

August 28, 2019

# **“Bezeq” - The Israel Telecommunication Corp. Ltd.**

## **Quarterly report for period ended June 30, 2019**

Update to Chapter A (Description of Company Operations) of the Periodic Report for 2018

Directors' Report on the State of the Company's Affairs for the period ended June 30, 2019

Interim Financial Statements as at June 30, 2019

Quarterly report on the effectiveness of internal control over financial reporting and disclosure for the period ended June 30, 2019



## Update to Chapter A (Description of Company Operations) of the Periodic Report for 2018



The information contained in this report constitutes a translation of the report 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.

**Update to Chapter A (Description of Company Operations) <sup>1</sup>  
to the Periodic Report for 2018 ("Periodic Report")  
of "Bezeq" - The Israel Telecommunication Corporation Ltd. ("the Company")**

**1. General development of the Group's business**

**Section 1.1 - Group activities and business development**

**Section 1.1.2 - Control of the Company**

On proposals to purchase shares of Internet Gold and B Communications (BCOM) - based on the reports of these companies, in April and May 2019, two proposals were received from Searchlight Group and Zeevi Group for the purchase of shares of BCOM. Subsequently, on August 8, 2019, BCOM updated the Company that further to the signing of a binding agreement with Searchlight and a company controlled by the Fuhrer family for the purchase of the shares of Internet Gold-Golden Lines Ltd. in BCOM and an additional investment in BCOM on June 24, 2019, all the approvals required by BCOM and its parent company, Internet Gold-Golden Lines Ltd., have been obtained and BCOM believes that this represents a significant milestone for the advancement and completion of the transaction. Furthermore, on August 18, 2019, BCOM informed the Company that on that same day the court's approval had been received for the creditor's arrangement in connection with the transaction and that completion of the transaction is still subject to obtaining approval from the Ministry of Communications. On this, see also Immediate Reports filed by the Company on April 8, 2019, April 10, 2019, April 17, 2019, April 19, 2019, May 2, 2019, May 14, 2019, May 20, 2019, June 12, 2019, June 23, 2019, June 24, 2019, July 29, 2019, August 8, 2019 and August 18, 2019, included here by way of reference.

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<sup>1</sup> The update is further to Regulation 39A of the Securities Regulations (Periodic and Immediate Reports), 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 the year 2018 and refers to the section numbers in Chapter A (Description of Company Operations) in the said periodic report.

**Section 1.5.4 - Main results and operational data**

**A. Bezeq Fixed Line (the Company's operations as a domestic carrier)**

	Q2 2019	Q1 2019	Q4 2018	Q3 2018	Q2 2018	Q1 2018
Revenues (NIS million)	1,020	1,043	1,026	1,043	1,064	1,063
Operating profit (NIS million)	875	531	(87)	451	387	473
Depreciation and amortization (NIS million)	204	207	217	218	211	204
EBITDA (Earnings before interest, taxes, depreciation and amortization) (NIS million) <sup>(1)</sup>	1,079	738	130	669	598	677
Net profit (NIS million)	562	321	(155)	257	202	263
Cash flow from current activities (NIS million)	416	471	600	583	507	516
Payments for investments in property, plant & equipment, intangible assets and other investments (NIS million)	333*	210	225	233	313*	205
Proceeds from the sale of property, plant & equipment and intangible assets (NIS million)	340**	39**	270**	8	(58)**	7
Payments for leases	27	34	9	28	29	33
Free cash flow (NIS million) <sup>(2)</sup>	396***	266***	636***	330	107***	285
Number of active subscriber lines at the end of the period (in thousands) <sup>(3)</sup>	1,768	1,792	1,818	1,843	1,865	1,889
Average monthly revenue per line (NIS) (ARPL) <sup>(4)</sup>	49	50	51	51	52	53
Number of outgoing use minutes (million)	865	926	989	960	1,010	1,055
Number of incoming use minutes (million)	1,056	1,090	1,160	1,125	1,151	1,191
Total number of internet lines at the end of the period (thousands) <sup>(7)</sup>	1,613	1,635	1,656	1,663	1,662	1,653
The number of which provided as wholesale internet lines at the end of the period (thousands) <sup>(7)</sup>	612	624	626	617	600	574
Average monthly revenue per Internet subscriber (NIS) - retail (ARPU)	97	96	96	93	93	92
Average bundle speed per Internet subscriber - retail (Mbps) <sup>(5)</sup>	64.0	61.5	59.1	57.4	55.4	53.5
Telephony churn rate <sup>(6)</sup>	2.7%	3.0%	3.1%	2.7%	2.8%	3.0%

- (1) EBITDA (Earnings before interest, taxes, depreciation and amortization) is a financial index that is not based on generally accepted accounting principles. The Company presents this index as an additional index for assessing its business results since this index is generally accepted in the Company's area of operations which counteracts aspects arising from the modified capital structure, various taxation aspects and methods, and the depreciation period for fixed and intangible assets. This index is not a substitute for indices which are based on GAAP and it is not used as a sole index for estimating the results of the Company's activities or cash flows. Additionally, the index presented in this report is unlikely to be calculated in the same way as corresponding indices in other companies. The Company's EBITDA is calculated as operating profit before depreciation, amortization and ongoing losses from the impairment of property, plant and equipment and intangible assets. Commencing January 1, 2019, and to reasonably present economic activity, the Company presents ongoing losses from the impairment of property, plant and equipment and intangible assets in DBS and Walla under the item depreciation and amortization, and ongoing losses from the impairment of broadcasting rights under the item operational and general expenses (in the Income Statement). On this matter, see Notes 3.1 and 5 to the Company's consolidated financial statements for the period ended March 31, 2019.
- (2) Free cash flow is a financial index which is not based on GAAP. Free cash flow is defined as cash from current activities less cash for the purchase/sale of property, plant and equipment, and intangible assets, net, and from 2018, with the application of IFRS 16, payments for leases are also deducted. The Company presents free cash flow as an additional index for assessing its business results and cash flows because the Company believes that free cash flow is an important indication of liquidity that reflects cash resulting from ongoing operations after cash investments in infrastructure and other fixed and intangible assets.
- (3) Inactive subscribers are subscribers whose Bezeq lines have been physically disconnected (not including a subscriber who neglected to pay his debt to the Company on time in (roughly) the first three months of the collection process).
- (4) Excluding revenues from transmission services and data communication, internet services, services to communications operators and contractor and other works. Calculated according to average lines for the period.
- (5) For bundles with a range of speeds, the maximum speed per bundle is taken into account.
- (6) The number of telephony subscribers (gross) who left Bezeq Fixed Line during the period divided by the average number of registered telephony subscribers in the period.
- (7) Number of active Internet lines including retail and wholesale lines. Retail - Internet lines provided directly by the Company. Wholesale - Internet lines provided through a wholesale service to other communications providers.
- (\*) In Q2 2018 - including permit fee payments in the amount of NIS 112 million (75% of the requirement) for the sale of the Sakia property. In Q4 2018 - including the payment of purchase tax in the amount of NIS 9 million. In Q2 2019 - including payment of a betterment levy in the amount of NIS 149 million on the sale of the Sakia property.
- (\*\*) In Q2 2018 - land appreciation tax paid on the sale of the Sakia property was recorded as a reduction of amounts received from the sale of property, plant and equipment in the amount of NIS 80 million; in Q4 2018 - including proceeds of the Sakia sale in the amount of NIS 155 million; in Q1 2019 - including proceeds of the Sakia sale in the amount of NIS 5 million, as well as a refund of land appreciation tax that was received in the amount of NIS 5 million. In Q2 2019 - including the proceeds of the Sakia sale in the amount of NIS 323 million.
- (\*\*\*) See the information in (\*) and (\*\*).

B. Pelephone

	Q2 2019	Q1 2019	Q4 2018	Q3 2018	Q2 2018	Q1 2018
Revenue from services (NIS million)	430	417	437	449	438	431
Revenue from the sale of terminal equipment (NIS million)	140	161	181	155	164	188
Total revenue (NIS million)	570	578	618	604	602	619
Operating profit (loss) (NIS million)	(8)	(10)	(4)	(2)	2	2
Depreciation and amortization (NIS million)	156	157	177	161	159	158
EBITDA (Earnings before interest, taxes, depreciation and amortization) (NIS million) <sup>(1)</sup>	148	147	173	159	161	160
Net profit (NIS million)	2	2	2	6	7	9
Cash flow from current activities (NIS million)	136	195	156	194	181	239
Payments for investments in property, plant & equipment, intangible assets and other investments, net (NIS million)	82	63	78	69	90	69
Payments for leases	46	69	70	64	50	75
Free cash flow (NIS million) <sup>(1)</sup>	8	63	8	61	41	95
Number of postpaid subscribers at the end of the period (thousand) <sup>(2) (5)</sup>	1,866	1,842	1,831	1,817	1,800	1,760
Number of prepaid subscribers at the end of the period (thousand) <sup>(2) (5)</sup>	397	382	374	368	801	786
Number of subscribers at the end of the period <sup>(2)</sup>	2,263	2,224	2,205	2,185	2,601	2,546
Average monthly revenue per subscriber (NIS) (ARPU) <sup>(3)</sup>	64	63	66	68	57	57
Churn rate <sup>(4)</sup>	7.5%	8.6%	9.0%	9.1%	7.3%	8.0%

- (1) On the definition of EBITDA (Earnings before interest, taxes, depreciation and amortization) and free cash flow, see comments (1) and (2) in the Bezeq Fixed Line table.
- (2) Subscriber data includes Pelephone subscribers (without subscribers from other operators hosted on the Pelephone network and excluding IOT subscribers from Q3 2018), and does not include subscribers connected to Pelephone services for six months or more but who are inactive. An inactive subscriber is one who in the past six months has not received at least one call, has not made one call / sent one SMS, or has performed no surfing activity on his phone or has not paid for Pelephone services. Prepaid subscribers are included in the list of active subscribers from the date on which the subscriber loaded his device, and are removed from the list of active subscribers if he makes no outgoing use of his device for six months or more. Notably, a customer may have more than one subscriber number ("line"). On the change in the definition of subscribers from Q3 2018, see comment (5) below.
- (3) Average monthly revenue per subscriber (postpaid and prepaid). The index is calculated by dividing the average total monthly revenues from cellular services, from Pelephone subscribers and other telecom operators, including revenues from cellular operators who use Pelephone's network, repair services and extended warranty in the period, by the average number of active subscribers in the same period. On the effect of the change in the definition of a subscriber from Q3 2018 on the ARPU index, see comment (5) below.
- (4) The churn rate is calculated at the ratio of subscribers who disconnected from the company's services and subscribers who became inactive during the period, to the average number of active subscribers during the period. On the effect of the change in the definition of a subscriber from Q3 2018 on the churn rate, see comment (5) below.
- (5) From Q3 2018, Pelephone updated the definition of an active subscriber so that its subscriber listing will no longer include IOT subscribers, and it added a separate comment for prepaid subscribers so that a prepaid subscriber will be included in the list of active subscribers from the date on which the subscriber loaded his device, and it will be removed from the list of active subscribers if no outgoing calls were made for six months or more. As a result of this change, at the beginning of Q3 2018, 426,000 prepaid subscribers and about two thousand IOT subscribers were written off Pelephone's subscriber listings. This led to an increase of NIS 11 in the ARPU index and an increase of 1.5% in the churn rate in Q3 2018.

C. Bezeq International

	Q2 2019	Q1 2019	Q4 2018	Q3 2018	Q2 2018	Q1 2018
Revenues (NIS million)	339	341	370	333	336	352
Operating profit (NIS million)	18	34	21	31	30	34
Depreciation and amortization (NIS million)	46	46	60	46	45	43
EBITDA (Earnings before interest, taxes, depreciation and amortization) (NIS million) <sup>(1)</sup>	64	80	81	77	75	77
Net profit (NIS million)	10	25	13	20	20	24
Cash flow from current activities (NIS million)	48	56	106	73	54	67
Payments for investments in property, plant & equipment, intangible assets and other investments, net (NIS million) <sup>(2)</sup>	34	33	25	26	44	31
Payments for leases	8	8	9	9	9	9
Free cash flow (NIS million) <sup>(1)</sup>	6	15	72	38	1	27
Churn rate <sup>(3)</sup>	6.2%	6.6%	7.7%	5.8%	6.0%	6.0%

- (1) On the definition of EBITDA (Earnings before interest, taxes, depreciation and amortization) and cash flows, see comments (1) and (2) in the Bezeq Fixed Line table.
- (2) The item also includes long-term investments in assets.
- (3) The number of Internet subscribers who left Bezeq International during the period, divided by the average number of registered Internet subscribers in the period.

D. DBS

	Q2 2019	Q1 2019	Q4 2018	Q3 2018	Q2 2018	Q1 2018
Revenues (NIS million)	337	343	356	367	375	375
Operating profit (loss) (NIS million)	(24)	(45)	(1,139)*	1	(17)	(1)
Depreciation, amortization and ongoing impairment (NIS million)	68	55	84	81	79	79
EBITDA (Earnings before interest, taxes, depreciation and amortization) (NIS million) <sup>(1)</sup>	44	10	(1,055)*	82	62	78
Net profit (loss) (NIS million)	(27)	(50)	(1,137)*	(2)	(10)	1
Cash flow from current activities (NIS million)	22	53	46	34	60	86
Payments for investments in property, plant & equipment, intangible assets and other investments, net (NIS million)	73	64	81	79	75	62
Payments for leases	7	8	6	9	8	8
Free cash flow (NIS million) <sup>(1)</sup>	(58)	(19)	(41)	(54)	(23)	16
Number of subscribers (at the end of the period, in thousands) <sup>(2)</sup>	565	568	574	584	582	580
Average monthly revenue per subscriber (ARPU) (NIS) <sup>(3)</sup>	198	200	206	210	215	214
Churn rate <sup>(4)</sup>	4.9%	5.6%	5.6%	5.1%	4.7%	6.1%

- (1) On the definition of EBITDA (Earnings before interest, taxes, depreciation and amortization) and free cash flow, see comments (1) and (2) in the Bezeq Fixed Line table.
- (2) Subscriber - a single household or small business customer. In the case of a business customer that has more than a certain number of decoders (such as a hotel, kibbutz, or gym), the number of subscribers is standardized. The number of business customers that are not small businesses, is calculated by dividing the total payment received from all the business customers that are not small businesses by the average revenue per small business customer, which is determined periodically. In Q4 2018, the standardization formula was updated as a result of which the number of subscribers fell by 7,000. This is partially due to the fact that the average revenue per small business customer in the special offers (at least 100 customers per offer) increased in the past year as a result of customers moving over to packages that are richer in content at a higher price.
- (3) Monthly ARPU is calculated by dividing total DBS revenues (from content and equipment, premium channels, advanced products, and other services) by the average number of customers in the period.
- (4) Number of DBS subscribers who left DBS during the period, divided by the average number of DBS registered subscribers in the period.
- (\*) See Note 5.2 to the Company's financial statements for the period ended June 30, 2019 concerning impairment of assets.

## **Section 1.6 - Group Outlook**

Following the extraordinary events in Q2 2019 (a write-off of a tax asset, impairment loss in Pelephone assets and a capital gain recorded in respect of the sale of the Sakia property), and the inclusion of projected costs for the early retirement of employees in the forecast data, the Bezeq Group is revising its forecast published in this section in the Periodic Report for 2018 ("the Original Forecast") as follows:

- Net loss for shareholders is expected to be NIS 1.1 billion (compared with a net profit of NIS 900 million to NIS 1.0 billion in the Original Forecast).
- EBITDA is expected to be NIS 2.9 billion (compared with NIS 3.9 billion in the Original Forecast).
- CAPEX<sup>2</sup> is expected to be NIS 1.7 billion (no change compared with the Original Forecast).

The revised forecast for the Company includes a write-off of the tax asset balance for DBS losses of NIS 1.166 billion, an impairment loss in Pelephone assets of NIS 951 million, and the recording of a capital gain of NIS 403 million for the sale of the Sakia property (on these matters see, respectively, Notes 6, 5.1 and 7 to the Company's financial statements for the period ended June 30, 2019). Furthermore, the revised forecast includes provisions for the early retirement of employees in the Company and in the subsidiaries Pelephone, Bezeq International and DBS in the amount of NIS 380 million (on this matter, see Note 9 to the Company's financial statements for the period ended June 30, 2019, and Note 18.5 to the Company's financial statements for the period ended December 31, 2018. Notably, of the amounts forecast for early retirement, in practice, NIS 360 million has not yet been recorded in the financial statements and it is a forecast which might not materialize).

The Company's forecasts in this section are forward-looking information, as defined in the Securities Law. The forecasts are based on the Company's estimates, assumptions and expectations, including that the forecasts also do not include the effects of the cancellation of structural separation in the Group and the merger proceedings with the subsidiaries and everything they entail (see Section 1.7.2 in the Periodic Report for 2018), if and insofar as they occur in 2019. The Group's forecasts are based, inter alia, on its estimates regarding the structure of competition in the telecommunications market and regulation in this sector, on the economic situation and accordingly, the Group's ability to implement its plans for 2019, and taking note of changes that may occur in the foregoing, in business conditions and the effects of regulatory decisions, technology changes, developments in the structure of the telecommunications market, etc. or insofar as one or more of the risk factors listed in Sections 2.20, 3.19, 4.14 and 5.19 in the Company's Periodic Report for 2018 and specifically, the risk factor detailed in Section 2.20.12 of this report with respect to the impairment in the value of subsidiaries.

The Company will report, as necessary, any deviation of more/less than 10% of the amounts stated in the forecast.

On the Group's forecast in connection with EBITDA, attention is drawn to the revised definition of EBITDA as specified in comment (1) to the table in the update to Section 1.5.4(A). As noted there, as of January 1, 2019, and in order to enable the proper presentation of economic activity, the Company presents ongoing losses from the impairment of property, plant and equipment and intangible assets in DBS and Walla under Depreciation and Amortization, and ongoing losses from the impairment of broadcasting rights under Operating and General Expenses (in the Income Statement). On this matter it is stipulated that ongoing losses from the impairment of assets will be classified under the same items in which expenses in respect of these assets were recorded in the past. The Company believes that in view of the forecast for continuing negative cash flows and negative value of activity in DBS and Walla, and in light of the fact that impairment is expected to continue in the future, this classification is more consistent with the method of presentation based on the nature of the expense and it is also more suited to understanding the Company's business. It is further stipulated that expenses in respect of an impairment loss resulting from a one-time adjustment of the forecast for coming years, will be reclassified as Other Operating Expenses in the income statement. On this matter, see also Notes 3.1 and 5 to the Company's financial statements for the period ended June 30, 2019.

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<sup>2</sup> CAPEX - payments (gross) for investment in property plant and equipment and intangible assets.

## **Section 1.7 - General environment and the influence of outside factors on the Group's activity**

### **Section 1.7.2 - Activities of Bezeq Group as a communications group and the structural separation restrictions**

Section 1.7.2.1 - Structural separation - on a petition filed by the Company in the HCJ against the Ministry of Communications for the immediate cancellation of the structural separation in Bezeq Group - despite the Company's objections, the State received several extensions for submitting its response to the petition, the last of which is until September 5, 2019. On this matter, see also Note 6 to the Company's financial statements for the period ended June 30, 2019.

Section 1.7.2.2 - Marketing joint service bundles with a subsidiary - on the marketing of joint service bundles of Internet infrastructure together with ISP - on April 16, 2019, the Company submitted its comments whereby the solution is to market a reverse bundle which meets the customer's basic requirements for assurance and continuity of service, which is not limited in time and allows the customer to disconnect at any time. On this matter, it is noted that on May 26, 2019, the Company received a preliminary supervisory report on the reverse bundle, for the Company's response. According to the information in the report, its findings show that the Company ostensibly deviated from the provisions of Section 9A of its license ("Joint Service Bundle") and the regulations prescribed on this subject. On June 30, 2019, the Company submitted its response to the report whereby the Company did not deviate from the aforementioned provisions.

On July 24, 2019, the Company received hearing documents from the Ministry of Communications, in part concerning a change in the marketing formula of the "reverse bundle". According to the information in the hearing documents, the Ministry is considering changing the formula presented at the hearing on March 26, 2019, and determining, inter alia, that the Company will not be obligated to market a reverse bundle for ISPs that have accumulated over 100,000 wholesale BSA customers on the Company's network and have also provided accessibility to over 100,000 households to their independent optical fiber infrastructure on the Company's physical infrastructure. The Ministry will also determine that the provisions for breaking up the bundle after 12 months will be cancelled. According to the hearing, this format will enter into force after the launch of the Company's fiber project and a reasonable possibility will be provided to purchase the BSA service on the fiber network. On this matter, see also the Company's Immediate Report dated July 25, 2019, included here by way of reference. The Company intends to submit its comments on the hearing by September 8, 2019.

### **Section 1.7.4 - Additional regulatory aspects relevant to the entire Group or several Group companies**

Subsection 1.7.4.4(B) - On a hearing concerning the Ipv6 protocol (Internet addresses) - on July 3, 2019, the Ministry of Communications published a decision on the hearing in which the transition to Ipv6 protocol will take place in accordance with the defined milestones. For the Company (as the holder of a domestic carrier license) and for the owners of Internet access licenses, it was determined, among other things, that within 12 months of date of the amendment of the license, a license holder will adapt the network and its components to fully support the Ipv6 protocol and in a manner that provides access for subscribers to the Ipv6 Internet protocol service from all terminal equipment that supports Ipv6 protocol; license holders will voluntarily transfer existing and new subscribers with terminal equipment that supports Ipv6 to addresses on Ipv6 protocol. The subscribers will be transferred according to milestones so that up to 24 months from the date of the amendment, 50% of the subscribers will be transferred, up to 36 months - 75% and up to 48 months - 100% (excluding - as noted in a footnote - subscribers in possession of private terminal equipment that does not support the Ipv6 protocol and have decided not to replace it, provided that the license holder signs them on a waiver). With respect to the holders of cellular licenses (such as Pelephone), it was determined that the voluntary transfer will reach 100% within 24 months.

Section 1.7.4.6 - Enforcement and financial sanctions - on April 17, 2019, a new request for information under the Consumer Protection Law was sent to the Company, stating that the Consumer Protection and Fair Trade Authority is conducting an investigation against the Company on suspicion of violation of the Consumer Protection Law, including a suspected breach on the subject of misleading consumers when a transaction is performed and the non-cancellation of transactions according to the law. The Company submitted the requested information to the Consumer Protection Authority.



## **Section 1.8 - Bezeq Group's business strategy**

During the first half of 2019, the Board of Directors continued to review, implement and update the Group's business strategy which includes various streamlining processes and organizational changes. This, in part, against the ongoing decline in revenues in the domestic fixed-line sector, including a continuing decline in revenues from fixed-line telephony services and retail Internet services, as well as lower revenues in the quarter from wholesale Internet services (see update to Section 1.5.4), and the estimate is that if the streamlining measures are not implemented, the decline in the Group's profitability is expected to continue in forthcoming years. To address this ongoing trend, the Group companies have introduced various streamlining measures and in this context the Board of Directors granted approval to the Company and the subsidiaries Pelephone, Bezeq International and DBS to take action to implement such measures.

The estimates detailed above are forward-looking information which might be affected by various factors, including future changes in the Israeli market in general and in the communications market in particular, strategic and other measures that the Company and its subsidiaries might introduce, regulatory changes, changes in the Company's competitive status, etc. Furthermore, the foregoing could be affected by the materialization of any of the risk factors listed in Sections 2.20, 3.19, 4.14 and 5.19 in Chapter A of the Periodic Report for 2018.

## **2. Bezeq ("the Company") - Domestic Fixed-Line Communications**

### **Section 2.6.3 - Internet infrastructure segment**

According to publications in the media, on May 13, 2019, HOT announced that it is starting to market a 500 Mbs high-speed Internet service.

Subsection 2.6.3.1 - To the best of the Company's knowledge, on July 28, 2019, the Ministry of Communications adopted the recommendations of the advisory committee at that date concerning application of the universal deployment obligation on HOT. According to the committee's recommendations and the Minister's decision, HOT will be compelled to provide its services in areas without infrastructure based on a technology neutral format, i.e. without being under obligation to deploy physical infrastructure, but it will be permitted to make immediate use of any cellular network to provide its services at download speeds of 12/30 Mbps. The adopted recommendations also prescribed milestones for upgrading the network for the alternative cellular network, minimum service quality and reporting obligations.

### **Section 2.6.5 - Competition from IBC and other competing companies**

To the best of the Company's knowledge, the acquisition of IBC by Cellcom and another investor (Israel Infrastructures Fund) was completed on July 31, 2019.

### **Section 2.6.6 - The Company's deployment and ways of coping with the intensifying competition**

Subsection 2.6.6.7 on the Company's new router, Be - at the end of Q2 2019, the number of Company customers using the Be router is 215,000 (more than 20% of the Company's retail Internet customers).

### **Section 2.7.2 – Infrastructure and domestic fixed-line communications equipment**

Following are several clarifications concerning deployment of optical fibers by the Company - the main advantage of optical fiber over copper is the possibility of transmitting higher speeds. There are also operating advantages which are insignificant compared with this advantage. The reason for the Company's decision to freeze the fiber deployment is that there is no economic justification for the Company to launch the service in view of the major investments entailed in completing the deployment and operating the service on the one hand, and absence of the certainty necessary to pursue a business plan that is economically sustainable on the other. At this time, the deployment of fibers by the Company's competitors is intensifying competition in the areas of deployment with a negative impact on the Company. Nevertheless, the Company believes that due to its operational advantages, and principally the access to skilled, professional manpower, in the medium and long term its technological superiority will be maintained. The Company believes that at this point in time, placing the deployment on hold does not affect the Company's compliance with the regulations, which are currently under review by the Minister of Communications (see below the update to the call for public comments). The Company believes that from such time as a decision is made to launch services based on the fiber network, it will

be possible to reach significant cover<sup>3</sup> of more than 50% of households in Israel within a period of 4-5 years.

The estimates detailed above are forward-looking information based on the Company's assumptions and expectations the materialization of which is uncertain. The information might be affected by various factors, including the Company's future capabilities, changes in technology, regulatory decisions, etc. or the materialization of any of the risk factors detailed in Sections 2.20, 3.19, 4.14 and 5.19 of the 2018 Periodic Report.

On a call for public comments by the Ministry of Communications concerning the policy for the deployment of ultra-wide bandwidth infrastructure in Israel - on April 8, 2019, the Company submitted its comments on the secondary call for public comments, in which it stated that this issue cannot be based on the application of a universal obligation that is not economically viable. The Company set out principles for a dynamic regulatory mechanism the application of which will facilitate and encourage large-scale deployment of ultra-high-speed Internet infrastructures on the basis of business considerations and economic feasibility, rather than coercion.

On July 24, 2019, the Company received hearing documents from the Ministry of Communications, inter alia on the subject of determining a maximum tariff for access to ultra-wide bandwidth managed on the Company's fiber network. According to the Ministry, the hearing on this subject is part of the comprehensive fiber plan being formulated by the Ministry. The key recommendations are, among others, as follows: recommendation for setting a maximum tariff for BSA service over fiber - the maximum recommended tariff, including installation and repair of faults, for accessibility service and data transfer on the core network at a maximum broadband speed of 400 Mbps will be NIS 71 per line per month (excluding VAT); and for this service at a maximum broadband speed of 1,000 Mbps - the maximum tariff will be NIS 85 per line per month (excluding VAT). The broadband speed is calculated in the hearing documents as the total of the upload rate and download rate. The maximum broadband speed will have a different breakdown between the download and upload rates, based on the decision of the service provider using the BSA service over fiber, and it will be limited to an upload rate of 50% of the download rate. According to the hearing documents, the maximum tariff is temporary and will be applicable immediately upon provision of the service. This tariff will remain in force until a tariff is set by the Company in accordance with the regulatory guidelines to be adopted following publication of the fiber plan. It is stipulated that the Company does not currently operate an optical fiber network that reaches the homes of private customers and that provision of the BSA service will only be possible when such a network has been established, if it is established. The Company requested clarifications from the Ministry of Communications and it intends to submit its comments on the hearing in by September 8, 2019.

On August 4, 2019, the Company received hearing documents from the Ministry of Communications concerning a standard tariff for fiber based Internet services (FTTP). According to the hearing documents, this is another layer in the regulations that will apply to the provision of fiber-based Internet services, whereby the Ministry is considering to determine that the provision of FTTP services by service providers (who do not have a deployment obligation) cannot discriminate against subscribers based on the type of infrastructure they are using, including if the infrastructure belongs to the service provider or to another infrastructure owner or other party. The Company intends to submit its comments on the hearing by September 8, 2019.

On this matter, see also Immediate Reports of the Company dated July 25, 2019 and August 5, 2019, included here by way of reference.

#### **Section 2.7.4 – Real estate**

Sakia property - On May 5, 2019, the transaction was completed and the full outstanding consideration, in the amount of NIS 377 million (including VAT), was received for the sale of the property. Upon receipt of the outstanding payment, the Company paid half of the betterment levy in the amount of NIS 75 million, and it provided a bank guarantee for the other half of the levy, without this derogating from and/or prejudicing the steps taken and/or to be taken by the Company to cancel or reduce this levy. The Company recorded a capital gain of NIS 403 million in its financial statements for Q2 2019. The capital gain that was recorded is based on the Company's assessment and in practice it could change. On this matter, see also Note 7 to the Company's financial statements for the period ended June 30, 2019.

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<sup>3</sup> The percentage of households that are able to receive ultra-high-speed Internet service based on advanced technologies within a reasonable period given that suitable infrastructure is available in close proximity to them.

### **Section 2.9.5 - Officers and senior management in the Company**

In the matter of compensation for attendance and annual compensation payable to directors serving in the Company and its subsidiaries (hereinafter together - "Directors Compensation") - pursuant to changes in the data for the equity of the Company and some of its subsidiaries, as they appear in their 2018 audited balance sheet, changes were made in the Directors Compensation, in accordance with the Companies (Rules for the Compensation and Expenses of External Directors) Regulations, 2000, and a resolution passed by a general meeting of the Company's shareholders on September 17, 2018.

On May 3, 2019, the Chairman of the Board, Mr. Shlomo Rodav, informed the Company of his request and of a request from the Israel Lighterage & Supply Co. Ltd. ("Mr. Rodav" and "Lighterage", respectively), a private company in which Mr. Rodav holds 50% of the means of control and through which Mr. Rodav provides the Company with services as Chairman of the Board, in accordance with the management agreement between Lighterage and the Company, to reduce the management fees to which Lighterage is entitled under the aforesaid agreement by 20% for the whole of 2019 (in other words - retroactively from the payment in respect of January 2019). For additional information about the management agreement, see an Immediate Report of the Company dated August 12, 2018, included here by way of reference, and Section 7D in Chapter D (Additional Information about the Company) in the Company's Periodic Report for 2018. Furthermore, on May 29, 2019, the director Mr. Ami Barlev, announced that he will forgo his entitlement to any compensation payable to him for serving as a director in the Company, effective from June 1, 2019 until further notice.

On the convening of a special general meeting of the Company's shareholders to re-approve the compensation policy for the Company's senior officers - on May 23, 2019, the general meeting affirmed the compensation policy in accordance with Section 267A of the Companies Law, including updating the policy, for three years, commencing January 1, 2019, as specified in the Company's Supplementary Immediate Report dated May 15, 2019 on convening the meeting, included here by way of reference.

### **Section 2.9.6 - Labor disputes**

On notice of a strike or stoppage received by the Company on January 23, 2019 - the parties are negotiating, and subsequent to joint motions that were filed in the court, the hearings that were due to take place in the case were postponed and the Company must give notice by September 7, 2019 of an application regarding further proceedings.

### **Section 2.11 – Working capital**

For information about the Company's working capital, see Section 1.3 in the Directors Report.

### **Section 2.13 - Financing**

#### **Section 2.13.4 – Credit received in the Reporting Period; and Section 2.13.5 - Company debentures**

In June 2019, the Company raised debt in the amount of NIS 500 million by means of a private loan from a financial institution with an average duration of 7.15 years and fixed shekel interest of 3.6%. The terms of the loan are similar to other loans taken by the Company, as set out in Note 15.3 of the 2018 financial statements.

In July 2019, the Company completed a private placement of debentures (Series 11 and 12) ("the Debentures") to institutional investors, as follows: 427,891,000 debentures (Series 11) with a par value of NIS 1 each, unlinked, at an interest rate of 3.6% and an average duration of 7.7 years, and 461,740,000 debentures (Series 12) with a par value of NIS 1 each, of the Company, CPI-linked and bearing interest at a rate of 2.1% with an average duration of 8.25 years. The total consideration received by the Company for this placement (gross) is NIS 890 million. The debentures were listed for trading on the TASE's TACT (Tel Aviv Continuous Institutional Trading System). The Company intends to register the debentures for trading on the stock exchange, subject to the statutory provisions, to publish a prospectus and to obtain the necessary permits. In the event of registration for trading of the Debentures on the TASE's main list, the interest rate that will be paid for the balance of the principal of the Debentures from the date of registration on the TASE main list, will be reduced by 0.4%. The terms of the Debentures are similar to the terms of the Debentures from the existing series of the Company (Series 6, 7, 9, and 10), as set out in Note 15.3 to the 2018 financial statements. The proceeds of the placement will be used to refinance the Company's debt. On this matter, see the Company's Immediate Reports dated June 23, 2019 and July 10, 2019 (results of an institutional tender, summary of the conditions of the debentures and trust deeds), included here by way of reference.

Notably, in July 2019, the Company made early repayment of bank loans bearing variable interest, in the amount of NIS 438 million.

#### **Section 2.13.6 - Credit rating**

On April 8, 2019, Midroog Ltd. ("Midroog") affirmed an Aa2.il rating for the Company's debentures (Series 6, 7, 9, and 10) and it changed the rating outlook from stable to negative; on May 7, 2019, S&P Global Rating Maalot Ltd. ("Maalot") affirmed the Company's iIAA rating with a negative rating outlook. On these and on the aforementioned rating reports, see Immediate Reports of the Company dated April 8, 2019 (Midroog) and May 7, 2019 (Maalot).

In connection with a private placement of debentures (Series 11 and 12) of the Company (see update to Sections 2.13.4-2.13.5) - on July 10, 2019, Midroog determined the same rating (Aa2.il with a negative outlook) and Maalot also determined the same rating (iIAA, negative rating outlook) for the placement of new debentures of the Company (Series 11 and 12) with a scope of up to NIS 1 billion. On these matters and on the aforementioned rating reports, see immediate reports of the Company dated June 25, 2019 and July 10, 2019 concerning rating reports issued by Midroog and Maalot.

Furthermore, on August 6, 2019, Midroog published an issuer's comment in connection with the Company's debentures (Series 6, 7, 9, 10, 11 and 12) and left unchanged the Aa2.il rating, negative outlook, for these debentures. On this, see also an Immediate Report of the Company dated August 6, 2019.

On August 12, 2019, Maalot announced a downgrade of the rating for the Company and its subsidiaries and it issued a rating of iIAA-, negative outlook, for the Company's debentures. On this, see also an Immediate Report of the Company dated August 12, 2019.

On this matter, see also Section 3 of the Directors Report.

#### **Section 2.13.7 - the Company's assessment for raising financing in 2019 and possible sources**

On a resolution passed by the Company's Board of Directors on March 27, 2019 concerning the filing of an application for permission to publish a supplementary prospectus based on its financial statements at December 31, 2018 - in view of the fact that discussions with the ISA in the context of the draft prospectus have not been completed, the application for permission is to publish a supplementary prospectus which will be based on the Company's financial statements at a later date, after discussions with the ISA have been concluded. At this stage, as set out in the update to Sections 2.13.4-2.13.5, the Company made a private placement of debentures and it intends to register the debentures for trading on the stock exchange, subject to the statutory provisions, to publish a prospectus and to obtain the necessary permits.

On the convening of a general meeting from March 28, 2019, for which the agenda includes approval for increasing the Company's registered capital as a preliminary step towards raising potential capital through a rights issue - on April 8, 2019, the Company's Board of Directors resolved, in view of discussions with shareholders that were held on the subject and as a response to their requests, that the subject of the increase in registered capital would be removed from the agenda of the general meeting.

The Company is continuing to adjust the structure of its debt to its requirements and sources, in part by extending durations through the raising of long-term debt and repaying short-term debt while reducing the debt.

#### **Section 2.14 - Taxation**

On the deferred tax asset in respect of losses in DBS, further to discussions held between representatives of the Company and the Authority's senior management concerning the Company's application for permission to publish the Prospectus, on August 23, 2019 the Company received the response of the Authority's senior management concerning the propriety of the accounting treatment applied by the Company to recognition of the Tax Asset including the formulated position of the Authority's senior management in the matter, which referred to the question whether the Company was justified in its forecast test that underlay the ability to continue to recognize the Tax Asset. According to the formulated position of the Authority's senior management there are difficulties in the Company's position of recognition of the Tax Asset, and it would appear that the Authority's position is that the Company has not met the onus required to base the forecast for use of the Tax Asset in respect of the cumulative existence of three events: cancellation of the structural separation by the Ministry of Communications, extension of the validity of the taxation ruling concerning use of the Tax Asset each year until the cancellation of the structural separation, the existence of adequate income over time after

the date of cancellation of the structural separation of Bezeq merged with DBS that will facilitate use of the Tax Asset. In the formulated position of the Authority's senior management it is noted that the assessment is correct as of the date of the 2018 financial statements and onwards, and not for earlier periods. This takes into account that some of the issues related to the structural separation are at the heart of a criminal investigation of matters of senior officers of the Company in the years 2013-2017. In this matter see the Company's Immediate Report dated August 23, 2019, which is included in this report by way of reference.

For the purpose of assessing the probability of making use of the Tax Asset as of June 30, 2019, the Company took into account inter alia in the absence of developments that occurred in its discussions with the authorities and government ministries, various developments in recent months and the impact of the passage of time. In the light of the foregoing, the Company's assessment of the probability of making use of the Tax Asset no longer meets "more likely than not", and accordingly it has written off the Tax Asset by changing the estimate starting from the financial statements for Q2 2019. Therefore the Company has recognized tax expenses of NIS 1,166 million in the income statement for the three month period ended June 30, 2019.

As stated, in accordance with the formulated position of the Authority's senior management, the assessment was correct as of the date of the Company's 2018 financial statements and onwards, which is different from the Company's position that ceasing recognition of the Tax Asset commenced from the financial statements for the period ended June 30, 2019. If the Company's position will not be accepted, there is a possibility that the Company will be required to restate its 2018 and subsequent financial statements.

In this matter see Note 6 to the Company's financial statements for the period ended June 30, 2019.

#### **Section 2.16.1 - Control of Company tariffs**

On May 19, 2019, the Ministry of Communications sent the Company a preliminary supervisory report on the subject of price quotes for transmission services. According to the supervisory report, for which the review commenced at the beginning of 2017, the Company ostensibly deviated from the provisions of its license by submitting a tender offer that includes reduced tariffs for transmission lines that were not offered transparently to all its business customers. The ministry argues that it was unaware of the discount included in these tariffs, the discount did not appear in the price lists for the transmission service submitted to the ministry in recent years, and it does not comply with the test of reasonability, under the provisions of Section 17 of the Communications Law. The ministry further stated that it seems that this practice continues to the present time for other services as well, particularly in other tenders. On June 30, 2019, the Company submitted its comments on the supervisory report stating the Company did not deviate from the provisions of its license and that, among other things, this model was reviewed by the Ministry of Communications and complies with the tests of reasonability, and that the service providers were even aware of it and used it.

Section 2.16.1.8 - Wholesale market - on May 5, 2019, the Company submitted its comments on a hearing on tariffs for the wholesale market. In its comments, the Company pointed to material errors in the calculation and the underlying assumption concerning tariffs for the BSA service and the obligation to link the tariff for a technician's visit to a relevant index; instead, the Company proposed a dynamic mechanism which addresses the model of demand in passive service as well (instead of the current assumption relating to demand the feasibility of which is unrealistic), and it submitted its objection to imposing the tariff retroactively.

#### **Section 2.16.4 - Wholesale market**

Subsection 2.16.4.2 on BSA services - on June 10, 2019, the Company's appeal against dismissal of the petition against the process of supervising the Company which had led to the imposition of penalties in the amount of NIS 8.5 million, was denied.

#### **Section 2.16.8 – Economic Competition Laws**

Subsection 2.16.8.7 on considering a determination by the Commissioner of the Economic Competition Authority that the Company had abused its position regarding use of the Company's passive infrastructures - the Company submitted its arguments on the additional findings and voiced its opinion at an oral hearing on August 4, 2019.

## **Section 2.18 – Legal proceedings**

### **Section 2.18.1 - Pending legal proceedings**

Subsection A - On a motion to approve a class action alleging reporting omissions and the concealment of material information from the investing public - at a hearing that took place on May 22, 2019 on a motion filed by the Company for a re-hearing on the decision to certify the claim as a class action, the court proposed transferring the case for mediation but when this proposal was rejected by the plaintiff, a hearing took place on July 18, 2019 to supplement the parties arguments on the request for a re-hearing and a decision on this request will be given at a later stage.

Subsections B, H, I, K and M (stay of legal proceedings in view of the investigation by the Israel Securities Authority and Israel Police) – based on current decisions of the various courts, at this stage the proceedings are stayed until October 31, 2019.

Subsection C - on the motion from March 2018 alleging abuse of monopoly status, on March 28, 2019, the court ruled to stay the proceedings in the case in view of the ISA's investigation and until any other decision is made the date for filing the response to the motion for certification was extended. The Attorney General's representative was asked to update the court and the parties attorneys on this matter within 6 months from the date of the decision.

Subsection D - on a motion to certify a class action against the Company, alleging that the Company deliberately restricts the broadband speed for ISPs and refrains from repairing malfunctions on this matter - on April 30, 2019, the court issued a ruling in which it approved the Plaintiffs' abandonment of the motion for certification after reaching the conclusion that there are evidential difficulties in conducting a proceeding against the Company, and this after inspecting the documents they received from the Company and the Company's response to the motion.

Subsection J - on a class action that was filed in the USA against B Communications Ltd., the Company's controlling shareholder, and senior executives therein, in which DBS and officers (past and present) of DBS and the Company, were also included - on March 28, 2019, the Company received notice of a ruling issued by a US court from that same date, which accepted the applications of DBS and the senior officers (past and present) of DBS and the Company, and it dismissed the claim against them outright, due to the absence of personal jurisdiction against them.

Subsection L - on a renewed motion from April 2018 to certify an action as a class action against the Company on the subject of sending spam messages which include a link to the Company's website, and a previous motion on the same subject from March 2015, where the Company filed a motion for permission to appeal the decision to certify as a class action - on June 6, 2019, the Supreme Court issued a judgment in which the motion for permission to appeal and the Company's appeal were accepted, and it was agreed that a motion for abandonment of the motion for renewed certification from April 2018 would be filed. Subsequently, on June 16, 2019, the motion to abandon this motion was accepted thus terminating both proceedings.

## **Section 2.20 – Discussion of Risk Factors**

### **Section 2.20.5 – Constraints concerning relations between the Company and the subsidiaries in the Bezeq Group**

Concerning the Tax Asset – see the update to section 2.14.

#### **Section 2.20.12 - Impairment of subsidiaries**

Pursuant to the accounting standards, the Company prepares valuations of its subsidiaries to periodically test for impairment of goodwill and to assess periodic impairment of assets regarding which there are indications of impairment.

Taking note of the business position of the subsidiaries and the discrepancy, if there is any, between the carrying amount in the Company's accounts and their recoverable amount as a cash-generating unit, any decline in the value of the subsidiaries' operations could lead to the recording of an impairment loss (write-off) in the Company's books.

Additionally, a significant change in circumstances that leads to a change in estimates could occur due to a high-intensity isolated event and/or as the result of a sequence of small changes that occur over time, which have a significant cumulative effect in the long term and/or due to a change in estimates (even on a small scale) regarding the long term. Valuations rely on assumptions which are correct at the date of the report but that might not materialize or could partially materialize and different perspectives affect, with varying intensity, the value of the measured unit, where assumptions relating

to the long term have a relatively large weight compared with assumptions regarding the short term. These assumptions are sensitive to values in the representative year, to the discounting interest rate and the permanent growth rate.

On this matter, see also Note 5 to the Company's financial statements for the period ended June 30, 2019 and Section 2.1 in the Directors Report.

### **3. Pelephone - Mobile radio-telephone (cellular telephony)**

#### **Section 3.1.8 - Structure of competition in the sector and changes occurring in it**

In August 2019, Suny Cellular Communications Ltd. began to market the cellular services of Hot Mobile. Suny's entry into this sector could affect competition in the industry.

#### **Section 3.7.1 - Infrastructure**

Section 3.7.1.4 - Network investments - Pelephone has begun to plan and prepare an outline for implementing 5G advanced data communications services. The outline is planned to be integrated with existing infrastructures and systems. The operation of these advanced services requires receiving additional frequency spectrum that the Ministry of Communications intends to allocate in the context of the tender (see Section 3.8.2.5).

#### **Section 3.8.2 - Frequency usage rights**

Section 3.8.2.5 - Tender for mobile radio telephony services over advanced bandwidths: on July 15, 2019, the Ministry of Communications published a tender for the allocation of additional frequencies, including 5G frequencies ("the Tender"). The main points of the Tender are, inter alia, as follows:

Proposed frequencies in the Tender in each frequency spectrum are:

- 700 MHz - bandwidth of 30 x2 MHz;
- 2.600 MHz - bandwidth of 60 x2 MHz;
- 3,500-3,800 MHz - bandwidth of 300 MHz;

Owners of existing networks will be able to compete in the Tender. Additionally, new players will be able to compete on 100 Mega (out of 300) in the 3,500 Mhz range, provided that they meet the qualifying conditions. The winners from among the new players will receive special licenses for the provision of specialist 5G services but they will not be permitted to provide cellular services for the previous generations and will only be 5G operators.

The Tender will allow bidders to compete simultaneously on all frequency spectrum and submit combined offers. Among other things, the Tender includes provisions for network coverage and quality requirements that will be formalized as part an amendment to the cellular telephony licenses of the existing operators.

Pelephone is studying the details of the Tender and at this stage it and/or the Company is unable to estimate its impact.

#### **Section 3.11.2 - Fair Credit Law**

On the Fair Credit Law which applies to transactions that will be performed from September 2019 - the activity of Pelephone with respect to all aspects of the sale of handsets, devices and other equipment in installments, constitutes "credit transactions" to which the Consumer Protection Law applies. Accordingly, the Fair Credit law which applies to a "credit transaction" does not apply to these transactions, including in light of its purpose, provisions and credit transactions that were excluded from the Law after its enactment.

#### **Section 3.15 – Material agreements**

Section 3.15.3 - agreement between Pelephone and the Accountant General at the Ministry of Finance - in May 2019, the State chose to exercise its right, as conferred upon it in the 2016 agreement to provide cellular services to the Accountant General, and the agreement was extended through August 2022.

#### **Section 3.16 – Legal proceedings**

Section 3.16.1(E) - motion to certify a class action alleging that Pelephone acted in a manner that amounted to harassment of a large consumer public by making repeated telephone calls aimed at

recruiting customers - on May 28, 2019 a judgment was issued dismissing the motion. In July 2019, the claimant filed an appeal on the judgment in the Supreme Court to certify the claim as a class action.

Section 3.16.1(N) - on a claim and motion for certification of a class action against Pelephone which alleges that Pelephone uses existing information in its possession regarding the location of its subscribers for its own business needs and sends them text messages pertaining to the sale of services relevant to their location - on July 8, 2019, the court authorized the applicants to abandon the motion for certification of the class action against Pelephone and it dismissed their personal claim against Pelephone.

In April 2019, a claim was filed in the Central District Court together with a motion for its certification as a class action against Pelephone and Bezeq International and against 6 other telecom companies (hereinafter together: "the Respondents"). The subject of the claim is the allegation that the Respondents neglect to inform their customers as necessary of the possible risks in use of the Internet and the option to subscribe to a free content filtering service, all this in contravention of the provisions of the Communications Law. Additionally, the Respondents provide a filtering service for websites and harmful content which, in their opinion, is inadequate. According to the petitioners, this represents, inter alia, a breach of the provisions of the Consumer Protection Law, breach of obligations under the Torts Ordinance, a breach of contract, and unjust enrichment. The overall loss assessment mentioned in the motion, for all the Respondents together as claimed, on the low side is tens of millions of shekels.

### **Section 3.19 – Discussion of Risk Factors**

#### **Section 3.19.3 – Risk factors for Pelephone**

Impairment of Pelephone's assets - in accordance with the accounting standards, Pelephone periodically tests for the impairment of assets regarding which there are indications of impairment.

Taking note of the business situation of Pelephone and the discrepancy, if there is any, between the carrying amount in the Pelephone's accounts and its recoverable amount as a cash-generating unit, any decline in the value of the activity could lead to the recording of an impairment loss (write-off) in Pelephone's books.

Additionally, a significant change in circumstances that leads to a change in estimates could occur due to a high-intensity isolated event and/or as the result of a sequence of small changes that occur over time, which have a significant cumulative effect in the long term and/or due to a change in estimates (even on a small scale) regarding the long term. Valuations rely on assumptions which are correct at the date of the report that might not materialize or could partially materialize and different perspectives affect, with varying intensity, the value of the activity, where assumptions for the long term have a relatively large weight compared with assumptions regarding the short term. These assumptions are sensitive to values in the representative year, to the discounting interest rate and the permanent growth rate.

On this matter, see also Note 5 to the Company's financial statements for the period ended June 30, 2019 and Section 2.1 in the Directors Report.

## **4. Bezeq International – International communications, Internet and NEP services**

### **Section 4.2 – Products and services**

In July 2019, Bezeq International expanded the marketing of bundles that include content services of yes in addition to Sting TV, together with Internet access services and Bezeq International's home phone line, and in addition DBS began to market the Internet access services of Bezeq International.

### **Section 4.8 – Human resources**

On July 11, 2019, Bezeq International signed a collective agreement with the New General Federation of Labor ("Histadrut") and the workers' representatives which includes streamlining measures and synergy for the period from July 11, 2019 through December 31, 2021. According to Bezeq International's plan and as per the agreement, Bezeq International will be able, inter alia, to cut back the employment of up to 325 workers (of which 150 are permanent employees, some as part of a voluntary retirement plan) in addition to the possibility of not recruiting new employees instead of those who terminate their employment. The agreement also includes granting a lump-sum bonus to employees who are not included in the retirement plan. The estimated cost of the agreement is about NIS 60 million,



assuming that all the rights of Bezeq International are exercised for the streamlining measures and that conditions for granting additional economic benefits to employees are satisfied.

#### **Section 4.11.5 – Key regulatory developments**

In June 2019 Bezeq International contacted the Ministry of Communications concerning the update of its engineering program to include the deployment of fiber optics, and on August 27, 2019 Bezeq International submitted to the Ministry of Communications a service file on the matter. These two issues are being examined by the Ministry.

#### **Section 4.12 – Legal proceedings**

Subsection A - On a class action from November 2011 concerning broadband speed, on July 9, 2019 a judgment was given accepting the class action and obligating Bezeq International to pay compensation to its private internet customers, in the total amount of NIS 9 million.

Subsection D - On a motion to certify a class action concerning the tariff for outgoing international calls - on July 4, 2019, a ruling was given denying the motion.

On July 25, 2019, a ruling of the Tel Aviv-Jaffa District Court was received certifying a motion for a class action against Bezeq International. The subject of the action is the allegation that excessive amounts were collected from its Internet service customers. The court ruled that the definition of the group will be any Bezeq International customer that entered into agreement with it for a fixed period and that after the fixed period, Bezeq International collected from the customer a higher price for the services provided to it under the agreement, without receipt of prior, written notice in accordance with the Consumer Protection Law, and without having given Bezeq International their agreement to receive notices and updates by email, in the seven years preceding the motion for certification and until today. The grounds for the claim for which the motion was certified are breach of a statutory duty and unjust enrichment. Bezeq International is studying the ruling and it will respond at the times stipulated by law. On a new motion to certify a class action that was filed against Bezeq International and Pelephone on the subject of content filtering services, see the update to Section 3.16. Notably, in 2015, a motion to certify a class action against Bezeq International was filed on similar grounds, which was certified as a class action in 2018 (described in Section 4.12(C) in the Description of Company Operations in the Company's Periodic Report for 2018).

#### **Section 4.14 – Discussion of Risk Factors**

Impairment of assets of Bezeq International

In accordance with the accounting standards, Bezeq International periodically tests for the impairment of assets regarding which there are indications of impairment.

Taking note of the business situation of Bezeq International and the discrepancy, if there is any, between the carrying amount in the Bezeq International's accounts and its recoverable amount as a cash-generating unit, any decline in the value of the activity could lead to the recording of an impairment loss (write-off) in Bezeq International's books.

Additionally, a significant change in circumstances that leads to a change in estimates could occur due to a high-intensity isolated event and/or as the result of a sequence of small changes that occur over time, which have a significant cumulative effect in the long term and/or due to a change in estimates (even on a small scale) regarding the long term. Valuations rely on assumptions which are correct at the date of the report that might not materialize or could partially materialize and different perspectives affect, with varying intensity, the value of the activity, where assumptions for the long term have a relatively large weight compared with assumptions regarding the short term. These assumptions are sensitive to values in the representative year, to the discounting interest rate and the permanent growth rate.

On this matter, see also Note 5 to the Company's financial statements for the period ended June 30, 2019 and Section 2.2 in the Directors Report.

### **5. Multi-channel television - DBS Satellite Services (1998) Ltd. ("DBS")**

#### **Section 5.2 – Products and services**

In July 2019, DBS began to market bundles that include its content services (satellite television services or Sting TV), together with Internet access services and Bezeq International's home phone line.

**Section 5.8.5 - Operating and encryption systems**

In June 2019, an assignment agreement was signed between DBS, Cisco and Synamedia in which Cisco's rights and liabilities under the agreement with DBS were transferred to Synamedia, and at the same time it was agreed that several past disputes that had emerged between DBS and Cisco will be settled between them separately.

**Section 5.11 – Human resources**

In Q2 2019, DBS began to implement the collective arrangement in connection with the streamlining and synergy processes. At August 28, 2019, DBS had a workforce of 1,350, a decrease of 12% compared with the number of employees at December 31, 2018.

**Section 5.13 - Financing**

In August 2019, the Company approved a credit facility or investment in the capital of DBS in the total amount of up to NIS 250 million, for a period of 15 months, from July 1, 2019. This approval is instead of similar approval given in May 2019 (and not in addition to it).

**Section 5.17.1 - Pending legal proceedings**

Subsection A - motion to certify a class action concerning electricity consumption by broadcasting equipment that belongs to DBS on apartment buildings - in June 2019, a ruling was received approving the compromise agreement that the parties submitted to the court at a cost of NIS 4 million to DBS. The compromise settlement also stipulates that DBS will take action to inform the apartment buildings with respect to bearing the cost of the communal electricity and will allow them to ask to disconnect the reception equipment from the communal electricity.

Subsection B - motion to certify a class action regarding advertisements allegedly sent by DBS to its customers - in June 2019, the court approved filing the action as a class action, solely on the grounds of a breach of the provisions of Section 30A of the Communications Law ("the Certification Decision"). The motion was approved with respect to non-financial loss only, while the applicants' arguments concerning financial loss were dismissed. Furthermore, the court ruled that the group will be defined as anyone who was a DBS customer from December 1, 2008 and up to the date of this ruling who received such advertisements, and had not given DBS their consent in advance to receive the advertisements. In July 2019, DBS filed a motion for permission to appeal the Certification Decision, together with a motion to stay its implementation, in the Supreme Court. In August 2019, the Supreme Court ruled a stay of implementation of the Certification Decision until a decision is made on the right to appeal. Similarly, in August 2019 the petitioners filed an application at the High Court to extend the date for submitting their appeal on the ratification ruling until a decision is made on the motion for permission to appeal.

Subsection D - motion to certify a class action which includes a claim that fixed-period transactions were renewed automatically while charging customers unilaterally and without their consent - in April 2019, a judgment was handed down in which the court approved the compromise settlement.

Subsection G, H and J (Pending legal proceedings in view of the investigation by the ISA and Israel Police) - see the update to Section 2.18.1, subsection H, I and L.

Subsection I - on a motion to certify a class action which was filed in the USA - see the update to Section 2.18 J.

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August 28, 2019

Date

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"Bezeq" The Israel Telecommunication Corporation Ltd.

Names and titles of signatories:

Shlomo Rodav, Chairman of the Board of Directors

Dudu Mizrahi, CEO

**Chapter B -  
Board of Directors' Report on the State of the  
Company's Affairs for the Period Ended  
June 30, 2019**



## Board of Directors' Report on the State of the Company's Affairs for the Period Ended June 30, 2019

We hereby present the Board of Directors' report on the state of affairs of "Bezeq" - The Israel Telecommunication Corporation Ltd. ("the Company") and the consolidated Group companies (the Company and the consolidated companies, jointly - "the Group"), for the six months ended June 30, 2019 ("Six Months") and the three months then ended ("Quarter").

The Board of Directors' report includes a condensed review of its subject-matter, and was prepared assuming the Board of Directors' report of December 31, 2018 is also available to the reader.

For information concerning the Israel Securities Authority and the Israel Police's investigation, see Note 1.2 to the financial statements.

The auditors have drawn attention to the matter in their opinion of the financial statements.

In its financial statements, the Group reports on four main operating segments:

1. **Domestic Fixed-Line Communications**
2. **Cellular Communications**
3. **International Communications, Internet and NEP Services**
4. **Multi-Channel Television**

It is noted that the Company's financial statements also include an "Others" segment, which comprises mainly online content services (through "Walla") and call center services (through "Bezeq Online"). The "Others" segment is immaterial at the Group level.

The Group's results were as follows:

	1-6.2019	1-6.2018	Increase (decrease)		4-6.2019	4-6.2018	Increase (decrease)	
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%
<b>Profit (loss)</b>	<b>(1,273)</b>	455	(1,728)	-	<b>(1,573)</b>	195	(1,768)	-
<b>EBITDA<sup>1</sup></b>	<b>1,361</b>	1,895	(534)	(28.2)	<b>384</b>	908	(524)	(57.7)

The decrease in the above results was mainly due to a decrease in operating profit, mainly due to NIS 951 million in impairment losses on goodwill in the Cellular Communications segment (see Note 5.1 to the financial statements). This decrease was partially offset by NIS 403 million in capital gains on the sale of a land asset in the Sakia property. See Note 7 to the financial statements.

The change in profits was also due to the Company's decision in the present Quarter to write-off the NIS 1,166 million tax asset for losses in DBS, by way of a change in an accounting estimate (see Note 6 to the financial statements).

EBITDA calculations	1-6.2019	1-6.2018	4-6.2019	4-6.2018
	NIS millions	NIS millions	NIS millions	NIS millions
Operating profit	417	833	(94)	371
Depreciation, amortization and impairment	944	1,062	478	537
<b>EBITDA</b>	<b>1,361</b>	1,895	<b>384</b>	908

<sup>1</sup> EBITDA - In light of the continued impairment of DBS's and Walla's property, plant and equipment and intangible assets, the definition for EBITDA was updated as from the first quarter of 2019, as follows: operating profit before depreciation and amortization and continued losses from impairment of property, plant and equipment and intangible assets (see Notes 3.1 and 5 to the financial statements).

**1. The Board of Directors' explanations on the state of the Company's affairs, the results of its operations, equity, cash flows, and additional matters**

**1.1 Financial position**

	June 30, 2019	June 30, 2018	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	
Cash and current investments	2,915	2,599	316	12.2	The increase was attributable to current investments in the Domestic Fixed-Line Communications segment, mainly in the second quarter of 2019.
Current and non-current trade and other receivables	2,567	2,582	(15)	(0.6)	
Inventory	100	96	4	4.2	
Broadcasting rights	59	467	(408)	(87.4)	The decrease was due to the asset's impairment in DBS. See Note 5.2 to the financial statements.
Usage right assets	1,394	1,424	(30)	(2.1)	
Property, plant and equipment	6,245	6,811	(566)	(8.3)	The decrease was mainly due to the asset's impairment in DBS. See Note 5.2 to the financial statements.
Intangible assets	977	2,687	(1,710)	(63.6)	The decrease was mainly due to a NIS 951 million impairment in goodwill attributed to the Cellular Communications segment in the present Quarter, and impairment and amortization of excess acquisition costs attributed to DBS and impairment of other intangible assets in DBS. See Note 5 to the financial statements.
Deferred tax assets	12	1,035	(1,023)	(98.8)	The decrease was due to the Company's decision to write off the tax asset from DBS's losses, to the amount of NIS 1,166 million starting from the present Quarter (see Note 6 to the financial statements). The decrease was slightly mitigated by the write-off of a tax reserve due to DBS's impairment in 2018.
Deferred costs and non-current investments	465	530	(65)	(12.3)	The decrease includes, among other things, impairment of a subscriber acquisition asset in DBS at the end of 2018, and impairment of assets in the International Communications, Internet, and NEP Services segment.
Investment property	-	130	(130)	(100)	The balance decreased after completion of the Sakia land asset's sale and recognition of capital gains. See Note 7 to the financial statements.
<b>Total assets</b>	<b>14,734</b>	<b>18,361</b>	<b>(3,627)</b>	<b>(19.8)</b>	

1.1. Financial Position (Contd.)

	June 30, 2019	June 30, 2018	Increase (decrease)	
	NIS millions	NIS millions	NIS millions	%
Debt to financial institutions and debenture holders	11,334	12,000	(666)	(5.6)
Liabilities for leases	1,456	1,451	5	0.3
Trade and other payables	1,427	1,583	(156)	(9.9)
Employee benefits	930	636	294	46.2
Tax liabilities	73	74	(1)	(1.4)
Other liabilities	350	360	(10)	(2.8)
<b>Total liabilities</b>	<b>15,570</b>	<b>16,104</b>	<b>(534)</b>	<b>(3.3)</b>
<b>Total equity (deficit equity)</b>	<b>(836)</b>	<b>2,257</b>	<b>(3,093)</b>	<b>-</b>

Explanation
Debenture and loan repayments, offset by new loans received and issuance of debentures in the Domestic Fixed-Line Communications segment.
The decrease was due, among other things, to timing differences on payments, due to the end of a month not being a business day in the corresponding period of last year.
The increase was due to a provision for an early retirement plan in the Domestic Fixed-Line Communications segment at the end of 2018, and in the Multi-Channel Television segment in the first half of 2019.
The equity deficit comprises 5.7% of the balance sheet total, as compared to positive equity of 12.3% of the balance sheet total on June 30, 2018. The transition to equity deficit was mainly due to the present Quarter's losses, incurred through goodwill impairment losses in the Cellular Communications segment and write-off of the tax asset for DBS's losses. Equity was further reduced by 2018's losses.

## 1.2 Results of operations

### 1.2.1 Highlights

	1-6.2019	1-6.2018	Increase (decrease)		4-6.2019	4-6.2018	Increase (decrease)	
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%
Revenues	<b>4,480</b>	4,694	(214)	(4.6)	<b>2,224</b>	2,333	(109)	(4.7)
General and operating expenses	<b>1,626</b>	1,679	(53)	(3.2)	<b>814</b>	838	(24)	(2.9)
Salaries	<b>981</b>	1,013	(32)	(3.2)	<b>489</b>	503	(14)	(2.8)
Depreciation, amortization and impairment	<b>944</b>	1,062	(118)	(11.1)	<b>478</b>	537	(59)	(11.0)
Other operating expenses (income), net	<b>(439)</b>	107	(546)	-	<b>(414)</b>	84	(498)	-
Impairment loss	<b>951</b>	-	951	-	<b>951</b>	-	951	-
Operating profit (loss)	<b>417</b>	833	(416)	(49.9)	<b>(94)</b>	371	(465)	-
Finance expenses, net	<b>235</b>	218	17	7.8	<b>136</b>	110	26	23.6
Share in losses of investees	<b>1</b>	2	(1)	(50.0)	<b>1</b>	1	-	-
Income tax	<b>1,454</b>	158	1,296	-	<b>1,342</b>	65	1,277	-
Profit (loss) for the period	<b>(1,273)</b>	455	(1,728)	-	<b>(1,573)</b>	195	(1,768)	-

Explanation
The decrease was due to lower revenues across all the Group's core segments (excluding the International Communications, Internet, and NEP segment, where revenues remained stable in the Quarter).
The decrease was mainly attributable to the Cellular Communications segment.
This decrease was attributable mainly to the International Communications, Internet and NEP Services segment.
The decrease in depreciation and amortization costs was mainly due to impairment of depreciable assets and excess costs in DBS in the fourth quarter of 2018. On the other hand, in the Quarter and Six Months the item included an ongoing impairment of DBS's assets (property, plant and equipment and intangible assets). See Note 5 to the financial statements.
The transition from expense to income was attributable to the Domestic Fixed Line Communications segment, mainly due to a capital gain of NIS 403 million on the sale of the Sakia land asset in the present Quarter (see Note 7 to the financial statements), and expenses from termination of employment by way of early retirement recognized in the same quarter last year. In the Six Months, this change was mitigated by NIS 45 million in expenses on an employee retirement arrangement in the Multi-Channel Television segment, (see Note 9.1 to the financial statements).
Loss from impairment of goodwill in Cellular Communications operations. See Note 5.1 to the financial statements.
The increase in net finance expenses was attributable to the Domestic Fixed-Line Communications and Multi-Channel Television segments.
In the present Quarter, the Company decided to write-off the tax asset from DBS's losses. The Company accordingly recognized NIS 1,166 million in tax expenses (see Note 6 to the financial statements). Furthermore, taxable profits were up, mainly due to capital gains on the sale of a land asset in the Sakia property.

1.2.2 Operating segments

A. Revenue and operating profit data, presented by the Group's operating segments:

	1-6.2019		1-6.2018		4-6.2019		4-6.2018	
	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues
<b>Revenues by operating segment</b>								
Domestic Fixed-Line Communications	2,063	46.0	2,127	45.3	1,020	45.9	1,064	45.6
Cellular Communications	1,148	25.6	1,221	26.0	570	25.6	602	25.8
International Communications, Internet and NEP Services	680	15.2	688	14.7	339	15.2	336	14.4
Multi-Channel Television	680	15.2	750	16.0	337	15.2	375	16.1
Other and adjustments	(91)	(2.0)	(92)	(2.0)	(42)	(1.9)	(44)	(1.9)
<b>Total</b>	<b>4,480</b>	<b>100</b>	<b>4,694</b>	<b>100</b>	<b>2,224</b>	<b>100</b>	<b>2,333</b>	<b>100</b>

	1-6.2019		1-6.2018		4-6.2019		4-6.2018	
	NIS millions	% of segment revenues	NIS millions	% of segment revenues	NIS millions	% of segment revenues	NIS millions	% of segment revenues
<b>Operating profit by segment</b>								
Domestic Fixed-Line Communications	1,406	68.2	860	40.4	875	85.8	387	36.4
Cellular Communications *	(18)	(1.6)	4	0.3	(8)	(1.4)	2	0.3
International Communications, Internet and NEP Services	52	7.6	64	9.3	18	5.3	30	8.9
Multi-Channel Television	(67)**	(9.9)	(18)	(2.4)	(8)**	(2.4)	(17)	(4.5)
Other and adjustments	(956)	-	(77)	-	(971)	-	(31)	-
<b>Consolidated operating profit (loss) / % of Group revenues.</b>	<b>417</b>	<b>9.3</b>	<b>833</b>	<b>17.7</b>	<b>(94)</b>	<b>(4.2)</b>	<b>371</b>	<b>15.9</b>

\* Impairment losses in Cellular Communications operations, detailed in Note 5.1 to the financial statements, are presented under adjustments.

\*\* The results of Multi-Channel Television operations are adjusted for impairment losses as detailed in Note 5.2 to the financial statements. These impairment losses are presented under adjustments.



1.2.2 Operating segments (contd.)

**B. Domestic Fixed-Line Communications Segment**

	1-6.2019	1-6.2018	Increase (decrease)		4-6.2019	4-6.2018	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Fixed-line telephony	533	593	(60)	(10.1)	264	291	(27)	(9.3)	The decrease was due to lower average revenues per phone line and a decrease in the number of lines.
Internet - infrastructure	793	799	(6)	(0.8)	396	403	(7)	(1.7)	Revenues were down, mainly due to a decrease in retail internet subscribers, offset by higher retail ARPU, alongside a downward trend in revenues from wholesale internet services since the start of 2019.
Transmission, data communications and others	598	607	(9)	(1.5)	292	304	(12)	(3.9)	The decrease was mainly due to lower revenues from data communications.
Digital and cloud services	139	128	11	8.6	68	66	2	3.0	The increase was mainly due to IP Centrex services.
Total revenues	2,063	2,127	(64)	(3.0)	1,020	1,064	(44)	(4.1)	
General and operating expenses	274	285	(11)	(3.9)	133	145	(12)	(8.3)	The decrease was mainly due to lower advertising expenses and lower payments to telecom operators, offset by higher expenses on terminal equipment and materials.
Salaries	464	460	4	0.9	231	232	(1)	(0.4)	
Depreciation and amortization	411	415	(4)	(1.0)	204	211	(7)	(3.3)	
Other operating expenses (income), net	(492)	107	(599)	-	(423)	89	(512)	-	The change was mainly due to capital gains on real estate sales, primarily NIS 403 million in capital gains on the sale of the Sakia land property in the present Quarter (see Note 7 to the financial statements). Furthermore, in the Six Months, the provision for termination of employment by way of early retirement was reduced, as compared to expenses from termination of employment by way of early retirement in the corresponding period and quarter of last year.
Operating profit	1,406	860	546	63.5	875	387	488	126.1	
Finance expenses, net	247	240	7	2.9	141	119	22	18.5	Net finance expenses were up, mainly due to finance expenses on employee benefits. This increase was offset in the Six Months by finance expenses recognized in the same period last year, following impairment in the fair value of the amount expected to have been returned to the Company on acquiring DBS.
Income tax	276	155	121	78.1	172	66	106	160.6	
Segment profit	883	465	418	89.9	562	202	360	178.2	

1.2.2 Operating segments (contd.)

**C. Cellular Communications segment**

	1-6.2019	1-6.2018	Increase (decrease)		4-6.2019	4-6.2018	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Services	<b>846</b>	869	(23)	(2.6)	<b>430</b>	438	(8)	(1.8)	The decrease was mainly due to lower rates and migration of existing customers to cheaper plans offering greater data volumes at current market prices. This decrease in rates was partially offset by growth in the post-paid customer base.
Equipment sales	<b>302</b>	352	(50)	(14.2)	<b>140</b>	164	(24)	(14.6)	The decrease was mainly due to a decrease in the number of handsets sold, and lower income per unit due to changes in the handset sales mix.
Total revenues	<b>1,148</b>	1,221	(73)	(6.0)	<b>570</b>	602	(32)	(5.3)	
General and operating expenses	<b>662</b>	703	(41)	(5.8)	<b>324</b>	345	(21)	(6.1)	The decrease was mainly due to a reduction in the cost of handset sales and continued downsizing and streamlining of operating expenses.
Salaries	<b>189</b>	195	(6)	(3.1)	<b>95</b>	95	-	-	The decrease in salary expenses in the first half of 2019 was mainly due to a decrease in the number of employee positions.
Depreciation and amortization	<b>312</b>	317	(5)	(1.6)	<b>156</b>	159	(3)	(1.9)	
Other operating expenses, net	<b>3</b>	2	1	50.0	<b>3</b>	1	2	200.0	
Operating profit (loss)	<b>(18)</b>	4	(22)	-	<b>(8)</b>	2	(10)	-	
Finance income, net	<b>23</b>	17	6	35.3	<b>10</b>	6	4	66.7	
Income tax	<b>1</b>	5	(4)	(80.0)	-	1	(1)	(100.0)	
Segment profit	<b>4</b>	16	(12)	(75.0)	<b>2</b>	7	(5)	(71.4)	

For information concerning impairment in the Cellular Communications segment, see Note 5.1 to the financial statements.

1.2.2 Operating segments(contd.)

**D. International Communications, Internet and NEP Services**

	1-6.2019	1-6.2018	Increase (decrease)		4-6.2019	4-6.2018	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Revenues	680	688	(8)	(1.2)	339	336	3	0.9	In the Six Months, the decrease was mainly due to lower revenues from international calls and internet operations and the sale of outsourcing operations in the second quarter of 2018. This decrease was offset by higher revenues from services and equipment to businesses.
General and operating expenses	388	377	11	2.9	194	187	7	3.7	The increase was due to higher local and international bandwidth expenses and higher cost of sales on licensing and equipment to businesses. The increase was partially offset, mainly by lower international call expenses.
Salaries	133	158	(25)	(15.8)	66	75	(9)	(12.0)	The decrease was due to a reduction in the number of employees and the sale of outsourcing operations in the second quarter of 2018.
Depreciation and amortization	92	88	4	4.5	46	45	1	2.2	The increase was due to an increase in the amortization of the subscriber acquisition asset and amortization of international bandwidth.
Other finance expenses (income)	15	1	14	-	15	(1)	16	-	The increase was due to an increase in provisions for legal claims.
Operating profit	52	64	(12)	(18.8)	18	30	(12)	(40.0)	
Finance expenses, net	7	7	-	-	5	4	1	25.0	
Tax expenses	10	13	(3)	(23.1)	3	6	(3)	(50.0)	
Segment profit	35	44	(9)	(20.5)	10	20	(10)	(50.0)	

1.2.2 Operating segments (contd.)

**E. Multi-Channel Television**

	1-6.2019*	1-6.2018	Increase (decrease)		4-6.2019*	4-6.2018	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Revenues	<b>680</b>	750	(70)	(9.3)	<b>337</b>	375	(38)	(10.1)	The decrease was mainly due to a decrease in the customer base and in ARPU.
General and operating expenses	<b>448</b>	483	(35)	(7.2)	<b>222</b>	246	(24)	(9.8)	The decrease was mainly due to lower advertising, marketing, and content expenses.
Salaries	<b>106</b>	118	(12)	(10.2)	<b>51</b>	60	(9)	(15.0)	The decrease was mainly due to a decrease in the number of employee positions.
Depreciation and amortization	<b>159</b>	158	1	0.6	<b>81</b>	79	2	2.5	
Other operating expenses (income), net	<b>34</b>	9	25	-	<b>(9)</b>	7	(16)	-	In the Six Months, the increase was mainly due to expenses from an employee retirement agreement (see Note 9.1 to the financial statements), offset by an update to the provision for legal claims. In the Quarter, the change, was mainly due to an update to the provision for legal claims.
Operating loss	<b>(67)</b>	(18)	(49)	-	<b>(8)</b>	(17)	9	(52.9)	
Finance expenses (income), net	<b>7</b>	(10)	17	-	<b>2</b>	(7)	9	-	The change in net finance expenses was mainly due to a change in the fair value of financial assets.
Tax expenses	<b>1</b>	1	-	-	<b>1</b>	-	1	-	
Segment loss	<b>(75)</b>	(9)	(66)	-	<b>(11)</b>	(10)	(1)	10.0	

\* The Multi-Channel Television segment's results for the Six Months and Quarter are presented net of impairment. See Notes 5.2 and 17 to the financial statements. This matches the way that the Group's chief operating decision maker assesses the segment's performance and decides on resource allocations for the segment. Furthermore, see Note 18.3 for highlights from DBS's financial statements.

### 1.3 Cash flow

	1-6.2019	1-6.2018	Change		4-6.2019	4-6.2018	Change		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Net cash from operating activities	1,389	1,715	(326)	(19.0)	624	806	(182)	(22.6)	The decrease in net cash from operating activities was mainly due to changes in working capital and employee retirement payments, partially offset by a decrease in income tax payments on final tax assessments in the corresponding period last year. The decrease in net cash was reported across all of the Group's core segments.
Net cash used in investing activities	(1,049)	(2,311)	1,262	(54.6)	(781)	(860)	79	(9.2)	The present Quarter included inflows from the sale of the Sakia property, as compared to betterment tax payments on this sale in the same quarter last year. Furthermore, in the Six Months there was a decrease (in the Quarter - an increase) in net investment in bank and other deposits in the Domestic Fixed-Line Communications segment.
Net cash used in financing activities	(259)	(662)	403	(60.9)	(137)	(849)	712	(83.9)	The decrease in net cash used in financing activities was due to a loan received in the present Quarter in the Domestic Fixed-Line Communications segment, and a dividend payment in the same quarter last year, offset by an increase in loan repayments.
Net increase (decrease) in cash	81	(1,258)	1,339	-	(294)	(903)	609	(67.4)	

#### Average volume in the reporting Period:

Long-term liabilities (including current maturities) to financial institutions and debenture holders - NIS 11,206 million.

Supplier credit: NIS 854 million. Short-term credit to customers: NIS 1,759 million. Long-term credit to customers: NIS 330 million.

#### Working Capital

As of June 30, 2019, the Group had a working capital surplus of NIS 950 million, as compared to a working capital surplus of NIS 555 million on June 30, 2018.

According to its separate financial statements, the Company had a working capital surplus of NIS 763 million as of June 30, 2019, as compared to a working capital surplus of NIS 490 million on June 30, 2018.

This increase in the Group's and the Company's working capital surplus was mainly due to an increase in current investments and a decrease in current liabilities on debentures and loans.

#### 1.4 Disclosure concerning the Company's forecast cash flows

According to Regulation 10(b)(14) to the Securities Regulations (Periodic and Immediate Reports), 1970 and given the warning sign of a deficit in equity in the Company's separate financial statements and in the consolidated statements, the Company hereby presents its forecasted cash flow statement, detailing its monetary sources and uses for the period starting July 1, 2019 and ending December 31, 2021.

Forecast cash flows	From Jul. 1, 2019 to Dec. 31, 2019	From Jan. 1, 2020 to Dec. 31, 2020	From Jan. 1, 2021 to Dec. 31, 2021
Company – separate	NIS millions	NIS millions	NIS millions
<b>Cash and cash equivalents – opening balance</b>	<b>648 *</b>	<b>776</b>	<b>1,424</b>
<b><u>Sources – Company</u></b>			
<b>Total net cash from operating activities</b>	<b>946</b>	<b>1,892</b>	<b>1,976</b>
Proceeds from sale of fixed assets	53	270	29
Proceeds from redemption of bank and other deposits	1,328	639	-
Misc.	1	14	22
<b>Total cash from investing activities</b>	<b>1,382</b>	<b>923</b>	<b>51</b>
Debt issues and loans	1,888	350	400
<b>Total cash from financing activities</b>	<b>1,888</b>	<b>350</b>	<b>400</b>
<b>Total sources – Company</b>	<b>4,216</b>	<b>3,165</b>	<b>2,427</b>
<b><u>Sources from investees</u></b>			
Dividends from investees	-	-	36
Loans from investees	40	-	45
Repayment of loans issued to investees	15	63	52
Misc.	1	3	1
<b>Total cash from investees</b>	<b>56</b>	<b>66</b>	<b>134</b>
<b>Total sources</b>	<b>4,272</b>	<b>3,231</b>	<b>2,561</b>
<b><u>Expected liabilities (expected uses) – Company</u></b>			
Fixed asset purchases and investment in intangible assets	(376)	(912)	(915)
Investment in bank deposits and securities	(55)	-	-
<b>Total cash used in investing activities</b>	<b>(431)</b>	<b>(912)</b>	<b>(915)</b>
Repayment of bank loans	(921)	(216)	(216)
Repayment of debentures (public)	(1,112)	(669)	(679)
Repayment of private debentures and off-bank credit	(1,167)	(62)	(123)
Principal and interest payments on leases	(59)	(113)	(102)
Interest payments and other financing expenses	(287)	(339)	(319)
Misc.	(44)	(48)	(24)
<b>Total cash used in financing activities</b>	<b>(3,590)</b>	<b>(1,447)</b>	<b>(1,463)</b>
<b>Total uses – Company</b>	<b>(4,021)</b>	<b>(2,359)</b>	<b>(2,378)</b>

\* The Company has investments in deposits and monetary funds to the amount of NIS 1,911 million, available for short-term use.

Forecast cash flows	From Jul. 1, 2019 to Dec. 31, 2019	From Jan. 1, 2020 to Dec. 31, 2020	From Jan. 1, 2021 to Dec. 31, 2021
Company – separate	NIS millions	NIS millions	NIS millions
<b><u>Uses for investees</u></b>			
Investment in a subsidiary	(95)	(195)	(125)
Interest payment	(28)	(29)	(31)
<b><u>Total cash used in investees</u></b>	<b>(123)</b>	<b>(224)</b>	<b>(156)</b>
<b>Total uses</b>	<b>(4,144)</b>	<b>(2,583)</b>	<b>(2,534)</b>
<b>Cash and cash equivalents – closing balance</b>	<b>776</b>	<b>1,424</b>	<b>1,451</b>

**The assumptions underlying the cash flow forecast:**

1. The Company's forecast concerning cash flows from operating activities and cash flows used in investing activities:
  - a. The Company's and its investees' forecast for the period of July 1, 2019 to December 31, 2019 is based on the Company's budget and the budgets of its investees, with such adjustments as required in light of actual performance and changing conditions.
  - b. The Company's cash flow forecast for 2020 and 2021 is based on the long-term plan and relies, among other things, on the Company's performance in recent years and assessments concerning expected trends in the telecom market in the coming years. This includes assessments concerning market competition, price levels, consumer preferences, regulatory arrangements, technological developments, and the general condition of the Israeli economy. Operating, sales and marketing expenses have been adjusted to the projected scope of operations, and the forecast includes assumptions concerning streamlining of the Company's workforce and the associated retirement and salary costs.
  - c. Cash flow forecasts for the investees are identical to the forecasts used in estimating the recoverable amount as detailed in Note 11 to the Company's consolidated financial statements as of December 31, 2018 and Note 5 to the interim consolidated financial statements as of June 30, 2019.
  - d. The forecasts do not include the effects of cancelling the structural separation in the Group, the merger with the subsidiaries, and the subsequent implications of such merger, should it occur in the forecast period.

2. Material liabilities expected to be settled in the first six months of the forecast cash flow period

Principal repayments for the period of July 1, 2019 to December 31, 2019, based on the Company's amortization schedules:

October 2019 – NIS 56 million in repayment of bank loans.

November 2019 – NIS 62 million in repayment of bank loans; and NIS 67 million in repayment of public debentures, private debentures and off-bank credit.

December 2019 – NIS 775 million in repayment of public debentures; and NIS 50 million in repayment of private debentures and non-bank credit.

Early repayments in the period of July 1, 2019 to December 31, 2019:

July 2019 – early repayment was made on bank loans, to the amount of NIS 438 million.

In the period of September-December 2019, the Company plans to make early repayments on its public debentures, private debentures, off-bank credit and bank loans, to a total amount of NIS 1,752 million.

Sources for liability settlement

The Company has sufficient sources for meeting its liabilities, both by cash from its operating activities, and by cash balances and investments in deposits and monetary funds available for short-term use, and by raising debt from both banking and off-bank sources.

3. The Board of Directors has reviewed and approved the sources included in the disclosure concerning the forecast cash flows after having found them reasonable in terms of the monetary value of each source and its expected timing. The Board of Directors has further reviewed whether there are any restrictions on receiving dividends, loans, and loan repayments from investees, and is satisfied that they are expected to be received on time.

**The above information concerning the forecast cash flows constitutes forward-looking information.**

**The Company's assumptions and estimates concerning the forecast cash flows, sources for settling the Company's existing and expected liabilities, and concerning the assumptions underlying the forecast cash flows are based on data available to the Company as of the reporting date, and assuming it will continue to operate under the normal course of its business. There is no guarantee that these assumptions and estimates or any part thereof will materialize, as they depend on external factors outside the Company's control or on which the Company has limited control, and in light of current uncertainty in the Israeli telecom market in general. Actual data may differ materially from the above assessments should a change occur in any of the factors underlying these assessments.**



## **2. Disclosure Concerning the Company's Financial Reporting**

### **2.1 Disclosure of valuations**

The following table discloses valuations pursuant to Regulation 8B to the Securities Regulations (Periodic and Immediate Reports), 1970:

	<b>DBS - Extremely Material Valuation Attached to the financial statements as of June 30, 2019</b>	<b>Pelephone - Extremely Material Valuation Attached to the financial statements as of June 30, 2019</b>
Subject of valuation	Net disposal value of DBS Satellite Services (1998) Ltd.'s assets, to test for impairment of intangible assets.	Pelephone's EV to test for impairment of goodwill attributed for its operations in the Company's financial statements pursuant to IAS 36.
Date of valuation	June 30, 2019; valuations signed on August 25, 2019.	
Value prior to the valuation	Negative amount of NIS (80) million.	NIS 2,165 carrying amount of Pelephone's net operating assets * (NIS 1,027 million - balance of goodwill).
Value set in the valuation	Negative amount of NIS (199) million.	NIS 1,214 million. The Company concluded that there is impairment requiring a write-down of NIS 951 million in goodwill recognized in the Company's books.
Assessor's identity and profile	Prometheus Financial Advisory Ltd. The work was done by a team headed by Mr. Gideon Peletz, CPA, who holds a BA in Accounting and Economics from the Tel Aviv University. Mr. Peletz has extensive experience performing valuations, financial statement analyses, preparing expert opinions, and providing various financial advisory services for companies and businesses. The assessor has no dependence on the Company. The Company has undertaken to indemnify the assessor for damages exceeding three times their fee, unless they acted maliciously.	
Valuation model	Disposal value	Discounted Cash Flow method (DCF)
Assumptions used in the valuation	Assumptions concerning the net disposal value of DBS's assets.	Discount rate – 10.27% Permanent growth rate - 2.5% Scrap value of total value set – 96%

\* Pelephone's net operating assets do not include trade receivable balances from installment-based handset sales, which are presented at present value.

**For more information, see Note 5 to the financial statements.**

Despite the negative value of DBS's operations, the Company supports DBS by approving credit facilities or investing in DBS's equity (see Note 4.3 to the financial statements). The Company's support of DBS as aforesaid is due, among other things, to the Multi-Channel Television segment's current and expected contribution to the Bezeq Group's overall operations.

### **2.2 Testing for impairment of International Communications, Internet Services and NEP operations**

Following on Section 3.2 to the Company's Board of Directors' Report of December 31, 2018, concerning a material valuation of Bezeq International, the latter performed a formal review to test for signs of impairment as of June 30, 2019. This review was performed in accordance with IAS 36 and in view of the small difference measured as of December 31, 2018 between the value of Bezeq International's operations (NIS 1,061), and the carrying amount of its net operating assets (NIS 828 million). As of the financial statements' date, no signs were found for impairment.

It is clarified that the value of these operations are affected by assessments and forecasts concerning a long list of factors with various levels of influence on the value of operations, and that cash flows in the representative year significantly affect EV and changes in assessments concerning these cash flows significantly affect the valuation. It is further clarified that internet operations are a key source of profit for Bezeq International, and changes in market trends in this segment without an offsetting effect in Bezeq International's other operations may materially affect the valuation.

- 2.3** Due to claims filed against the Group, and for which exposure cannot yet be estimated or assessed at this time, the auditors have drawn attention to the matter in their opinion of the financial statements.
- 2.4** For information on **material events subsequent to the financial statements' date**, see Notes 19, 9.2, and 8 to the financial statements.

**3. Details of debt certificate series**

On April 8, 2019, Midroog Ltd. ("Midroog") maintained its Aa2.il rating for the Company's Debentures (Series 6,7,9, and 10) and changed its outlook from stable to negative (see immediate report, ref. no. 2019-01-032406). Furthermore, on May 7, 2019, S&P Global Ratings Maalot Ltd. ("Maalot") affirmed its ilAA/Negative rating for the Company (see immediate report, ref. no. 2019-01-039834).

On August 6, 2019, Midroog posted an issuer comment concerning the Company's debentures, while maintaining its Aa2.il/Negative rating for the debentures (see immediate report, ref. no. 2019-01-067917).

On August 12, 2019, Maalot announced that it was downgrading the Company and its subsidiaries, and of the Company's debentures, to ilAA-/Negative following continued erosion in its operating results (see immediate report, ref. no. 2019-01.068886).

The rating reports are included in this Board of Directors' Report by way of reference.

**4. Miscellaneous**

For information concerning the liabilities balances of the reporting corporation and those companies consolidated in its financial statements as of June 30, 2019, see the Company's reporting form on the MAGNA system, dated August 29, 2019.

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

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Shlomo Rodav  
Chairman of the Board

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Dudu Mizrahi  
CEO

Signed: August 28, 2019

# Part C: Condensed Consolidated Interim Financial Statements as at June 30, 2019 (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.

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Review Report to the Shareholders of  
**“Bezeq” -The Israel Telecommunication Corporation Ltd.**

*Introduction*

We have reviewed the accompanying financial information of “Bezeq” -The Israel Telecommunication Corporation Ltd. and its subsidiaries (hereinafter – “the Group”) comprising of the condensed consolidated interim statement of financial position as of June 30, 2019 and the related condensed consolidated interim statements of income, comprehensive income, changes in equity and cash flows for the six-month and three-month periods then ended. The Board of Directors and Management are responsible for the preparation and presentation of this interim financial information in accordance with IAS 34 “Interim Financial Reporting”, and are also responsible for the preparation of financial information for this interim period in accordance with Section D of the Securities Regulations (Periodic and Immediate Reports), 1970. Our responsibility is to express a conclusion on this interim financial information based on our review.

We did not review the condensed interim financial information of a certain consolidated subsidiary whose assets constitute 1 % of the total consolidated assets as of June 30, 2019, and whose revenues constitute 1% of the total consolidated revenues for the six-month and three-month periods then ended. The condensed interim financial information of that company was reviewed by other auditors whose review report thereon was furnished to us, and our conclusion, insofar as it relates to amounts emanating from the financial information of that company, is based solely on the said review report of the other auditors.

*Scope of Review*

We conducted our review in accordance with Standard on Review Engagements 1, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" of the Institute of Certified Public Accountants in Israel. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards in Israel and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

*Conclusion*

Based on our review and the review report of other auditors, nothing has come to our attention that causes us to believe that the accompanying financial information was not prepared, in all material respects, in accordance with IAS 34.

In addition to that mentioned in the previous paragraph, based on our review and the review report of other auditors, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not comply, in all material respects, with the disclosure requirements of Section D of the Securities Regulations (Periodic and Immediate Reports), 1970.

Without qualifying our abovementioned conclusion, we draw attention to Note 1.2 which refers to Note 1.2 to the annual consolidated financial statements, regarding the Israel Securities Authority’s (ISA) investigation of the suspicion of committing offenses under the Securities’ Law and Penal Code, in respect to transactions related to the former controlling shareholder, and the transfer of the investigation file to the District Attorney’s



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Office, and as mentioned in that note regarding the joint investigation by the Securities Authority and the Unit for Combating Economic Crime at Lahav 433 and to the publication of the Attorney General's decision, by which he is considering charging the former controlling shareholder with criminal charges. As stated in the above note, at this stage, the Company is unable to assess the effects of the investigations, their findings and their results on the Company, and on the financial statements and on the estimates used in the preparation of these financial statements, if any.

In addition, without qualifying our abovementioned conclusion, we draw attention to lawsuits filed against the Group which cannot yet be assessed or the exposure in respect thereof cannot yet be estimated, as set forth in Note 10.

Somekh Chaikin  
Certified Public Accountants (Isr.)

August 28, 2019

**Condensed Consolidated Interim Statements of Financial Position**

		June 30, 2019	June 30, 2018	December 31, 2018
		(Unaudited)	(Unaudited)	(Audited)
Assets	Note	NIS million	NIS million	NIS million
Cash and cash equivalents		971	923	890
Investments		1,944	1,676	1,404
Trade receivables		1,744	1,822	1,773
Other receivables		288	313	267
Inventory		100	96	97
<b>Total current assets</b>		<b>5,047</b>	<b>4,830</b>	<b>4,431</b>
Trade and other receivables		535	447	470
Broadcasting rights, net of rights exercised		59	467	60
Right-of-use assets		1,394	1,424	1,504
Fixed assets		6,245	6,811	6,214
Intangible assets	5.1	977	2,687	1,919
Deferred tax assets	6	12	1,035	1,205
Deferred expenses and non-current investments		465	530	462
Investment property	7	-	130	58
<b>Total non-current assets</b>		<b>9,687</b>	<b>13,531</b>	<b>11,892</b>
<b>Total assets</b>		<b>14,734</b>	<b>18,361</b>	<b>16,323</b>

The attached notes are an integral part of the condensed consolidated interim financial statements

**Condensed Consolidated Interim Statements of Financial Position (Contd.)**

		June 30, 2019	June 30, 2018	December 31, 2018
		(Unaudited)	(Unaudited)	(Audited)
Liabilities and equity	Note	NIS million	NIS million	NIS million
Debentures, loans and borrowings	8	1,625	1,796	1,542
Current maturities of liabilities for leases		434	417	445
Trade and other payables		1,427	1,583	1,690
Employee benefits	9	443	369	581
Provisions	10	148	110	175
Current tax liabilities		20	-	-
<b>Total current liabilities</b>		<b>4,097</b>	<b>4,275</b>	<b>4,433</b>
Loans and debentures	8	9,709	10,204	9,637
Liability for leases		1,022	1,034	1,106
Employee benefits	9	487	267	445
Derivatives and other liabilities		163	210	174
Liabilities for deferred taxes		53	74	56
Provisions		39	40	38
<b>Total non-current liabilities</b>		<b>11,473</b>	<b>11,829</b>	<b>11,456</b>
<b>Total liabilities</b>		<b>15,570</b>	<b>16,104</b>	<b>15,889</b>
<b>Total equity (deficit)</b>		<b>(836)</b>	<b>2,257</b>	<b>434</b>
<b>Total liabilities and equity</b>		<b>14,734</b>	<b>18,361</b>	<b>16,323</b>

**Shlomo Rodav**  
Chairman of the Board of Directors

**Dudu Mizrahi**  
CEO

**Yali Rothenberg**  
Bezeq Group CFO

Date of approval of the financial statements: August 28, 2019



<b>Condensed Consolidated Interim Statements of Income</b>					
	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Revenues (Note 13)</b>	<b>4,480</b>	4,694	<b>2,224</b>	2,333	9,321
<b>Costs of activity</b>					
General and operating expenses (Note 14)	<b>1,626</b>	1,679	<b>814</b>	838	3,379
Salaries	<b>981</b>	1,013	<b>489</b>	503	1,992
Depreciation, amortization, and impairment losses (Notes 3.1 and 5)	<b>944</b>	1,062	<b>478</b>	537	2,189
Other operating expenses (income), net (Note 15)	<b>(439)</b>	107	<b>(414)</b>	84	634
Impairment loss (Note 3.1 and 5)	<b>951</b>	-	<b>951</b>	-	1,675
<b>Total operating expenses</b>	<b>4,063</b>	3,861	<b>2,318</b>	1,962	9,869
<b>Operating profit (loss)</b>	<b>417</b>	833	<b>(94)</b>	371	(548)
<b>Financing expenses (income)</b>					
Financing expenses	<b>262</b>	256	<b>149</b>	129	516
Financing income	<b>(27)</b>	(38)	<b>(13)</b>	(19)	(81)
Financing expenses, net	<b>235</b>	218	<b>136</b>	110	435
<b>Profit (loss) after financing expenses, net</b>	<b>182</b>	615	<b>(230)</b>	261	(983)
<b>Share in losses of equity-accounted investees</b>	<b>(1)</b>	(2)	<b>(1)</b>	(1)	(3)
<b>Profit (loss) before income tax</b>	<b>181</b>	613	<b>(231)</b>	260	(986)
<b>Taxes on income (see Note 6)</b>	<b>1,454</b>	158	<b>1,342</b>	65	80
<b>Profit (loss) for the period</b>	<b>(1,273)</b>	455	<b>(1,573)</b>	195	(1,066)
<b>Earnings per share (NIS)</b>					
<b>Basic earnings (loss) per share (in NIS)</b>	<b>(0.46)</b>	0.16	<b>(0.57)</b>	0.07	(0.39)

**Condensed Consolidated Interim Statements of Comprehensive Income (Loss)**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Profit (loss) for the period	(1,273)	455	(1,573)	195	(1,066)
Remeasurement of a defined benefit plan	(2)	-	-	-	16
Items of other comprehensive income (loss) (net of tax)	5	26	(10)	5	26
<b>Total comprehensive income (loss) for the period</b>	<b>(1,270)</b>	<b>481</b>	<b>(1,583)</b>	<b>200</b>	<b>(1,024)</b>

**Condensed Consolidated Interim Statements of Changes in Equity (Equity Deficit)**

	Share capital	Share premium	Capital reserve for transactions between a corporation and a controlling shareholder	Other reserves	Deficit	Total
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Attributable to shareholders of the Company</b>						
<b>Six months ended June 30, 2019 (Unaudited):</b>						
<b>Balance as at January 1, 2019</b>	3,878	384	390	(59)	(4,159)	434
Loss for the period	-	-	-	-	(1,273)	(1,273)
Other comprehensive income (loss) for the period, net of tax	-	-	-	5	(2)	3
Total comprehensive income (loss) for the period	-	-	-	5	(1,275)	(1,270)
<b>Balance as at June 30, 2019</b>	<b>3,878</b>	<b>384</b>	<b>390</b>	<b>(54)</b>	<b>(5,434)</b>	<b>(836)</b>
<b>Six months ended June 30, 2018 (Unaudited):</b>						
<b>Balance as at January 1, 2018</b>	3,878	384	390	(85)	(2,423)	2,144
Profit for the period	-	-	-	-	455	455
Other comprehensive income for the period, net of tax	-	-	-	26	-	26
Total comprehensive income for the period	-	-	-	26	455	481
<b>Transactions with shareholders recognized directly in equity</b>						
Dividend to Company shareholders	-	-	-	-	(368)	(368)
<b>Balance as at June 30, 2018</b>	<b>3,878</b>	<b>384</b>	<b>390</b>	<b>(59)</b>	<b>(2,336)</b>	<b>2,257</b>
<b>Three months ended June 30, 2019 (Unaudited)</b>						
<b>Balance as at April 1, 2019</b>	3,878	384	390	(44)	(3,861)	747
Loss for the period	-	-	-	-	(1,573)	(1,573)
Other comprehensive loss for the period, net of tax	-	-	-	(10)	-	(10)
Total comprehensive income for the period	-	-	-	(10)	(1,573)	(1,583)
<b>Balance as at June 30, 2019</b>	<b>3,878</b>	<b>384</b>	<b>390</b>	<b>(54)</b>	<b>(5,434)</b>	<b>(836)</b>
<b>Three months ended June 30, 2018 (Unaudited)</b>						
<b>Balance as at April 1, 2018</b>	3,878	384	390	(64)	(2,163)	2,425
Profit for the period	-	-	-	-	195	195
Other comprehensive income for the period, net of tax	-	-	-	5	-	5
Total comprehensive income for the period	-	-	-	5	195	200
<b>Transactions with shareholders recognized directly in equity</b>						
Dividend to Company shareholders	-	-	-	-	(368)	(368)
<b>Balance as at June 30, 2018</b>	<b>3,878</b>	<b>384</b>	<b>390</b>	<b>(59)</b>	<b>(2,336)</b>	<b>2,257</b>

The attached notes are an integral part of the condensed consolidated interim financial statements

**Condensed Consolidated Interim Statements of Changes in Equity (Equity Deficit) (Contd.)**

	Share capital	Share premium	Capital reserve for transactions between a corporation and a controlling shareholder	Other reserves	Deficit	Total
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Attributable to shareholders of the Company</b>						
<b>Year ended December 31, 2018 (Audited)</b>						
Balance as at January 1, 2018	3,878	384	390	(85)	(2,423)	2,144
Loss in 2018	-	-	-	-	(1,066)	(1,066)
Other comprehensive income for the year, net of tax	-	-	-	26	16	42
<b>Total comprehensive income (loss) for 2018</b>	-	-	-	26	(1,050)	(1,024)
<b>Transactions with shareholders recognized directly in equity</b>						
Dividend to Company shareholders	-	-	-	-	(686)	(686)
<b>Balance as at December 31, 2018</b>	<b>3,878</b>	<b>384</b>	<b>390</b>	<b>(59)</b>	<b>(4,159)</b>	<b>434</b>

**Condensed Consolidated Interim Statements of Cash Flows**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Cash flows from operating activities</b>					
Profit (loss) for the period	(1,273)	455	(1,573)	195	(1,066)
Adjustments:					
Depreciation, amortization, and impairment losses	944	1,062	478	537	2,189
Impairment loss of assets	951	-	951	-	1,675
Share in losses of equity-accounted investees	1	2	1	1	3
Financing expenses, net	224	224	128	113	445
Capital gain, net	(461)	(6)	(417)	(5)	(15)
Taxes on income (see Note 6)	1,454	158	1,342	65	80
Change in trade and other receivables	18	134	46	60	241
Change in inventory	(9)	13	-	18	(5)
Change in trade and other payables	(176)	(110)	(185)	(152)	(138)
Change in provisions	(27)	15	3	7	81
Change in employee benefits	(98)	84	(52)	77	489
Change in other liabilities	(6)	(16)	6	(17)	-
Net income tax paid	(153)	(300)	(104)	(93)	(467)
<b>Net cash from operating activities</b>	<b>1,389</b>	<b>1,715</b>	<b>624</b>	<b>806</b>	<b>3,512</b>
<b>Cash flow used for investing activities</b>					
Purchase of fixed assets	(551)	(581)	(281)	(308)	(1,216)
Investment in intangible assets and deferred expenses	(198)	(206)	(95)	(111)	(390)
Investment in bank deposits and securities	(1,780)	(1,934)	(669)	(764)	(2,338)
Proceeds from bank deposits and others	1,237	563	71	488	1,244
Proceeds from the sale of fixed assets	49	31	18	23	160
Receipts on account of sale of the Sakia property	328	-	323	-	155
Payment of permit fees, betterment tax, and purchase tax for the Sakia property	(149)	(112)	(149)	(112)	(121)
Receipt (payment) of betterment tax for the sale of the Sakia property	5	(80)	-	(80)	(80)
Miscellaneous	10	8	1	4	34
<b>Net cash used in investing activities</b>	<b>(1,049)</b>	<b>(2,311)</b>	<b>(781)</b>	<b>(860)</b>	<b>(2,552)</b>

The attached notes are an integral part of the condensed consolidated interim financial statements

**Condensed Consolidated Interim Statements of Cash Flows (Contd.)**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Cash flow from financing activities</b>					
Issue of debentures and receipt of loans	500	320	500	-	891
Repayment of debentures and loans	(362)	(182)	(362)	(182)	(1,567)
Payments of principal and interest for leases	(207)	(221)	(90)	(96)	(422)
Interest paid	(190)	(204)	(185)	(199)	(421)
Dividends paid	-	(368)	-	(368)	(686)
Miscellaneous	-	(7)	-	(4)	(46)
<b>Net cash used for financing activities</b>	<b>(259)</b>	<b>(662)</b>	<b>(137)</b>	<b>(849)</b>	<b>(2,251)</b>
<b>Increase (decrease) in cash and cash equivalents, net</b>	<b>81</b>	<b>(1,258)</b>	<b>(294)</b>	<b>(903)</b>	<b>(1,291)</b>
Cash and cash equivalents at beginning of period	890	2,181	1,265	1,826	2,181
Cash and cash equivalents at end of period	971	923	971	923	890

## **1. General**

### **1.1 Reporting Entity**

Bezeq – The Israel Telecommunication Corporation Limited (“the Company”) is a company registered in Israel whose shares are traded on the Tel Aviv Stock Exchange. The condensed consolidated financial statements of the Company as at June 30, 2019 include those of the Company and its subsidiaries (jointly referred to as “the Group”). The Group is a principal provider of communication services in Israel (see also Note 17 – Segment Reporting).

### **1.2 Investigations of the Israel Securities Authority and the Police Force**

For information about the investigations of the Israel Securities Authority and the Police Force, see Note 1.2 to the Annual Financial Statements.

As set out in Note 1.2.3 to the Annual Financial Statements, the Company does not have full information about the investigations, their content, the materials, and the evidence in the possession of the legal authorities. Accordingly, the Company is unable to assess the effects of the investigations, their findings, and their results on the Company, as well as on the financial statements, and on the estimates used in the preparation of these financial statements, if any. Once the constraints on carrying out reviews and controls related to issues that arose in the Investigations are lifted, the review of all matters related to subjects that arose during those Investigations will be completed as required.

### **1.3 Control in the Company**

On August 8, 2019, B Communications Ltd. (the controlling shareholder, linked, of the Company, which is controlled by Internet Gold - Golden Lines Ltd. (“Internet Gold”) informed the Company that, following the signing of a binding agreement with Searchlight Partners Capital LP (“Searchlight”) and a corporation controlled by the Fuhrer family for the acquisition of shares of Internet Gold at B Communications and another investment in B Communications on June 24, 2019, all the approvals required by the organs of B Communications and the parent company, Internet Gold, for the approval of the transaction have been obtained. B Communications believes that this represents a significant milestone for the advancement and completion of the transaction. In addition, on August 18, 2019, B Communications notified the Company that on the same day, the court approved the creditors' settlement for the transaction, and that completion of the transaction is still subject to approval from the Ministry of Communications.

## **2. Basis of Preparation**

**2.1** The condensed consolidated interim financial statements have been prepared in accordance with IAS 34 – Interim Financial Reporting, and Chapter D of the Securities Regulations (Periodic and Immediate Reports), 1970.

**2.2** The condensed consolidated interim financial statements do not contain all the information required in full annual financial statements, and should be reviewed in the context of the annual financial statements of the Company and its subsidiaries as at December 31, 2018 and the year then ended, and their accompanying notes (“the Annual Financial Statements”). The notes to the condensed interim financial statements include only the material changes that have occurred from the date of the most recent Annual Financial Statements until the date of these consolidated interim financial statements.

**2.3** The condensed consolidated interim financial statements were approved by the Board of Directors on August 28, 2019.

### **2.4 Use of estimates and judgments**

The preparation of the condensed consolidated interim financial statements in conformity with International Financial Reporting Standards (IFRS) requires management to make judgments and use estimates, assessments and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenues, and expenses. Actual results may differ from these estimates.

Other than as set out below, the judgments made by management, when applying the Group's accounting policies and the key assumptions used in assessments that involve uncertainty, are consistent with those applied the preparation of the Annual Financial Statements.

Information about a significant estimate, for which changes in the assessments and assumptions could potentially have a material effect on the financial statements:

Subject	Principal assumptions	Possible effects	Reference
Provisions and contingent liabilities, including levies	The Company's assessments of the estimated payment to the authorities for the levies on the real estate asset in the Sakia property	Change in capital gain for the sale of a real estate asset in the Sakia property	Note 7

In addition, see Note 6 on the write-off of the tax asset for the losses of DBS by way of a change in estimate.

### 3. **Reporting Principles and Accounting Policy**

The Group's accounting policy applied in these condensed consolidated interim financial statements is consistent with the policy applied in the Annual Financial Statements, except as described in this section below.

#### 3.1 **Presentation of impairment loss of assets**

An impairment loss arising from a non-recurring adjustment of forecasts for the coming years is classified as other expenses in the statement of income. On the other hand, an impairment loss of assets arising from the continuous adjustment of non-current assets of the Group companies to their fair value, less disposal costs (arising due to the expected negative cash flow and negative operating value of those companies) is classified under the same items as the current expenses for these assets. This classification is more consistent with the presentation method based on the nature of the expense and is more suitable for understanding the Group's business.

Accordingly, as from the first quarter of 2019, impairment of the broadcasting rights in DBS and Walla is presented under "operating and general expenses", while impairment of fixed assets and intangible assets is presented under "depreciation, amortization and impairment" in the statement of income.

#### 3.2 **Initial application of new standards**

##### IFRIC 23, Uncertainty Over Income Tax Treatments

As from January 1, 2019, the Group applies the interpretation of IFRIC 23, Uncertainty Over Income Tax Treatments. IFRIC 23 clarifies application of recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. Application of IFRIC 23 did not have a material effect on the Group's financial statements.

### 4. **Group entities**

4.1 A detailed description of the Group entities appears in Note 14 to the Annual Financial Statements. Below is a description of the material changes that occurred in connection with the Group entities since publication of the Annual Financial Statements.

4.2 See Note 14.1.2 to the Annual Financial Statements for information about the decision of the Company's Board of Directors on February 13, 2019 to approve the request of each of the subsidiaries Pelephone, Bezeq International, and DBS to apply to the Ministry of Communications for approval to change the corporate structures.

#### 4.3 **DBS Satellite Services (1998) Ltd. ("DBS")**

4.3.1 On March 13, 2019, the Company's Board of Directors approved a resolution of the Board of Directors of DBS to approve an plan for migration from satellite broadcasts to



broadcasts over the internet, in a gradual, long-term process that expected to spread over seven years.

- 4.3.2 As at June 30, 2019, DBS has an equity deficit in the amount of NIS 188 million and a working capital deficit in the amount of NIS 359 million. According to the forecasts of DBS, it expects to continue to accumulate operational losses in the coming years and therefore will be unable to meet its obligations and continue operating as a going concern without the Company's support.

Further to Note 14.2.3 to the Annual Financial Statements, on February 13, 2019, the Company provided DBS with a credit facility or capital investments in the amount of NIS 250 million, which DBS can withdraw for a period of 15 months from that date.

In May 19, 2019, the Company's Board of Directors approved an irrevocable undertaking of the Company to DBS to provide a credit facility or a capital investment of NIS 250 million for a period of 15 months, commencing from April 1, 2019 and until June 30, 2020.

In August 28, 2019, the Company's Board of Directors approved an irrevocable undertaking of the Company to DBS to provide a credit facility or a capital investment of NIS 250 million for a period of 15 months, commencing from July 1, 2019 and until September 30, 2020.

Insofar as the Company elects to provide credit, the repayment date of the credit will not be earlier than the end of the term of the credit facility. The undertaking of August 28, 2019 will replace the undertakings that were provided in accordance with the resolutions of the Board of Directors on February 13, 2019 and May 19, 2019, as aforesaid (and not in addition to).

In March 2019, the Company invested NIS 70 million and in July 2019 another NIS 50 million, in accordance with the undertakings of February 13, 2019 and May 19, 2019.

The management of DBS believes that the financial resources at its disposal, which include the working capital deficit, the credit facility, and the Company's capital investments, as set out above, will be adequate for the operations of DBS for the coming year.

- 4.3.3 See Note 5.2 below for information about the impairment of assets recognized by DBS in the financial statements as at June 30, 2019.

## **5. Impairment**

### **5.1 Impairment in the cellular communications segment**

In view of the review of Pelephone's performance in the first half of 2019 and its possible implications on the forecasts, and in view of a decrease in expectations of market recovery, partly due to the establishment of a sixth operator in the market, Pelephone identified indications of possible impairment and updated its forecasts for the coming years. As a result, the Company estimated the recoverable amount of the cash-generating cellular communications unit as at June 30, 2019.

The value in use of the cellular communications cash-generating unit for Bezeq Group was calculated by discounting future cash flows (DCF) based on a five year cash flow forecast as at the end of the current period with the addition of the salvage value. The cash flow forecast is based, among other things, on Pelephone's performance in recent years and assessments regarding the expected trends in the cellular market in the coming years (competitive dynamics, price level, regulation, and technological developments).

The main assumption underlying the forecast is that competition in the market will continue with high intensity in the short term and that a stable and certain gradual increase in prices will occur in the medium to long term. The revenue forecast is based on assumptions regarding the number of Pelephone subscribers, average revenue per user, and sales of terminal equipment. The expense forecast is based, among other things, on streamlining of fixed expenses (which does not result in a restructuring) and, in particular, on assumptions regarding the extent of the decrease in the number of Pelephone employees and the related wage expenses. The other

operating expenses and level of investments were adjusted to the forecasted scope of Pelephone's operations

The nominal capital price taken into account for the valuation is 10.3% (after tax) (in 2018, 10.3%). In addition, a permanent growth rate of 2.5% was assumed (in 2018 - 2.5%). The valuation is sensitive to changes in the permanent growth rate and the discount rate. In addition, the valuation is sensitive to the net cash flow in the representative year in general, and to the average revenue per user (ARPU) and number of users at the end of the range of the forecast in particular (a change of NIS 1 in ARPU results in a change in the value of operations amounting to NIS 285 million).

It should be noted that Pelephone has operating losses, therefore the value in use of the cellular communications cash-generating unit is based entirely on Pelephone's projections for improved profitability in the coming years.

The valuation was prepared by an external appraiser. Based on the valuation as described above, the value of Pelephone's operations amounted to NIS 1,214 million, compared with the value in the Company's financial statements in the amount of NIS 2,165 million. Accordingly, the Company recognized a loss from impairment of goodwill attributable to the cellular communications cash-generating unit in the amount of NIS 951 million. The balance of goodwill attributable to the cash-generating cellular communications unit after recognition of impairment is NIS 76 million and the unit's recoverable amount is the same as its carrying amount.

## 5.2 Impairment in the multi-channel television segment

Further to Note 11.4 to the Annual Financial Statements regarding impairment recognized in 2018 for the multi-channel television cash-generating unit, the valuation as at December 31, 2018 presented a value in use that is significantly lower than the carrying amount of DBS. Based on reviews performed by an external appraiser as at June 30, 2019 and March 31, 2019, and according to the assessment of the management of DBS, it was found that there were no changes in the projected financial results of DBS, there were no material changes in market expectations, and no regulatory changes were made. Accordingly, in view of the negative value of the operations as determined in the valuation as at December 31, 2018, DBS amortized the non-current assets as at June 30, 2019, up to the net disposal value of these assets.

Accordingly, in the six- and three-months period ended June 30, 2019, the Group recognized an impairment loss of NIS 207 million, and NIS 119 million, respectively. The impairment loss was attributed to fixed assets, broadcasting rights, and intangible assets, as set out below, and was included in depreciation, amortization, and impairment expenses and in operating and general expenses in the statement of income, as set out in Note 3.1 above.

Attribution of impairment loss to Group assets:

	Impairment loss of assets	
	Six months ended June 30, 2019	Three months ended June 30, 2019
	(Unaudited)	(Unaudited)
	NIS million	NIS million
Broadcasting rights - less rights utilized (the expense was presented under operating and general expenses)	113	67
Fixed assets (the expense was presented under depreciation and impairment expenses)	68	41
Intangible assets (the expense was presented under depreciation and impairment expenses)	26	11
Total impairment recognized	207	119

For information about the method used by DBS to measure the fair value (Level 3) of the assets, less disposal costs, see Note 11.4 to the Annual Financial Statements.

## 5.3 Assessment of indications of impairment in the international communications and internet services segment

Further to Note 11.6 to the Annual Financial Statements regarding Bezeq International's impairment assessment, Bezeq International performed a routine assessment for indications of

impairment as at June 30, 2019, in accordance with the provisions of IAS 36 and noting the low gap measured on December 31, 2018 between the value of Bezeq International's operations and the carrying amount of its net operating assets. As at the date of the financial statements, there were no indications of impairment.

## **6. Income tax**

Further to Note 7.5 to the Annual Financial Statements regarding the deferred tax asset for the losses in DBS in the amount of NIS 1,166 million and further to the discussions between the Company and the Israel Securities Authority (ISA) regarding the Company's application for permission to publish the prospectus, on August 23, 2019, the Company received the response of the ISA's staff concerning the propriety of the Company's accounting for recognition of the tax asset, including the staff position that the ISA is formulating on the matter, which addresses the question of whether the Company established the forecast test underlying the ability to continue to recognize the tax asset.

In accordance with the staff position of the ISA which is being formulated, there are difficulties in the Company's position for recognition of the tax asset and it appears that the ISA is formulating a position whereby the Company has not met the onus required to establish the forecast for use of the tax asset regarding the cumulative existence of three events: cancellation of the structural separation by the Ministry of Communications; extension of the validity of the taxation ruling concerning use of the tax asset each year until cancellation of the structural separation; and the existence of adequate income over time after the date of cancellation of the structural separation of Bezeq and the merger with DBS that will allow use of the tax asset.

As part of the formulating staff position of the ISA, it is noted that the assessment is valid from the 2018 financial statements and onwards, and not for earlier periods. This takes into account that some of the issues related to the structural separation are at the heart of a criminal investigation concerning senior officers of the Company between 2013 and 2017, as set out in Note 1.2 above.

For the purpose of assessing the probability of utilization of the tax asset as at June 30, 2019, the Company considered, among other things, the absence of developments in its discussions with authorities and government agencies, various developments in recent months, and the effect of the passage of time. In view of the aforesaid, the Company's estimate regarding the probability of utilizing the tax asset is no longer "more likely than not", and therefore the Company wrote off the tax asset by adjusting the estimate as of the financial statements for the second quarter of 2019.

Accordingly, the Company recognized tax expenses of NIS 1,166 million in the statement of income for the three months ended June 30, 2019.

As aforesaid, in accordance with the formulating staff position of the ISA, the assessment is correct as at the date of the financial statements for 2018 onwards, contrary to the Company's position according to which the tax asset is no longer recognized as of the financial statements for the period ended June 30, 2019. If the Company's position is not accepted, there is a possibility that the Company will be required to restate its financial statements for 2018 onwards.

Regarding the petition that the Company filed with the High Court of Justice against the Ministry of Communications for immediate cancellation of the structural separation in the Bezeq Group, despite the Company's objections, the State received several extensions to file its response to the petition, the most recent of which is until September 5, 2019.

## **7. Investment property**

Further to Note 13 to the Annual Financial Statements regarding the Company's agreement for the sale of a real estate asset in the Sakia property, on May 5, 2019, the transaction was completed and the entire balance of the consideration for the sale of the asset in the amount of NIS 323 million (plus VAT) was received. This completed the receipt of the consideration for the transaction in a total amount of NIS 511 million.

Upon receipt of the balance of the consideration, the Company paid the demand for betterment tax in the amount of NIS 149 million, and in July 2019, it received a refund of half of the amount of the payment, against which it provided a bank guarantee, without this derogating from and/or impairing the steps taken and/or to be taken by the Company to cancel or reduce this fee.

The Company included capital gain of NIS 403 million in its financial statements for the second quarter of 2019. Recognition of the capital gain is based on the Company's estimates of the amount to be paid

to the authorities. It should be noted that if the Company's estimates do not materialize, the final capital gain will be between NIS 250 million and NIS 450 million.

## 8. Debentures, loans and borrowings

- 8.1 In June 2019, the Company raised debt in the amount of NIS 500 million through a private loan from an institutional entity with an average duration of 7.15 years and at a fixed NIS interest rate of 3.6%. The terms of the loan are similar to those of other loans taken by the Company, as set out in Note 15.3 to the Annual Financial Statements.
- 8.2 Subsequent to the reporting date, in July 2019, the Company completed a private placement of Debentures (Series 11 and 12) to institutional investors. The debentures were listed for trading on the TACT-Tel Aviv Continuous Institutions Trading system of the Tel Aviv Stock Exchange Ltd. The total consideration (gross) that was received amounted to NIS 889 million, as set out below:

	Gross consideration (NIS)	Annual weighted interest	Linkage terms
Series 11	427,891,000	3.6%	Unlinked
Series 12	461,740,000	2.1%	Linked to the increase in the CPI

The bond principal will be repaid in five equal payments between 2026 and 2030. The interest is payable twice a year as from December 1, 2019.

The Company intends to continue to take steps to list the debentures for trading on the TASE, subject to the law, the publication of a prospectus, and the receipt of the required permits. If the Debentures (Series 11 and 12) are listed on the main list of the TASE, the interest rate payable on the principle of the debentures as from their listing date on the main list, will decrease by 0.4%.

The terms of the debentures are similar to the terms of the debentures from the Company's existing series (Series 6, 7, 9, and 10) as set out in Note 15.3 to the Annual Financial Statements. The consideration of the issuance is earmarked for refinancing the Company's debt.

- 8.3 In July 2019, the Company prematurely repaid the bank loan of NIS 438 million bearing variable interest.

## 9. Employee benefits

- 9.1 On March 14, 2019, DBS signed a collective arrangement with the Histadrut Federation of Labor and the employees' representatives regarding retrenchment and synergy procedures, commencing on June 1, 2019 until December 31, 2021 ("the Arrangement"). According to the arrangement, in the Arrangement years, DBS will be entitled to terminate the employment of up to 325 employees. In addition, according to the Arrangement, DBS may also retrench by not recruiting employees to replace employees whose employment has terminated. Following the Arrangement and the submission of the efficiency plan outline to the employees' representatives, DBS recognized expenses of NIS 45 million, mainly severance benefits. The expenses were included under other operating expenses in the statement of income for the first quarter of 2019.
- 9.2 On July 11, 2019, Bezeq International signed a collective agreement with the Histadrut General Federation of Labor, which includes streamlining and synergy processes for the period from July 11, 2019 to December 31, 2021. Under to the agreement, Bezeq International may retrench up to 325 employees (of which 150 are permanent employees, some as part of voluntary early retirement), in addition to the option of not hiring employees to replace the employees who are terminating their employment. The agreement also includes a one-time bonus for employees who are not included in the retirement plan. The estimated cost of the agreement is NIS 60 million, assuming full exercise of the rights of Bezeq International to retrenchment and the fulfillment of conditions for providing additional financial benefits to the employees.

## 10. Contingent liabilities

During the normal course of business, legal claims were filed against Group companies or there are pending claims against the Group ("in this section: "Legal Claims").

In the opinion of the managements of the Group companies, based, among other things, on legal opinions as to the likelihood of success of the Legal Claims, the financial statements include adequate

provisions of NIS 142 million, where provisions are required to cover the exposure arising from such Legal Claims.

In the opinion of the managements of the Group companies, the additional exposure (beyond these provisions) as at June 30, 2019 for claims filed against Group companies on various matters and which are unlikely to be realized, amounted to NIS 4.6 billion. There is also additional exposure of NIS 4.5 billion for claims, the chances of which cannot yet be assessed.

In addition, motions for certification of class actions have been filed against the Group companies, for which the Group has additional exposure beyond the aforesaid, since the exact amount of the claim is not stated in the claim.

The amounts of the additional exposure in this note are linked to the CPI and are stated net of interest.

For updates subsequent to the reporting date, see section 10.4 below.

**10.1** Following is a detailed description of the Group's contingent liabilities as at June 30, 2019, classified into groups with similar characteristics:

Claims group	Nature of the claims	Balance of provisions	Additional exposure	Exposure for claims that cannot yet be assessed
		NIS million		
Customer claims	Mainly motions for certification of class actions concerning contentions of unlawful collection of payment and impairment of the service provided by the Group companies.	125	4,492	630 <sup>(1)</sup>
Claims by enterprises and companies	Claims alleging liability of the Group companies in respect of their activities and/or the investments made in various projects.	-	-	3,833 <sup>(3)(2)</sup>
Claims of employees and former employees of Group companies	Mainly individual lawsuits filed by employees and former employees of the Group, regarding various payments.	-	3	-
Claims by the State and authorities	Various claims by the State of Israel, government institutions and authorities ("the Authorities"). These are mainly procedures related to regulations relevant to the Group companies and financial disputes concerning monies paid by the Group companies to the Authorities (including property taxes). See also Note 7.	17	21	-
Supplier and communication provider claims	Legal claims for compensation for alleged damage as a result of the supply of the service and/or the product.	-	63	16
Claims for punitive damages, real estate and infrastructure	Claims for alleged physical damage or damage to property caused by Group companies and in relation to real estate and infrastructure. The additional amount of exposure for punitive damages does not include claims for which the insurance coverage is not disputed.	-	67	-
Total legal claims against the Company and subsidiaries		142	4,646	4,479

(1) Including exposure in the amount of NIS 300 million against a subsidiary and against four additional defendants.

(2) Including exposure of NIS 2 billion for a motion for certification as a class action filed by a shareholder against the Company and officers in the Company, referring to alleged reporting omissions by the Company regarding the wholesale market and the reduction of interconnect fees, which the plaintiff estimates at NIS 1.1 billion or NIS 2 billion (depending on the method used to calculate the damage). On August 27, 2018, the court certified the claim as a class action. On October 28, 2018, the Company filed a motion for a rehearing of the certification ruling. Subsequently, the court decided to stay the proceedings until a ruling is made on the motion for a rehearing.

In the hearing on May 22, 2019 of the motion filed by the Company for another hearing, the Court proposed transferring the case to mediation. The plaintiff rejected the proposal. On July 18, 2019, a

hearing was held to complete the parties' arguments in the motion for a re-hearing application and the ruling will be handed down at a later stage.

- (3) Two motions for certification of a class action amounting to a total of NIS 1.8 billion, filed in June 2017 against the Company, officers in the Group and companies in the group of the Company's controlling shareholders regarding the transaction for the Company's acquisition of DBS shares from Eurocom DBS Ltd. In accordance with the court's decision, a joint motion is expected to be filed instead of these two motions. The proceedings are stayed in view of the investigation (as described in Note 1.2) and at the request of the Attorney General, until October 31, 2019.

- 10.2** Further to Note 19.3 to the Annual Financial Statements, regarding a class action filed in the United States against B Communications, Ltd., the controlling shareholder of the Company, and its officers, to which DBS and officers (both past and present) in DBS and in the Company were added, as well as motions filed by the defendants for the dismissal in limine of the motion and the claim, on March 28, 2019, the Company was notified of the ruling of the US court on that date, which accepted the petitions of DBS and of the officers (both past and present) in DBS and in the Company, and dismissed the case in limine due to the absence of jurisdiction against them.
- 10.3** For further proceedings against the Group companies and officers, see Notes 19.2 and 19.4 to the Annual Financial Statements (at this stage, the proceedings are stayed until October 31, 2019), and Note 19.5.
- 10.4** Subsequent to the financial statements, claims with exposure of NIS 127 million and two claims without a monetary estimate came to an end.

## **11. Agreements**

Further to Notes 20.1 and 20.2 to the Annual Financial Statements, since Space Communications Ltd. ("Spacecom") did not enter into an agreement which entered into force with a satellite manufacturer for the construction of the Amos 8 satellite by June 5, 2019, DBS has the option of notifying Spacecom of the termination of the agreement between the parties and the agreement will come to an end on February 26, 2021. If DBS does not exercise the opt out option, and Amos 8 does not start operations by February 1, 2022, then the satellite agreement will terminate at the end of the life of Amos 3, which Spacecom estimates to be on January 31, 2026.

It should be emphasized that the total amount of agreement that was presented for the space segments under Note 20.1, as presented in the Annual Financial Statements, is NIS 822 million, and a total of NIS 236 million of this amount will not be exercised if the satellite agreement ends on January 31, 2026, as aforesaid.

## **12. Equity**

- 12.1** Further to Note 22.1 to the Annual Financial Statements regarding the approval of the Board of Directors to convene a general meeting to approve an increase in the Company's registered share capital, on April 8, 2019, the Board of Directors of the Company resolved to remove the issue of an increase in the registered share capital from the agenda of the general meeting, due to discussions with shareholders and the response to their requests.
- 12.2** For further information, see Note 22.2.1 to the Annual Financial Statements regarding the resolution of the Board of Directors of the Company on March 27, 2019 to cancel the Company's dividend distribution policy.

**13. Revenues**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Domestic fixed-line communication (Bezeq Fixed-Line)</b>					
Internet - infrastructure	754	766	377	386	1,525
Fixed-line telephony	522	580	259	286	1,130
Transmission and data communication	380	387	186	191	769
Cloud and digital services	139	128	68	66	260
Other services	109	111	51	57	199
	1,904	1,972	941	986	3,883
<b>Cellular telephony - Pelephone</b>					
Cellular services and terminal equipment	827	848	420	428	1,713
Sale of terminal equipment	302	352	140	164	688
	1,129	1,200	560	592	2,401
<b>Multi-channel television - DBS</b>					
	680	750	337	375	1,473
<b>International communications, ISP, and NEP services - Bezeq International</b>					
	653	664	330	325	1,338
<b>Others</b>					
	114	108	56	55	226
	4,480	4,694	2,224	2,333	9,321

**14. General and operating expenses**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Terminal equipment and materials	357	360	173	171	737
Interconnectivity and payments to domestic and international operators	383	388	194	196	789
Maintenance of buildings and sites	133	139	65	68	286
Marketing and general	241	291	118	146	555
Consumption and impairment of content (see Note 3.1)	336	325	176	169	653
Services and maintenance by sub-contractors	138	139	68	68	277
Vehicle maintenance	38	37	20	20	82
	<b>1,626</b>	<b>1,679</b>	<b>814</b>	<b>838</b>	<b>3,379</b>

**15. Other operating expenses (income), net**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Capital gain (mainly from the sale of real estate (see also Note 7))	(461)	(6)	(417)	(5)	(1)
Expenses (income) for severance pay in voluntary redundancy	(24)	93	1	81	559
Provision for claims	1	20	2	8	91
Expenses for severance due to the efficiency agreement in DBS (see Note 9.1)	45	-	-	-	-
Profit from sale of an associate	-	-	-	-	(14)
Others	-	-	-	-	(1)
<b>Total operating expenses (income), net</b>	<b>(439)</b>	<b>107</b>	<b>(414)</b>	<b>84</b>	<b>634</b>



**16. Financial instruments****16.1 Fair value****16.1.1 Financial instruments at fair value for disclosure purposes only**

The table below shows the differences between the carrying amount and the fair value of financial liabilities. The methods used to estimate the fair values of financial instruments are described in Note 31.8 to the Annual Financial Statements.

	June 30, 2019		June 30, 2018		December 31, 2018	
	Carrying amount (including accrued interest)	Fair value	Carrying amount (including accrued interest)	Fair value	Carrying amount (including accrued interest)	Fair value
	(Unaudited)		(Unaudited)		(Audited)	
	NIS million		NIS million		NIS million	
Loans from banks and institutions (unlinked)	4,490	4,659	4,689	4,839	4,235	4,324
Debentures issued to the public (CPI-linked)	3,492	3,672	4,096	4,293	3,464	3,602
Debentures issued to the public (unlinked)	2,209	2,293	1,646	1,658	2,215	2,214
Debentures issued to financial institutions (CPI-linked)	8	8	13	13	8	8
Debentures issued to financial institutions (unlinked)	151	157	252	268	202	211
	<b>10,350</b>	<b>10,789</b>	10,696	11,071	10,124	10,359

**16.1.2 Fair value hierarchy**

The table below presents an analysis of the financial instruments measured at fair value, with details of the evaluation method. The methods used to estimate the fair value are described in Note 31.7 to the Annual Financial Statements.

	June 30, 2019	June 30, 2018	December 31, 2018
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Level 1: Investment in marketable securities at fair value through profit or loss	546	9	18
Level 2: forward contracts	(131)	(157)	(135)
Level 3: contingent consideration for a business combination	-	25	-

**17. Segment Reporting****17.1 Operating segments**

Six months ended June 30, 2019 (Unaudited):							
	Domestic fixed-line communication	Cellular communications*	International communications and internet services	Multi-channel television**	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	1,903	1,129	653	680	115	-	4,480
Inter-segment revenues	160	19	27	-	4	(210)	-
Total revenues	2,063	1,148	680	680	119	(210)	4,480
Depreciation and amortization	411	312	92	159	6	(36)	944
Segment results – operating profit (loss)	1,406	(18)	52	(67)	(2)	(954)	417
Financing expenses	259	8	8	9	-	(22)	262
Financing income	(12)	(31)	(1)	(2)	-	19	(27)
Total financing expenses (income), net	247	(23)	7	7	-	(3)	235
Segment profit (loss) after financing expenses, net	1,159	5	45	(74)	(2)	(951)	182
Share in losses of associates	-	-	-	-	(1)	-	(1)
Segment profit (loss) before income tax	1,159	5	45	(74)	(3)	(951)	181
Income tax	276	1	10	1	-	1,166***	1,454
Segment results – net profit (loss)	883	4	35	(75)	(3)	(2,117)	(1,273)

\* The impairment loss in the cellular communications segment described in Note 5.1 is presented under adjustments.

\*\* Results of the multi-channel television segment are presented net of the impairment loss set out in Note 5.2. The impairment loss is presented as part of the adjustments. This is in accordance with the manner in which the Group's chief operating decision maker evaluates the performance of the segment and makes decisions regarding the allocation of resources to the segment. In addition, see Note 18.3 for condensed selected information from the financial statements of DBS.

\*\*\* See Note 6 for information about the write-off of the tax assets for the losses of DBS.

## 17.1 Operating Segments (contd.)

Six months ended June 30, 2018 (Unaudited):							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	1,972	1,200	663	750	109	-	4,694
Inter-segment revenues	155	21	25	-	7	(208)	-
Total revenues	2,127	1,221	688	750	116	(208)	4,694
Depreciation and amortization	415	317	88	158	11	73	1,062
Segment results – operating profit (loss)	860	4	64	(18)	(13)	(64)	833
Financing expenses	254	10	8	15	1	(32)	256
Financing income	(14)	(27)	(1)	(25)	-	29	(38)
Total financing expenses (income), net	240	(17)	7	(10)	1	(3)	218
Segment profit (loss) after financing expenses, net	620	21	57	(8)	(14)	(61)	615
Share in losses of associates	-	-	-	-	(2)	-	(2)
Segment profit (loss) before income tax	620	21	57	(8)	(16)	(61)	613
Income tax	155	5	13	1	-	(16)	158
Segment results – net profit (loss)	465	16	44	(9)	(16)	(45)	455

## 17.1 Operating Segments (contd.)

Three months ended June 30, 2019 (Unaudited):							
	Domestic fixed-line communication	Cellular communications*	International communications and internet services	Multi-channel television **	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	940	560	330	337	57	-	2,224
Inter-segment revenues	80	10	9	-	1	(100)	-
Total revenues	1,020	570	339	337	58	(100)	2,224
Depreciation and amortization	204	156	46	81	4	(13)	478
Segment results – operating profit (loss)	875	(8)	18	(8)	(3)	(968)	(94)
Financing expenses	148	5	5	4	-	(13)	149
Financing income	(7)	(15)	-	(2)	-	11	(13)
Total financing expenses (income), net	141	(10)	5	2	-	(2)	136
Segment profit (loss) after financing expenses, net	734	2	13	(10)	(3)	(966)	(230)
Share in losses of associates	-	-	-	-	(1)	-	(1)
Segment profit (loss) before income tax	734	2	13	(10)	(4)	(966)	(231)
Income tax	172	-	3	1	-	1,166***	1,342
Segment results – net profit (loss)	562	2	10	(11)	(4)	(2,132)	(1,573)

\* The impairment loss in the cellular communications segment described in Note 5.1 is presented under adjustments.

\*\* Results of the multi-channel television segment are presented net of the impairment loss set out in Note 5.2, Impairment Loss, is presented as part of the adjustments. This is in accordance with the manner in which the Group's chief operating decision maker evaluates the performance of the segment and makes decisions regarding the allocation of resources to the segment. In addition, see Note 18.3 for condensed selected information from the financial statements of DBS.

\*\*\* See Note 6 for information about the write-off of the tax assets for the losses of DBS.

## 17.1 Operating Segments (contd.)

Three months ended June 30, 2018 (Unaudited):							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	986	592	325	375	55	-	2,333
Inter-segment revenues	78	10	11	-	4	(103)	-
Total revenues	1,064	602	336	375	59	(103)	2,333
Depreciation and amortization	211	159	45	79	5	38	537
Segment results – operating profit (loss)	387	2	30	(17)	(5)	(26)	371
Financing expenses	127	7	4	4	1	(14)	129
Financing income	(8)	(13)	-	(11)	1	12	(19)
Total financing expenses (income), net	119	(6)	4	(7)	2	(2)	110
Segment profit (loss) after financing expenses, net	268	8	26	(10)	(7)	(24)	261
Share in losses of associates	-	-	-	-	(1)	-	(1)
Segment profit (loss) before income tax	268	8	26	(10)	(8)	(24)	260
Income tax	66	1	6	-	-	(8)	65
Segment results – net profit (loss)	202	7	20	(10)	(8)	(16)	195

## 17.1 Operating Segments (contd.)

Year ended December 31, 2018 (Audited)							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television*	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	3,883	2,401	1,338	1,473	226	-	9,321
Inter-segment revenues	313	42	53	-	15	(423)	-
Total revenues	4,196	2,443	1,391	1,473	241	(423)	9,321
Depreciation and amortization	850	655	194	323	21	146	2,189
Segment results – operating profit (loss)	1,224	(2)	116	(56)	(36)	(1,794)	(548)
Financing expenses	502	22	16	16	-	(40)	516
Financing income	(32)	(56)	(1)	(27)	-	35	(81)
Total financing expenses (income), net	470	(34)	15	(11)	-	(5)	435
Segment profit (loss) after financing expenses, net	754	32	101	(45)	(36)	(1,789)	(983)
Share in profits (losses) of associates	-	-	1	-	(4)	-	(3)
Segment profit (loss) before income tax	754	32	102	(45)	(40)	(1,789)	(986)
Income tax	187	8	25	3	-	(143)	80
Segment results – net profit (loss)	567	24	77	(48)	(40)	(1,646)	(1,066)

\* Results of the multi-channel television segment are presented net of the impairment loss set out in Note 11.4 to the Annual Financial Statements. The impairment loss is presented as part of the adjustments. In addition, see Note 18.3 for condensed selected information from the financial statements of DBS.

**17.2 Adjustment of profit or loss for reporting segments**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Operating profit for reporting segments	1,373	910	877	402	1,282
Financing expenses, net	(235)	(218)	(136)	(110)	(435)
Adjustments for the multi-channel television segment	(3)	-	(17)	-	-
Loss for operations classified in other categories and other adjustments	(2)	(13)	(3)	(5)	(36)
Share in losses of associates	(1)	(2)	(1)	(1)	(3)
Impairment loss of assets	(951)	-	(951)	-	(1,638)
Amortization of surplus cost for intangible assets	-	(64)	-	(26)	(156)
Profit (loss) before taxes on income	181	613	(231)	260	(986)

**18. Condensed Financial Statements of Pelephone, Bezeq International, and DBS**

In the fourth quarter of 2018, Pelephone, Bezeq International, and DBS decided to change the presentation method in the statement of income to a classification method based on the nature of the expense, similar to the method used in the Group's reports. The comparative figures for the six- and three-months period ended June 30, 2018 were reclassified according to the new classification method.

**18.1 Pelephone Communications Ltd.**

Selected data from the statement of financial position

	June 30, 2019	June 30, 2018	December 31, 2018
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	973	931	913
Non-current assets	3,146	3,171	3,211
<b>Total assets</b>	<b>4,119</b>	<b>4,102</b>	<b>4,124</b>
Current liabilities	638	655	619
Long-term liabilities	778	741	806
<b>Total liabilities</b>	<b>1,416</b>	<b>1,396</b>	<b>1,425</b>
Equity	2,703	2,706	2,699
<b>Total liabilities and equity</b>	<b>4,119</b>	<b>4,102</b>	<b>4,124</b>

Selected data from the statement of income

	Six months ended June 30		Three months ended June 30		Year ended December 31,
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from services	846	869	430	438	1,755
Revenues from sales of terminal equipment	302	352	140	164	688
<b>Total revenues from services and sales</b>	<b>1,148</b>	<b>1,221</b>	<b>570</b>	<b>602</b>	<b>2,443</b>
<b>Costs of activity</b>					
General and operating expenses	662	703	324	345	1,402
Wages	189	195	95	95	379
Depreciation and amortization	312	317	156	159	655
<b>Total operating expenses</b>	<b>1,163</b>	<b>1,215</b>	<b>575</b>	<b>599</b>	<b>2,436</b>
Other operating expenses, net	3	2	3	1	9
<b>Operating profit (loss)</b>	<b>(18)</b>	<b>4</b>	<b>(8)</b>	<b>2</b>	<b>(2)</b>
Financing expenses (income)					
Financing expenses	8	10	5	7	22
Financing income	(31)	(27)	(15)	(13)	(56)
<b>Financing income, net</b>	<b>(23)</b>	<b>(17)</b>	<b>(10)</b>	<b>(6)</b>	<b>(34)</b>
<b>Profit before income tax</b>	<b>5</b>	<b>21</b>	<b>2</b>	<b>8</b>	<b>32</b>
Income tax	1	5	-	1	8
<b>Profit for the period</b>	<b>4</b>	<b>16</b>	<b>2</b>	<b>7</b>	<b>24</b>



**18.2 Bezeq International Ltd.**

Selected data from the statement of financial position

	June 30, 2019	June 30, 2018	December 31, 2018
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	446	434	513
Non-current assets	812	890	831
<b>Total assets</b>	<b>1,258</b>	<b>1,324</b>	<b>1,344</b>
Current liabilities	297	302	345
Long-term liabilities	149	236	222
<b>Total liabilities</b>	<b>446</b>	<b>538</b>	<b>567</b>
Equity	812	786	777
<b>Total liabilities and equity</b>	<b>1,258</b>	<b>1,324</b>	<b>1,344</b>

Selected data from the statement of income

	Six months ended June 30		Three months ended June 30		Year ended December 31,
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Revenues</b>	<b>680</b>	688	<b>339</b>	336	1,391
<b>Costs of activity</b>					
General and operating expenses	388	377	194	187	776
Wages	133	158	66	75	297
Depreciation and amortization	92	88	46	45	194
Other expenses, net	15	1	15	(1)	8
<b>Total operating expenses</b>	<b>628</b>	624	<b>321</b>	306	1,275
<b>Operating profit</b>	<b>52</b>	64	<b>18</b>	30	116
<b>Financing expenses (income)</b>					
Financing expenses	8	8	5	4	16
Financing income	(1)	(1)	-	-	(1)
Financing expenses, net	7	7	5	4	15
Share in the profits of equity-accounted investees	-	-	-	-	1
<b>Profit before income tax</b>	<b>45</b>	57	<b>13</b>	26	102
Income tax	10	13	3	6	25
<b>Profit for the period</b>	<b>35</b>	44	<b>10</b>	20	77

**18.3 DBS Satellite Services (1998) Ltd.**

Selected data from the statement of financial position

	June 30, 2019	June 30, 2018	December 31, 2018
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	193	251	220
Non-current assets	290	1,324	286
<b>Total assets</b>	<b>483</b>	<b>1,575</b>	<b>506</b>
Current liabilities	552	644	575
Long-term liabilities	119	170	112
<b>Total liabilities</b>	<b>671</b>	<b>814</b>	<b>687</b>
Capital (capital deficit)	(188)	761	(181)
<b>Total liabilities and equity</b>	<b>483</b>	<b>1,575</b>	<b>506</b>

Selected data from the statement of income

	Six months ended June 30		Three months ended June 30		Year ended December 31,
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Revenues</b>	<b>680</b>	750	<b>337</b>	375	1,473
<b>Costs of activity</b>					
Operating expenses, general, and impairment	482	483	248	246	956
Depreciation, amortization, and impairment losses	123	158	68	79	323
Wages	110	118	54	60	233
Other operating expenses (income), net	34	9	(9)	7	17
Impairment loss	-	-	-	-	1,100
<b>Total operating expenses</b>	<b>749</b>	768	<b>361</b>	392	2,629
<b>Operating loss</b>	<b>(69)</b>	(18)	<b>(24)</b>	(17)	(1,156)
Financing expenses (income)					
Financing expenses	9	13	4	3	15
Financing income	(2)	(25)	(2)	(11)	(27)
Financing expenses for shareholder loans	-	2	-	1	1
<b>Financing expenses (income), net</b>	<b>7</b>	(10)	<b>2</b>	(7)	(11)
<b>Loss before income tax</b>	<b>(76)</b>	(8)	<b>(26)</b>	(10)	(1,145)
Income tax expenses	1	1	1	-	3
<b>Loss for the period</b>	<b>(77)</b>	(9)	<b>(27)</b>	(10)	(1,148)

## **19. Additional Subsequent Material Events**

Further to Note 33.3 to the Annual Financial Statements regarding the resolution of the Company's Board of Directors on March 27, 2019 to apply for a permit to publish a prospectus for completion, which is based on the Company's financial statements as at December 31, 2018, since the discussions with the Israel Securities Authority have not been completed, the application for a permit is for the publication of a prospectus for completion that will be based on the Company's financial statements at a later date after completion of the discussions with the ISA. At this stage, as set out in Note 8.2 above, the Company has executed a private placement of debentures and it intends to continue to take steps to list the debentures for trading on the TASE, subject to the law, the publication of a prospectus, and the receipt of the required permits.

# Condensed Separate Interim Financial Information as at June 30, 2019



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.

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Somekh Chaikin  
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**To:**  
**The Shareholders of “Bezeq”- The Israel Telecommunication Corporation Ltd.**

**Subject: Special auditors’ report on separate interim financial  
Information according to Regulation 38D of the Securities  
Regulations (Periodic and Immediate Reports) – 1970**

### *Introduction*

We have reviewed the separate interim financial information presented in accordance with Regulation 38D of the Securities Regulations (Periodic and Immediate Reports) – 1970 of “Bezeq”- The Israel Telecommunication Corporation Ltd. (hereinafter – “the Company”) as of June 30, 2019 and for the six-month and three-month periods then ended. The separate interim financial information is the responsibility of the Company’s Board of Directors and of its Management. Our responsibility is to express a conclusion on the separate interim financial information based on our review.

We did not review the separate interim financial information of an investee company the investment in which amounted to NIS 26 million as of June 30, 2019, and the loss from this investee company amounted to NIS 7 million and NIS 2 million for the six-month and three-month periods then ended, respectively. The financial statements of that company were reviewed by other auditors whose review report thereon was furnished to us, and our conclusion, insofar as it relates to amounts emanating from the financial statements of that company, is based solely on the said review report of the other auditors.

### *Scope of Review*

We conducted our review in accordance with Standard on Review Engagements 1, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" of the Institute of Certified Public Accountants in Israel. A review of separate interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards in Israel and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

### *Conclusion*

Based on our review and the review report of other auditors, nothing has come to our attention that causes us to believe that the accompanying separate interim financial information was not prepared, in all material respects, in accordance with Regulation 38D of the Securities Regulations (Periodic and Immediate Reports) – 1970.

Without qualifying our abovementioned conclusion, we draw attention to Note 6.1, which refers to Note 1.2 to the annual consolidated financial statements, regarding the Israel Securities Authority’s (ISA) investigation of the suspicion of committing offenses under the Securities’ Law and Penal Code, in respect to transactions related to the former controlling shareholder, and the transfer of the investigation file to the District Attorney’s Office, and as mentioned in that note regarding the joint investigation by the Securities Authority and the Unit for Combating Economic Crime at Lahav 433 and to the publication of the Attorney General’s decision, by



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which he is considering charging the former controlling shareholder with criminal charges. As stated in the above note, at this stage, the Company is unable to assess the effects of the investigations, their findings and their results on the Company, and on the financial statements and on the estimates used in the preparation of these financial statements, if any.

In addition, without qualifying our abovementioned conclusion, we draw attention to lawsuits filed against the Company which cannot yet be assessed or the exposure in respect thereof cannot yet be estimated, as set forth in Note 5.

Somekh Chaikin  
Certified Public Accountants (Isr.)

August 28, 2019

**Condensed Interim Information of Financial Position**

	June 30, 2019 (Unaudited) NIS million	June 30, 2018 (Unaudited) NIS million	December 31, 2018 (Audited) NIS million
<b>Assets</b>			
Cash and cash equivalents	648	632	527
Investments	1,928	1,658	1,384
Trade receivables	689	710	699
Other receivables	205	249	201
Loans granted to investees	73	100	100
<b>Total current assets</b>	<b>3,543</b>	<b>3,349</b>	<b>2,911</b>
Trade and other receivables	243	101	152
Fixed assets	5,032	4,975	4,993
Intangible assets	236	227	227
Goodwill	265	265 *	265
Investment in investees	3,471	7,041 *	5,557
Loans granted to investees	32	191	90
Right-of-use assets	256	302	294
Non-current investments and other	128	143	126
Deferred taxes	18	-	45
Investment property	-	130	58
<b>Total non-current assets</b>	<b>9,681</b>	<b>13,375</b>	<b>11,807</b>
<b>Total assets</b>	<b>13,224</b>	<b>16,724</b>	<b>14,718</b>

The accompanying additional information is an integral part of these condensed separate interim financial information



**Condensed Interim Information of Financial Position (contd.)**

	June 30, 2019 (Unaudited) NIS million	June 30, 2018 (Unaudited) NIS million	December 31, 2018 (Audited) NIS million
<b>Liabilities</b>			
Debentures, loans and borrowings	1,604	1,775	1,520
Trade and other payables	603	604	788
Current tax liabilities	9	-	-
Employee benefits	362	306	524
Current maturities for lease liabilities	106	100	116
Provisions (Note 5)	96	74	132
<b>Total current liabilities</b>	<b>2,780</b>	<b>2,859</b>	<b>3,080</b>
Debentures and loans	9,710	10,185	9,630
Loan from an investee	835	755	815
Employee benefits	420	225	404
Lease liabilities	162	212	192
Derivatives and other liabilities	153	193	163
Deferred tax liabilities	-	38	-
<b>Total non-current liabilities</b>	<b>11,280</b>	<b>11,608</b>	<b>11,204</b>
<b>Total liabilities</b>	<b>14,060</b>	<b>14,467</b>	<b>14,284</b>
<b>Equity</b>			
Share capital	3,878	3,878	3,878
Share premium	384	384	384
Reserves	336	331	331
Deficit	(5,434)	(2,336)	(4,159)
<b>Total equity (deficit) attributable to equity holders of the Company</b>	<b>(836)</b>	<b>2,257</b>	<b>434</b>
<b>Total liabilities and equity (deficit)</b>	<b>13,224</b>	<b>16,724</b>	<b>14,718</b>

**Shlomo Rodav**  
Chairman of the Board of  
Directors

**Dudu Mizrahi**  
CEO

**Yali Rothenberg**  
Bezeq Group CFO

\* Reclassified - Goodwill created with the acquisition of DBS is presented separately as it is attributed to the Company

Date of approval of the financial statements: August 28, 2019

The accompanying additional information is an integral part of these condensed separate interim financial information

**Condensed Interim Information of Profit or Loss**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Revenues (Note 2)</b>	<b>2,063</b>	2,127	<b>1,020</b>	1,064	4,196
<b>Costs of activity</b>					
Payroll	464	460	231	232	912
Depreciation and amortization	411	415	204	211	850
Operating and general expenses (Note 3)	274	285	133	145	596
Other operating expenses (income), net (Note 4)	(492)	107	(423)	89	614
<b>Total operating expenses</b>	<b>657</b>	1,267	<b>145</b>	677	2,972
<b>Operating profit</b>	<b>1,406</b>	860	<b>875</b>	387	1,224
Finance expenses (income)					
Financing expenses	259	254	148	127	502
Financing income	(12)	(14)	(7)	(8)	(32)
Financing expenses, net	247	240	141	119	470
<b>Profit after financing expenses, net</b>	<b>1,159</b>	620	<b>734</b>	268	754
<b>Share in losses of investees, net</b>	<b>(2,156)</b>	(10)	<b>(2,135)</b>	(7)	(1,633)
<b>Profit (loss) before income tax</b>	<b>(997)</b>	610	<b>(1,401)</b>	261	(879)
<b>Income tax</b>	<b>276</b>	155	<b>172</b>	66	187
<b>Profit (loss) for the period</b>	<b>(1,273)</b>	455	<b>(1,573)</b>	195	(1,066)

**Condensed Interim Information on Comprehensive Income**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Profit (loss) for the period	(1,273)	455	(1,573)	195	(1,066)
Items of other comprehensive income (loss), net of tax	3	26	(10)	5	42
<b>Total comprehensive income for the period</b>	<b>(1,270)</b>	481	<b>(1,583)</b>	200	(1,024)

The accompanying additional information is an integral part of these condensed separate interim financial information

**Condensed Interim Information of Cash Flows**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Cash flows from operating activities</b>					
Profit (loss) for the period	(1,273)	455	(1,573)	195	(1,066)
Adjustments:					
Depreciation and amortization	411	415	204	211	850
Share in losses of investees, net	2,156	10	2,135	7	1,633
Financing expenses, net	209	232	120	118	447
Capital gain, net	(460)	(4)	(416)	(3)	(11)
Income tax expenses	276	155	172	66	187
Change in trade and other receivables	13	(50)	31	14	(16)
Change in trade and other payables	(89)	(18)	(99)	(115)	30
Change in provisions	(36)	15	(10)	10	73
Change in employee benefits	(147)	78	(50)	78	487
Miscellaneous	(7)	-	(6)	(1)	5
Net cash (used in) from operating activities due to transactions with subsidiaries	(9)	8	5	10	19
Net income tax paid	(157)	(273)	(97)	(83)	(432)
<b>Net cash from operating activities</b>	<b>887</b>	<b>1,023</b>	<b>416</b>	<b>507</b>	<b>2,206</b>
<b>Cash flows from investment activities</b>					
Investment in intangible assets and other investments	(65)	(59)	(33)	(29)	(113)
Proceeds from the sale of fixed assets	46	29	17	22	152
Proceeds from sale of the Sakia complex	328	-	323	-	155
Investment in bank deposits and securities	(1,780)	(1,934)	(669)	(764)	(2,324)
Proceeds from bank deposits and others	1,235	558	69	482	1,233
Purchase of fixed assets	(329)	(348)	(151)	(172)	(742)
Payment of betterment levies, permit fees and purchase tax for the Sakia complex	(149)	(112)	(149)	(112)	(121)
Receipt (payment) of betterment tax for the sale of the Sakia property	5	(80)	-	(80)	(80)
Investments in a subsidiary	(70)	-	-	-	(100)
Miscellaneous	9	9	2	5	20
Net cash from investment activities due to transactions with subsidiaries	90	80	18	121	146
<b>Net cash used in investing activities</b>	<b>(680)</b>	<b>(1,857)</b>	<b>(573)</b>	<b>(527)</b>	<b>(1,774)</b>

The accompanying additional information is an integral part of these condensed separate interim financial information

**Condensed Interim Information of Cash Flows (contd.)**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
<b>Cash flow from financing operations</b>					
Issue of debentures and receipt of loans	500	320	500	-	891
Repayment of debentures and loans	(355)	(175)	(355)	(175)	(1,544)
Dividends paid	-	(368)	-	(368)	(686)
Interest paid	(190)	(203)	(185)	(197)	(419)
Payments of principal and interest for leases	(61)	(62)	(27)	(29)	(99)
Miscellaneous	-	-	-	-	(37)
Net cash from financing activities due to transactions with subsidiaries	20	185	20	45	220
<b>Net cash from (used for) financing operations</b>	<b>(86)</b>	<b>(303)</b>	<b>(47)</b>	<b>(724)</b>	<b>(1,674)</b>
<b>Increase (decrease) in cash and cash equivalents, net</b>	<b>121</b>	<b>(1,137)</b>	<b>(204)</b>	<b>(744)</b>	<b>(1,242)</b>
Cash and cash equivalents at beginning of period	527	1,769	852	1,376	1,769
<b>Cash and cash equivalents at the end of the period</b>	<b>648</b>	<b>632</b>	<b>648</b>	<b>632</b>	<b>527</b>

The accompanying additional information is an integral part of these condensed separate interim financial information

<b>Notes to the Condensed Separate Interim Financial Information</b>
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**1. Manner of preparing financial information****1.1 Definitions**

"The Company": Bezeq The Israel Telecommunication Corporation Limited

"Investee", the "Group", "Subsidiary": as these terms are defined in the Company's consolidated financial statements for 2018.

**1.2 Principles used for preparing financial information**

The condensed separate interim financial information is presented in accordance with Regulation 38(D) of the Securities Regulations (Periodic and Immediate Reports),1970 ("the Regulation") and the Tenth Addendum of the Securities Regulations (Periodic and Immediate Reports),1970 ("the Tenth Addendum") with respect to the separate interim financial information of the corporation. They should be read in conjunction with the separate financial information for the year ended December 31, 2018 and in conjunction with the condensed interim consolidated financial statements as at June 30, 2019, ("the Consolidated Financial Statements").

The accounting policies used in preparing these condensed separate interim financial information are in accordance with the accounting policies set out in the separate financial information as of and for the year ended December 31, 2018.

**2. Revenues**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Internet - infrastructure	793	799	396	403	1,596
Fixed-line telephony	533	593	264	291	1,156
Transmission and data communication	484	491	238	244	977
Cloud and digital services	139	128	68	66	260
Other services	114	116	54	60	207
	<b>2,063</b>	<b>2,127</b>	<b>1,020</b>	<b>1,064</b>	<b>4,196</b>

**3. Operating and general expenses**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Maintenance of buildings and sites	63	65	30	31	143
Marketing and general	73	89	34	49	183
Interconnectivity and payments to communications operators	49	55	24	27	108
Services and maintenance by sub-contractors	37	40	19	20	83
Vehicle maintenance	17	15	9	8	37
Terminal equipment and materials	35	21	17	10	42
	<b>274</b>	<b>285</b>	<b>133</b>	<b>145</b>	<b>596</b>

**4. Other operating expenses (income), net**

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2019	2018	2019	2018	2018
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Expenses (income) for severance pay in voluntary redundancy	(25)	93	-	81	547
Capital gains (primarily from sale of property)	(460)	(4)	(416)	(3)	(11)
Others	(7)	18	(7)	11	78
<b>Total operating income, net</b>	<b>(492)</b>	<b>107</b>	<b>(423)</b>	<b>89</b>	<b>614</b>

**5. Contingent liabilities**

- 5.1 During the normal course of business, legal claims were filed against the Company or there are various legal proceedings pending against it ("in this section: "Legal Claims").

In the opinion of the Company's management, based, inter alia, on legal opinions as to the likelihood of success of these litigations, the financial statements include appropriate provisions in the amount of NIS 96 million, where provisions are required to cover the exposure arising from such litigation.

Furthermore, other claims have been filed against the Company as class actions with respect to which the Company has additional exposure beyond the aforesaid amounts, which cannot be quantified as the exact amounts of the claims are not stated in the claims.

At June 30, 2019

Balance of provisions	Amount of additional exposure for which probability of realization cannot be foreseen	Exposure for claims that cannot yet be assessed
NIS million		
96	716	4,097 <sup>(1)</sup> <sup>(2)</sup>

\* CPI-linked and prior to addition of interest.

- (1) Including exposure of NIS 2 billion for a motion for certification as a class action filed by a shareholder against the Company and officers in the Company, referring to alleged reporting omissions by the Company regarding the wholesale market and the reduction of interconnect fees, which the plaintiff estimates at NIS 1.1 billion or NIS 2 billion (depending on the method used to calculate the damage). On August 27, 2018, the court certified the claim as a class action. On October 28, 2018, the Company filed a motion for a rehearing of the certification ruling. Subsequently, the court decided to stay the proceedings until a ruling is made on the motion for a rehearing.

In the hearing on May 22, 2019 of the motion filed by the Company for another hearing, the Court proposed transferring the case for mediation. The plaintiff rejected the proposal. On July 18, 2019, a hearing was held to complete the parties' arguments in the motion for a re-hearing application and the ruling will be handed down at a later stage.

- (2) Two motions for certification of a class action amounting to a total of NIS 1.8 billion, filed in June 2017 against the Company, officers in the Group and companies in the group of the Company's controlling shareholders regarding the transaction for the Company's acquisition of DBS shares from Eurocom DBS Ltd. In accordance with the court's decision, a joint motion is expected to be filed instead of these two motions. The proceedings were stayed due to the investigation described in Note 1.2 to the Consolidated Financial Statements and at the request of the Attorney General, until October 31, 2019.

- 5.2 Further to that stated in Note 11.3 to the condensed annual separate financial information regarding a class action filed in the United States against B Communications, Ltd., the Company's controlling shareholder and officers, to which (current and former) officers of DBS and the Company were joined, and motions filed by the defendants for summary dismissal of the motion and the claim, on March 28, 2019 the Company was notified of the decision of the US court of the same date that the motions filed by DBS and the officers (current and past) of DBS and the

Company for the summary dismissal of the motion and the claim, were accepted on grounds of lack of personal jurisdiction.

- 5.3** See Notes 11.2 and 11.4 in the separate annual financial information regarding additional proceedings against the Company. The proceedings are stayed at this stage, until October 31, 2019

For further information concerning contingent liabilities see Note 10 to the Consolidated Financial Statements.

## **6. Events in and subsequent to the Reporting Period**

- 6.1** For further information concerning investigations by the Israeli Securities Authority and Israel Police, see Note 1.2 to the Consolidated Financial Statements.

- 6.2** With regard to the loss due to impairment with regard to Pelephone and DBS, see Note 5 to the Consolidated Financial Statements.

On February 13, 2019, the Company provided DBS with a credit facility or capital investments in the amount of NIS 250 million, that DBS may withdraw over a period of 15 months from said date. If such support is provided by way of credit, the repayment date of the said credit will not be earlier than the end of the credit facility period.

- 6.3** In May 2019, the Company's Board of Directors approved an irrevocable undertaking by the Company to DBS to provide a credit facility or capital investment in the amount of NIS 250 million, for a period of 15 months, as of April 1, 2019. This undertaking will replace the undertaking given under the decision of the Board of Directors dated February 13, 2019, as aforesaid (and not in addition thereto).

In March 2019, the Company invested NIS 70 million and in July 2019 a further NIS 50 million was invested, in accordance with the undertakings set out above.

See Note 4.3.2 to the Consolidated Financial Statements.

- 6.4** For information concerning the Company's engagement in an agreement for the sale of a real estate property in the Sakia complex, see Note 7 to the consolidated financial statements.

- 6.5** With regard to the new loan that the Company received from Institutional Investors, early repayment of bank loans bearing variable interest and a private placement to institutional investors by the Company subsequent to Reporting Date, see Note 8 to the consolidated financial statements.

- 6.6** For further information concerning the removal of the deferred tax asset due to the DBS carried forward losses as a result of a change in estimates, see Note 6 to the consolidated financial statements.

- 6.7** For further information concerning application for approval to issue a prospectus, see Note 19 in the consolidated financial statements.

# **Chapter E:**

## **Quarterly report on the effectiveness of internal control over financial reporting and disclosure for the period ended June 30, 2019**



The information contained in this report constitutes a translation of the report 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.



## 1. Report of internal control over financial reporting and disclosure:

### **Quarterly report on the effectiveness of internal control over financial reporting and disclosure, pursuant to Regulation 38C(a) of the Periodic and Immediate Reports Regulations, 1970:**

Management, under the supervision of the Board of Directors of Bezeq – The Israel Telecommunication Corp Limited, ("the Company"), is responsible for establishing and maintaining appropriate internal control over financial reporting and disclosure in the Company.

For this matter, the members of Management are:

1. Dudu Mizrahi, CEO
2. Ehud Mezuman, VP Human Resources Division
3. Udi Atar, VP Private Division
4. Eyal Kamil, VP Operations and Logistics Division
5. Izak Ben Eliezer, VP Technologies and Network Division
6. Amir Nachlieli, Legal Counsel
7. Erez Hasdai, VP Regulation and Economics
8. Guy Hadass, VP Corporate Communications
9. Yali Rothenberg, CFO Bezeq Group
10. Yaacov Paz, VP Business Division
11. Keren Laizerovitz, VP Marketing & Innovation Division

In addition to the said members of Management, the following serve in the Group's headquarters

1. Yehuda Porat, Head of Security Unit
2. Lior Segal, Internal Auditor
3. Shelly Bainhoren, Group Corporate Secretary and Internal Compliance Officer

Internal control over financial reporting and disclosure includes controls and procedures in the Company, which were planned by the CEO and the most senior financial officer, or under their supervision, or by whoever fulfills those functions in practice, under the supervision of the Board of Directors of the Company, and were designed to provide reasonable assurance as to the reliability of the financial reporting and the preparation of the reports in accordance with the provisions of the law, and to ensure that information that the Company is required to disclose in the reports it publishes in accordance with the provisions of the law is collected, processed, summarized and reported on the date and in the format laid down in law.

Internal control includes controls and procedures planned to ensure that the information that the Company is required to disclose as aforesaid, is accumulated and forwarded to the Management of the Company, including to the CEO and the most senior financial officer or to whoever fulfills those functions in practice, in order to enable decisions to be made at the appropriate time in relation to the disclosure requirements.

Due to its structural limitations, the internal control over financial reporting and disclosure is not intended to provide absolute assurance that misstatement or omission of information from the reports will be prevented or will be detected.

In the quarterly report on the effectiveness of internal control over financial reporting and disclosure that was attached to the Periodic Report for the period ended March 31, 2019 ("the Last Quarterly Report on Internal Control"), the internal control was found to be effective.

Up until the reporting date no event or matter was brought to the attention of the Board and Management that would change the assessment of the effectiveness of the internal control as produced in the Last Quarterly Report on Internal Control; it should be noted that on August 23, 2019 the Company received

the opinion of the senior management of the Israel Securities Authority concerning the propriety of the accounting treatment applied by the Company to recognition of the tax asset. For further information, see section 2.14 of the Chapter on the Description of Company Operations.

At the reporting date, based on the assessment of the effectiveness of internal control in the Last Quarterly Report on Internal Control, the internal control is effective.

Concerning the investigations of the Israel Securities Authority and the Israel Police see section 1.1.5 of the Chapter, Description of Company Operations in the 2018 Periodic Report and the Company's Immediate Reports referred to in that section. The Company does not have complete information about the Investigations, their content, nor the material and evidence in the possession of the statutory authorities on this matter. Accordingly, the Company is unable to assess the effects of the investigations, their findings and their effect on the Company and on the financial statements and on the estimates used in the preparation of these financial statements, if any. Once the constraints on carrying out reviews and controls related to issues that arose in the Investigations are lifted, the review of all matters related to subjects that arose during those Investigations will be completed as required.

## **2. Declaration of Executives:**

### **A. Declaration of the CEO in accordance with Regulation 38C(d)(1) of the Israel Securities Regulations (Periodic and Immediate Reports), 1970:**

I, Dudu Mizrahi, declare that:

1. I have reviewed the quarterly report of Bezeq – The Israel Telecommunication Corp Limited, ("the Company") for the second quarter of 2019 ("the Reports").
2. To the best of my knowledge, the reports do not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the reporting period.
3. To the best of my knowledge, the financial statements and other financial information in the Reports fairly present in all material respects, the financial condition, results of operations and cash flows of the Company as of the dates and for the periods presented in the Reports.
4. I have disclosed the following to the auditor of the Company, to the Company's Board of Directors, and to the Audit and the Financial Statements Committees of the Board of Directors of the Company, based on my most recent evaluation of internal control over financial reporting and disclosure:
  - A. All the significant deficiencies and material weaknesses in the design or operation of the internal control over financial reporting and disclosure which are reasonably likely to adversely affect the Company's ability to record, process, summarize and report financial information, in a way that could cast doubt on the reliability of the financial reporting and the preparation of the financial statements in accordance with the provisions of the law;
  - B. Any fraud, whether or not material, that involves the CEO or anyone directly subordinate to the CEO, or which involve other employees who have a significant role in the Company's internal control over financial reporting and disclosure
5. I, alone or together with others in the Company:
  - A. Established controls and procedures, or ensured the establishment and maintaining of controls and procedures under my supervision, designed to ensure that material information relating to the Company, including its subsidiaries as defined in the Israel Securities Regulations (Annual Financial Statements), 2010 is brought to my knowledge by others in the Company and in the subsidiaries, particularly during the period of preparation of the Reports.
  - B. Established controls and procedures, or ensured the establishment and maintaining of controls and procedures under my supervision, designed to provide reasonable assurance regarding the reliability of the financial reporting and the preparation of the financial statements in accordance with the provisions of the law, including in accordance with accepted accounting principles.
  - C. No event or matter that occurred in the period between the date of the last report (quarterly or periodic, as applicable) and this reporting date was reported to me that would change the conclusions of the Board of Directors and Management concerning the effectiveness of internal controls over the Company's financial reporting and disclosure.

Nothing in the foregoing shall derogate from my responsibility or that of anyone else in law.

Date: August 28, 2019

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Dudu Mizrahi, CEO;

**B. Declaration of the CFO of the Company and the Group in accordance with Regulation 38C(d)(2) of the Israel Securities Regulations (Periodic and Immediate Reports), 1970:**

I, Yali Rothenberg, declare that:

1. I have reviewed the interim financial statements and other financial information included in the reports for the interim period of Bezeq – The Israel Telecommunication Corp Limited, ("the Company") for the second quarter of 2019 ("the Reports" or "the Reports for the Interim Period").
2. To the best of my knowledge, the interim financial statements and other financial information included in the Reports for the Interim Period do not include any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by the Reports.
3. To the best of my knowledge, the interim financial statements and other financial information in the Reports for the Interim Period fairly present, in all material respects, the financial condition, results of operations and cash flows of the Company as of, and for, the dates and periods presented in the Reports:
4. I have disclosed the following to the auditor of the Company, to the Company's Board of Directors, and to the Audit and the Financial Statements Committees of the Board of Directors of the Company, based on my most recent evaluation of the internal control over financial reporting and disclosure:
  - A. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting and disclosure, insofar as they refer to the interim financial statements and other financial information included in the Reports for the Interim Period, which are reasonably likely to adversely affect the Company's ability to record, process, summarize or report financial information in a way that could cast doubt on the reliability of the financial reporting and the preparation of the financial statements in accordance with the provisions of the law
  - B. Any fraud, whether or not material, that involves the CEO, or anyone directly subordinate to the CEO, or which involve other employees who have a significant role in the Company's internal control over financial reporting and disclosure
5. I, alone or together with others in the Company:
  - A. Established controls and procedures, or ensured the establishment and maintaining of controls and procedures under our supervision, designed to ensure that material information relating to the Company, including its subsidiaries as defined in the Israel Securities Regulations (Annual Financial Statements), 2010, is brought to my knowledge by others in the Company and in the subsidiaries, particularly during the period of preparation of the Reports
  - B. Established controls and procedures or ensured the establishment and maintaining of controls and procedures under my supervision, designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements in accordance with the provisions of the law, including in accordance with accepted accounting principles
  - C. No event or matter that occurred in the period between the date of the last report (quarterly or periodic, as applicable) and this reporting date was reported to me in respect of the interim financial statements and to any other financial information included the Reports for the Interim Period, that would change in my opinion the conclusions of the Board and Management concerning the effectiveness of the internal control over the Company's financial reporting and disclosure.

Nothing in the foregoing shall derogate from my responsibility or that of anyone else in law.

Date: August 28, 2019

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Yali Rothenberg,  
CFO Bezeq Group