed in the District Court in November 1997– on April 14, 2008 a hearing was held in which the court proposed that Bezeq International accept a settlement, as explained in the aforementioned Note 17A(19). Bezeq International is now awaiting the ruling of the Supreme Court on the appeal on its merits, i.e. should the decision of the District Court to dismiss the application for certification as a class action be reversed or not.

(4) Further to Note 17A(30) to the financial statements at December 31, 2007, concerning a class action filed against DBS and the cable companies in connection with the broadcasting of commercials during world cup football games – on March 17, 2008 the applicant filed an application for consensual withdrawal without an order to pay costs, giving as their reasons that following the position filed by the Council on September 10, 2007, they had concluded that their claim was unlikely to succeed. On March 18, 2008, the court gave its decision acceding to the applicant's application to withdraw their claim.

(5) Further to Note 17A(32) to the financial statements at December 31, 2007, in connection with claims filed against DBS in the matter of disruptions in broadcasts – on April 13, 2008, DBS filed its response to the application for certification.

(6) Further to Note 17A(1) to the financial statements at December 31, 2007, in connection with the claim and application for certification as a class action, claiming public switching cartels. The process of certification as a class action, valued by the plaintiff at approximately NIS 1.75 billion, is still in its preliminary stages and in April 2008 the plaintiff filed a further request for access to documents and a request to subpoena witnesses. The Company has filed its objection to the plaintiff's request.

B. Claims which cannot yet be assessed or in which the exposure cannot be calculated

For a detailed description of the claims in respect which cannot be assessed or in respect of which the exposure cannot yet be calculated, see Note 17B to the Group's annual financial statements as at December 31, 2007. Details of material changes since December 31, 2007 are provided below:

<u>Claims in respect of which the exposure cannot be recorded</u>

(1) Further to Note 17B(1) to the financial statements at December 31, 2007, in the matter of a claim against the Company and against the Makefet Fund filed by employees who retired from the Company under a retirement agreement from November 2007 – in March 2008 an additional and identical claim was filed in the Tel Aviv District Labour Court by another 17 Company retirees.

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

B. Claims which cannot yet be assessed or in which the exposure cannot be calculated (contd.)

Claims which cannot yet be assessed

(2) In April 2008, three claims were filed against Bezeq International in the Tel Aviv and Petach Tikva District Courts, concerning the use of international phone cards for calling destinations in the Philippines, Thailand and Nepal, together with applications for their certification as class actions.
The plaintiffs have applied for their claims to be certified as class actions by virtue of the Class Actions Law, 5766-2006, in the name of a group that includes every person who, during the seven years prior to filing the claim and during its proceeding, purchased phone cards of the type referred to in the claims. The plaintiffs estimate the loss sustained by all the members of the group at approximately NIS 200 million in the claim of the Filipino citizens; NIS 150 million in the claim of the Thai citizens and NIS 58 million in the claim of the Nepalese citizens.

(3) In April 2008, a claim was filed in the Tel Aviv District Court against Pelephone, together with an application for its certification as a class action in a total amount of approximately NIS 60 million. The claim is for the restitution of amounts which the plaintiffs allege were over-collected from Pelephone's subscribers, and is divided into three causes and three separate groups of plaintiffs.
The first alleges that Pelephone does not enable free calls from any telephone (in any network) to its service center, in ostensible contravention of the provisions of the law. The amount claimed for this cause is NIS 30 million. The second alleges that when making a "continued" call from the voice mail box (i.e. continuation of the call from the voice mail directly to the caller who left the message without disconnecting the call), Pelephone debits for airtime also during the time until the called party (who left the message) answers, which ostensibly contravenes Pelephone's license. The amount claimed for this cause is NIS 10.7 million. The third alleges that when a subscriber who has signed up for a package that includes minutes, dials within that package to 1-800 destinations, the full duration of that call is deducted from the package, despite the fact that calls to 1-800 destinations are supposed to be at a lower tariff. The claim relates to those subscribers who exceeded the minutes package and were debited for calls beyond the package. The amount claimed for this cause is NIS 20 million.

(4) In May 2008, a claim was filed in the Tel Aviv District Court against Pelephone and another defendant, in the amount of NIS 479.5 (the statement of claim is headed "Class Action" but gives no amount claimed on behalf of the group and does not include separate processes of court – "Statement of Claim" and "Application for Certification as a Class Action", as required).
As mentioned the total amount of the claim is not defined. Pelephone is Defendant No. 2, while Defendant No. 1 is the other company. The claim is for restitution of amounts by Defendant 1, which the plaintiff alleges it collected, through Pelephone, from its customer club, for services provided to those customers.
According to the plaintiff, the engagement between Defendant 1 and the members of the customer club, on the basis of which they became members of the club and monies were collected from them, was flawed, and therefore the aforementioned amounts should be refunded.
The specific allegation against Pelephone is that the debit for the services of Defendant 1 is not clearly differentiated in the phone bill that is sent by Pelephone to its customers, ostensibly in contravention of its license.

(5) In May 2008, the Company received a claim and application for certification as a class action, which were filed in the Tel Aviv District Court against Pelephone, Cellcom Israel Ltd. and Partner Communications Ltd. The amount of the class action (against the three companies together) is NIS 50 million. The claim is for restitution of amounts which the plaintiffs allege were over-collected from the defendants' subscribers in the "callback" service (calls made from abroad to Israel which Pelephone calls "Savings Service"). According to the plaintiffs, the defendants, contrary to their licenses, debit their subscribers who use this service for a call from the time the connection (call) is made between the caller and the system through which the service is provided, even if a call to the final addressee with whom the caller wishes to speak, is not actually made. The plaintiffs contend that if no call is actually made to the final addressee, no debit should be made for the service.

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

C. Other contingencies

For a detailed description of other contingencies, see Note 17C to the Group's annual financial statements as at December 31, 2007. Details of material changes since December 31, 2007 are provided below:

(1) Further to Note 17C(1) to the financial statements at December 31, 2007, in the matter of the Antitrust Commissioner's determination that the Company abused its status in the market when it disconnected its network from HOT's network – on March 16, 2008, the Company filed an appeal against the Commissioner's determination.

(2) Further to Note 17C(2)(b) to the financial statements at December 31, 2007, in the matter of a shareholder's letter, pursuant to Section 194 of the Companies Law, on the matter of approval of transfer of funds from the Company to DBS despite the decisions of Ministers of Communications – on April 6, 2008, the shareholder filed an application for leave to file a derivative claim against the Company and a statement of claim against directors who were party to the decision. The Company's applications to the court to file a response to the application for leave to file a derivative claim by July 15, 2008, and to file statements of defence, insofar as necessary, within 60 days of the date of approval of filing the derivative claim, were allowed. It is noted that on March 25, 2008 the Minister of Communications rejected the appeal filed by the Company relating to forfeiture of NIS 10 million of the guarantee, and the guarantee was subsequently rendered forfeit.

(3) Further to Note 17C(6) to the financial statements at December 31, 2007, in connection with a claim filed by the cable companies ("HOT") against DBS – on March 12, 2008, HOT filed a notice in the court requesting that the claim not be struck out or dismissed, and that the court be satisfied with an order to pay costs. The court acceded to HOT's request not to dismiss the claim, and imposed the costs of DBS on HOT. In addition, a pre-trial hearing was scheduled for July 13, 2008.

(4) Further to Note 17C(7) to the financial statements at December 31, 2007, in the matter of the operation of facilities that emit electromagnetic radiation – after termination of the strike at the Ministry for Protection of the Environment, the proceeding for issue of operating permits for communications and broadcasting installations by the Supervisor of radiation is moving forward.
In addition, on April 17, 2008, the Company submitted its reservations concerning the proposed text of National Outline Plan for Communications – NOP/36A Small Broadcasting Installations, and of National Outline Plan for Communications – NOP/36B Large Broadcasting Installations. In brief, the reservations are that the plans as proposed, and in particular as they relate to changing the definitions of small broadcasting installations and large broadcasting installations, create practical difficulties which could prevent the Company from granting the public some of the varied services it provides and which it is obligated to provide.

(5) Further to Note 17C(9) to the financial statements at December 31, 2007, in the matter of an application for certification of a class action against Pelephone in the amount of NIS 12 billion – the claim was struck out without an order to pay costs.

(6) Further to Note 17C(10) to the financial statements at December 31, 2007 – on February 28, 2008 the DBS shareholder applied to the Tel Aviv District Court Company for the appointment of an arbitrator. The Company filed a response to the application in which it explained that there is no cause for the appointment of an arbitrator. On May 4, 2008, the court ruled that in view of the difficulty in understanding the essence of the claim that the shareholder wishes to bring before the arbitrator, she must first file a draft of such a claim in the court.

(7) In February 2008, the Ministry of Industry, Trade and Employment (in this sub-section (7) and in sub-section (8) – "the Ministry"), instituted an investigative proceeding with DBS concerning the terms of employment of a certain group of employees at DBS, and DBS was required to submit various documents to the Ministry, which it did. The investigative proceeding is in its initial stages and its full extent is not yet known.

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

C. Other contingencies (contd.)

(7) (contd.)

Furthermore, in December 2007, DBS received a letter from 19 of its employees (18 of whom are no longer employed by DBS) regarding various periods between 2001 and 2007, in which they allege that during the period of their employment at DBS they were not paid all the monies due to them. On April 21, 2008, DBS sent its reply to those employees, rejecting all their allegations.

At this stage, the extent of the investigation being conducted by the Ministry is unknown, and no action has been filed by the employees.

NOTE 8 – TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES

On April 17, 2008, the Board of Directors of the Company resolved, after having received approval from its Compensation Committee on April 10, 2008 and after having received approval from its Audit Committee on April 15, 2008, to approve the terms of employment of the Chairman of the Board of the Company. Below are the main points of the engagement with the Chairman of the Board:

a. The Chairman is employed under a personal employment agreement as acting Chairman of the Board of Directors of the Company, in a full-time position, effective from September 4, 2007, the date on which the Chairman actually started working in the Company.
b. The salary of the Chairman is NIS 175,000 per month, linked to the CPI. In addition, the Chairman is entitled to contributions to senior employees insurance, study fund and loss of earning capacity insurance. The Company will provide the Chairman with a company car and will bear all the car maintenance expenses.
c. The Chairman will be granted 9,000,000 options, as described in Note 9B below.
d. A decision on the award of an annual bonus will be made at the Board of Directors' discretion and subject to the approval of its Audit Committee and the general meeting. The amount of the annual bonus, if awarded, will be between six and eight monthly salaries.
e. Immediately after the approval of the general meeting of the agreement, the Company will make a special payment to the Chairman, as a "signature bonus", in the amount of NIS 1.2 million.
f. The Company will insure the Chairman with officer-director insurance and will indemnify him from time to time as is customary in respect of other directors in the Company.
g. The engagement between the Company and the Chairman is for an unlimited period, where each party is entitled to bring it to an end for any reason by giving 12 months' notice (the Company) or 6 months' notice (the Chairman).

The engagement with the Chairman of the Board requires also the approval of the General Meeting of the shareholders of the Company, which has been called for June 1, 2008.

NOTE 9 – SHARE-BASED PAYMENTS

A. On November 20, 2007, the Board of Directors of the Company resolved to adopt a new stock options plan for managers and senior employees in the Company and/or in associates, which would allocate up to 65,000,000 non-negotiable options, exercisable for up to 65,000,000 shares of the Company and constituting approximately 2.5% of the issued capital of the Company, and at full dilution – 2.36% of the share capital.

On December 25, 2007, the Company published an outline for the allocation of 41,350,000 options (including to the CEO of the Company) from the plan (of which 40,100,000 have actually been allocated at the date of the financial statements), in accordance with the Securities (Details of an outline offer of securities to employees) Regulations, 5760-2000, which described, *inter alia*, the terms of the plan, and a private placement report in accordance with the Securities (Private placement of securities in a listed company) Regulations, 5760-2000.

NOTE 9 – SHARE-BASED PAYMENTS (CONTD.)

In addition, on March 11, 2008 the Company published an outline for the allocation of an additional 5,600,000 options from the plan (all the options were actually allocated by the date of the financial statements), in accordance with the Securities (Details of an outline offer of securities to employees) Regulations, 5760-2000, which set out, among other things, the terms of the plan.

The options plan and the allocation of all the options in accordance with it, were approved by the General Meeting of the Company on January 31, 2008, in accordance with the Company's Articles of Association. Exercise of the options under the plan is contingent upon receipt of the necessary approvals as prescribed in the provisions of the Communications (Telecommunications and broadcasts) (Determination of an essential service provided by Bezeq, The Israel Telecommunication Corp. Ltd.) Order, 5757-1997 ("the Telecommunications Order"), and such exercise might necessitate amendment of the Telecommunications Order or some other solution. It is noted that on March 30, 2008, a letter was received from the Ministry of Communications dismissing the possibility of amendment of the Telecommunications Order. Nevertheless, the Company will find a solution enabling the allocation of Company shares while complying with the Telecommunications Order.

The options will vest in three equal annual portions. The vesting dates of each portion will fall at the end of each of the first, second and third years after the grant date, respectively, and the expense for each portion will be spread according to its vesting period. In addition, the plan prescribes conditions which, if fulfilled, will bring forward the vesting dates.

The exercise price of each option is NIS 5.50, which reflects a discount of approximately 16.8% on the closing price of the Company's share on the Tel Aviv Stock Exchange on January 31, 2008, the date of the approval by the general meeting.

The theoretical economic value of all the option warrants in the plan, based on a weighted Black and Scholes model, is approximately NIS 170 million, while the theoretical economic value of all the options approved and/or allocated (45,700,000 options), is approximately NIS 118 million, based, *inter alia*, on the share price on the grant date (for options approved and/or allocated) and the share price close to the date of approval of the financial statements (for options not yet approved or allocated), a risk-free annual interest rate of 5.09% - 5.68%, a weighted average of expected duration of between 4.5 and 5.5 years, the exercise price noted above, an annual standard deviation of 22.7% - 24.3% and an annual reduction of 5% in respect of forfeitures. The limitation described above pursuant to the Telecommunications Order was taken into account in calculating the theoretical economic value of the options, on the assumption that the limitation is resolvable. The Company has not yet decided on the exercise price of future option allocations, if any, under the plan. The grant date was set as the later of the date of the general meeting and the date of the notice to the employees.

B. On April 17, 2008, the Board of Directors of the Company resolved to allocate 9,000,000 options to the Chairman of the Board in accordance with the plan described in Section A above, subject to a number of changes relating to the terms of his options. The allocation to the Chairman requires also the approval of the general meeting of the shareholders of he Company, which has been called for June 1, 2008.

The Chairman's options will vest in 12 equal quarterly portions. The vesting dates of each portion will fall at the end of each quarter from the grant date, and the expense will be spread for each portion in accordance with its vesting period. In addition, the plan states terms which, upon their fulfilment, will bring forward the vesting dates.

The exercise price of each option is NIS 6.4405 per share. The price was set according to the share price on the date on which the Chairman commenced office – September 4, 2007 (which was NIS 6.649 per share) and after adjustment for distribution of a net dividend, the X-day of which was April 14, 2008, of NIS 0.26 per share. The closing price of the Company's share on April 14, 2008, immediately after the approval of the Audit Committee, was NIS 6.40 per share.

NOTE 9 – SHARE-BASED PAYMENTS (CONTD.)

The theoretical economic value of the options grated to the Chairman, based on a weighted Black and Scholes model, is approximately NIS 14 million, based, *inter alia*, on the share price on the grant date, an annual risk-free interest rate of 4.73%, a weighted average expected duration of 4 years, the exercise price noted above, and an annual standard deviation of 23.14%, as well as resolution of the limitation described in Section A above pursuant to the Telecommunications Order.

C. The terms of the grants are as shown below (all the options are cleared by way of physical delivery of the shares).

Date of grant / eligible employees	No. of instruments in thousands	Vesting terms	Contractual life of options
A. Grant of options from the State to employees on October 11, 2005	122,698	Immediate (subject to lock-up, commencing at the end of 2 years, to 3 years – one third each year)	4 years
B. Grant of options to employees on February 22, 2007 (1)	78,151	Immediate (subject to lock-up for two years)	5 years
C. Approval and/or grant of options to managers, senior employees and officers up to the date of approval of the financial statements	45,700	Three equal annual portions	8 years
Total stock options granted	246,549		

(1) The expenses in respect of this grant were recorded in 2006 as a promise was made to the employees in 2006, along with the conditions of the grant.

The number and weighted average of the exercise price of the stock options are as follows:

	No. of options (in thousands) March 31, 2008	No. of options (in thousands) March 31, 2007	No. of options (in thousands) 2007
Balance in circulation at January 1	**200,849**	200,849	200,849
Options granted during the period	**45,700**	-	-
Options exercised during the period	**(17,748)**	-	-
Balance in circulation at the end of the period	**228,801**	200,849	200,849
Exercisable at the end of the period	**183,101**	200,849	200,849

After the balance sheet date, approximately 471 thousand options granted by the State to employees on October 11, 2005, were exercised.

The weighted average exercise price in the three-month period ended March 31, 2008 and in 2007 is NIS 3.04 per share and NIS 2.852 per share, respectively.

The average share price in the three-month period ended March 31, 2008 and 2007 is NIS 6.92 per share and NIS 6.82 per share, respectively.

The range of the exercise price of the balance of the issued options at March 31, 2008 is between NIS 2.43 and NIS 5.5, and the weighted average of the remaining contractual life is 3.537 years.

The fair value of the services received in consideration of the options for shares granted, is based on the fair value of the options granted, which was measured according to the Black and Scholes model on the basis of the following parameters:

NOTE 9 – SHARE-BASED PAYMENTS (CONTD.)

The fair value of the options and the discounts

	March 31, 2008	March 31, 2007	December 31, 2007
Weighted average of the fair value on the grant date	**2.84**	-	-
Share price	**NIS 6.61 - 7.049**	-	-
Exercise price	**NIS 5.5**	-	-
Expected volatility (weighted average)	**22.7% - 24.3%**	-	-
Duration of the option (expected weighted average)	**4.5 - 5.5 years**	-	-
Risk-free interest rate (based on Government bonds)	**5.09% - 5.68%**	-	-

Salary expenses

	March 31, 2008	March 31, 2007	2007
	NIS millions	NIS millions	NIS millions
Stock options granted in the reporting period	**13**	–	–

NOTE 10 – REVENUE

	For the three month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Fixed-line domestic communications			
Landline telephony	**915**	986	3,798
Internet – infrastructure	**198**	164	711
Transmission, data communication and others	**229**	230	935
	1,342	1,380	5,444
Cellular telephones			
Cellular services and terminal equipment	**842**	814	3,669
Sale of terminal equipment	**258**	254	711
	1,100	1,068	4,380
International communications, internet services and network end point	**294**	306	1,226
Multi-channel television	**358**	332	1,331
Others	**6**	3	19
	3,100	3,089	12,400

NOTE 11 – OPERATING AND GENERAL EXPENSES

	For the three month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Cellular telephone expenses	**442**	452	1,828
General expenses	**276**	263*	1,187
Materials and spare parts	**217**	220	924
Consumption of satellite services content	**115**	104	426
Services and maintenance by sub-contractors	**84**	102	381
Building maintenance	**78**	82	332
International communication expenses	**68**	93*	338
Motor vehicle maintenance expenses	**46**	46	183
Royalties to the Government of Israel	**32**	48	194
Collection fees	**12**	13	48
	1,370	1,423	5,841

* See Note 3C

NOTE 12 – CONDENSED DATA FROM THE INTERIM SEPARATE FINANCIAL STATEMENTS OF THE COMPANY

A. Income statement

	For the three-month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Income (see B below)	**1,408**	1,442	5,713
Costs and expenses			
Depreciation and amortization	**218**	237	941
Salary	**316**	310	1,293
General and operating expenses	**485**	533	2,121
Other expenses (income), net	**21**	(7)	79
	1,040	1,073	4,434
Operating income for the period	**368**	369	1,279

B. Income segmentation

	For the three-month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Telephony	**933**	1,008	3,905
Internet	**198**	164	712
Transmission and data communications	**192**	183	754
Other services	**85**	87	342
	1,408	1,442	5,713

NOTE 13 – SEGMENT REPORTING

The Company and the investee companies operate in various segments of the communications sector. Data on activities by segment are stated by the segments of operation of these companies.

	For the three-month period ended March 31, 2008 (unaudited)						
	Domestic fixed–line communications	**Cellular telephone**	**International communications and internet services**	**Multi-channel television**	**Others**	**Adjustments**	**Consolidated**
	NIS millions	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**
Revenue							
Revenues from external sources	**1,323**	**1,100**	**294**	**377**	**6**	**-**	**3,100**
Inter-segment revenues	**85**	**73**	**20**	**4**	**13**	**(195)**	**-**
Total revenue	**1,408**	**1,173**	**314**	**381**	**19**	**(195)**	**3,100**
Segment results	**368**	**214**	**55**	**27**	**-**	**-**	**664**

	For the three-month period ended March 31, 2007 (unaudited)						
	Domestic fixed–line communications	**Cellular telephone**	**International communications and internet services**	**Multi-channel television**	**Others**	**Adjustments**	**Consolidated**
	NIS millions	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**
Revenue							
Revenues from external sources	1,362	1,068	306	350	3	-	3,089
Inter-segment revenues	80	80	17	4	11	(192)	-
Total revenue	1,442	1,148	323	354	14	(192)	3,089
Segment results	369	213	51	24	-	-	657

NOTE 13 – SEGMENT REPORTING (CONTD.)

	For the year ended December 31, 2007 (audited)						
	Domestic fixed–line communications	**Cellular telephone**	**International communications and internet services**	**Multi-channel television**	**Others**	**Adjustments**	**Consolidated**
	NIS millions	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**
Revenue							
Revenues from external sources	5,373	4,380	1,226	1,402	19	-	12,400
Inter-segment revenues	340	304	78	12	46	(780)	-
Total revenue	5,713	4,684	1,304	1,414	65	(780)	12,400
Segment results	1,279	804	203	50	-	-	2,336

NOTE 14 – SELECTED CONDENSED DATA FROM THE FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., D.B.S. SATELLITE SERVICES (1998) LTD., AND BEZEQ INTERNATIONAL LTD.

1. Pelephone Communications Ltd.

A. Balance sheet

	March 31, 2008	March 31, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**2,081**	1,614*	1,976
Non-current assets	**2,336**	2,492*	2,363
	4,417	4,106	4,339
Current liabilities	**1,058**	1,171	1,106
Long-term liabilities	**1,112**	1,283	1,154
Total liabilities	**2,170**	2,454	2,260
Shareholders' equity	**2,247**	1,652	2,079
	4,417	4,106	4,339

* See Note 3C

B. Income statement

	For the three month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Income from services and sales	**1,173**	1,147	4,684
Cost of services and sales	**830**	808	3,347
Gross profit	**343**	339	1,337
Sales and marketing expenses	**97**	102	430
General and administrative expenses	**31**	24	102
	128	126	532
Operating income	**215**	213	805
Financing expenses	**26**	21	114
Financing income	**(35)**	(29)	(109)
Financing expenses (income), net	**(9)**	(8)	5
Profit before income tax	**224**	221	800
Income tax	**61**	67	215
Net profit for the period	**163**	154	585

NOTE 14 – SELECTED CONDENSED DATA FROM THE FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., D.B.S. SATELLITE SERVICES (1998) LTD., AND BEZEQ INTERNATIONAL LTD. (CONTD.)

2. D.B.S. Satellite Services (1998) Ltd.

A. Balance sheet

	March 31, 2008	March 31, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**442**	376	400
Non-current assets	**709**	668	700
	1,151	1,044	1,100
Current liabilities	**684**	1,928	1,483
Long-term liabilities	**3,161**	2,025	2,246
Total liabilities	**3,845**	3,953	3,729
Capital deficit	**(2,694)**	(2,909)	(2,629)
	1,151	1,044	1,100

B. Income statement

	For the three month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Income	**381**	354	1,415
Cost of income	**286**	270	1,117
Gross profit	**95**	84	298
Sales and marketing expenses	**39**	35	138
General and administrative expenses	**29**	25	104
	68	60	242
Operating income	**27**	24	56
Financing expenses	**111**	85	394
Financing revenues	**(19)**	(13)	(226)
Financing expenses, net	**92**	72	168
Loss before income tax	**(65)**	(48)	(112)
Income tax	**-***	-*	6
Net loss for the period	**(65)**	(48)	(118)

* Less than NIS 500,000

NOTE 14 – SELECTED CONDENSED DATA FROM THE FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., D.B.S. SATELLITE SERVICES (1998) LTD., AND BEZEQ INTERNATIONAL LTD. (CONTD.)

3. Bezeq International Ltd.

A. Balance sheet

	March 31, 2008	March 31, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**446**	411	431
Non-current assets	**459**	422	456
	905	833	887
Current liabilities	**287**	351	312
Long-term liabilities	**25**	50	26
Total liabilities	**312**	401	338
Shareholders' equity	**593**	432	549
	905	833	887

B. Income statement

	For the three month period ended March 31		For the year ended December 31
	2008	2007	2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Revenue	**314**	323	1,304
Operating expenses	**190**	216	859
Gross profit	**124**	107	445
Sales and marketing expenses	**43**	35	147
General and administrative expenses	**26**	22	94
Other (income) expenses, net	**-****	(1)	-**
	69	56	241
Operating income	**55**	51	204
Financing expenses	**5**	4	13
Financing revenues	**(6)**	(3)	(14)
Financing costs (revenues), net	**(1)**	1	(1)
Equity in earnings of an associate accounted by the equity method	**2**	-**	6
Earnings before income tax	**58**	50	211
Income tax	**16**	14	58
Net profit for the period	**42**	36	153

* The above financial statements are presented in accordance with IFRSs only

** Less than NIS 500,000.

NOTE 15 – MATERIAL EVENTS DURING THE REPORTING PERIOD AND EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

A. On March 10, 2008, the Board of Directors of the Company resolved to recommend to the General Meeting of the shareholders of the Company to distribute a cash dividend to the shareholders in the amount of NIS 679 million (approximately NIS 0.26 per share). On April 3, 2008 the General Meeting approved payment of the dividend and it was paid on April 28, 2008.

B. On March 26, 2008, the Company signed an agreement in the matter of the sale of its satellite communications operation ("Inmarsat" and "Bezeq Sat") and related assets in the same operation, including the satellite communications site in Emek Ha'ela. Under the agreement, the operation will be sold in consideration of approximately USD 15 million plus VAT, subject to adjustments in the price resulting from various stipulations and from changes that occur, if they occur, in the operation in the period up to the date of closing the transaction. The closing of the transaction is subject to various approvals, in addition to the approval of the regulators from the Ministry of Defense, the Ministry of Communications and the Antitrust Commissioner. If the transaction is closed at the maximum price noted above, then the Company expects to record a capital gain, subject to changes in the representative exchange rate of the US dollar, of approximately NIS 47 million (before tax).

C. In May 2008, an amendment to the new collective agreement was signed, in the matter of bringing forward completion of the implementation of the organizational structure and in the matter of bringing forward the dates of retirement and changing the mix of retirees of those who are scheduled to retire, pursuant to the new collective agreement, by the end of 2008.

NOTE 16 – DETAILS OF ADDITIONAL MOVEMENTS IN THE SHAREHOLDERS' EQUITY

	Share capital	Premium on shares	Capital reserve in respect of a transaction between a corporation and a controlling shareholder	Capital reserve in respect of assets available for sale	Capital reserve in respect of options for employees	Balance of deficit	Total	Minority rights	Total shareholders' equity
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
	Refers to shareholders of the Company								
Three-month period ended March 31, 2008									
Balance at January 1, 2008 (audited)	**6,132**	**-**	**390**	**4**	**287**	**(2,268)**	**4,545**	**(373)**	**4,172**
Total earnings (losses) recognized in the period (unaudited)	**-**	**-**	**-**	**(4)**	**-**	**398**	**394**	**(13)**	**381**
Share-based payments (unaudited)	**-**	**-**	**-**	**-**	**13**	**-**	**13**	**-**	**13**
Balance at March 31, 2008 (unaudited)	**6,132**	**-**	**390**	**-**	**300**	**(1,870)**	**4,952**	**(386)**	**4,566**
Three-month period ended March 31, 2007									
Balance at January 1, 2007 (audited)	6,309	1,623	384	1	287	(2,849)	5,755	(564)	5,191
Total earnings (losses) recognized for the period (unaudited)	-	-	-	-*	-	399	399	(14)	385
Dividends to shareholders – distribution that does not pass the earnings test (unaudited)	(177)	(1,623)	-	-	-	-	(1,800)	-	(1,800)
Balance at March 31, 2007 (unaudited)	6,132	-	384	1	287	(2,450)	4,354	(578)	3,776

* Less than NIS 500,000.

NOTE 16 – DETAILS OF ADDITIONAL MOVEMENTS IN THE SHAREHOLDERS' EQUITY (CONTD.)

	Share capital	Premium on shares	Capital reserve in respect of a transaction between a corporation and a controlling shareholder	Capital reserve in respect of assets available for sale	Capital reserve in respect of options for employees	Balance of deficit	Total	Minority rights	Total shareholders' equity
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
	Refers to shareholders of the Company								
Year ended December 31, 2007 (audited)									
Balance at January 1, 2007	6,309	1,623	384	1	287	(2,849)	5,755	(564)	5,191
Total recognized income and expense	-	-	-	3	-	1,341	1,344	31	1,375
Dividends to Company shareholders	-	-	-	-	-	(760)	(760)	-	(760)
Dividends to Company shareholders – distribution that does not pass the earnings test	(177)	(1,623)	-	-	-	-	(1,800)	-	(1,800)
Change in the repayment date of a loan provided by the minority in a subsidiary	-	-	-	-	-	-	-	160	160
Payments to a former senior officer	-	-	6	-	-	-	6	-	6
Balance at December 31, 2007	6,132	-	390	4	287	(2,268)	4,545	(373)	4,172