

Bezeq - The Israel Telecommunication Corp. Ltd.

Compensation Policy for Officers



May 2016

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1.

Definitions

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| Stock Options | - | Phantom Stock Options and Regular Stock Options. |
| Phantom Stock Options | - | A form of virtual options representing a theoretical holding of a certain number of options for Company shares. Phantom stock options grant the recipient the right to receive in cash the benefit component arising from the phantom options, if such benefit arises on the exercise date. On the exercise date, the recipient will receive an amount equal to the difference between the adjusted theoretical exercise price of each option and the share price on that date. |
| Regular Stock Options | - | Stock options that are exercisable for ordinary shares of the Company. |
| Bezeq | - | Bezeq Israel Telecommunication Corp. Ltd. |
| Bezeq International | - | Bezeq International Ltd. |
| Advance Notice | - | Notice given to an employee by the Company prior to his dismissal, and notice given to the Company by an employee prior to his resignation from the Company, in accordance with the provisions of the Advance Notice for Dismissal and Resignation Law, 2001 and/or in accordance with the employee's employment agreement. |
| The Company | - | Bezeq or each of the material subsidiaries, as the case may be. |
| Significant subsidiaries | - | Pelephone, Bezeq International, yes and all other companies controlled by Bezeq where the compensation committee and Bezeq's board of directors determined that it is a significant subsidiary of the group. |
| The Law or the Companies Law | - | The Companies Law, 1999. |
| The CEOs | - | The CEO of Bezeq, CEOs of the material subsidiaries and Senior Group Managers. |
| The VPs | - | Any Officer at Bezeq, as defined in the Companies Law, who is not a director and not a CEO. |
| The Group | - | Bezeq together with its significant subsidiaries. |
| Compensation Committee | - | A committee of the Board of Directors of Bezeq which meets the conditions prescribed in Section 118A of the Companies Law concerning a compensation committee. |
| yes | - | D.B.S. Satellite Services (1998) Ltd. |
| The Compensation Policy or the Policy | - | Compensation policy for Officers of Bezeq in accordance with the provisions and |

		requirements of Amendment 20 to the Companies Law.
The Officers	-	The Officers who are subject to the Compensation Policy pursuant to the provisions of section 4.1 of this document.
The Officers of Bezeq	-	The CEO of Bezeq and the VPs.
Pelephone	-	Pelephone Communications Ltd.
Terms of office and employment	-	As this term is defined in the Companies Law, as may be revised from time to time. At the date of approval of the compensation policy according to this document, the language of the Law is: the terms of office or employment of an officer, including the grant of an exemption, insurance, undertaking to indemnify or indemnification under a permit to indemnify, termination bonus, and any bonus, other payment, or undertaking to make such payment, which are given on account of the said office or employment.
Regulations for compensation of external directors	-	The Companies (Rules Concerning Compensation and Expenses for an External Director) Regulations, 2000.
EBITDA	-	Earnings before interest, taxes, depreciation and amortization.

2. **Purpose of the document**

- 2.1 The purpose of this document is to define and detail the compensation policy for the Officers in the Group who are subject to this Policy as described in section 4.1 below. The Policy addresses the scope and composition of the compensation, and the manner in which it is determined in accordance with the requirements of Amendment 20 to the Companies Law and under any law. The policy relates to the overall compensation for the Company's officers for their work and/or the services they render to the Company and/or the Group, as the case may be.
- 2.2 It is emphasized that this Policy does not grant the Officers any right to receive any compensation as specified in this Compensation Policy by virtue of the adoption of this Compensation Policy. The compensation to which the Officers currently serving in the Group or officers who serve in it in the future will be entitled, will be based on the specific conditions defined for them and approved by the competent organs, subject to the provisions of any law.

3. **Objective of the policy and considerations in its determination**

The objectives of the compensation policy are as follows:

- To help advance the goals of the Company and the Group, work plans, and their long-term view, and to ensure that there is a correlation between the goals of the Company and the Group and the goals of management, and the compensation paid to the Officers.

- To create an appropriate set of incentives for the Officers, taking into account, inter alia, the size of the Group or the Company, the nature of their business activity, their risk management policy, and the goals which it aspires to achieve from time to time.
- To enable the Company and the Group to recruit and retain senior managers with the ability to lead them to long-term business success, to attain their goals and to confront the challenges they face.
- To motivate the Officers to make decisions and show excellent business results, all without deviating from the risk management policy of the Group and of the Company.
- To create an appropriate balance between the various compensation components - fixed and variable, short-term versus long-term, etc.

4. **The Officers**

4.1 The Officers referred to in the Compensation Policy are the CEOs¹ and the VPs at Bezeq.

4.2 The Compensation Policy also addresses the terms of office of directors of Bezeq (Section 9), which for the purposes of this document are not included in the definition of "Officers".

5. **Parameters for reviewing the compensation conditions**

Following are general parameters which are taken into account when reviewing the compensation conditions of the Officers:

- The qualifications, skills, expertise, professional experience and achievements of the officer.
- The position, degree of responsibility, and previous salary agreements signed with the Officer.
- The Officer's contribution to the performance, profit and stability of the Company and/or the Group, as the case may be.
- The degree of responsibility imposed on the Officer in respect of his position in the Company and/or the Group, as the case may be.
- The Company's and/or the Group's need to retain the Officer in view of his skills, knowledge and/or special expertise.
- The size of the Group and/or the Company and the nature of their activity.
- The market conditions, competition and regulatory environment in which the Company and/or the Group operates.
- The reasonability of the compensation mechanisms and scope of the amounts, also in relation to accepted conditions in the market for officers serving in similar positions in similar companies.
- Examination of the ratio of the fixed component to the variable components based on the definitions prescribed as part of the Policy.
- Examination of the ratio between compensation of the Officer to the average and median compensation of the other employees of the Group and/or of the Company (including temporary placement workers). At the time of approval of the Compensation Policy by the Compensation Committee and the Board of Directors of Bezeq, the ratio of

¹ It is clarified that subject to any law, in the event of merger of Bezeq with a material subsidiary, the provisions of the Compensation Policy will continue to apply to the CEO of the material subsidiary, and for the purpose of the Compensation Policy he will continue to be considered CEO of a material subsidiary even if his title in the Group is different.

the average cost of the compensation of the Officers at Bezeq to the average and median cost of wages of the other Bezeq workers (including temporary placement workers), is 7.5 and 8.2, respectively.

6. **Entities involved in setting the Policy**

- The Compensation Committee – makes recommendations to the Board of Directors of Bezeq for a compensation policy for the Officers, and for its renewal/extension and revision from time to time.
- The Board of Directors of Bezeq - sets the compensation policy for the Officers after considering the recommendation of the Compensation Committee, reviews the policy from time to time, and is responsible for revision as necessary.
- The general meeting of the shareholders - approves the compensation policy of Bezeq for the Officers insofar as such approval is required by the Law and with the reservations prescribed in the Law.

7. **Structure of the compensation in the Group - General**

The overall compensation of the Officers comprises several components so that each component compensates the Officer for a different aspect of his contribution to the Company or the Group, as applicable:

7.1 **The fixed component**

7.1.1 **Base salary**²

7.1.1.1 This component is designed to compensate the Officer for performing the ongoing requirements of the position and for the time he invests in decision making and performing the duties imposed on him as part of his position. The base salary reflects the Officer's abilities and skills and incorporates the areas of responsibility and authority within the context of the officer's position.

7.1.1.2 The base salary of the CEO shall not be more than NIS 2.5 million per annum.

7.1.1.3 The base salary of the VPs shall be in the range of NIS 40,000-100,000 per month.

7.1.1.4 The base salary is linked to the CPI and will be revised each year in line with the increase in the CPI. Insofar as the CPI falls in relation to the base index, the salary will not be reduced.

7.1.1.5 It is clarified that a deviation of up to 10% above or below the base salary ranges noted above will not be seen as exceeding or deviating from the Compensation Policy.

7.1.2 **Benefits and social benefits**

7.1.2.1 This component includes social benefits which are in addition to the base salary component, some of which are prescribed by law (e.g. pension savings, provision for severance pay, vacation days, sick pay, convalescence, etc.) and some of which are granted according to accepted practice in the labor market (e.g. education fund savings plan, insurance for work disability, etc.). The benefits and social benefits are designed to maximize the advantages for the Officer and also for the Company and/or the Group themselves, in part through tax benefits which the State offers in respect of these payments, and in an effort to supplement the base salary and compensate the Officer for expenses he incurs while fulfilling his duties (e.g. refund of per diem expenses).

7.1.2.2 Pension insurance - the Company will make provision for contributions to a pension provider or pension arrangement agent, as chosen by the Officer in writing, and in accordance with the provisions of the applicable law in this matter. The provisions will be made from the officer's base salary only and will not include any other compensation

2 The salary amounts specified in the chapter "The base salary" are in gross terms.

components. The Company's provision for pension insurance will be contingent on deducting the appropriate amount for the employee's share of the provisions from the Officer's salary. The Company will insure the Officers for work disability insurance as part of their membership in a pension fund or as an additional policy for the Officers who have managers insurance. Provision for work disability made by the Company shall not be more than 2.5% of the Officer's regular salary.

7.1.2.3 Education fund - every month, the Company will deposit 7.5% of the Officer's base salary in an education fund, and will deduct a further 2.5% from his salary and transfer these amounts to an education fund of the Officer's choice.

7.1.2.4 Company car - the Company will provide its Officers with a company car, or equivalent, for the purpose of performing their duties and for their personal use, according to the Company's accepted practice and in line with its procedures.

7.1.2.5 Other social benefits - additionally, Officers will be entitled to other accepted benefits such as: mobile phone, landline, managers' review, refund of expenses incurred while performing their duties, and subject to individual approval of the Compensation Committee – grossing up of expenses in relation to the benefits and social conditions referred to in this section 7.1.2, and all in accordance with Company practices and in accordance with its procedures, as well as other related social conditions which are accepted for managers.

7.1.2.6 With the approval of the Compensation Committee of Bezeq, the Company may grant additional benefits to Officers at a rate not exceeding 10% of the monthly cost of the fixed component of the relevant Officer's salary (calculated annually).

7.1.3 Severance pay and retirement conditions

7.1.3.1 For incumbent officers (who are not signed on Section 14 of the Severance Pay Law, 1963), the Compensation Committee is entitled, at the recommendation of the Chairman/CEO, as applicable, to approve payment of the full severance pay or part thereof even if the employee resigns (as opposed to being dismissed) or in the event of consensual termination of employment, subject to an individual arrangement made between the Company and the relevant Officer.

7.1.3.2 Officers will not be entitled to retirement bonuses except in extraordinary cases, as described in and subject to section 7.3.3.2 below.

7.1.3.3 For the CEOs, the period of advance notice shall be 6 months³ and for the VPs the advance notice period will be between 3 and 6 months. During the advance notice period, the relevant Officer is required to continue to work in his position, unless the Company actually waives his work.

7.2 **The variable component**

7.2.1 Performance-linked bonus

7.2.1.1 This bonus is designed to compensate the Officer for his achievements and contribution to attaining the goals of the Company or the Group, as applicable, during the period for which the bonus is paid.

7.2.1.2 Structure of the bonus - the performance-linked bonus can have all or some of three components, at the discretion of the Compensation Committee and the Board of Directors of Bezeq, subject to the provisions of section 7.2.1.3 below, for each of the Officers:

- (i) **Component based on the targets of the** - Targets which will apply to the bonus plans for all the Officers in a particular year, where separate targets are

³ Except for an existing agreement with the CEO of yes dated August 28, 2006, according to which he is entitled to advance notice of 12 months from yes or 6 months from the CEO of yes, and the CEO of yes will give yes an additional 3 months advance notice if and insofar as he is requested to do so in a written communication from yes.

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| | Company and the Group | to be defined for the Officers of Bezeq and for CEOs of the material subsidiaries. |
| | (ii) Component based on personal targets | - Targets which correspond to the relevant Officer's position and to the specific subjects and targets that the Company or the Group wishes him to promote in that year. |
| | (iii) Discretionary bonus component | - The Company's officers will be entitled to a bonus component which is not measurable, based on a qualitative evaluation of their performance by their superior. |
- 7.2.1.3 The Compensation Committee and the Board of Directors of Bezeq may delegate their authority for the matter of determining the composition of the bonus, so that for the VPs the structure of the bonus will be decided by the CEO of Bezeq, subject to the approval of the Chairman of Bezeq, and for the CEOs of the material subsidiaries the structure of the bonus will be decided by the Compensation Committee alone.
- 7.2.1.4 As a rule, eligibility for a performance-linked bonus for any year will be contingent upon the Officer being an employee of the Company or of the Group, as the case may be, at the end of the relevant year. If the Officer is not an employee of the Company or of the Group at the end of the relevant year, the Officer will be entitled to a proportionate part of the performance-linked bonus for that year unless the Compensation Committee decides otherwise, and the bonus amount will be paid to him close to the date of termination of office or on the date of approval of the bonuses for all the Officers, as decided by the Compensation Committee. In special cases, the Compensation Committee and the Board of Directors of Bezeq may, after receipt of a recommendation from the CEO or the Chairman of the Board, as applicable, approve bringing forward payment on account of the bonus that is payable to an Officer, provided that the on-account payment does not exceed 50% of the maximum annual bonus to which that Officer might be entitled (subject to the provisions of section 7.2.1.6.2 below). For the sake of caution, it is clarified that if at the end of that year it is decided that the Officer is not entitled to a bonus or is entitled to a bonus that is less than the on-account payment, the Company will demand that the Officer pay back the advance that was paid to him as aforesaid.
- 7.2.1.5 The total amount of all bonuses for all the Officers shall not exceed 1% of the group EBITDA of the financial year for which the performance-based bonuses were given. Without derogating from the foregoing, the total bonus amount actually distributed each year will be calculated according to the extent of attainment of the targets set out above.
- 7.2.1.6 Eligibility for a performance-linked bonus will be decided on the basis of measurable quantitative criteria and/or non-measurable qualitative criteria, subject to the aforesaid in this section 7.2. The targets and weightings for the bonus will be decided upon by the competent organs in the Group as described in sections 7.2.1.2 and 7.2.1.3 above, each year in advance, by no later than the end of February of that year, and will be structured individually and separately for each of the Officers in the manner described below:
- 7.2.1.6.1 The weighting of the component based on targets of the Company and the Group (component (i) above) will be up to 60% of all the targets of each Officer, where up to 20% of all the targets will be Group targets. The weighting of the component based on personal targets (component (ii) above) will be up to 50% of all the targets of each Officer. This section does not apply to the CEO of Bezeq, for whom the targets and weightings each year will be as described in section 2.1.6.3 below.
- 7.2.1.6.2 As part of the target of the Company and the Group (component (i) above), the EBITDA target and/or the cash flow target of the Company or the Group will be the largest or most

heavily weighted of all the targets of the Company/Group. The weighting of the EBITDA target and/or the cash flow target for each Officer will be determined in relation to his position in the Company or the Group, as the case may be.

The EBITDA target will be a long-term target and the bonus for this target will be paid over two years, so that the officer must meet the EBITDA target set for him over a two-year period to entitle him to his full annual bonus.⁴ If the officer works in one particular year and meets the EBITDA target, but his term of office terminates before completing the subsequent year of work, or alternatively he moves to another position within the Group before or during the subsequent year - in this case the Group's Compensation Committee will, at its discretion, determine whether the officer is entitled to the performance-linked bonus or part thereof, on the date of termination/change of position, taking note, inter alia, of the forecasts for the subsequent year (insofar as is relevant).

7.2.1.6.3 The targets and weightings defined by the competent organs in the Group as described in sections 7.2.1.2 and 7.2.1.3 above, for the CEO of Bezeq for the performance-linked bonus in any year, will be from the list of targets and in accordance with the range of the weightings noted, as follows: (a) the EBITDA target for Bezeq (separate) will be weighted at up to 30% of the bonus calculated annually; (b) the free cash flow (FCF) target for Bezeq (separate) will be weighted at up to 30% of the annual bonus; (c) the after-tax profit target for Bezeq (separate) will be weighted at up to 20% in the calculation of the annual bonus; (d) the operating profit target for Bezeq (separate) will be weighted at up to 20% in the calculation of the annual bonus; (e) a Group target based on one of the parameters (a) to (c) above, to be decided on by the Compensation Committee and the Board of Directors of Bezeq, will be weighted at up to 30% of the annual bonus. In addition, there will be a Chairman of the Board's assessment target set for the CEO of Bezeq, which will consider the performance of the CEO and will be weighted at up to 25% of the annual bonus or three monthly salaries, whichever is the higher.

7.2.1.6.4 Regarding the threshold conditions for receipt of the annual performance-linked bonus for the CEOs, the Compensation Committee and the Board of Directors of Bezeq will determine, immediately after approval of the budget for the calendar year, one of the following alternatives: For the CEO of Bezeq and the CEO of Bezeq International, one of the following two alternatives: (1) the FFO⁵ results of Bezeq and/or of Bezeq International (as the case may be) in a calendar year have not declined more than 20% from the FFO results of Bezeq and/or of Bezeq International, as the case may be, in the year preceding the year for which the bonus is paid (the "Comparison Alternative"), or (2) the FFO results of Bezeq and/or of Bezeq International (as the case may be) in a calendar year have not declined more than 20% from the target set in the budget of Bezeq and/or of Bezeq International, as the case may be (the "Budget Alternative"). For the CEO of Pelephone and the CEO of yes, one of the following two alternatives: (1) the EBITDA result of Pelephone and/or of yes (as the case may be) in a calendar year has not declined more than 40% from the EBITDA of Pelephone and/or of yes, as the case may be, in the year preceding the year for which the bonus is paid (the "EBITDA Comparison Alternative"), or (2) the FFO results of Pelephone and/or of yes (as the case may be) in the calendar year have not declined more than 25% from the target set in the budget of Pelephone and/or of yes, as the case may be, for that year (the "Budget Alternative").

If any of the above fails to meet the FFO or EBITDA target as described above and as the case may be, he will not be entitled to the performance-linked bonus that year even if he

4 If the officer meets the target in one year but fails to meet the target in the subsequent year, he will be entitled to a partial bonus for the year in which he met the target.

5 (FFO) Funds from Operation - cash flow from operations before changes in working capital and before changes in other asset and liabilities items. This target may be subject to adjustments for events detailed in section 7.2.1.14 of the compensation policy.

meets the other targets for the annual performance-linked bonus. If the EBITDA Comparison Alternative is chosen when considering the CEO of Pelephone and the CEO of yes, Bezeq will publish the EBITDA data of Pelephone and/or yes (as the case may be) in its financial statements for the financial statements year, and if the Comparison Alternative is chosen when considering the CEO of Bezeq and the CEO of Bezeq International, Bezeq will publish the FFO data of Bezeq and of Bezeq International (as the case may be) for that year. If the Budget Alternative is chosen with regard to each of the aforementioned CEOs, Bezeq will publish in its financial statements the FFO targets of the relevant company, for the year following the reporting year. It is clarified that the budget targets are set at the beginning of every year, after discussion of the estimates and forecasts which form the basis for the budget, as they are on the date of determining the budget, and the budgets of Bezeq International, of Pelephone and of yes are approved first by the Board of Directors of the relevant company, and thereafter they are presented for approval by the Board of Directors of Bezeq.

In addition, Bezeq will publish, as part of its Periodic Report, the rate of compliance of each Officer for whom disclosure was made in the Additional Details chapter in Bezeq's Periodic Report, with all the bonus targets defined for each of them with regard to that calendar year.

7.2.1.6.5 The following rules will be used to set the targets and to ascertain whether they have been met:

- a. Each target will be given a relative weighting which determines its importance and its weight in the total weight of the bonus budget.
- b. A quantitative target bar will be set for each measurable target, to be derived from the work plan (budget) or directly from the area which requires change or improvement (excluding a Chairman/CEO assessment target).
- c. When the target is a parameter that is included in or derived from the budget, then the target will be considered to have been met in full only if the quantitative target bar set in or derived from the budget is met.
- d. Each target will receive a separate score indicating compliance with the target and the relevant bonus will be computed pro rata to its relative weight.
- e. A lower quantitative bar will also be set for each target. If performance is below the lower bar, no bonus will be paid for the specific target.
- f. A bonus of 60% of the specific target weight will be given for reaching the quantitative bar defined as the lower bar, and for performance above this level a bonus of between 60% and 100% will be given, to be calculated on a linear basis (in relation to the difference between the target and the lower bar). If the target is met, a score of 100% will be given for this index.
- g. An upper bar will be set for each target for performance which surpasses the target. For reaching the upper bar or above, a bonus of 125% of the specific target weight will be given, and for performance between the target and the upper bar, a bonus of between 100% and 125% will be given, to be calculated on a linear basis (in relation to the difference between the target and the upper bar).

7.2.1.7 The maximum performance-linked bonus for the CEO and the CEOs of the significant subsidiaries will be limited to up to 100% of their annual base salary (assuming that targets are met 100%), with an option of up to 125% of the annual salary in the case of outstanding performance, as described in Section 7.2.1.6.5 (g) above, and for the VPs the maximum performance-linked bonus will be limited to up to 50% of the annual salary (assuming that targets are met 100%) and in the case of outstanding performance, up to 62.5%.

7.2.1.8 It is clarified that deviation of up to 10% above or below the ranges of the performance-based bonus noted above will not be seen as a deviation from the Compensation Policy.

7.2.1.9 "Elimination" of uncertain events

The Compensation Committee and the Board of Directors of Bezeq may "eliminate" from the calculation of performance for the purpose of the bonus, implications for the financial results of the relevant company and/or the Group, that will stem from accounting changes, taxation changes, business changes, regulatory changes or material failures, provided that their impact was not taken into account in the Company's budget., insofar as such changes occur, as described below:

Accounting changes: Changes in the accounting standards during the year or in the interpretation of the accounting bodies or the Securities Authority concerning how they are applied, early adoption of accounting standards, change in application of an accounting policy, change in an accounting classification, change in a material estimate, an event necessitating restatement of comparison numbers of prior years or prior quarters and which has a material implication for the results of the reporting period, and the like ("Accounting Changes").

The elimination of Accounting Changes will be made close to the time of approving the bonuses, when the external auditors of the relevant company submits its opinion detailing the Accounting Changes that were made during the financial year applicable to the bonus, and the repercussions of those changes on the relevant targets with regard to granting the bonuses. The opinion must be submitted to the Compensation Committee, and will serve as a basis for its decision on whether to eliminate repercussions of the Accounting Changes when calculating the bonuses of the Officers

Taxation changes: Changes in tax rates, changes in legislation, regulations, or in the position of the tax authorities in Israel, or an arrangement or ruling with the tax authorities, following which material changes occurred in the tax expenses or tax payments, changes in the tax expense or tax payments in respect of prior years, whether owing to an agreement or an order, etc.

Regulatory changes: New regulation or material changes in existing regulation (whether in laws, secondary legislation, decisions of judicial instances, or service portfolios) which have a material effect on the results of the Company/Group in the reporting period in areas of competition and antitrust, the tariffs, the relations between Bezeq Group and its competitors (including in the wholesale market), cooperation between the companies of the Group, the licensing and ordering of the areas of operation of the Company/Group, the activities of Bezeq as a public company, etc.

Material failures: system-wide malfunction or material failure having a total or ongoing impact on the Company/Group (including owing to cyber attack), force majeure events or an general emergency situation that have a material effect on the results of the Company/Group in the reporting period, etc.

Elimination of the implications of such events can increase or decrease the bonus, depending on the nature and impact of the event.

In the event that the aforementioned uncertain events will be eliminated in the calculation of the bonus to officers, Bezeq will provide such disclosure in the chapter for other details in its periodic report.

7.2.1.10 **Discretionary bonus component**

7.2.1.10.1 Notwithstanding provisions elsewhere in this section 7.2.1, the Compensation Committee and the Board of Directors of Bezeq may determine, with regard to the VPs, that some or all of the variable components of those Officers will be granted on the basis of non-measurable qualitative criteria as described in section 7.2,1.10.3 below, including to

determine a bonus structure that differs from the structure described in this section 7.2.1, all subject to the Total Bonus Ceiling as defined in section 7.4 below. It is clarified that those organs may increase, for the relevant Officer, at the time of calculating the bonuses, the discretionary component and may even determine that it will be the only component for calculation of the bonus. For the discretionary component of the CEO of Bezeq, the provisions of section 7.2.1.6.3 above will apply.

7.2.1.10.2 The discretionary component of the bonus for the CEOs will be decided according to the assessment of the Chairman of the Board of Bezeq, while the discretionary component of the bonus for the VPs will be decided according to the assessment of the CEO of Bezeq, all subject to the approval of the Compensation Committee and the Board of Directors of Bezeq.

7.2.1.10.3 The discretionary component will be based on "qualitative" criteria such as the contribution of the Officer to the business of the Company and/or the Group, its profits, its strength and stability; the need of the Company and/or Group to retain an Officer because of his special skills, knowledge or expertise; the measure of responsibility imposed on the Officer; changes that have occurred in the responsibility of the Officer during the year; satisfaction from the functioning of the Officer (including assessment of the extent to which the Officer demonstrates involvement and concern in fulfilling his function); assessment of the Officer's ability to work in cooperation and coordination with the team; the Officer's contribution to corporate governance and an appropriate control and ethical environment, and the like.

7.2.1.10 **Authority to reduce the bonus**

The Compensation Committee and Board of Directors of Bezeq may, at their discretion, reduce the amount of the bonus to which the Officer is entitled, when there are extraordinary circumstances which justify such a reduction.

7.2.1.11 **"Clawback" - return of compensation given on the basis of erroneous financial information**

The Officer will be required to return to the Company any surplus amounts he was paid as part of the terms of his employment, if they were paid on the basis of information which later emerged as erroneous and were restated in the Group's financial statements, provided that no more than three years have elapsed since the date of the financial statement on which the surplus payments were based. The amount of the surplus payments will be determined as the difference between the amount received by the Officer and the amount he would have received according to the corrected financial data which were restated in the financial statements. The Company is entitled to offset such amount owed to it from any amount it payable to the Officer (even if his employment has ended).

7.2.2 Equity-based compensation

7.2.2.1 This compensation is intended to link raised value for the shareholders as reflected in a rise in the value of Bezeq's shares over time, with the compensation paid to the Officers. It creates a convergence of interests between the officers and the shareholders, and assists in generating the motivation and retention of key office-holders in the Company and in the Group.

7.2.2.2 The Compensation Committee and the Board of Directors of Bezeq may adopt an equity-based compensation plan for the Officers (the "Plan").

7.2.2.3 The approved Plan will incorporate the following principles:

7.2.2.3.1 The securities allotted as part of the Plan will be Phantom Stock Options and/or Regular Stock Options, and the grant of one type only of those types of equity-based compensation will be permitted in any calendar year.

- 7.2.2.3.2 The holding or vesting period for the options will, as a rule, be in the range of 3-5 years (the "Vesting Period"). This Vesting Period is designed to constitute a long-term healthy and worthy incentive. In the event of a change of control at Bezeq, a merger or reorganization ("Acceleration Event"), the Compensation Committee may accelerate the Vesting Period of the portion of the options whose vesting date is nearest to the Accelerating Event. For example, if an Accelerating Event occurred during the second Vesting period of the Plan, then subject to the approval of the Compensation Committee the second portion of the portions of options allotted to the offeree will vest (in addition to the vesting of the first portion, which has already occurred).
- 7.2.2.3.3 The exercise price of the options, for calculating the benefit component, will be determined according to the average closing prices of the Bezeq share in the 30 trading days prior to the date of approval of allotment of the options by the Board of Directors of Bezeq or the General Meeting (if required), whichever is the later, plus 5%, or according to the closing price of the Bezeq share on the stock exchange at the close of trading on the day prior to the date of Bezeq's decision to grant the options, whichever is the higher. The exercise price will be subject to the adjustment provisions prescribed in the stock options Plan (as the Plan is worded from time to time) or in the letter of allotment.
- 7.2.2.3.4 Grant of the options under the Plan is subject to the following limitations:
- The value of a packet of options that is not cleared in cash per year (according to the B&S formula) on the grant date should not exceed the following percentages out of the maximum total annual salary (base salary + maximum bonus) to which the officer is entitled in the grant year, and these are the percentages:
 - ◊ For the CEOs – 55%.
 - ◊ For the VPs – 35%.
 - A ceiling for cash-cleared options – on the exercise date: The maximum cash amount an officer can receive for exercise of all the cash-cleared options granted to him under the Plan shall not exceed the product of the maximum annual salary (base salary + maximum bonus) to which that officer is entitled in the grant year, multiplied by the number of years of the entire Vesting Period prescribed in the Plan.
- 7.2.2.3.5 In a year in which a grant of one of the types of equity-based options is approved for an Officer, a bonus of the special types described in section 7.2.3 below will not be approved for that Officer unless the ratio of the fixed component to all the variable components, for that Officer, does not deviate, that year, from the ratios set for this matter in section 7.4 below (the value of the equity-based compensation for each year will be equal, for this matter, to the value of the full equity-based bonus as calculated on the grant date for the purpose of the financial statements, when divided by the number of years from the grant date of the equity-based compensation to the vesting date of the final portion).
- 7.2.2.3.6 Total maximum dilution in a case of grant of Regular Stock Options shall not exceed 10% of the issued and paid up capital of Bezeq.
- 7.2.2.3.7 The expiration date of the options shall not be earlier than one year from the vesting date and not later than 10 years from the allotment date.
- 7.2.2.3.8 The Plan should include terms for cases of the Officer leaving in various circumstances (moving between companies in the Group, termination, resignation, death or disability).

7.2.2.3.9 The Plan should prescribe conditions for adjustment of the exercise price in the event of a distribution, rights issue, etc.

7.2.3 **Special bonuses**

7.2.3.1 In addition to everything stated in this section 7.2, the Compensation Committee and the Board of Directors of Bezeq may award to any of the Officers a special bonus in an amount not exceeding 4 monthly salaries (gross) of the Officer, provided that the total amount of the Special Bonus granted to the officer throughout the entire compensation policy period does not exceed 12 monthly salaries (gross) of that officer. The special bonus will be awarded in special and unusual cases that meet the following criteria: accomplishment of a project that was not included in the work plan of the Company/Group (as the case may be); investment of exceptional and extraordinary effort in promoting and implementing a project of the Company/Group (as the case may be); in a case of a spot need to recruit personnel; in a case of retirement after at least 5 years of employment, and subject to review by the Compensation Committee and the Board of Directors of Bezeq of the terms of office and employment of the Officer during the period of his employment, of the performance of the Company/Group (as the case may be) in that period and the contribution of the Officer to achieving the targets of the Company/Group (as the case may be) and to increasing its profits (as the case may be) and the circumstances of the retirement; retirement owing to illness or in exceptional personal circumstances.

In any case of award of a special bonus to an Officer concerning whom a disclosure was made as part of the Additional Details chapter in the Periodic Report of Bezeq, Bezeq will publish in that report the criteria and reasons behind the decision to award the special bonus to that Officer.

7.2.3.2 Retirement bonus

The Compensation Committee and the Board of Directors of Bezeq may decide on grant of a retirement bonus for an Officer, as part of this employment agreement or alternatively at the time of his retirement, which shall not exceed 6 monthly base salaries (not including social benefits). Grant of a retirement bonus can be decided retroactively only if the Officer worked for at least 3 years in the Company or in the Group. In making its decision, the Compensation Committee and the Board of Directors of Bezeq will consider the contribution of the Officer to the Company and/or the Group, as the case may be, during the period of his employment, the performance of the Company and/or the Group, as the case may be, during his term of office and the extent to which the Officer contributed to them, and the circumstances of his retirement.

7.2.3.3 The Compensation Committee and the Board of Directors of Bezeq may, subject to the terms set out below and in special cases or in cases such as change of control at Bezeq or expected structural changes in the Group and the like, approve payment of a "retention bonus" to an Officer, the purpose of which is to enable the Group to compensate successful Officers for their undertaking to continue working in the Group companies. Payment of the retention bonus is subject to the following conditions:

(a) The retention bonus will not exceed 50% of the total annual salary (calculated according to the base salary at the time of the decision on the retention bonus) + the maximum performance-linked bonus, excluding any equity-based compensation as described in section 7.2.2 above) of the Officer.

(b) The Officer must undertake, against payment of the retention bonus, to continue to work in the Company or in the Group, as the case may be, for at least one year commencing on the date of payment of the retention bonus.

7.3 **Benchmark analysis (analysis in relation to the market)**

To ensure congruence between all the compensation components listed above, when Bezeq's organs come to discuss approval of each of the compensation components for an Officer, all components of the compensation package of the Officer will be presented to them. Additionally, the salary ranges and the other terms of office and employment prescribed in the Compensation Policy were decided, in part, in comparison with the market and with similar positions in similar companies. Such a review also gave weight to the Bezeq's performance, comparing its performance with that of comparable companies who appear in a benchmark analysis, with respect to pre-determined parameters. To this end, figures for salaries paid in large communications and hi-tech companies and in comparison with the large companies in the economy were examined. The benchmark analysis prepared by Professor Moshe Zviran is attached as an appendix to this Compensation Policy.

7.4 **Ratio of the fixed component to the variable components**

When approving the compensation targets for the Officers, the Compensation Committee and Board of Directors of Bezeq examined the ratio of the all the fixed components to all the variable components of the personal compensation plan for the relevant Officer, as noted in the rules set in this Policy. The purpose of this examination is to find an appropriate balance between the fixed and variable components. Appropriate balance means that the incentive given to the Officer is consistent with the interests of the Group in maximizing its long-term goals.

The desired ratio range⁶ in percentage terms, between components of the overall compensation package for the Officers, should be as shown in the following table:

Rank	Fixed component*	Variable components**
CEOs	20%-50%	50%-80%
VPs	30%-65%	35%-70%

* Base salary, benefits and social benefits, as described in section 7.1 above.⁷

** Performance-linked bonus, equity-based compensation (depending on value, as described in section 7.2.2.3.5 above) and the special bonuses described in section 7.2 above. It is clarified that the ceilings noted in section 7.2 above for these components are cumulative (together: "Total Bonus Ceiling"), with attention to the maximum ratio possible shown in the above table and subject to any law.

7.4.2 It is clarified that a deviation of up to 10% above or below the rates specified in the above ranges will not be deemed a deviation from the Compensation Policy.

8. **Additional terms of office and employment**

In addition to the compensation described above in Section 7, the Officers and directors at Bezeq will be entitled to professional liability insurance, indemnification and exemption in accordance with the conditions set out below.

⁶ It is emphasized that this refers to the possible ratio range only, based on the present fixed components of the Officers and assuming receipt of all possible variable components in the Compensation Policy. It is emphasized that the actual ratio, in any given year, will be determined on the basis of the relevant variable compensation components for that Officer at that time, on the special circumstances for that year and on the various conditions for receipt of each of the components of the variable compensation.

⁷ Under this component, sick days and vacation days to which the Officer is entitled as part of social benefits, were not calculated. In granting vacation and sick days, the Company acts in accordance with market standards and the provisions of the law.

8.1 Insurance

Bezeq will enter into agreements from time to time with an insurance company/ies to provide Directors and Officers liability insurance (D&O) for its directors and other Officers, as may be from time to time. Bezeq will also be able to include other directors and Officers in its subsidiaries in these policies. The limit of liability in the insurance policies shall be between USD 100 to USD 250 million per claim and in aggregate for each insurance year, and an additional USD 20 million for legal expenses. The amount of the annual premium to be paid by the Company shall not be more than USD ~~500,000~~ 1 million with a deductible of up to USD 1 million.

8.2 Indemnification

Bezeq will provide its Officers and directors with letters of indemnity with an undertaking for indemnification in respect of any liability or expense imposed on any of the Officers or the directors, resulting from their ex-officio activities as Officers (including activities in Bezeq's subsidiaries), and all subject to the provisions of the law. The amounts of indemnity that Bezeq will undertake to pay, cumulatively, to all its Officers and directors is limited to a ceiling of 25% of the equity of Bezeq as at the time of giving the indemnification. The undertaking for indemnification will not apply to an event for which the insurance company recognizes its liability according to the insurance policy and has paid the Officer the required amount. The letter of indemnity will apply to a list of categories of events which are accepted in letters of indemnity for companies with specifications similar to those of Bezeq.

8.3 Exemption

Bezeq may grant its Officers and directors exemption, in advance, from liability for breach of the duty of care towards it, pursuant to any law, including Officers who are a controlling shareholder or his relatives, subject to receipt of the legally required approvals. Such exemption shall not apply to a decision or transaction in which the controlling shareholder or any Officer (including another Officer who is not the Officer to whom the exemption is granted) has a personal interest, and all subject to the provisions of the Companies Law and the Articles of Association of Bezeq.

9. Directors' fees

The compensation for external and independent directors of Bezeq will be the prescribed maximum permitted amounts and limitations for an external director according to the Compensation for External Directors Regulations, as they may be from time to time, and will be uniform for all those directors. An employee-director shall not be entitled to additional compensation for his service as a director, beyond the salary paid to him as an employee of Bezeq.

Directors will be entitled only to compensation for which their entitlement is specifically noted in this document, and all the other Policy provisions will not apply to them.

Furthermore, the directors will be entitled to a reimbursement of travel expenses and they will be included in Bezeq's D&O insurance and letters of indemnity and exemption which were or will be given during this period, as noted in Section 8.1 above.

10. Existing arrangements

The Compensation Policy makes no attempt to make any adverse change in existing agreements between the Company and its employees, and the Company will uphold the present arrangements which are in force on the date of approval of this Compensation Policy, for as long as such agreements remain in force.

11. **Rules of control, reporting and correction of irregularities**
- 11.1 Bezeq will operate subject to any existing and future provisions of law concerning the Compensation Policy for Officers of the Company.
- 11.2 Any deviation from the Compensation Policy laid down in this document or from the principles therein must be approved by the Compensation Committee and Board of Directors of Bezeq, or in another manner which is consistent with the requirements of the Companies Law. However, non-material changes in the terms of office and employment of the CEOs require prior approval of the Compensation Committee only, if it has confirmed that the change in the terms of employment is not material. Non-material changes in the terms of office and employment of VPs will be approved by the CEO of Bezeq and the Chairman of the Board of Bezeq, and the Compensation Committee will be advised accordingly, all within the limits set in the Compensation Policy. To this end, it is determined that all non-material changes in the terms of office and employment of an Officer which are approved by those organs in any reporting year, shall not exceed 5% (in real terms) in relation to all the terms of office and employment of an Officer which were approved by the competent organs of the Group for that reporting year.
- 11.3 At least once a year, before the date of grant of the annual bonus to the Officers, the CEO or whoever acts on his behalf shall submit a report to the Compensation Committee and the Board of Directors of Bezeq on the compensation given to the VPs, which addresses the outline of the compensation determined for that VP, the targets he met or the extent to which he met them, and computation of the amounts. The Chairman of the Board will submit a similar report to the Compensation Committee and the Board of Directors of Bezeq on the CEOs of the relevant companies.
- 11.4 The VP Human Resources and CFO of the Group must ascertain that the payment of compensation to the Officers is consistent with the instructions set out in this document.
- 11.5 At least once in three years, the internal auditor of Bezeq will prepare a designated report on the Bezeq's compliance with the Compensation Policy, as decided by the Board of Directors of Bezeq. The internal auditor's report on implementation of the Compensation Policy will be submitted as required by the Companies Law (to the Chairman of the Board, the CEO and the Chairman of the Audit Committee of Bezeq). If it is found that Bezeq has deviated from the Compensation Policy approved by the Compensation Committee and Board of Directors of Bezeq, the internal auditor's report will be submitted for immediate discussion by the Compensation Committee and Board of Directors of Bezeq.

The above information constitutes a translation of the Compensation Policy 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.