August 2, 2010

"Bezeq" The Israel Telecommunication Corp. Limited

Quarterly Report for the period ending 30.6.2010

Update of Chapter A (Description of Company Operations) of the Periodic Report for 2009

Directors' Report on the State of the Company's Affairs for the period ended June 30, 2010

Condensed Interim Consolidated Financial Statements as at June 30, 2010

UPDATE OF CHAPTER A (DESCRIPTION OF THE COMPANY'S BUSINESS)[1]
OF THE PERIODIC REPORT FOR 2009 ("THE PERIODIC REPORT")
OF "BEZEQ" – THE ISRAEL TELECOMMUNICATION CORP. LTD. ("THE COMPANY")

In this report, which contains an update of the chapter "Description of the Company's Business" from the 2009 Periodic Report, the Company has included, concerning itself and with regard to the market, forward-looking information as defined in the Securities Law, 5728-1968 ("the Securities Law"). Such information includes, inter alia, forecasts, targets, assessments and estimates relating to future events or matters, the realization of which is not certain and is beyond the Company's control. Forward-looking information in this report will usually be identified specifically, or by statements such as "the Company expects", "the Company assesses", "it is the Company's intention", and the like.

Forward-looking information is not proven fact and relies only on the Company's subjective assessment, based, inter alia, on a general analysis of the information available at the time of drafting of this report, including public announcements, studies and surveys, which contained no undertaking as to the correctness or completeness of the information in them, and which were not checked independently the Company for their correctness. The Company's assessments vary from time to time, depending on circumstances.

In addition, the occurrence and/or non-occurrence of the forward-looking information will be affected by factors that cannot be assessed in advance and are not within the Company's control, including the risk factors that characterize its operations, the developments in the general environment, and the external factors and the regulation that affect the Company's operations.

1. Description of General Development of Bezeq Group Operations

For Section 1.1 – Group Activity and Description of its Business Development

Regarding the chart describing the structure of holdings in the Company and the Company's holdings in its subsidiaries and affiliates: for closing the transaction for sale of the core control of Ap.Sb.Ar. Holdings, Ltd. ("Ap.Sb.Ar.") to B Communications, Ltd.[2] ("B Communications"), see the update to Section 1.3.1(a) below. On purchase of shares in Walla! Communications Ltd. ("Walla") by Bezeq International, Ltd. ("Bezeq International") and a tender offer of Bezeq International to purchase additional shares in Walla, see the update to Section 4.14.1 below.

For Section 1.1.2 – Mergers and Acquisitions

D.B.S. Satellite Services (1998) Ltd. ("DBS") – On June 23, 2010, the Company received a notice from Eurocom D.B.S. Ltd. ("Eurocom DBS"), a shareholder in DBS, stating that Eurocom DBS had entered into purchase agreements for all the holdings and rights of other shareholders in DBS,[3] and that in

1 The update is pursuant to Article 39A of the Securities (Periodic and Immediate Reports) Regulations, 5730-1970, and includes material changes or innovations that have occurred in the Company's business in any matter which must be described in the Periodic Report. The update relates to the Company's periodic report for the year 2009, and relates to the section numbers in Chapter A (Description of the Company's Business) in that periodic report.

2 On March 16, 2010, 012 Smile Communications changed its name to B Communications Ltd.

3 The other shareholders are Gilat D.B.S. Ltd., Lidan Investment Agencies (1994) Ltd. and Polar Communications Ltd. Subsequently, Eurocom DBS also gave notice of the execution of such an agreement with Mr. Yoav Harlap and his company Naniach Ltd.

accordance with the Articles of Association of DBS and the DBS shareholders agreement, it is proposing that the Company exercise its right of first refusal. Subsequently, the Company gave notice that it has decided not to exercise the right of first refusal, provided that the sale of the other holdings and rights as aforesaid is completed by no later than December 31, 2010, in view of the ruling of the Supreme Court on August 20, 2009 forbidding the Company from increasing its holdings in DBS beyond 50%.

Bezeq International – On the purchase of "Yad 2" by Walla, see the update to Section 4.14.1 below.

For Section 1.1.4 – Holdings in the Company

The following are details of the rates of current holdings in the Company at June 30, 2010 and August 1, 2010, and also at full dilution (assuming exercise of all of the options allocated to Group employees).

Shareholders	Percentage of holdings			
	June 30, 2010	June 30, 2010 at full dilution	August 1, 2010	August 1, 2010 at full dilution
B Communications (SP2), Ltd.	30.43%	29.77%	30.42%	29.77%
Amitim	6.60%	6.45%	6.60%	6.45%
The public	62.97%	63.78%	62.98%	63.78%

For Section 1.2 – Segments of Operation

The operations of Walla are reported under the "Others" segment since its consolidation into the financial reports of Bezeq International. On this matter, see Note 5(b)(1) to the financial statements of the Company for the period ended June 30, 2010, which are included in this quarterly report.

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

1.3.1(a) - Transactions in Bezeq shares – sale of core control

A. On April 14, 2010, the transaction was closed between Ap.Sb.Ar. and B Communications for the off-exchange sale of all the Company shares owned by Ap.Sb.Ar. – 814,211,545 ordinary shares of NIS 1 par value each, constituting on that date approximately 30.44% of the Company’s issued and paid up share capital. According to information provided to the Company, the transaction was closed after all preconditions to the agreement, including the regulatory approval required by law, were met. These include the following:

1. Approval of the Ministry of Communications for the transaction (including grant of control permits). The approval was made conditional on compliance with several conditions, whose principle points are that transactions for the purchase of end-user equipment between the Eurocom Group[4] and Pelephone be considered extraordinary transactions pursuant to Section 270(4) of the Companies Law and requires, in addition to the internal approval process within Pelephone, an approval process in the Company; discussions of the matter by the Company’s Board of Directors must be documented in detailed, comprehensive minutes and submitted to the scrutiny of the Director General of the Ministry of Communications (these two conditions were applied also to DBS, with regard to purchase of satellite end-equipment, see Section 5.17.3 below); Eurocom Group will not transfer to Pelephone information relating to supplies of products and services to its competitors; an employee of Nokia Cellular Communications Ltd. may not serve as a director of Pelephone and an employee of Pelephone may not serve as a director of Nokia Cellular Communications, Ltd.

[4] In this regard, “Eurocom Group” means all of the corporations controlled, directly or indirectly, by Eurocom Holdings (1979) Ltd. and/or Eurocom Media-Net Holdings, Ltd. with the exception of the Company, Pelephone Communications Ltd., Bezeq International Ltd. and B.I.P. Communications Solutions LP, as well as the employees of Bezeq and the aforementioned corporations, who do not work in other companies in the Group.

2. Approval of the Antitrust Commissioner, which was made conditional on compliance with several conditions, mainly the imposition of a prohibition on Eurocom Group[5] from involvement in the decision on commercial conditions that a cellular company purchasing handsets from Eurocom Cellular Communications, Ltd. offers to consumers in Israel, other than participation in their financing, and obliging Eurocom Group to sell its holdings in DBS. Until completion of this sale, Eurocom Group must transfer its shares in DBS to a Trustee who will act as owner of the shares and use its authority and/or rights to the best of its judgment for the benefit of DBS alone.

3. Approval of the Prime Minister and the Minister of Communications in accordance with the provisions of the Communications (Telecommunications and Broadcasts) Law, 5742-1982, and the provisions of the Communications (Telecommunications and Broadcasts) (Determination of an essential service provided by Bezeq, The Israel Telecommunication Corp. Ltd) Order, 5767-1997.

Purchase of the shares in the Company was contracted through B Communications (SP2) Ltd., a private company, registered in Israel, wholly owned and controlled by B Communications (SP1) Ltd. which is wholly owned and controlled by B Communications, Ltd. which is an Israeli public company registered both on the Tel Aviv Stock Exchange and on NASDAQ. The controlling shareholder in B Communications is Internet Gold – Golden Lines, Ltd., which is owned and controlled by Eurocom Communications, Ltd.

For additional information on the closing of the transaction and on those who have become interested parties in the Company as a result of the transaction, see the Supplementary Immediate Report on an Event or Matter not in the Ordinary Course of the Corporation's Business, dated April 14, 2010, and the Immediate Report of the same date concerning the parties who have become interested parties in the Company by virtue of their holdings.

B. On the matter of approval of transactions with the B Communications Group – After the transfer of control in the Company, the competent bodies of the Company approved various engagements of the Company and its subsidiaries[6] with B Communications Group, including extraordinary transactions. Such transactions are approved from time to time in accordance with the needs of the Company and its subsidiaries, and are duly reported to the public.

<u>For Section 1.3.2 – Employee stock option plans</u>

A. Regarding the 2007 employee stock options plan, in light of the expectation that the exercise price of the options will fall below the nominal value of Company's share (NIS 1) as a consequence of adjusting the exercise price of the options for the distribution of a dividend – On March 18, 2010 the Board Of Directors of the Company gave its approval for the Company to convert part of the premium registered in the Company's books to share capital, in an amount equal to the difference between the nominal value of the share and the exercise price of the options that would be exercised in this plan, up to a total not exceeding NIS 22,469,081. Conversion of the premium to share capital will be recorded on the Company's books against the actual exercise of options at the time of exercise.

B. Regarding the stock options plan from November 2007 for managers and senior employees of the Group – On March 3, 2010, after publishing its financial statements for 2009, the Company published an updated outline of the securities offered to employees.

For Section 1.4 – Distribution of Dividends.

<u>For Section 1.4.2 – Distribution of a dividend</u>

On April 8, 2010 the Company's General Meeting of shareholders resolved (following the recommendation of the Company's Board of Directors from March 2, 2010) to distribute a cash dividend to the shareholders of the Company in the total sum of NIS 2,453 million, which were, at the determining date for the distribution (April 15, 2010) NIS 0.9170679 per share and 91.70679% of the Company's issued and paid up capital. The dividend was paid on May 3, 2010.

---

[5] For this matter, "Eurocom Group" means all the corporations controlled, directly or indirectly, by Eurocom Holdings (1979) Ltd. and/or Eurocom Media-Net Holdings, Ltd., as well as and any person associated with these corporations, with the exception of the Company and companies in which the Company holds more than 50% of the shares.

[6] Approval of engagements of the subsidiaries Pelephone Communications Ltd., Bezeq International Ltd. and Bezeq On Line Ltd. and of DBS. The approval in the Company is given after approval of the transactions by the competent bodies of those companies.

The distributable retained earnings at the date of the report – NIS 1,280 million (surpluses accumulated in the past two years). On August 2, 2010, the Board of Directors of the Company resolved to recommend to the general meeting of the shareholders of the Company that a cash dividend of NIS 1,280 million be distributed to the shareholders.

For Section 1.5 – Financial Information Regarding Segments of Operation of Bezeq Group

For Section 1.5.4 – Principal results and operational data

A. Bezeq Fixed-line (the Company's activity as domestic operator) (NIS millions except where stated otherwise)

	Q2 2010	Q1 2010	Q4 2009	Q3 2009	Q2 2009	Q1 2009
Revenue	1,307	1,304	1,316	1,343	1,318	1,326
Operating profit	503	490	161	491	434	437
Depreciation and amortization	171	170	194	184	205	211
EBITDA (Earnings before interest, taxes, depreciation and amortization)	674	660	355	675	639	648
Cash flow from operating activities	523	393	651	526	408	635
Payments for investment in property, plant & equipment and intangible assets	247	238	220	204	191	238
Proceeds from sale of property, plant & equipment and intangible assets	26	15	9	19	9	49
Number of active subscriber lines at end of period (in thousands)	2,425	2,458	2,489	2,518	2,547	2,579
Average monthly revenue per line (NIS)* (ARPL)	81	80	82	83	81	81
No. of outgoing minutes (in millions)	2,763	2,773	2,964	3,096	3,014	3,123
No. of incoming minutes (in millions)	1,634	1,627	1,674	1,737	1,664	1,654
No. of ADSL subscribers at end of period (in thousands)	1,051	1,045	1,035	1,026	1,016	1,011
Average monthly revenue per ADSL user (NIS) (ARPU)	75	75	72	72	69	68

* Not including revenue from data transmission and communication services, internet services, services to communication operators, contract work and others.

B. Pelephone (NIS millions except where stated otherwise)

	Q2 2010	Q1 2010	Q4 2009	Q3 2009	Q2 2009	Q1 2009
Revenue	1,429	1,393	1,393	1,372	1,346	1,265
Operating profit	362	322	251	316	321	302
Depreciation and amortization	149	149	158	155	151	139
EBITDA (Earnings before interest, taxes, depreciation and amortization)	511	471	410	471	472	441
Net profit	267	259	181	231	233	230
Cash flow from operating activities	378	350	55	395	290	375
Payments for investment in property, plant & equipment and intangible assets	114	92	101	146	163	149
No. of subscribers at end of period (in thousands)	2,807	2,789	2,766	2,721	2,694	2,669
Average monthly minutes of use (MOU) per subscriber (minutes)	348	336	339	339	329	323
Average monthly revenue per subscriber (NIS) (ARPU)	136	133	132	136	131	128
No. of 3G subscribers at end of period (in thousands)	1,698	1,619	1,531	1,407	1,307	1,217
% Revenue from value added services and content, of revenues from cellular services (%)	23.0%	22.6%	20.8%	20.0%	19.1%	18.5%

C. Bezeq International (NIS millions except where stated otherwise)

	Q2 2010*	Q1 2010	Q4 2009	Q3 2009	Q2 2009	Q1 2009
Revenue	342	343	334	332	327	324
Operating profit	121	62	67	66	68	60
Depreciation and amortization	27	23	23	21	21	20
EBITDA (Earnings before interest, taxes, depreciation and amortization)	147	84	89	88	88	80
Net profit	105	46	49	51	56	44
Cash flow from operating activities	66	59	72	82	83	84
Payments for investment in property, plant & equipment and intangible assets**	33	37	39	33	26	21

* Second quarter results do not include the activities of Walla. However, they do include one-time profit generated from the consolidation of Walla's operations in the financial statements of Bezeq International.

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

D. DBS (NIS millions except where stated otherwise)

	Q2 2010	Q1 2010	Q4 2009	Q3 2009	Q2 2009	Q1 2009
Revenue	396	391	390	380	376	384
Operating profit	7	59	63	61	59	66
Depreciation and amortization	68	64	63	59	56	57
EBITDA (Earnings before interest, taxes, depreciation and amortization)	75	122	126	120	115	122
Net profit (loss)	(143)	(8)	(38)	(88)	(95)	(1)
Cash flow from operating activities	109	121	91	135	93	91
Payments for investments in property, plant & equipment & intangible assets *	63	61	53	87	60	61
No. of subscribers at end of period (in thousands)	573	571	571	567	562	560
Average monthly revenue per subscriber (NIS) (ARPU)	231	229	229	224	224	228

* This item also includes investments in the cost of subscriber acquisition.

For Section 1.7 – General environment and the effects of external factors on Group operations

In July 2010, the Ministry of Communications distributed a memo – The Israel Communications Authority Law 5770-2010, concerning the establishment of a communications authority, which would be the main regulatory body in communications in Israel, for telecommunications and for broadcasts and would hold the powers of the Ministry of Communications, the Second Television and Radio Authority, the Second Authority Council and the Council for Cable and Satellite Broadcasts. According to the provisions of the memo, the Government will appoint a Communications Council, which will set the Authority's policy for communications, except as concerns broadcast content, and will have various powers that will be granted by legislation for communications except on the matter of broadcast content, including grant of licenses, supervision of license-holders and setting fees, license fees and other payments noted in the memo, which will be paid by the license-holders. The Government will also appoint a Broadcast Content Council, which will set the policy of the Communications Authority for the content of broadcasts and will hold various positions and powers with regard to broadcast content, including supervision of license-holders' compliance with broadcasts on the terms of their licenses with regard to the content of broadcasts.

2. Fixed-line Domestic Communications – Bezeq, The Israel Telecommunication Corp. Ltd. ("the Company")

For Section 2.3 – Breakdown of revenue and profitability of products and services

For data updates on the breakdown of Company revenues by products and services, see Note 9 to the Company's financial statements and Note 2 to the financial data from the consolidated financial statements attributed to the Company as parent, for the period ended June 30, 2010, which are attached to this quarterly report.

For Section 2.6 – Competition

For Section 2.6.1 – Telephony

For sub-section A – On March 22, 2010, the Ministry of Communications published a hearing for HOT regarding the marketing of packages that include broadcast, telephony and internet access services, whereby it is considering determining that the maximum commitment period will be 18 months for all the services in the package, including broadcasts. In the opinion of the Ministry, this limitation will also apply to similar joint packages offered by the Company and its subsidiaries when they are permitted.

For sub-section D – On the Government's decision to increase competition in the cellular segment – see Section 3.18.3.2 below.

For Section 2.6.2 – Broadband internet access (and for Sections 2.1.8, 2.6.3, 2.6.4)

On July 15, 2010, during its discussions of the Budget Law, the Government decided to instruct the Minister of National Infrastructures and the Minister of Finance to exercise their authority under the Electricity Economy Law, 5756-1996 ("the Electricity Economy law"), to permit Israel Electric Corporation ("IEC") to operate in communications, on certain terms, principally these: a "communications company" will be established to use the fixed-line communications infrastructure on the electricity grid; IEC will not hold more than 49% of the means of control in the communications company and will not control it; the controlling shareholder will be selected in a public election proceeding by an election committee to which IEC will appoint half the representatives and the State the other half; a communications license-holder, its controlling interest or a company they hold, shall not hold means of control in the communications company unless approved by the Minister of Communications; the communications company shall have a non-exclusive right of use of the infrastructures held by IEC; there will be full corporate, managerial and accounting separation between IEC and the communications company, and no cross-subsidization between them. The decision requires the Government's economics cabinet to make a decide on the establishment of the communications company within 45 days, and the necessary legislative amendments for implementation of the decision will be made to the Electricity Economy Law and the Communications (Telecommunications and broadcasts) Law, 5742-1982 ("the Communications Law").

For Section 2.6.7 – Adoption of the conclusions of the Gronau Committee

Concerning tariff flexibility for Bezeq – alternative payments baskets – On July 15, 2010, the Government decided, during its discussions of the Budget Law, to amend the Communications Law and to modify the proceeding for approval of an alternative basket of payments in a way that shortens the proceeding and also allows approval in the absence of opposition within a certain time, based on a law memo that was distributed on June 30, 2010.

Concerning royalties – For the Government's decision on July 15, 2010 during its discussions of the Budget Law – see Section 2.16.3 below.

For Section 2.6.8

Regarding the appointment of a committee to consider a tariff arrangement, the committee’s writ of appointment was issued on March 28, 2010. According to the writ, subjects not included therein may be brought for discussion in the committee only if the Minister of Communications does not object within seven days of the subject having been brought to his attention. Furthermore, if the committee considers formulating recommendations that are not consistent with recommendations of the Gronau Committee, as approved by the Minister of Communications (see section 2.6.7 in Chapter A of the Company’s Periodic Report at December 31, 2009), the committee will open the subject to public comment prior to making its recommendations. As requested, the Company presented its position to the committee.

For Section 2.7 – Property, Plant and Equipment, and Installations

2.7.4 Real estate

During the first six months of 2010, the Company sold six properties with a total of area of approximately 14,000 sq. mtr. of land and 12,000 sq. mtr. built up, for a total amount of approximately NIS 145 million.

For Section 2.9 – Human Resources

On March 25, 2010, the Company received notice of a strike pursuant to the Labor Disputes Law, 5717-1957, which was declared by the Histadrut, commencing April 11, 2010. The issues in dispute, according to the notice, are disregard of union demands, action not yet been taken with regard to the transfer of control, and negotiations for signing a new collective agreement for regulating employees’ rights following transfer of the controlling share in the Company. As a result, negotiations are taking place between the management of the Company and representatives of the employees. It is noted that on May 2, 2010, the union embarked upon limited sanctions.

For Section 2.9.6 – Employee compensation plans

For Section 2.9.6.2 concerning adjustment of the exercise price lower than the nominal value of a Company share in the 2007 employee stock options plan, and for Section 2.9.6.3 concerning publication of update of the stock options plan for managers – see Section 1.3.2 above.

For Section 2.10 – Raw Materials and Suppliers, Purchase of Equipment, and Suppliers

For Section 2.10.3 – Dependence on suppliers

The Company is dependent on Verse Networks for public switching equipment.

For Section 2.13 – Financing

For Section 2.13.1 – Average and effective interest rate on loans, and for Section 2.13.4 – Credit received after December 31, 2009

On April 15, 2010, the Company completed raising debt in the amount of NIS 1.5 billion, through loans from Israeli banks for an average duration of 4.6 years. On May 6, 2010, the Company recycled bank loans received on March 12, 2009 in the amount of NIS 400 million, through loans from Israeli banks for an average duration of 4.6 years (see Note 13(B) to the financial statements of the Company for the period ended June 30, 2010, which are included in this quarterly report).

Further, below are up-to-date data on the average effective interest rate on the Company's bank loans at today's date:

Source of financing	Amount at May 6, 2010	Type of currency or linkage	Average interest rate	Effective interest rate
Banks	NIS 1,100 million	Unlinked NIS	Prime minus 0.21%	Prime* minus 0.19%
Banks	NIS 800 million	Unlinked NIS	5.56%	5.64%

* For prime at 3.25% as of August 2010.

For Section 2.13.7 – Credit rating

On May 27, 2010, the Company received notice from Standard & Poor's, which set the Company's international rating at (BBB plus), and from Standard & Poor's Maalot which set the rating of the Company and its debentures at (AA plus), ratifying these ratings and removing them from CreditWatch with negative outlook. The rating forecast is stable.

For Section 2.16 – Limitations and supervision of the Company's activities

For Section 2.16.1 – Supervision of the Company's tariffs

In accordance with the Communications (Telecommunications and broadcasts) (Calculation and linkage of telecommunications payments) Notice, 5770-2010, the Company's tariffs were updated effective from June 1, 2010, based on the formula set in the Communications (Calculation and linkage of telecommunications payments) (Amendment) Regulations. 5770-2010, so that the fixed monthly payment for a telephone line and for a line in the combination digital network basic service increased by 3.9147% and fees for the other controlled services provided by the Company increased by 0.5669%. In addition, in accordance with the amendment to the Communications (Telecommunications and broadcasts) (Payments for interconnect) (Amendment No. 2) Regulations, 5770-2010, interconnect fees paid by cellular operators and domestic operators for call completion in a domestic operator network and interconnect fees paid by the international operators for international calls originating or ending in a domestic network, increased by 0.5669% commencing June 1, 2010.

For Section 2.16.2 – The Company's general license

In the matter of the Minister of Communications' policy letter "Marketing Bundles", dated May 10, 2010, the Company's general license was amended so that subject to conditions, the Company may market to an individual subscriber a bundle of services that includes services provided by a subsidiary. Those conditions include the existence of a group of services in similar format marketed by another license-holder, approval by the Director General of the Ministry of Communications for the requested bundle (including by his non-opposition within a fixed time), allowing the customer to purchase each service or package of services in the bundle separately, on the same terms as those offered for the bundle. The licenses of the subsidiaries were also amended, allowing them, subject to conditions, to market bundles that contain services of the Company. Subsequently, the Company started filing applications and receiving approvals for marketing such bundles.

During April 2010, the Ministry of Communications published a hearing for all communications operators on the subject of exit fees that a license-holder may demand of a private subscriber who does not comply with the commitment in the agreement between him and the license-holder. The hearing states that responses should be filed by June 1, 2010.

The main points of the hearing:

1. Limitation of the maximum penalty to a uniform formula: the product of 10% of the average monthly payment from the start of the commitment period multiplied by the number of months remaining to the end of the commitment on the date of its violation. The maximum penalty will include all the types of components of the "return of benefits" and nothing will be paid in excess of that amount.

2. "One-time" benefits such as gifts (laptop, packages of free services, etc.) will not be included in the return of benefits that can be demanded from the customer.

3. A customer who purchased a handset in a transaction on installments will not be required to pay the balance due for the handset in one payment when he exits and violates his commitment, but rather, the installments will continue as initially determined.

For the Government decision on July 15, 2010 in the matter of exit fees relating to the cellular operators, see the update to Section 3.18.3.2 below.

<u>For Section 2.16.3 – Royalties</u>

On July, 15, 2010, the Government decided, during its discussions of the Budget Law to instruct the Ministers of Finance and Communications to amend the Royalties Regulations, as an emergency directive for a period of three years, so that the percentage to be paid as royalties by domestic operator license-holders, except for a general special domestic operator license-holder, and cellular, satellite and cable broadcast operator license-holders, will increase from 1% in 2010 to 2% in 2011 and 2.5% in 2012 and 2013. Amendment of the royalties regulations applicable to the Company require approval by the Knesset Finance Committee.

<u>For Section 2.16.4 – Authority for real estate</u>

On June 21, 2010, the Planning and Construction (Application for a permit, its terms and fees) Regulations, 5770-2010 were published and will come into force 90 days after their publication, imposing on an applicant for a permit to erect a residential building a duty to install infrastructure for telephone, radio, television and internet, so that the customer can choose whichever provider he wants. In commercial buildings, if communications infrastructures are installed, the infrastructures must be installed underground. The Ministry of Communications announced on July 14, 2010 that it intends to amend the domestic operator and satellite operator licenses so as to impose on their holders a duty to provide maintenance service for the interior wiring in apartments, which was installed by the permit applicant, which will not grant ownership or any proprietary rights to the license-holders. The license-holders were requested to respond by August 10, 2010.

<u>For Section 2.16.8 – The Telegraph Ordinance</u>

In the matter of the dispute in respect of fees in Judea, Samaria and Gaza – On May 26, 2010 a letter from the Attorney General's office demanded payment of approximately NIS 73.5 million in respect of a frequency debt. As noted in the Company’s Periodic Report at December 31, 2009, the sum is in dispute.

<u>For Section 2.16.11 – Erecting broadcasting facilities</u>

Following a meeting in July 2009 of the Main Planning Subjects Sub-Committee of the National Council, in which the Ministry of Communications and Ministry of Transport were instructed to consider, prior to approval of NOP 36B by the National Council, grant of Civil Aviation Authority approvals for the existing broadcasting facilities of the Company that are supposed to be included in the plan, the Company, in coordination with the Ministry of Communications and the Ministry of Transport, mapped all the aforementioned broadcasting sites and obtained approval in principle for them from the Civil Aviation Authority.

For Section 2.17 – Substantial Agreements

For Section 2.17.5 – The Management Agreement

Following the sale of the core control in the Company by Ap.Sb.Ar. (see update to Section 1.3.1(a) above), the management agreement with a company owned and controlled by the shareholders in Ap.Sb.Ar. was terminated on April 14, 2010.

Furthermore, on June 10, 2010, the general meting of the shareholders of the Company approved (after approval by the Audit Committee and the Board of Directors) the Company's engagement with Eurocom Communications, Ltd. in a new management agreement, under which the Company will receive ongoing management and advice services for USD 1.2 million per year. The term of the agreement is three years, commencing June 1, 2010.

For Section 2.18 – Legal Proceedings

For Section 2.18.2 – In the matter of a claim filed in January 2004 against the Company and Makefet Fund by 320 employees on the matter of selection of a pension track: Following a decision to deny the claim and an appeal of that decision, a petition filed by the plaintiffs in the High Court of Justice for revocation of the decision of the National Labor Court was dismissed *in limine* on June 6, 2010.

For Section 2.18.3 – In the matter of the suit and application for certification as a class action filed in September 2000 against the Company, alleging that the Company unlawfully collected “collection expenses": In March 2010, the District Court certified the case as a class action suit, where the cause of claim is restitution of the fee that the Company collected unlawfully, by virtue of Section 1 of the Unlawful Enrichment Law, and the class of the claim is whoever who was debited for collection expenses despite having paid their bill before the Company began collection proceedings, from November 3, 1999 through December 7, 2006. The Company intends to file an application for leave to appeal this decision.

For Section 2.18.5 – In the matter of a claim filed in January 2002 against the Company and against Bezeq International by an international communications operator, for payment of monetary compensation and writs of mandamus in connection with customer allocation to the international call operators: On May 13, 2010, the Court allowed the plaintiff to amend the statement of claim so as to extend the period covered by the claim, change the manner of calculating the damages, and include some new facts (the original amount of the claim remained unchanged at NIS 53 million). On this matter, see also the update for Section 4.19.2 below.

For Section 2.18.7 – In the matter of a claim and application for certification as a class action, which was filed in May 2006 against the Company, alleging deception in advertising in the matter of a charge for calls from a Bezeq line to a cellular line: On May 10, 2010, the Court certified the claim as a class action, where the cause of claim is deception relating to advertising the cost of a call minute from a Bezeq line to a cellular line, and the class is Company subscribers who made calls from the Company's lines to cellular lines between July 1, 2005 and September 1, 2005 at the earliest. The Company has filed an application for leave to appeal the certification decision and an application for a stay of proceedings until a decision is made by the appellate instance.

For Section 2.18.14 – In the matter of a claim for arbitration dated October 26, 2008, filed by one of the shareholders in DBS against the Company and another DBS shareholder: On June 30, 2010, following the parties' application for a stay of the arbitration proceedings in light of the plaintiff's execution of an agreement for the sale of its shares in DBS, the arbitrator decided to stay the arbitration proceedings until receipt of other notification from the parties. According to the plaintiff's notice, upon fulfillment of the preconditions in the agreement and it taking force, it will not wish to continue the proceeding.

For Section 2.18.16 – In the matter of a claim and application for certification as a class action, which was filed in November 2009 on the subject of the 144 information service: On May 27, 2010 the plaintiff gave notice that it was withdrawing the application for certification and the Court allowed the notice of withdrawal, dismissed the claim and stuck out the application for certification. On July 12, 2010, an action and application for certification as a class action were filed against the Company in the Central District Court, alleging that the Company offers its customers call tracks for a fixed monthly payment which results in loss of money for the customers for whom the track is not worthwhile, and misleads them. The plaintiff is claiming restitution of the difference between the amount paid by the customers in the monthly track and the amount that they would have paid in the regular track, a sum it estimates at "tens of millions of shekels", as well as compensation of NIS 1,500 per customer for alleged intrusion of privacy.

On July 28, 2010 the Company received an action together with an application for its certification as a class action, which were filed against it in the Tel Aviv District Court. According to the plaintiff, as a result of a malfunction in the telephone lines (which was not repaired by the Company for 34 hours), Company subscribers were denied the ability to call the telephony subscribers of Hot Telecom LP ("Hot"). It is alleged that this resulted in the Company causing its subscribers various wrongs, in respect of which the plaintiff demands compensation of NIS 100 per subscriber. The total amount of the claim is estimated by the plaintiff at NIS 250 million. The plaintiff is seeking certification of this claim as a class action in the name of the Company's subscribers. It is noted that in 2006, an application was filed for certification of a class action on the same subject in the name of Hot's subscribers, and that claim ended in 2009 in a settlement agreement (see Section 2.18.18 of the Company 2009 Periodic Report).

3. Cellular Telephone – Pelephone Communications Ltd. ("Pelephone")

For Section 3.7.2 4 – Competition

Further to the work of team to formulate conditions for the frequencies tender, in March 2010 the Ministry of Communications published a hearing on communications infrastructure cooperation among cellular communication licensees. According to the Ministry's proposal, after the frequencies are allocated to the new operator by tender and during the interim period until the new operator is able to fully deploy its cellular network, the new operator will be allowed to share the infrastructure of existing operators. The Ministry is proposing several ways for sharing infrastructure: sharing sites, sharing masts, sharing buildings, sharing imported equipment and sharing antennas. The Ministry is considering requiring existing licensees to share communications infrastructure, and the current hearing requests the operators' position on how this might be implemented. Pelephone submitted its response to the hearing, stating that cooperation among operators already exists in the use of infrastructure (e.g. masts) where there is no restriction on such cooperation because of the Antitrust Law, and that it is technically possible and financially justifiable for such cooperation to exist. The Ministry of Communications has not yet formulated its decision on the matter.

For Section 3.7.2.7 – Competition

MVNO licenses were recently granted to a number of companies, and applications have been submitted to the Ministry of Communications by other companies for receipt of such licenses.

For Section 3.15.6 – Credit rating

Following the notice of Standard & Poor's Maalot transferring the rating of Pelephone's October 2009 local debenture to CreditWatch, in May 2010 the rating agency ratified the AA+ rating for the issuer and for its debentures. The rating outlook is stable, and reflects the Standard & Poor's Maalot assessment that Pelephone will remain a material core holding in Bezeq Group.

For Section 3.17.1 – The environment

The regulations mentioned in this section do not include a chapter that was proposed, the subject of which was permitted maximum levels of human exposure to radiation from a source of radiation and the safety ranges from communication transmission facilities. The chapter also included a restriction on positioning a radiation source on roof balconies. Therefore, the Ministry for Protection of the Environment distributed to government ministries a proposed text for amendment of the Non-Ionizing Radiation (Amendment – Safety ranges and permitted maximum exposure levels for the matter of radiation in radio frequencies) Regulations, 5769-2009 ("the Proposed Regulations"). The text as proposed was opposed by the Minister of Communications due to the implications for the communications economy. However, the Ministry for Protection of the Environment recently sent to the Ministry of Communications a revised text of the regulations, which allow a source of radiation to be positioned on roof balconies. These regulations will be discussed on behalf of the Government by the Knesset's Domestic and Environment Committee. In addition, on June 27, 2010, an injunction was given (as part of a petition to the High Court of Justice, which is pending, concerning non-promulgation of regulations for the supervision of radiation), ordering the Minister for Protection of the Environment and the Minister of Communications to explain why the proposed regulations should not be brought immediately for approval of the Knesset's Domestic and Environment Committee, and the State is required to file its response affidavits by October 5, 2010.

The Ministry for Protection of the Environment has been working recently to promote a move for the continuous supervision and monitoring of transmission centers. This does not refer to external monitoring of the radiation strength of the radio transmissions from the base sites, but rather, to the use of computerized recordings from a control system at the transmission sites and their examination for verification of relevant transmission data according to the system. The technology is a new one, and its application faces various impediments – technical, technological and legal. Pelephone is working with the Ministry for Protection of the Environment to advance the process while responding adequately to these difficulties. As part of this effort, Pelephone submitted to the Supervisor of Radiation large quantities of requested data even though those data had been submitted in the past, in the technical form requested. Nevertheless, the process has not been completed and some of the difficulties have not been resolved. The Ministry for Protection of the Environment is trying to show the difficulties that have been raised and the time that has elapsed as unjustified, and in July 2010 it announced that it was halting the issue of new set-up and operating permits. Pelephone is continuing its efforts to advance the move, while considering its steps and safeguarding its rights,

For Section 3.18 – Restrictions on and regulation of Pelephone's operations

For Section 3.81.2.1 – Controlled tariffs, and for Section 3.7.2.3 – Competition

In May 2010, the Ministry of Communications published a hearing on lowering interconnect tariffs in the networks of the cellular operators in the following manner (not including VAT):

A. For call completion – from 25.1 agorot to 4.14 agorot commencing August 1, 2010, followed by gradual reductions down to 2.57 agorot by January 1, 2014.

B. SMS completion – from 2.85 agorot to 0.19 agorot commencing August 1, 2010, followed by gradual reductions down to 0.13 agorot by January 1, 2014.

The recommendation for the reduction is based on the results of the cost model built for the Ministry by NERA Consulting.

In June 2010, Pelephone submitted its detailed position on the hearing, stating that the Ministry of Communications' recommendation is extreme, disproportionate, and based on a theoretical model that requires adjustments and on erroneous assumptions and costs. Pelephone hired the services of TASC Consulting for preparing its position.

At the beginning of July 2010, Pelephone representatives appeared for a frontal hearing before the Minister of Communications and members of his staff, for an oral presentation of Pelephone's position. NERA is expected to present its response to the remarks of the operators concerning the gaps in the cost model, at the beginning of August 2010, and following that response, the Ministry of Communications is expected to formulate its final decision on lowering the interconnect tariffs.

Pelephone is unable at this stage to asses the full impact of this amendment over time, but believes that if the tariffs are lowered as described in the hearing, it could have a significantly adverse effect on the results of its operations.

For Section 3.18.3.2 – Principal changes in Pelephone's license

A. During March 2010, the Ministry of Communications published a hearing for a list of changes to the MRT license in several consumer fields. The two central and most significant changes for Pelephone are:

   Receiving the express permission of existing customers for using various content services (for example, receiving paid SMS, sending SMS messages at a special rate, access to the Company's cellular portal, etc.) rather those services being the default situation if instructions to block the services is not received from customers.

   Informing customers by SMS when they have used 75% and 90% of a package of services.

   These two changes are likely to have substantive business and operational consequences. Pelephone prepared its responses to all of the proposed changes and particularly to these two items, and requested frontal discussions with the Ministry of Communications on these issues.

B. At the end of April 2010, the Ministry of Communications published a hearing on exit fees, the main points of which are these:

   1. An exit fee will be calculated by the following formula: 10% * (average monthly bill) * (number of months remaining to the end of the commitment). The exit fee is a fee that Pelephone charges subscribers who wish to disconnect from the service during the commitment period defined in the agreement.

   2. Transactions for the purchase of terminal equipment will be made only by means of credit transactions on installments and not by standing order that debits the subscriber's credit

card, so as to enable the subscriber to continue the payment schedule even after violating the commitment and abandoning the operator from which it purchased the handset.

Pelephone submitted its response to the hearing, stating that calculation of the exit fees according to the proposed formula significantly lowers the amount of the fee and does not reflect return of the benefit granted to the subscriber in the engagement, and that debiting transactions for the purchase of terminal equipment will harm the ability of cellular customers to purchase advanced terminal equipment and benefit from an easy payment schedule. The Ministry of Communications' decision on the matter has not yet been given.

C. In the draft 2011 Budget Law and the Arrangements Law submitted for Government approval, in the chapter dealing with communications, the following main steps were approved at the meeting on July 15, 2010:

1. To amend the Communications Law so as to require cellular operators that own infrastructure to allow a new operator domestic roaming on their networks for a period of up to 10 years or until full deployment of an independent network by the new operator. In the absence of agreement on a roaming tariff between a cellular operator that owns infrastructure and a new operator, the tariff will be set at the interconnect tariff until a final tariff is set by the Minister of the Finance and the Minister of Communications.

2. To implement a legislative amendment so that the exit penalties are calculated in the format proposed by the Ministry of Communications in a hearing it published on the subject (as described above).

3. To implement a legislative amendment to ensure complete neutrality in the cellular internet network.

4. To implement a legislative amendment so as to grant the Minister of Communications authority to determine various directives concerning competition in the terminal equipment market.

The above four items must be approved by the Knesset, since they necessitate legislative amendments.

5. To implement a legislative amendment so as to increase the percentage of royalties from communications operators to 2% in 2011 and to 2.5% in 2012-2013.

6. Subject to the Ministry of Communications holding hearings, Government decisions to promote the following matters were approved:

   - Shortening the commitment period to 12 months.
   - Shortening the credits period in respect of purchasing terminal equipment, to 12 months.
   - Promotion of grant of licenses to VOC operators.
   - Appointment of an inter-ministry committee to consider ways for sharing cellular infrastructure.

Pelephone is unable at this stage to assess the impact of all the legislative amendments, amendments to the license and the steps described above. However, Pelephone believes that full or partial application of these steps could adversely affect the results of its operations.

For Section 3.18.3.2B – Principal changes in Pelephone's license

Following the Ministry of Communications' notice to the High Court of Justice concerning changing its position on amendment of the license with regard to a mechanism for identifying users of erotic services as adults, on February 24, 2010 the petition on this matter was struck out at the request of the petitioner. Subsequent to that notice, a hearing was published for the operators, in which a more stringent adult identification mechanism was proposed, by means of adding a personal identification detail. Pelephone submitted its response to the hearing, stating that it opposes the change to the existing mechanism.

For Section 3.18.3.2G – Principal changes in Pelephone's license

Further to the Ministry of Communications policy document concerning the marketing of joint packages by the Company and its subsidiaries when the Company's share in the fixed-line telephony market falls to 85%, in May 2010 the Ministry of Communications published a final amendment to the licenses of the Company and Pelephone. See also the update for Section 2.16.2 above.

For Section 3.18.3.2H – Principal changes in Pelephone's license

In May 2010, the Knesset Technology Science and Technology Committee decided that by the end of 2010, cellular operators would offer tariff plans in which the customer is allowed to limit its monthly bill to a particular sum, and that the matter would be regulated by the Ministry of Communications without need for legislation. Accordingly, the private bill on the matter was removed from the agenda.

For Section 3.18.5 – Site construction licensing

NOP 36/A/1

Amendment of NOP 36/A – The Ministry of Communications submitted its remarks on the text of the new NOP as approved by the National Council's Sub-committee for Planning, proposing mainly the removal/narrowing of various restrictions on the erection of new transmission facilities and joining existing facilities. On June 1, 2010, the National Council discussed the Ministry of Communications' remarks and decided to reject most of them and to approve the new text as approved by the Planning Sub-committee, while making minor changes. Approval of the NOP in its new version is now subject to the approval of the Government and publication in the Official Gazette for it to come into force.

Wireless access facility regulations

On March 9, 2010 a revised notice was filed in the HCJ on behalf of the State, stating that on March 7, 2010, the Minister of the Interior had submitted to the Knesset Economics Committee the draft Planning and Construction (Installation of a wireless access facility for cellular communication) Regulations, 5770-2010 ("the Wireless Access Regulations"). The proposed Wireless Access Regulations are very narrow and lay down extremely restrictive conditions for exemption from a building permit for a wireless access facility. The Regulations were also forwarded for consultation with the National Planning and Construction Council. In view of the foregoing, it was determined that the State will issue a revised notice on the matter by July 1, 2010, without requested interlocutory orders being given as to termination of the use of this track.

On July 15, 2010, a revised notice was filed in the HCJ on behalf of the State, stating that on May 26, 2010 the Knesset Economics Committee had discussed the application of the Minister of the Interior for the approval of the Committee for the draft Wireless Access Regulations. At that meeting, the Economics Committee decided that it would discuss the draft Regulations further only after the fulfillment of the duty of consultation with the National Planning and Construction Council. On June 1, 2010, the National Council discussed the draft Wireless Access Regulations and decided, inter alia, that in view of regulation of the erection of communications facilities in NOP 36/A/1, the possibility of grant of exemption also according to the Regulations should be narrowed to the extent of its complete cancellation, and in these circumstances, it does not see fit to recommend that the Minister of the Interior promulgate the Regulations. On June 28, 2010, the Ministry of the Interior approached the Knesset Economics Committee and requested that the Committee hold another urgent discussion of the draft Wireless Access Regulations. In view of the foregoing, the HCJ will be requested not to give an interlocutory order at this time, and to allow the State an extension for filing another revised notice by September 15, 2010.

In Pelephone's estimation, if the Wireless Access Regulations are approved as proposed, the possibility of using the exemption from a building permit track for setting up cellular access facilities will be very significantly reduced. This, together with the proposed severity of the conditions for erecting the base sites in the parallel track of the new NOP 36/A, can be expected to considerably raise the height of barriers to the erection of new transmission sites and access facilities, and also to adversely affect the quality of the cellular network.

For Section 3.21 – Legal proceedings

For Section 3.21.3 – In the matter of a claim and application for its certification as a class action filed in the District Court in December 2002 against Pelephone and Cellcom, in respect of interconnect fees for incoming calls for a total of NIS 4 billion, of which NIS 2.4 billion against Pelephone: In May 2010, the appeal against dismissal of the claim filed by the plaintiff, was dismissed.

For Section 3.21.6 – In the matter of a claim and application for its certification as a class action which was filed in the District Court in June 2007 against Pelephone, concerning subscribers of an immigrants program in which the subscribers were debited in units of one minute, and concerning failure to include a list of tariffs with the agreements, in a total amount of NIS 239 million: In July 2010 the claim was dismissed.

For Sections 3.21.12 and 3.21.13 – In the matter of two claims with applications for certification as class actions filed in January 2009 in the District Court for restitution of amounts allegedly collected by Pelephone for surfing on a handset while the handset is being repaired, one for NIS 219 million and the other for NIS 570 million: In June 2010 the two actions were dismissed following a settlement agreement between the parties.

In March 2010, a claim was filed in the Tel Aviv District Court together with an application for its certification as a class action. The total amount of the claim is NIS 4.2 billion, and the amount against Pelephone is NIS 2.1 billion. According to the applicants, Pelephone acts in contravention of its license and the law in that is does not purchase insurance covering liability for bodily harm arising from exposure to cellular radiation. The application also includes relief requested for an order instructing Pelephone to take out such insurance.

In May 2010, a claim was filed in the Central District Court together with an application for its certification as a class action. The action was filed against the four cellular companies (Pelephone, Partner, Cellcom and Mirs) where the amount against each of Pelephone, Partner and Cellcom is NIS 3.68 billion and the total amount of the action (against the four companies) is more than NIS 12 billion. According to the applicants, the cellular companies are in dereliction of the following duties: (1) to erect cellular antenna sites of the required scope, proportion and deployment; (2) to check, correct and provide information about the non-ionizing radiation values in cellular handsets after repair, etc.; (3) to warn against the risks involved in how the cellular handset is held. The application includes numerous other declaratory reliefs and applications for writs of mandamus relating to the above matters.

In June 2010, a claim was filed in the Central District Court together with an application for its certification as a class action. The amount of the personal claim is NIS 958 (plus linkage and interest). The total amount of the action is not stated, but the application notes that it is estimated in the hundreds of millions of shekels. According to the applicant, Pelephone collects payment from its customers for services to which the customers have not requested to subscribe, and transfers their personal information to external suppliers without approval, which contravenes the agreement and the law. The claim is for restitution of those moneys. The application also includes reliefs for orders instructing Pelephone, inter alia, to cease these debits and to cease transferring the information to suppliers.

4. International communications, internet and NEP services – Bezeq International Ltd. ("Bezeq International")

For section 4.1.2 – Legislative and statutory restrictions applicable to Bezeq International

In March 2010, the Ministry of Communications published a request for positions of cellular license-holders in the matter of providing broadband telephone services for a subscriber who is outside Israel. A possible decision by the Ministry of Communications on this question, allowing Bezeq International and the other companies to provide telephone services by means of broadband access to the internet, could impact positively on the business of Bezeq International.

For Section 4.1.2.7 – Amendment of the general license – Sale of service bundles – On May 10, 2010 Bezeq International received a letter from the Director General of the Ministry of Communications, containing amendments to the licenses of the Company, Bezeq International and the other subsidiaries of the Company, relating to the marketing of bundles of services. See also the update to Section 2.16.2 above.

For Section 4.14.1 – Walla! Communications Ltd. ("Walla")

Following notice from Haaretz Newspaper Publishing, Ltd. (hereinafter, “Haaretz”) on March 14, 2010 that it had entered into an agreement to sell all its shares in Walla, Bezeq International notified Haaretz on March 18, 2010 of its decision to exercise its right of first-refusal to purchase the shares in Walla owned by Haaretz, meaning 14,807,939 shares (“the Purchased Shares”) for NIS 6.00 per share, totaling NIS 88,847,634. The transaction was closed on April 25, 2010, after all of preconditions were met. Upon receipt of the Purchased Shares, Bezeq International transferred 9,902,467 of the Purchased Shares to a trustee, who will hold the shares in a blind trust so that after the transfer was completed, Bezeq International holds 20,468,231 shares, which are approximately 44.99% of the issued and paid up capital of Walla.

On August 2, 2010, Bezeq International filed a specification for a special tender offer in accordance with the Companies Law, 5759-1999 and the Securities (Tender offer) Regulations, 5760-2000, for the purchase of 2,274,299 shares of Walla, which at the date of publication of the specification account for approximately 5% of the issued and paid up capital and voting rights in Walla which are held by Walla's shareholders. In the tender offer, Bezeq International proposes to purchase the Walla shares from the shareholders at NIS 6 per share, and the total consideration for the shares which are the subject of the tender offer is NIS 13,645,794. If the tender offer is completed, Bezeq International intends to file an application in the office of the Antitrust Commissioner, for approval of the transfer of additional Walla shares which are currently held for Bezeq International by a trustee. Subject to approval of the merger,[7] 9,902,467 Walla shares will be transferred from the trustee back to Bezeq International. Bezeq International intends to sell all its holdings in Walla to the Company.

On July 11, 2010, Walla announced that it has entered into an agreement (through a wholly-owned subsidiary) on July 8, 2010 for the acquisition of Coral Tel Ltd. ("Yad 2"), a private company that operates, inter alia, the Yad 2 website whereby Walla will purchase 75% of the share capital of Yad 2 from Yad 2's shareholders in consideration of NIS 117.5 million, plus an additional sum to be paid to some of the shareholders of Yad 2, based on the amount of Yad 2's working capital and subject to adjustments. Closing the transaction is subject to fulfillment of preconditions, all as described in the immediate report of Walla dated July 11, 2010. See also Note 5(b)(2) to the financial statements of the Company for the period ended June 30, 2010, which are included in this quarterly report.

<u>For Section 4.17 - Restrictions and supervision of Bezeq International's operations</u>

On the hearing in April 2010 which relates also to Bezeq International on the matter of exit fees that a license-holder is entitled to demand of a private subscriber, see the update for Section 2.16.2 above.

<u>For Section 4.19 – Legal Proceedings</u>

A. <u>Section 4.19.1</u> – In the matter of the claim and application for certification as a class action filed on September 16, 2001 against Bezeq International and the State of Israel, based on the allegation that Bezeq International's tariffs for international telecommunication services in the period from May 10, 1996 through July 8, 1997 were exorbitant and unreasonable, and which was certified as a class action on December 25, 2003: On April 26, 2010, the Supreme Court allowed the appeal filed by Bezeq International and the State (after hearing applications for leave to appeal that they filed as if they had been granted leave to appeal), and ruled that there is no justification for certifying the claim as a class action.

B. <u>Section 4.19.2</u> – In the matter of a claim filed in January 2002 against the Company and against Bezeq International by an international call operator, for payment of monetary compensation and writs of mandamus in connection with the proceedings for the allocation of customers to international call operators: The additional mediation proceeding between the parties was unsuccessful and the claim was returned to the court. In the pre-trial hearings, the court allowed the plaintiff's request and permitted it to amend the statement of claim. The Company and Bezeq International filed an appeal in the Supreme Court against the decision of the lower court to allow the statement of claim to be amended, and that appeal is still pending. See also the update for Section 2.18.5 above.

C. On April 13, 2010, Partner Communications, Ltd. filed a petition in the Supreme Court sitting as the High Court of Justice, in which it asked the Court to order revocation of Article 11(B)(3) of the Communications (Telecommunications and broadcasts) (Proceedings and conditions for receipt of a general license for providing international telecommunications services) Regulations, 5764-2004, which prevents it, as the cellular license-holder, or its subsidiary, from receiving a general license for providing international communication services. In its petition, Partner argues, inter alia, that the decision of the Minister of Communications in the matter of the subject of the petition was intended to protect the existing holders of licenses for providing international telecommunication services, and for this reason, Bezeq International was added as a respondent to the petition. Partner's entry into the international telecommunication market, if the petition is allowed, could have an adverse effect on Bezeq International in this area.

D. On May 24, 2010, Partner Communications Ltd. filed another petition in the Supreme Court, in which it requests an order nisi prohibiting the Ministry of Communications from amending the Communications (Telecommunications and broadcasts) (Payments for interconnect) Regulations, 5760-2000, so as to determine in them that for outgoing calls from a cellular telephone to abroad, a uniform interconnect fee will be set which is the same as the interconnect fee for incoming calls. According to the petitioner, such a decision narrows its license and is harmful to competition. Partner attached to its petition an application for an interlocutory injunction, in which Partner

[7] It is noted that a preemptive opinion of the Antitrust Commission given on July 12, 2010, states that there is no impediment to unconditional approval of the acquisition of control in Walla by Bezeq International and the Company.

requested that the decision on amendment of the regulations be delayed and not to allow amendment of the regulations until the petition is heard. Since the Minister of Communications' decision to amend the regulations is linked to his decision to allow Partner to compete in the international calls market, Bezeq International (and its other competitors in this market) was joined as a respondent to the petition. Bezeq International filed its response to the petition, as did the other parties, following which the Court decided that the application for an interlocutory order should be dismissed and that the petition should be heard before a bench. At the date of this report, Bezeq International does not appear to be at risk in this petition.

5. Multi-Channel Television – D.B.S. Satellite Services (1998) Ltd. ("DBS")

For Section 5.1.3 – Market developments in the segment of operation

Section 5.1.3.1 – In July 2010 the Government decided to impose on the Ministry of Communications and the Ministry of Finance, together with the Second Authority for Television and Radio and the Council, the formulation of recommendations for expansion of the DTT array and how it should operate, including in the matter of legislative amendments required for the purpose, and to submit them for Government approval by the end of 2010.

Section 5.1.3.2 – In May 2010, the Government withdrew the Television Broadcasts (Legislative amendments) Bill, 5760-2009.

In July 2010, the Second Authority for Television and Radio (Amendment No. 33) (Transition from franchises to licenses in television broadcasts) Bill, 5770-2010, which deals mainly with a change in the regulation method in commercial broadcasts (following the recommendation of the committee headed by the Director General of the Ministry of Communications mentioned in Section 5.1.3.4 of the Company's 2009 Periodic Report), with a transition from a franchise method to the grant of licenses for commercial television broadcasts for all, which meets the threshold conditions laid down in the Bill without a tender proceeding ("Commercial Licensee-Holder"). In the Bill, the transition date between the methods is given as January 1, 2012. Under the Bill, inter alia, every Commercial License-Holder will be entitled to be included in the array of DTT broadcasts and may broadcast the dedicated channel in Hebrew, if it requests to be included in the DTT array. The dedicated channel broadcaster in Hebrew will be exempt from transition fees to DBS and the cable company for the first two years of its broadcasts. The Bill also states that the Council may to set the number of channels of the television franchisees, of the Knesset channel, of the dedicated channels and of the IBA broadcasts, and that the Council, together with the Second Television and Radio Authority Council, will decide on the location of the channel number on which the Commercial License-Holders will broadcast, and a tender will be held for the identity of the license-holders who will use the channel number on which franchisees currently broadcast.

For Section 5.1.6 – Main entry and exit barriers for the segment of operation, and for Section 5.1.7 - Substitutes for and changes in products in the segment

On the matter of the recent erosion of the main entry barriers to the segment of operation – Keshet Broadcasts Ltd., a franchisee for broadcasting on the second commercial channel, recently launched an application on the mako website enabling easy viewing of a range of content channels through a computer.

In the second quarter of 2010, Israel Electric Corporation ("IEC") received a license for the provision of high-speed internet services at speeds higher than the current standard in Israel, using its own optical fiber infrastructure. The provision of such high-speed internet services by IEC could expedite the development of a trend for transferring video content via the internet. See also the update for Section 2.6.2 above.

For Section 5.4 – New products

In March 2010, DBS launched VOD services for its subscribers. DBS believes that its offering of VOD services accords with the regulation to which it is currently subject. This position of DBS is subject to publication of the conclusions of the committee appointed by the Minster of Communications to consider the regulation of broadcasts using new platforms and technologies (see Section 5.1.3.6 of the Company’s 2009 Periodic Report), which could result in the imposition of conditions and restrictions on the provision of VOD services by DBS, including the very fact of their provision.

In May and June 2010, the cable company addressed DBS by letter (which were forwarded to the Ministry of Communications), in which it alleged, inter alia, that it had identified unusual and severe electronic disturbances in its internet and telephony services and that the source of these disturbances was in DBS's customer connection to the VOD services (in one of the ways used by DBS for this purpose) using wiring that is also used by the cable company for transmitting DBS's services. The cable company demanded that DBS cease use of the cable company's infrastructure, repair every installation made allegedly unlawfully, and cease provision of the VOD service. DBS rejected the demand to cease its VOD service and proposed a joint investigation of the existence and source of the disturbances. In July 2010 the Ministry of Communications hosted a meeting on the matter, to which representatives of the cable company and DBS were invited, and at which it was agreed that the matter would be investigated further and ways to resolve the disturbances would be considered.

For Section 5.7.4 – Positive and negative factors in competition

In June 2010 the Minister of Communications amended the license of DBS. The amendment states, inter alia, that DBS may offer services bundled with a service of the Company. See also the update for Section 2.16.2 above.

For Section 5.10.1 – Licenses

Section 5.10.1.2 – In May 2010 the head of the Civil Administration for Judea and Samaria extended the license of DBS for broadcasting in those areas, to December 2016.

For Section 5.11 – Broadcasting rights

Section 5.11.2 – According to the immediate report published by the cable company in July 2010, an award was given in the arbitration between the cable company and the Union of Composers, Songwriters and Publishers of Israeli Music Ltd. ("AKUM"), in connection with deciding on a mechanism for the computation of annual royalties for the use of works whose rights are protected by AKUM. According to the report, the arbitrator's award accepted in principle the model outline for computing the royalties as presented by AKUM in the proceeding, except for certain modifications, and determined that the model should apply also for the matter of the royalties difference from 2003 onwards, according to a calculation that would be made by the parties to the arbitration in an agreed way. The cable company noted that it intends to appeal the arbitrator's award. Since the award and the other arbitration documents were not submitted to DBS, DBS does not know the model adopted and the reasons for the arbitrator's award.

Nevertheless, as agreed between DBS and AKUM, the royalty amounts paid to AKUM since 2003 might be revised, inter alia, depending on the agreement that is reached by the cable company and AKUM, and according to AKUM, depending also on the decision of the arbitrator. Accordingly, DBS's management estimates that following the award, DBS could be charged with payment differences in significant amounts in respect of the past, and with royalty payments that are significantly higher than the sums paid to date. Therefore, DBS revised its estimate for royalties since 2003. Revision of the royalties estimate was based on the model outline for the computation of royalties that was accepted by AKUM a short time after the arbitrator gave his award, with adjustments as assessed by the management of DBS, and on that basis DBS made a material provision in its financial statements at June 30, 2010.

With the other copyright organizations, payment of royalties for the period of engagement with them has been agreed with some of them, and for the rest, DBS might be required to pay non-material differences.

For Section 5.13 – Raw materials and suppliers

For the matter of a debt arrangement from May 2010 between DBS and the Company – see Note 5(a)(2) to the financial statements of the Company for the period ended June 30, 2010, which are included in this quarterly report.

For Section 5.15 – Financing

For Sections 5.15.2 and 5.15.3 – Credit restrictions applicable to the Company

In March 2010, an amendment to DBS's bank financing agreement ("the Financing Agreement") was signed and came into force. According to this agreement, inter alia, an additional Israeli bank ("the Additional Bank") joined DBS's current bank consortium ("the Current Banks"). In this context, the Additional Bank provided DBS with a proportionate share of DBS's current credit facility, and also granted DBS NIS 255 million in long-term credit, most of which was used for joining (proportionately)

DBS's long-term credit facility for repayment and early repayment of DBS's debts to the Current Banks, and the balance, NIS 46 million, will be used to meet DBS's current needs.

Pursuant to the amended agreement, DBS created a floating charge in favor of the Additional Bank similar to those listed in favor of the Current Banks, and the Additional Bank was added to the fixed charge in favor of the Current Banks. Furthermore, shareholders in DBS[8] signed amendments to the deeds of liability, deeds of pledge and guarantees, as the case may be, that they signed in the past in favor of the Current Banks, concerning the joining of the Additional Bank.

According to the amended agreement, the repayment period for bank credit (both the long-term loans and at the current credit facility) was extended to the end of 2015, and the banks also agreed that the loans extended to DBS by institutionals (see Section 5.18.5 of the Company's 2009 Periodic Report) can be repaid on schedule.

Under the amended agreement, the financial covenants listed in the Financing Agreement have been replaced with new ones, which will apply until 2015 and are suited to DBS's business plan The new covenants:
A. Minimum repayment ability
B. Minimum EBITDA.
C. Maximum and minimum supplier credit.

The values for compliance with the financial covenants are variable, and are measured quarterly. Non-compliance with the covenants grants the banks a right to demand early repayment of the loans in accordance with the conditions of the Financing Agreement.

DBS is in compliance with the covenants in the Financing Agreement as of June 30, 2010, after being granted a relief by the banks in August 2010 in relation to the target of one of the covenants, which was needed in view of the material provision made by DBS as aforesaid in Section 5.11.2 above. Since that relief was granted after the balance sheet date, the bank loans are stated under short-term liabilities. The management of DBS estimates that since the covenants targets are cumulative on an annual basis, DBS will require a similar relief for the targets of the financial covenants on September 30, 2010 and December 31, 2010, and DBS is working to obtain such relief from the banks.

For Section 5.15.8 – Private issue of debentures

In April 2010, the rating agency Maalot announced that it had raised the rating of the debentures (Series A) issued by DBS one grade from (ilBBB-) to (ilBBB), inter alia because of its evaluation of the substantive improvement in DBS's liquidity because of the new loan received from the Additional Bank, as described in the update to section 5.15.2 above, and because of the ongoing improvement in the coverage ratios, the ability to generate cash flows, and liquidity of DBS since the previous rating date. In addition, the rating company added DBS to the CreditWatch with positive outlook, noting that it hopes to complete its consideration of a possible improved rating within three months, after a deeper study of DBS's business plan and its impact on its financial profile.

In June 2010 Maalot raised the rating of DBS and of its debenture (series A) another grade, from ilBBB to ilBBB+, and removed the rating from CreditWatch with positive outlook. The higher rating was explained, inter alia, by the improving trend in financial rations and the ability to generate cash flows, even though the rating agency still had concerns about the possibility that DBS might deviate in the medium term from its goals according to its business plan. Maalot gave DBS a positive rating outlook.

For Section 5.17 – Restrictions on and supervision of the Company

For Section 5.17.1 – Subjection of activities to specific laws

In April 2010, the subsidiary of Bank Leumi notified DBS that it has closed the transaction for the sale of all its holdings in Keshet broadcasts Ltd.

On the matter of the Government decision to raise the royalties percentage, see the update for Section 2.16.3 above.

For Section 5.17.3 – Principal restrictions under the law and the broadcasting license

At the date of this report, the Council is holding a hearing regarding shortening the period of campaigns offered by DBS (and the cable companies) to its subscribers and setting a uniform special

[8] Other than Lidan, to which DBS undertook to use its best efforts so that as soon as possible after the amended agreement comes into force, Lidan will sign the amendment to its deed of liabilities in favor the banks and the of pledge in favor of the banks.

offer period for all service components. At the hearing, the Council is considering, among other things amendment of DBS's license so that the commitment period for subscribers to its services in consideration of a benefit or discount will be limited to only 18 months. DBS has submitted its opposition to such an amendment. The Council has not yet made its decision in the hearing. Concurrently with the hearing proceedings, the Ministry of Communications announced in March 2010 that it is considering amending the license of Hot Telecom LP, so that a private subscriber who purchased a service package that also includes broadcasts from the cable company, for which the commitment period for the broadcast component is limited by the broadcast license, the limit would apply to the services included in that package.

In the matter of the dedicated channels – In March 2010 a bill mandating that the dedicated channels would be exempt from payment of transition fees to the cable company and to DBS, passed its fist reading in the Knesset. In July 2010, the bill was approved for its second and third reading in the Knesset.

In April 2010, in the context of the Ministry of Communications' approval of DBS's request, as required by its license for approval of transferring the means of control in the company (direct and indirect) in respect of the purchase of control in the company (see section 1.3.1a, above) and the transfer of the holdings of Eurocom DBS Ltd. in DBS to a trustee, the Ministry of Communications decided to apply the following main conditions to DBS:

A. No change, direct or indirect, in the trustee's holdings of the means of control in DBS may be made unless the change received the prior written approval of the Minister of Communications, after he has consulted with the Council.

B. The trustee will not act in accordance with guidance received from any party which has a direct or indirect interest in an area of regulation of the Ministry of Communications, unless it has received the approval from the Ministry of Communications.

C. A transaction between DBS and Eurocom Group[9] concerning satellite terminal equipment will be considered an extraordinary transaction as defined in section 270(4) of the Companies Law and therefore, in addition to the approval proceeding in DBS's organs, it requires approval by the organs of the Company pursuant to section 275 of the Companies Law.

D. Discussions by the board of directors of DBS concerning transactions as described in paragraph C, above, will be documented in detailed, comprehensive minutes that are signed by the chairman of the meeting and submitted to the Director General of the Ministry of Communications for his scrutiny.

For the matter of using infrastructure in the subscriber's home – In July 2010 an agreement was signed between DBS and the cable company, in which DBS will pay the cable company approximately NIS 4 million in settlement of its demands in respect of the use of infrastructure in the subscriber's home which was installed by the cable company up to the end of 2010. Under the agreement, commencing 2011, there will be no obligation for one of the parties to pay the other for the use of wiring. In addition, the parties agreed on a joint approach to the Ministry of Communications concerning amendment of the administrative provisions, mainly cancellation of the duty to give notice so that a licensee to which a subscriber connects will forward the disconnection notice from the subscriber to the licensee from which the subscriber was disconnected only after the connection is made to the other licensee. The agreement will come into force only after approval by the Antitrust Commissioner for exemption from his approval as a cartel. The agreement was submitted to the Antitrust Commissioner, who has not yet given his decision.

In June 2010, DBS learned that the Ministry of National Infrastructures is preparing draft regulations ("the Draft Regulations") pursuant to the Sources of Energy Law, 5750-1989, which will define the maximum output in waiting mode for instruments that are listed in the Draft Regulations and which include digital converters. The output cited in the Draft Regulations for digital converters is considerably lower than the actual and accepted consumption if digital converters in general, including those used by DBS. DBS approached the Ministry on the matter and requested that the digital converters be excluded from application of the regulations and at least that the progress of the regulations be halted so that the matter can be studied and the right to a hearing be exercised.

[9] For the definition of "Eurocom Group" for this matter, see Footnote 4.

For Section 5.20 – Legal proceedings

In July 2010, a claim and application for certification as a class action were filed against DBS in the Tel Aviv District Court. According to the applicant, DBS is violating the Consumer Protection Regulations ("the Regulations") in that the size of the letters and the space between the lines in its agreements with its customers do not meet the requirements of the Regulations. The amount of the personal claim is NIS 50, and the total amount of the claim is estimated at NIS 50 million. The applicant is also petitioning for declaratory relief that will determine that those agreements are not in keeping with the Consumer Protection Regulations and for a writ of mandamus instructing DBS to correct them.

August 2, 2010	
Date	Bezeq – The Israel Telecommunication Corp. Ltd.

Names and titles of signatories:

Shlomo Rodav, Chairman of the Board
Avraham Gabbay, CEO

Chapter B of the Periodic Report

Directors' Report on the State of the Company's Affairs
for the six-month and three-month periods ended June 30, 2010

We respectfully present the Directors' Report on the state of affairs of Bezeq - The Israel Telecommunication Corp. Limited ("the Company") and the consolidated Group companies (the Company and the consolidated companies together are hereinafter referred to as “the Group"), for the six-month period ended June 30, 2010 and for the three-month period then ended ("Quarter").

The Directors' Report contains a condensed review of its subject-matter, and it assumes that the Directors' Report at December 31, 2009 is also available to the reader.

Commencing August 21, 2009, the Company ceased to consolidate the financial reports of D.B.S. Satellite Services (1998) Ltd. ("DBS"), and since that date its investment in DBS is stated by the equity method (see Note 4 to the financial statements). However, the Group continues to report on multi-channel television operations in its financial statements.

The Group's balance sheet at June 30, 2009 and the statements of cash flows for the period and the Quarter then ended, include DBS balances, while the income statement for the corresponding period and for the Quarter was restated and does not contain the results of DBS's operations as an ongoing operation.

The Group reports on four main segments in its financial statements:

1) **Fixed-line domestic communications**

2) **Cellular**

3) **International communications, internet and NEP services**

4) **Multi-channel television**

The Company has other areas of operation which are not material to the activities of the Group, and these are included in the financial statements as the “Other” business segment. This covers the operation of a portal and content sites and an online commercial site (through Walla), customer center services and investment in a venture capital fund.

Profit for the reporting period amounted to NIS 1,280 million[1] compared with NIS 1,111 million in the corresponding period, an increase of approximately 15.2%. Profit attributed to the owners of the Company in the period was NIS 1,280 million, compared with NIS 1,149 million in the corresponding period, an increase of about 11.4%.

Profit for the reporting Quarter was NIS 638 million, compared with NIS 502 million in the corresponding quarter, an increase of approximately 27.1%. Profit attributed to the owners of the Company in the Quarter was NIS 638 million, compared with NIS 541 million in the corresponding quarter, an increase of about 17.9%.

The increase in profit in the period and in the Quarter stemmed primarily from a rise in revenue from ongoing operations and from other operations and a decrease in depreciation and amortization expenses, which were offset by an increase in operating and general expenses. Financing expenses also increased.

The increase in profit for the period and for the Quarter is in the fixed-line domestic communications segment, the cellular segment and the International communications, internet and NEP segment. See below for further details.

[1] In this translation of the Directors' Report, all amounts should be understood by the reader to be rounded to the nearest million or thousand, as the case may be.

A. Board of Directors' explanations for the state of the Company's affairs, the results of its operations, its equity, cash flows and other matters

1. Financial condition

a. The Group's assets at June 30, 2010 amounted to NIS 13.82 billion, compared with NIS 14.62 billion on June 30, 2009, of which NIS 5.51 billion (40%) is property, plant and equipment, compared with NIS 6.17 billion (42%) on June 30, 2009.

The decrease in the Group’s assets stems from the termination of the consolidation of the results of operations of DBS in the Company's financial statements and the recording of the Company's investment in DBS by the equity method (DBS's assets at June 30, 2009 amounted to NIS 1.213 billion). The decrease is reflected mainly in property, plant and equipment and in broadcasting rights. Intangible assets also decreased, due to the write-off of goodwill. The decrease was offset by stating the investment in DBS at the date of exit from consolidation by the equity method at NIS 1.175 billion.

In addition, an increase of NIS 340 million in the Group's assets stemmed from the consolidation of the assets of Walla with those of the Group and recording surplus cost in intangible assets (see Note 5B to the financial statements). In addition, the assets of the cellular segment increased, an increase that was offset by a decrease in the assets of the fixed-line domestic communications segment (excluding investment in associates), and in the international communications, internet and NEP segment (excluding investment in associates), as explained below.

In the fixed-line domestic communications segment there was a decrease of NIS 144 million in assets, excluding investment in associates, compared with June 30, 2009, due mainly to a decrease in cash balances and in deferred tax balances, which were offset by an increase in the balances of property, plant and equipment and of intangible assets.

In the cellular segment, assets increased from NIS 4.77 billion on June 30, 2009 to NIS 4.85 billion at June 30, 2010. Most of the increase stems from a rise in customer balances, mainly due to an increase in revenue from sales of terminal equipment on installments.

In the international communications, internet and NEP services segment, assets (excluding investment in associates) decreased from NIS 1,062 million on June 30, 2009 to NIS 1,005 million at June 30, 2010. Most of the decrease stemmed from a decrease in cash balances, modified by additional acquisitions of capacity usage rights.

In the multi-channel television segment there was an increase in assets from NIS 1,213 million on June 30, 2009 to NIS 1,245 million at June 30, 2010, which stemmed mainly from an increase in net investment balances, intangible assets and property, plant and equipment.

b. The Group's debt to financial institutions and debenture holders at June 30, 2010 amounted to NIS 5.23 billion, compared with NIS 5.92 billion on June 30, 2009. The decrease stemmed primarily from the termination of the consolidation of DBS (DBS's debt to financial institutions and debenture holders on June 30, 2009 was NIS 1.75 billion), and also from repayment of debentures in the fixed-line domestic communications segment and in the cellular segment.

Conversely, debt to financial institutions in the fixed-line domestic communications segment increased due to loans received from banks (see Note 13B to the financial statements).

2. Results of operations

a. Result highlights

Condensed consolidated income statement:

	For the six months ended June 30				For the three months ended June 30,			
	2010	2009	Increase		2010	2009	Increase	
	NIS millions	NIS millions	(decrease)	Change	NIS millions	NIS millions	(decrease)	Change
Ongoing operations:								
Revenue	5,896	5,663	233	4.1%	2,981	2,872	109	3.8%
Costs and expenses	4,032	4,046	(14)	(0.3%)	1,991	2,054	(63)	(3.1%)
Operating profit	1,864	1,617	247	15.3%	990	818	172	21.0%
Finance income (expenses), net	(13)	29	(42)	-	(35)	(1)	(34)	-
Profit after finance income (expenses), net	**1,851**	**1,646**	**205**	**12.5%**	**955**	**817**	**138**	**16.9%**
Equity in profits (losses) of associates	(109)	4	(113)	-	(86)	2	(88)	-
Profit before income tax	**1,742**	**1,650**	**92**	**5.6%**	**869**	**819**	**50**	**6.1%**
Income tax	462	443	19	4.3%	231	222	9	4.1%
Profit from ongoing operations	1,280	1,207	73	6.0%	638	597	41	6.9%
Profit (loss) from discontinued operations	-	(96)	96	100%	-	(95)	95	100%
Profit for the period	**1,280**	**1,111**	**169**	**15.2%**	**638**	**502**	**136**	**27.1%**
Attributed to:								
Company owners	1,280	1,149	131	11.4%	638	541	97	17.9%
Non-controlling rights	-	(38)	38	100%	-	(39)	39	100%
Profit for the period	**1,280**	**1,111**	**169**	**15.2%**	**638**	**502**	**136**	**27.1%**
Earnings per share:								
Base earnings per share (NIS)	0.48	0.44	0.04	9.1%	0.24	0.21	0.03	14.3%
Diluted earnings per share (NIS)	0.47	0.43	0.04	9.3%	0.24	0.20	0.04	20%

While most of the increase in the Group's revenue stems from the cellular segment, an increase was also recorded in the international communications, internet and NEP segment. The increase was moderated by a decrease in revenue in the fixed-line domestic communications segment.

The Group’s depreciation and amortization expenses in the first half amounted to NIS 691 million, compared with NIS 748 million in the corresponding period, a decrease of 7.6%.
The Group’s depreciation and amortization expenses in the Quarter amounted to NIS 348 million, compared with NIS 377 million in the corresponding quarter, a decrease of 7.7%.
The decrease stems from the fixed-line domestic communications segment.

The Group’s salary expense in the first half amounted to NIS 994 million, compared with NIS 989 million in the corresponding period, an increase of 0.5%.
The Group’s salary expense in the Quarter amounted to NIS 489 million, compared with NIS 484 million in the corresponding period, an increase of 1%.
The increase in the salary expense stems mainly from the "Other" segment, and is due to consolidation of the financial statements of Walla in the Group's consolidated financial statements, and was offset by a decrease in the salary expense in the fixed-line domestic communications segment.

The Group’s operating and general expenses in the first half amounted to NIS 2,442 million compared with NIS 2,325 million in the corresponding period an increase of 5%.

The Group’s operating and general expenses in the Quarter amounted to NIS 1,224 million compared with NIS 1,189 million in the corresponding quarter, an increase of 2.9%.

The increase is due mainly to an increase in expenses in the cellular segment, and also in the international communications, internet and NEP segment. The increase was moderated by a decrease in the expenses of the fixed-line domestic communications segment.

Revenue from the Group's other operations, net, in the first half amounted to NIS 95 million, compared with NIS 16 million in the corresponding period.
Revenue from the Group's other operations, net, in the Quarter amounted to NIS 70 million, compared with expenses of NIS 4 million in the corresponding quarter.
The increase stems from the international communications, internet and NEP segment and from the fixed-line domestic communications segment.

b. Segments of operation

Below are data by segment, presented in accordance with the Group's segments of operation:

Revenue by operating segment	**1-6/2010**		**1-6/2009**		**4-6/2010**		**4-6/2009**	
	NIS millions	**% of revenue**	**NIS millions**	**% of revenue**	**NIS millions**	**% of revenue**	**NIS millions**	**% of revenue**
Fixed-line domestic communications	2,611	44.3%	2,644	46.7%	1,307	43.8%	1,318	45.9%
Cellular	2,822	47.9%	2,611	46.1%	1,429	47.9%	1,346	46.8%
International communications, internet and NEP services	685	11.6%	651	11.5%	342	11.5%	327	11.4%
Multi-channel television	787	13.3%	760	13.4%	396	13.3%	376	13.1%
Other and offsets*	(1,009)	(17.1%)	(1,003)	(17.7%)	(493)	(16.5%)	(495)	(17.2%)
Total	5,896	100%	5,663	100%	2,981	100%	2,872	100%

* Offsets are mainly in respect of a segment that is an associate.

Operating profit by operating segment	**1-6/2010**		**1-6/2009**		**4-6/2010**		**4-6/2009**	
	NIS millions	**% of revenue**	**NIS millions**	**% of revenue**	**NIS millions**	**% of revenue**	**NIS millions**	**% of revenue**
Fixed-line domestic communications	993	38.0%	871	32.9%	503	38.5%	434	32.9%
Cellular	684	24.2%	623	23.9%	362	25.3%	321	23.9%
International communications, internet and NEP services	182	26.6%	128	19.7%	121	35.4%	68	20.8%
Multi-channel television	66	8.4%	125	16.5%	7	1.8%	59	15.7%
Other and offsets*	(61)		(130)		(3)		(64)	
Consolidated operating profit /% of Group's revenues	1,864	31.6%	1,617	28.6%	990	33.2%	818	28.5%

* Offsets are mainly in respect of a segment that is an associate.

Fixed-line domestic communications segment

Revenue:

Segment revenue in the first half of 2010 totaled NIS 2,611 million compared with NIS 2,644 million in the corresponding period, a decrease of 1.2%.
Segment revenue in the Quarter totaled NIS 1,307 million compared with NIS 1,318 million in the corresponding quarter, a decrease of 0.8%.
The decrease in segment revenue stemmed primarily from a decrease in telephony revenues as a result of the fall in the number of lines and in call traffic, which was moderated by an increase in revenue from high-speed internet, data communication and transmission. In addition, revenue from interconnect fees to the cellular networks decreased in the first half compared with the corresponding period (with a corresponding decrease in the expense).

Costs and expenses:

Depreciation expenses in the first half of 2010 amounted to NIS 341 million compared with NIS 416 million in the corresponding period, a decrease of 18%.
Depreciation expenses in the Quarter amounted to NIS 171 million compared with NIS 205 million in the corresponding period, a decrease of 16.6%.
The source of the decrease is the end of depreciation of property, plant and equipment and a change in the salvage value of property, plant and equipment.

The salary expense in the first half of 2010 amounted to NIS 527 million, compared with NIS 542 million in the corresponding period, a decrease of 2.8%.
The salary expense in the Quarter amounted to NIS 250 million, compared with NIS 264 million in the corresponding quarter, a decrease of 5.3%.
The decrease in the salary expense in the half resulted mainly from an increase in salary attributed to investment as well as a decrease in the number of employees, which was moderated by a rise in salaries and a provision in respect of a retirement agreement with a previous CEO. The decrease in the salary expense in Quarter stemmed primarily from revised provisions for employee benefits and the decrease in the number of employees, and was moderated by the rise in salaries.

Operating and general expenses in the first half of 2010 amounted to NIS 788 million compared with NIS 831 million in the corresponding period, a decrease of 5.2%.
Operating and general expenses in the Quarter amounted to NIS 396 million compared with NIS 411 million in the corresponding quarter, a decrease of 3.6%.
The decrease stems from a decrease in operating expenses due to the implementation of efficiency measures, as well as a decrease in royalty expenses following their reduction by 0.5%. In addition, interconnect fees to the cellular networks in the first half decreased in parallel with a decrease in revenue from interconnect fees.

Other net operating income in the first half of 2010 amounted to NIS 38 million, compared with income of NIS 16 million in the corresponding period.
Other net operating income in the Quarter amounted to NIS 13 million, compared with income of NIS 4 million in the corresponding quarter.
The increase stems mainly from reducing provisions for legal claims in the Quarter and a rise in capital gains from the sale of properties and copper, as well as profit from hedging transactions on the price of copper. The increase was moderated by a rise in expenses in respect of early retirement severance liabilities.

Operating profit:

Operating profit in the segment in the first half of 2010 amounted to NIS 993 million compared with NIS 871 million in the corresponding period, an increase of 14%.
Operating profit in the segment in the Quarter amounted to NIS 503 million compared with NIS 434 million in the corresponding period, an increase of 15.9%.
The increase stems from the changes described above in the revenue and expense items.

Cellular segment

Revenue:

Segment revenue in the first half of 2010 amounted to NIS 2,822 million compared with NIS 2,611 million in the corresponding half, an increase of 8.1%.
Segment revenue in the Quarter amounted to NIS 1,429 million compared with NIS 1,346 million in the corresponding quarter, an increase of 6.2%.

The segment's revenue from services in the half amounted to NIS 2,246 million, compared with NIS 2,069 million in the corresponding period, an increase of 8.6%.
The segment's revenue from services in the Quarter amounted to NIS 1,140 million, compared with NIS 1,050 million in the corresponding period, an increase of 8.5%. The increase in revenue from services is the result of an increase in the number of subscribers and in ARPU, which stemmed mainly from an increase in revenue from content services.
Revenue from the sale of terminal equipment in the half amounted to NIS 576 million compared with NIS 542 million in the corresponding period, an increase of 6.3%. The increase in revenue from the sale of terminal equipment is due mainly to the increase in the volume of sales.
Revenue from the sale of terminal equipment in the Quarter amounted to NIS 289 million compared with NIS 296 million in the corresponding quarter, a decrease of 2%. The decrease in revenue from the sale of terminal equipment is due mainly to the decrease in the volume of sales.

<u>Costs and expenses:</u>

Depreciation and amortization expenses in the first half of 2010 amounted to NIS 298 million compared with NIS 290 million in the corresponding quarter, an increase of 2.8%.
Depreciation and amortization expenses in the Quarter amounted to NIS 149 million compared with NIS 151 million in the corresponding quarter, a decrease of 1.3%.

The salary expense in the first half of 2010 and in the corresponding period amounted to NIS 299 million.
The salary expense in the Quarter amounted to NIS 149 million, compared with NIS 148 million in the corresponding quarter, an increase of 0.7%.

Operating and general expenses in the first half of 2010 amounted to NIS 1,541 million compared with NIS 1,399 million in the corresponding period, an increase of 10.2%. The increase stems mainly from a rise in service costs along with an increase in revenue from services (mainly call completion fees, content costs and roaming), and from an increase in the cost of terminal equipment, attributable to the increase in sales quantities and the increase in the costs of doubtful and bad debts.
Operating and general expenses in the Quarter amounted to NIS 769 million compared with NIS 726 million in the corresponding quarter, an increase of 5.9%. The increase stems mainly from a rise in the costs of services along with an increase in revenue from services (mainly call completion fees, content costs and roaming), which was offset by a decrease in the cost of terminal equipment due to the smaller quantities sold.

<u>Operating profit:</u>

Operating profit in the segment in the first half of 2010 amounted to NIS 684 million compared with NIS 623 million in the corresponding period, an increase of 9.8%.
Operating profit in the segment in the Quarter amounted to NIS 362 million compared with NIS 321 million in the corresponding quarter, an increase of 12.8%
The improvement in operating profit stems from the changes described above in the revenue and expense items.

<u>International communication, internet and NEP segment</u>

<u>Revenue:</u>

In the first half of 2010, segment revenue amounted to NIS 685 million compared with NIS 651 million in the corresponding period, an increase of 5.2%.
Segment revenue in the Quarter amounted to NIS 342 million compared with NIS 327 million in the corresponding quarter, an increase of 4.6%.
The increase in revenue in the reporting period stems primarily from growth in integration activities (IT and communications solutions for businesses) and data activities, as well as call transfer operations between carriers around the world (in the Quarter, these activities decreased compared with the corresponding quarter). Offsetting these was a decrease in revenue from outbound call minutes as traffic volume declined, and a decrease in revenue from inbound call minutes.

<u>Costs and expenses:</u>

Depreciation expenses in the first half of 2010 amounted to NIS 49 million, compared with NIS 40 million in the corresponding period, an increase of 22.5%.
Depreciation expenses in the Quarter amounted to NIS 26 million, compared with NIS 20 million in the corresponding quarter, an increase of 30%.

The increase in depreciation expenses stemmed mainly from the amortization of capacity usage rights, development expenses and subscriber acquisition costs.

The salary expense in the first half of 2010 amounted to NIS 126 million compared with NIS 123 million in the corresponding period, an increase of 2.4%.
The salary expense in the Quarter amounted to NIS 62 million compared with NIS 59 million in the corresponding quarter, an increase of 5%.

Operating and general expenses in the first half of 2010 amounted to NIS 385 million compared with NIS 360 million in the corresponding period, an increase of 7%.
Operating and general expenses in the Quarter amounted to NIS 189 million compared with NIS 179 million in the corresponding quarter, an increase of 5.6%.
The increase in these expenses parallels the increase in the segment's revenue.

Income from other operations, net, in the first half of 2010 and in the Quarter include a capital gain of NIS 57.4 million from revaluation of the holdings in Walla when control was assumed (see Note 5B to the financial statements).

Operating profit:

Operating profit in the segment in the first half of 2010 amounted to NIS 182 million compared with NIS 128 million in the corresponding period, an increase of 42.2%.
Operating profit in the segment in the Quarter amounted to NIS 121 million compared with NIS 68 million in the corresponding quarter, an increase of 77.9%.
The improvement in operating profit stems from the changes described above in the revenue and expense items.

Multi-channel television (stated by the equity method)

Revenue:

Segment revenue in the first half of 2010 amounted to NIS 787 million compared with NIS 760 million in the corresponding half, an increase of 3.6%.
Segment revenue in the Quarter amounted to NIS 396 million compared with NIS 376 million in the corresponding quarter, an increase of 5.3%.
The increase stems from a rise in revenue from premium channels and advanced products, as well as from an increase in the number of subscribers.

Costs and expenses:

Depreciation expenses in the first half of 2010 amounted to NIS 132 million compared with NIS 112 million in the corresponding period, an increase of 17.9%.
Depreciation expenses in the Quarter amounted to NIS 68 million compared with NIS 55 million in the corresponding quarter, an increase of 23.6%.
The increase is due to purchases of property, plant and equipment.

The salary expense in the first half of 2010 amounted to NIS 112 million compared with NIS 102 million in the corresponding period, an increase of 9.8%.
The salary expense in the Quarter amounted to NIS 56 million compared with NIS 49 million in the corresponding quarter, an increase of 14.3%.
The increase in the salary expense stemmed from the increased number of positions, mainly in the Customers department, due to preparation for entry into the world of VOD (customer service and technical array).

Operating and general expenses in the first half of 2010 amounted to NIS 477 million compared with NIS 421 million in the corresponding period, an increase of 13.3%.
Operating and general expenses in the Quarter amounted to NIS 265 million compared with NIS 212 million in the corresponding quarter, an increase of 25%.
The increase in these expenses stems from a provision for royalties in respect of copyright payable to AKUM see Note 5A to the financial statements).

Operating profit:

Operating profit in the segment in the first half of 2010 amounted to NIS 66 million compared with NIS 125 million in the corresponding period, a decrease of 47.2%.
Operating profit in the segment in the Quarter amounted to NIS 7 million compared with NIS 59 million in the corresponding quarter, a decrease of 88.1%.

The changes in operating profit stem primarily from the above-mentioned changes in the revenue and expense items.

c. Finance expenses, net

The Group's net finance expenses in the first half of 2010 amounted to NIS 13 million compared with net finance income of NIS 29 million in the corresponding period.
Net finance expenses in the Quarter amounted to NIS 35 million, compared with NIS 1 million in the corresponding quarter. Most of the change in net finance expenses stems from the fixed-line domestic communications segment, mainly as a result of hedging transactions on the CPI, an increase in credit at fixed and variable shekel interest, and from a decrease in finance income from shareholder loans to DBS.
Conversely, interest expenses and linkage differentials in respect of debentures decreased, due to a lower rate of rise in the CPI and a decrease in total liabilities.

d. Income tax

The Group's tax expenses in the reporting period amounted to NIS 462 million, representing approximately 26.5% of pre-tax profit, compared with NIS 443 million and 26.8% of pre-tax profit in the corresponding period.

3. Equity

Equity attributed to the Company's owners at June 30, 2010 amounted to NIS 5.4 billion, constituting 39.1% of the total balance sheet, compared with NIS 5.2 billion on June 30, 2009 and 35.6% of the balance sheet. The increase in equity stemmed mainly from the Group's profit, most of which was offset by the distribution of a dividend of NIS 3.6 billion during the second half of 2009 and the first half of 2010.

4. Cash flow

Consolidated cash flow for the six-month and three-month periods ended June 30, 2009 included cash flow from the activities of DBS (see Note 4 to the financial statements for details of the amounts). Consolidated cash flow for the present reporting period does not include those activities.

Consolidated cash flow generated by operating activities in the first half of 2010 amounted to NIS 1,782 million, compared with NIS 2,033 million in the corresponding period, a decrease of NIS 251 million. Most of the decrease stems from termination of consolidation of the financial statements of DBS (in the corresponding period, cash flow of NIS 184 million generated by the operating activities of DBS was included). In addition, cash flow from the operating activities of the fixed-line domestic communications segment decreased, mainly as a result of a decrease in current liabilities and an increase in current assets. The decrease was moderated by a rise in the cash flow from operating activities in the cellular segment, resulting from changes in the working capital and an increase in net profit.

Consolidated cash flow from operating activities in the Quarter amounted to NIS 976 million, compared with NIS 808 million in the corresponding quarter, an increase of NIS 168 million. The increase stems from the fixed-line domestic communications segment, mainly due to timing differences in payment to suppliers and other payables between the first and second quarters, and from the cellular segment due to changes in the working capital – primarily from changes in customers and an increase in net profit. The increase in consolidated cash flow was partially offset by the termination of consolidation of the financial statements of DBS (in the corresponding quarter, cash flow of NIS 93 million generated by the operating activities of DBS was included).

Consolidated cash flow from operating activities is one of the sources for financing the Group's investments. In the reporting period these included NIS 607 million in the development of communications infrastructure and NIS 158 million in intangible assets and deferred expenses, compared with investment of NIS 756 million and NIS 156 million respectively in the corresponding period. In addition, NIS 30 million net was used in the Quarter for business combinations in the purchase of shares of Walla. In contrast, the cellular segment received net proceeds of NIS 110 million from the sale of an investment in a money market fund, compared with an investment of NIS 100 million in a money market fund in the corresponding period.

In the reporting period, the Group repaid net debts and paid interest amounting to NIS 1,221 million, of which NIS 622 million of debentures, NIS 424 million of loans and NIS 175 million of interest payments, compared with net debt repayment and interest payments of NIS 929 million in the corresponding period. Conversely, the Group received NIS 1,900 million in long-term loans, NIS 225 million in short-term credit, and NIS 18 million in proceeds from the exercise of employee stock options, compared with receipt of loans of NIS 400 million, short-term credit pf 41 million and proceeds of NIS 97 million from the exercise of employee stock options in the corresponding period. Most of the cash flow for finance activity stems from the fixed-line domestic communications segment.

A cash dividend of NIS 2,453 million was paid in the reporting period, compared with NIS 792 million in the corresponding period.

The average of long-term liabilities to financial institutions and debenture holders in the reporting period was NIS 4,336 million.

Average short-term bank credit in the reporting period was NIS 79 million.

Average credit from suppliers in the reporting quarter was NIS 996 million, and average short-term customer credit was NIS 2,581 million. Average long-term customer credit was NIS 858 million.

The working capital deficit in the Group at June 30, 2010 amounted to NIS 482 million and in the Company was NIS 1,564 million, compared with NIS 358 million and NIS 648 million respectively on June 30, 2009. Most of the increase in the working capital deficit of the Company stems from the decrease in cash balances and the increase in short-term financial liabilities. The increase in the Company's deficit was partially offset by termination of the consolidation of DBS in the Company's financial statements (the working capital deficit of DBS on June 30, 2009 was NIS 634 million). In addition, working capital increased in the cellular segment.

The Board of Directors of the Company reviewed the projected cash flow of the Company, including sources of credit and options for raising it, and determined that despite the deficit in working capital, the Company is not in liquidity difficulties.

The above description includes forward-looking information based on the Company's assessments. Actual results might differ substantially from these assessments if a change occurs in one of the factors taken into account in making them.

5. Explanations of the Board of Directors relating to market risks and their management

a. Further to the description in the Directors' Report for 2009, hedging transactions against market risks associated with exposure to changes in exchange rates and to changes in the CPI, partially reduced this exposure.

b. In April and May 2010, the Company raised NIS 1.9 billion of debt by means of loans from Israeli banks, of which NIS 400 million is against early repayment of bank loans raised in March 2009, as described in Note 13B to the financial statements. As a result, the surplus assets exposed to changes in the nominal shekel interest rate as was on December 31, 2009 decreased by NIS 820 million. In addition, during the reporting period the Company made hedging transactions on copper prices for 1,339 tons at USD 7,657 per ton, for a total value of USD 10.3 million. In addition, the sensitivity tests for the fair value and the effect of the change in the market prices on the fair value of the balances on and off the balance sheet for which there is a firm commitment at June 30, 2010, do not differ significantly from the report of December 31, 2009.

c. The linkage bases report at June 30, 2010 does not differ significantly from the report of December 31, 2009, except for the decrease in CPI-linked liabilities of NIS 629 million, which stems mainly from repayment of debentures and loans in the Group.

B. Corporate governance

1. Disclosure on the proceeding for approving the Company's financial statements

The organ responsible for oversight is the Board of Directors. The Company's Board of Directors appointed the Financial Statements Review Committee, whose tasks and composition are described in the Directors' Report for 2009 (the committee was previously known as the Balance Sheet Committee).

The financial statements were discussed by the Financial Statements Review Committee and submitted to the Board of Directors for approval. The following officers attended the Board discussion: Board members – Shlomo Rodav, Shaul Elovitz. Or Elovitz, Aryeh Saban, Felix Cohen, Rami Nomkin, Yehuda Porat, Eliahu Holtzman, Amikam Shorer, Yitzhak Edelman and Mordechai Keret. In addition, the following officers attended: Avraham Gabbay – CEO, Alan Gelman – CFO and Deputy CEO, Amir Nachlieli – General Counsel. Representatives of Somekh Chaikin, the Company's auditors, also participated in the discussion.

2. Disclosure concerning the Company's stages of preparation and progress to date in the application of the provisions of the Securities (Periodic and immediate reports) (Amendment) Regulations, 5770-2009 ("the Regulations"), in the matter of internal control

The disclosure below is made pursuant to Article 8(a)(2) of the Regulations, concerning actions taken by the Group to the date of this report (beyond that described in Section 8C of the Directors Report for the year ended December 31, 2009).

a. The Group has assessed the risks of the internal control on the basis of which the business processes and existing internal controls of financial reporting and disclosure were documented.
b. The Group has analyzed existing gaps in the planning of the internal control of financial reporting and disclosure.
c. The Group has started examination of the effectiveness of the internal control of financial reporting and disclosure.
d. The Group has initiated auditing by its auditors relating to the existing internal control of financial reporting and disclosure.

It is noted that the Group received approval from the Securities Authority on June 20, 2010, so that when and as long as the Group applies the provisions of internal control in the format defined in the Sarbanes-Oxley Act of 2002 ("SOX") in accordance with US legal requirements, and as long as the Company is a subsidiary of a company that is traded in the US, then the Group's reports on the effectiveness of the internal control must be in the format required by SOX rather than in the format required by the Securities (Periodic and immediate reports) Regulations, 5730-1970. According to the current estimates of the Group in the matter of the timetables, the Group expects to start application of the SOX provisions in 2011.

C. Disclosure concerning the Company’s financial reporting

1. Critical accounting estimates

Preparation of the financial statements in accordance with IFRSs requires management to make assessments and estimates that affect the reported values of assets, liabilities, income and expenses, as well as disclosure in connection with contingent assets and liabilities. Management bases these assessments and estimates on past experience and on valuations, expert opinions and other factors which it believes are relevant in the circumstances. Actual results might differ from these assessments with different assumptions or conditions. The financial statements provide information about primary topics of uncertainty in critical estimates and judgments in the application of the accounting policy. We believe these assessments and estimates to be critical since any change in them and in the assumptions could potentially and materially affect the financial statements.

2. Given the significance of the claims filed against the Group, which cannot yet be assessed or in respect of which the exposure cannot yet be calculated, the auditors drew attention to them in their opinion on the financial statements.

3. Events after the balance sheet date

On August 2, 2010, the Board of Directors of the Company resolved to recommend to the general meeting of the shareholders of the Company the distribution of a cash dividend of NIS 1,280 million to the shareholders.

D. Details of a series of liability certificates

Following are the updated data at June 30, 2010.

		Debentures Series 4	**Debentures Series 5**
A.	Par value	NIS 300,000,000 [1]	NIS 2,386,967,000
B.	Par value revalued at the reporting date (linked to the CPI)	NIS 344,232,229	NIS 2,738,903,240 [2]
C.	Accrued interest	NIS 1,358,067	NIS 11,931,113
D.	Fair value	NIS 361,440,000	NIS 3,132,655,491
E.	Stock exchange value	NIS 361,440,000	NIS 3,132,655,491

1. On June 1, 2010, NIS 300,000,000 par value was repaid.
2. Of which, NIS 1,010 million is held by a wholly-owned subsidiary.

On May 27, 2010 the Company was notified by Standard & Poor's Maalot that the present rating of the Company and of its debentures (AA+) was ratified and they were removed from negative CreditWatch. The rating outlook is stable.

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

Shlomo Rodav Chairman of the Board	Avraham Gabbay CEO

BEZEQ THE ISRAEL TELECOMMUNICATION CORP. LIMITED

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
JUNE 30, 2010
(UNAUDITED)

Condensed Consolidated Interim Financial Statements as at March 31, 2010 (unaudited)

Contents

Somekh Chaikin
8 Hartum Street, Har Hotzvim
PO Box 212, Jerusalem 91001
Israel

Telephone 972 2 531 2000
Fax 972 2 531 2044
Internet www.kpmg.co.il

Review Report to the Shareholders of
"Bezeq" The Israel Telecommunication Corp. Limited

Introduction

We have reviewed the accompanying financial information of Bezeq The Israel Telecommunication Corporation Ltd**.** and its subsidiaries ("the Group"), comprising of the condensed consolidated interim statement of financial position as of June 30, 2010 and the related condensed consolidated interim statements of income, comprehensive income, changes in equity and cash flows for the six 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.

Review scope

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 accepted accounting principles 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, 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, 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 above conclusion, we draw attention to the claims made against the Group of which the exposure cannot yet be assessed or calculated, as described in Note 6.

Sincerely,

Somekh Chaikin
Certified Public Accountants

August 2, 2010

Condensed Consolidated Interim Statements of Financial Position

	June 30, 2010	June 30, 2009	December 31, 2009
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Assets			
Cash and cash equivalents	**195**	765	580
Investments, including derivatives	**47**	120	154
Trade receivables	**2,678**	2,458	2,491
Other receivables	**266**	193	171
Inventory	**169**	192	263
Current tax assets	**-**	2	-
Assets held for sale	**38**	64	40
Total current assets	**3,393**	3,794	3,699
Investments, including derivatives	**138**	156	130
Trade and other receivables	**940**	733	887
Broadcasting rights, net of rights exercised	**-**	317	-
Property, plant and equipment	**5,513**	6,174*	5,428*
Intangible assets	**2,058**	2,678	1,885
Deferred and other expenses	**308**	276*	301*
Investments in equity-accounted investees (mainly loans)	**1,136**	31	1,219
Deferred tax assets	**334**	461	392
Total non-current assets	**10,427**	10,826	10,242
Total assets	**13,820**	14,620	13,941

	June 30, 2010	June 30, 2009	December 31, 2009
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Liabilities			
Debentures, loans and borrowings	**1,182**	1,046	862
Trade payables	**988**	1,438	1,091
Other payables, including derivatives	**652**	769	697
Current tax liabilities	**195**	120	118
Deferred income	**33**	59	36
Provisions	**371**	368	380
Employee benefits	**454**	352	505
Total current liabilities	**3,875**	4,152	3,689
Debentures	**1,995**	3,382	2,716
Bank loans	**2,052**	1,321	558
Loans from institutions	**-**	168	-
Loans from non-controlling interests in a subsidiary	**-**	487	-
Employee benefits	**295**	270	294
Deferred income and others	**5**	17	5
Provisions	**73**	66	71
Deferred tax liabilities	**76**	62	70
Total non-current liabilities	**4,496**	5,773	3,714
Total liabilities	**8,371**	9,925	7,403
Equity			
Total equity attributable to Company shareholders	**5,400**	5,198	6,544
Non-controlling interests	**49**	(503)	(6)
Total equity	**5,449**	4,695	6,538
Total equity and liabilities	**13,820**	14,620	13,941

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

Date of approval of the financial statements: August 2, 2010

* Retrospective application by restatement, see Note 3

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

Condensed Consolidated Interim Statements of Income

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Continuing operations Revenue (Note 9)	**5,896**	5,663	**2,981**	2,872	11,519
Costs and expenses					
Depreciation and amortization	**691**	748	**348**	377	1,485
Salaries	**994**	989	**489**	484	1,990
Operating and general expenses (Note 10)	**2,442**	2,325	**1,224**	1,189	4,871
Other operating expenses (income), net	**(95)**	(16)	**(70)**	4	201
	4,032	4,046	**1,991**	2,054	8,547
Operating profit	**1,864**	1,617	**990**	818	2,972
Finance income (expenses)					
Finance income	**124**	192	**66**	110	429
Finance expenses	**(137)**	(163)	**(101)**	(111)	(398)
Finance income (expenses), net	**(13)**	29	**(35)**	(1)	31
Profit after finance income (expenses), net	**1,851**	1,646	**955**	817	3,003
Share in profits (losses) of equity-accounted investees	**(109)**	4	**(86)**	2	(34)
Profit before income tax	**1,742**	1,650	**869**	819	2,969
Income tax	**462**	443	**231**	222	807
Profit for the period from continuing operations	**1,280**	1,207	**638**	597	2,162
Discontinued operations					
Profit (loss) for the period from discontinued operations	**-**	(96)	**-**	(95)	1,379
Profit for the period	**1,280**	1,111	**638**	502	3,541

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

Condensed Consolidated Interim Statements of Income (Contd.)

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Attributable to:					
Company shareholders					
Profit for the period from continuing operations	**1,280**	1,205	**638**	596	2,157
Profit (loss) for the period from discontinued operations	**-**	(56)	**-**	(55)	1,446
	1,280	1,149	**638**	541	3,603
Non-controlling interests					
Profit for the period from continuing operations	**-****	2	**-****	1	5
Loss for the period from discontinued operations	**-**	(40)	**-**	(40)	(67)
	-	(38)	**-**	(39)	(62)
Profit for the period	**1,280**	1,111	**638**	502	3,541
Earnings per share					
Basic earnings per share (NIS)					
Profit from continuing operations	**0.48**	0.46	**0.24**	0.23	0.82
Profit from discontinued operations	**-**	(0.02)	**-**	(0.02)	0.55
	0.48	0.44	**0.24**	0.21	1.37
Diluted earnings per share (NIS)					
Profit from continuing operations	**0.47**	0.45	**0.24**	0.22	0.80
Profit from discontinued operations	**-**	(0.02)	**-**	(0.02)	0.54
	0.47	0.43	**0.24**	0.20	1.34

* Restatement due to discontinued operations, see Note 4

** Less than NIS 500,000

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

Condensed Consolidated Interim Statements of Comprehensive Income

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Profit for the period	**1,280**	1,111	**638**	502	3,541
Other comprehensive profit (loss)for the period, net of tax	**-**	1	**1**	(2)	(11)
Total comprehensive income for the period	**1,280**	1,112	**639**	500	3,530
Attributable to:					
Company shareholders					
Profit for the period from continuing operations	**1,280**	1,206	**639**	594	2,146
Profit (loss) for the period from discontinued operations	**-**	(56)	**-**	(55)	1,446
	1,280	1,150	**639**	539	3,592
Non-controlling interests					
Profit for the period from continuing operations	**-****	2	**-****	1	5
Comprehensive loss for the period from discontinued operations	**-**	(40)	**-**	(40)	(67)
	-	(38)	**-**	(39)	(62)
Total comprehensive income for the period	**1,280**	1,112	**639**	500	3,530

* Restatement due to discontinued operations, see Note 4

** Less than NIS 500,000

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

Condensed Consolidated Interim Statements of Changes in Equity

	Share capital	Premium on share capital	Translation reserve	Capital reserve for a transaction between a corporation and a controlling shareholder	Capital reserve for options for employees	Retained earnings (deficit)	Total	Non-controlling interests	Total equity
					NIS millions				
					Attributable to owners of the Company				
Six months ended June 30, 2010 (unaudited)									
Balance at January 1, 2010 (audited)	6,187	275	(5)	390	210	(513)	6,544	(6)	6,538
Comprehensive income for the period (unaudited)	**-**	**-**	**-**	**-**	**-**	**1,280**	**1,280**	**-**	**1,280**
Dividend to shareholders of the Company (unaudited)	**-**	**-**	**-**	**-**	**-**	**(2,453)**	**(2,453)**	**-**	**(2,453)**
Share-based payments (unaudited)	**-**	**-**	**-**	**-**	**11**	**-**	**11**	**-**	**11**
Exercise of options into shares (unaudited)	**16**	**70**	**-**	**-**	**(68)**	**-**	**18**	**-**	**18**
Non-controlling interests in a business combination (unaudited)	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**55**	**55**
Balance at June 30, 2010 (unaudited)	**6,203**	**345**	**(5)**	**390**	**153**	**(1,686)**	**5,400**	**49**	**5,449**
Six months ended June 30,2009(unaudited)									
Balance at January 1, 2009 (audited)	6,132	-	(4)	390	362	(2,165)	4,715	(471)	4,244
Comprehensive income for the period (unaudited)	-	-	1	-	-	1,149	1,150	(38)	1,112
Dividend to shareholders of the Company (unaudited)	-	-	-	-	-	(792)	(792)	-	(792)
Share-based payments (unaudited)	-	-	-	-	28	-	28	-	28
Exercise of options into shares (unaudited)	40	203	-	-	(146)	-	97	-	97
Transfer of funds by non-controlling interests(unaudited)	-	-	-	-	-	-	-	6	6
Balance at June 30, 2009 (unaudited)	6,172	203	(3)	390	244	(1,808)	5,198	(503)	4,695

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

Condensed Consolidated Interim Statements of Changes in Equity (contd.)

	Share capital	Premium on share capital	Translation reserve	Capital reserve for a transaction between a corporation and a controlling shareholder	Capital reserve for options for employees	Retained earnings (deficit)	Total	Non-controlling interests	Total equity
	NIS millions								
	Attributable to owners of the Company								
Three months ended June 30, 2010 (unaudited)									
Balance at April 1, 2010 (unaudited)	**6,201**	**338**	**(6)**	**390**	**154**	**129**	**7,206**	**(6)**	**7,200**
Comprehensive income for the period (unaudited)	**-**	**-**	**1**	**-**	**-**	**638**	**639**	**-**	**639**
Dividend to shareholders of the Company (unaudited)	**-**	**-**	**-**	**-**	**-**	**(2,453)**	**(2,453)**	**-**	**(2,453)**
Share-based payments (unaudited)	**-**	**-**	**-**	**-**	**5**	**-**	**5**	**-**	**5**
Exercise of options into shares (unaudited)	**2**	**7**	**-**	**-**	**(6)**	**-**	**3**	**-**	**3**
Non-controlling interests in a business combination (unaudited)	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**55**	**55**
Balance at June 30, 2010 (unaudited)	**6,203**	**345**	**(5)**	**390**	**153**	**(1,686)**	**5,400**	**49**	**5,449**
Three months ended June 30, 2009 (unaudited)									
Balance at April 1, 2009 (unaudited)	6,146	26	(1)	390	373	(1,557)	5,377	(465)	4,912
Comprehensive income for the period (unaudited)	-	-	(2)	-	-	541	539	(39)	500
Dividend to shareholders of the Company (unaudited)	-	-	-	-	-	(792)	(792)	-	(792)
Share-based payments (unaudited)	-	-	-	-	13	-	13	-	13
Exercise of options into shares (unaudited)	26	177	-	-	(142)	-	61	-	61
Transfer of funds by non-controlling interests (unaudited)	-	-	-	-	-	-	-	1	1
Balance at June 30, 2009 (unaudited)	6,172	203	(3)	390	244	(1,808)	5,198	(503)	4,695

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

Condensed Consolidated Interim Statements of Changes in Equity (contd.)

	Share capital	Premium on share capital	Translation reserve	Capital reserve for a transaction between a corporation and a controlling shareholder	Capital reserve for options for employees	Retained earnings (deficit)	Total	Non-controlling interests	Total equity
					NIS millions				
	Attributable to owners of the Company								
Balance at January 1, 2009 (audited)	6,132	-	(4)	390	362	(2,165)	4,715	(471)	4,244
Comprehensive income for the year (audited)	-	-	(1)	-	-	3,593	3,592	(62)	3,530
Dividends to Company shareholders (audited)	-	-	-	-	-	(1,941)	(1,941)	-	(1,941)
Share-based payments (audited)	-	-	-	-	49	-	49	-	49
Exercise of options into shares (audited)	55	275	-	-	(201)	-	129	-	129
Derecognition of non-controlling interests for deconsolidation of a company (audited)	-	-	-	-	-	-	-	551	551
Dividend paid to non-controlling interests less transfer of funds (audited)	-	-	-	-	-	-	-	(24)	(24)
Balance at December 31, 2009 (audited)	6,187	275	(5)	390	210	(513)	6,544	(6)	6,538

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

Condensed Consolidated Interim Statements of Cash Flows

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flows from operating activities					
Profit for the period	**1,280**	1,111	**638**	502	3,541
Adjustments:					
Depreciation	**546**	705*	**274**	358*	1,343*
Amortization of intangible assets	**133**	142	**68**	70	266
Amortization of deferred and other expenses	**12**	10*	**6**	5*	22*
Profit from deconsolidation of a subsidiary	**-**	-	**-**	-	(1,538)
Profit from a controlling shareholder in an investee	**(57)**	-	**(57)**	-	-
Share in losses (profits) of equity-accounted investees	**109**	(4)	**86**	(2)	34
Finance expenses, net	**34**	173	**40**	95	362
Capital gain, net	**(29)**	(24)	**(2)**	(4)	(64)
Share-based payments	**11**	28	**5**	13	49
Income tax expenses	**462**	443	**231**	221	807
Proceeds (payment) for derivatives, net	**(1)**	16	**-**	7	11
Change in inventory	**93**	(39)	**15**	(6)	(114)
Change in trade receivables	**(195)**	(243)	**(85)**	(165)	(583)
Change in other receivables	**(49)**	(17)	**13**	34	37
Change in other payables	**12**	102	**(11)**	(95)	55
Change in trade payables	**(168)**	72	**(3)**	(44)	192
Change in provisions	**(12)**	11	**(8)**	4	36
Change in broadcasting rights	**-**	(64)	**-**	(30)	(49)
Change in employee benefits	**(53)**	(55)	**(28)**	(5)	115
Change in deferred income and others	**(7)**	(48)	**(12)**	(2)	(41)
Income tax paid, net	**(339)**	(286)	**(194)**	(148)	(565)
Net cash flows from operating activities	**1,782**	2,033	**976**	808	3,916

* Retrospective application by restatement, see Note 3

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

Condensed Interim Statements of Cash Flows (contd.)

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flow used in investment activities					
Investment in intangible assets and deferred expenses	**(158)**	(156)	**(70)**	(93)	(349)
Proceeds from sale of property, plant and equipment and deferred expenses	**41**	62	**26**	11	90
Change in current investments, net	**110**	(94)	**(31)**	(100)	(134)
Purchase of property, plant and equipment	**(607)**	(756)	**(326)**	(348)	(1,363)
Proceeds from disposal of investments and long-term loans	**4**	41	**2**	34	93
Investments and long-term loans	**(3)**	(3)	**(2)**	(2)	(4)
Business combinations less cash acquired	**(30)**	-	**(30)**	-	-
Dividend received	**-**	5	**-**	5	6
Interest received	**7**	13	**7**	8	29
Net cash used for investment activities	**(636)**	(888)	**(424)**	(485)	(1,632)
Cash flow for finance activities					
Bank loans received	**1,900**	400	**1,900**	-	400
Repayment of debentures	**(622)**	(609)	**(416)**	(403)	(682)
Repayment of loans	**(424)**	(62)	**(415)**	(31)	(109)
Short-term borrowing, net	**225**	41	**225**	41	48
Dividend paid	**(2,453)**	(792)	**(2,453)**	(792)	(1,941)
Interest paid	**(175)**	(258)	**(145)**	(148)	(354)
Proceeds for derivatives, net	**-**	11	**-**	11	43
Transfer of funds by non-controlling interests less dividend distributed, net	**-**	6	**-**	1	(24)
Proceeds from exercise of options into shares	**18**	97	**3**	61	129
Net cash used for finance activities	**(1,531)**	(1,166)	**(1,301)**	(1,260)	(2,490)
Net decrease in cash and cash equivalents	**(385)**	(21)	**(749)**	(937)	(206)
Cash and cash equivalents at beginning of period	**580**	786	**944**	1,702	786
Cash and cash equivalents at end of period	**195**	765	**195**	765	580

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

NOTE 1 – REPORTING ENTITY

A. Bezeq – The Israel Telecommunication Corp. Ltd. ("the Company") is a company registered in Israel whose shares are traded on the Tel Aviv Stock Exchange. The condensed consolidated financial statements of the Company include those of the Company and its subsidiaries (together – "the Group"), as well as the interests of the Group in associates. The Group is a principal provider of communication services in Israel (see also Note 11 – Segment Reporting).

B. As from April 14, 2010, B Communications (SP2) Ltd. (B Communications) is the controlling shareholder of the Company, after acquiring the shares of the Company from Ab.Sp.Ar. At June 30, 2010, B Communications holds 30.43% of the Company's shares. B Communications is wholly owned and controlled by B Communications (SP1) Ltd., which is wholly owned and controlled by B Communications Ltd. (formerly 012 Smile Communications Ltd.).

C. The Company is subject to various sets of laws that regulate and restrict its business activities, including its tariffs. The Company's tariffs are regulated by provisions in the Communications Law. The Company's service fees are regulated and updated according to a linkage formula. The Company was declared a monopoly in the main areas in which it operates. All the operating segments of the Group are subject to competition. The operations of the Group are subject, in general, to government regulations regulation and supervision. The intensifying competition and changes in the communication market could have an adverse effect on the business results of the Group.

D. From August 21, 2009, the Company no longer consolidates the reports of DBS Satellite Services (1998) Ltd. ("DBS) in its financial statements and the investment in DBS is stated according to the equity method commencing from that date. See Note 4 below.

E. On April 25, 2010, Bezeq International completed an acquisition of the shares of Haaretz Newspaper Publishing Ltd. in Walla! Communications Ltd. (Walla) and started to consolidate Walla in its financial statements. See Note 5 below.

NOTE 2 - BASIS OF PREPARATION

A. The condensed interim consolidated financial statements have been prepared in accordance with IAS 34 – *Interim Financial Reporting*, and Chapter D of the Securities (Periodic and Immediate Reports) Regulations, 5730-1970.

B. 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 at December 31, 2009 and the year then ended, and their accompanying notes ("the annual financial statements"). The notes to the 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.

C. The condensed consolidated interim financial statements were approved by the Board of Directors on August 2, 2010.

D. **Use of estimates and judgment**
The preparation of condensed consolidated interim financial statements in accordance with 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 and liabilities, income and expenses. Actual results may differ from the estimates used.

The judgment of management, when applying the Group's accounting policy and the principal assumptions used in assessments that involve uncertainty are consistent with those used in the annual financial statements.

NOTE 3 – REPORTING PRINCIPLES AND ACCOUNTING POLICY

The significant accounting policies applied in these condensed financial statements are consistent with those applied in the annual financial statements for the year ended December 31, 2009, except for application of new standards and amendments to standards, as set out below.

Initial implementation of new accounting standards

Commencing from January 1, 2010, the Group applies the amendment to IAS 17 – *Leases: Classification of Leases of Land and Buildings* ("the Amendment"). The Amendment eliminates the requirement to classify a lease of land as an operating lease when the title is not expected to pass to the lessee at the end of the lease term.

The Company leases land from the Israel Land Administration, accounted for as an operating lease. Subsequent to adoption of the Amendment, the Company classified the lease of the land retrospectively as a finance lease. Accordingly, the land is stated as property, plant and equipment in the statement of financial position as at June 30, 2009 and December 31, 2009, in the amount of NIS 151 million and NIS 125 million, respectively.

NOTE 4 – DISCONTINUED OPERATIONS

Further to Note 5 to the 2009 financial statements, as from August 21, 2009, the Company no longer consolidates the reports of DBS in its financial statements and the investment in DBS shares is stated according to the equity method as from that date. The financial statements of DBS are attached to these financial statements.

The consolidated statements of income for the six and three months ended June 30, 2010 and for the year ended December 31, 2009 are stated without consolidation of the statements of DBS. The operational results of DBS for the period up to August 20, 2009 and comparative figures were presented as discontinued operations. The consolidated statement of income for the six and three months ended June 30, 2009 was restated in order to retrospectively reflect the discontinued operations, following deconsolidation, separately from continuing operations. The statement of financial position as at June 30, 2009 and statement of cash flow for the six and three months ended June 30, 2009 were not restated.

(1) Results of discontinued operations

	Six months ended June 30, 2009	Three months ended June 30, 2009	From January 1 to August 20, 2009
	(Unaudited)	(Unaudited)	(Unaudited)
	NIS millions	NIS millions	NIS millions
Revenue	760	376	970
Cost of revenue	514	256	663
Gross profit	246	120	307
Selling and marketing expenses	62	33	79
General and administrative expenses	59	28	74
	121	61	153
Operating profit	125	59	154
Finance expenses, net	221	154	313
Loss after finance expenses	(96)	(95)	(159)
Profit from deconsolidation of a subsidiary	-	-	1,538
Profit (loss) for the period from discontinued operations	(96)	(95)	1,379

NOTE 4 – DISCONTINUED OPERATIONS (CONTD.)

(2) Cash flow from discontinued operations

	Six months ended June 30, 2009	Three months ended June 30, 2009	From January 1 to August 20, 2009
	(Unaudited)	(Unaudited)	(Unaudited)
	NIS millions	NIS millions	NIS millions
Cash flow from operating activities	184	93	260
Cash flow used for investment activities	(121)	(60)	(176)
Cash flow used for finance activities	(63)	(33)	(84)
Cash flow from discontinued operations	-	-	-

NOTE 5 – GROUP ENTITIES

A detailed description of the Group entities appears in Note 13 to the Group's annual financial statements as at December 31, 2009. Below are details of the material changes that occurred in connection with the Group entities since publication of the annual financial statements.

A. Equity-accounted associates

DBS Satellite Services (1998) Ltd.

(1) On March 18, 2010, the board of directors of the Company, as a shareholder in DBS Satellite Services (1998) Ltd. ("DBS"), approved the amendment to the financing agreement between DBS and the banks that provide financing for the operations of DBS ("the banks"). Under the amendment, another bank will join the banks, and the amount and terms of the financing provided to DBS will be adjusted. Concurrently, amendments were approved to the deed of amendment to the shareholders' loans and the deed of amendment to the guarantee provided by the Company in favor of the banks, such that they would apply to the adjusted financing arrangement. These amendments do not significantly increase the Company's exposure (if at all).

(2) At June 30, 2010, the balance of DBS's current debt to the Company and its subsidiaries amounts to NIS 60 million, of which NIS 49 million is to the Company. Further to Note 13(A)(2) to the financial statements as at December 31, 2009 in respect of DBS's current debt to the Group companies, the Company formulated an arrangement for DBS's debt to the Company for communication services, amounting to NIS 31.5 million at July 31, 2009 (reflecting a compromise between the Company's position and that of DBS). Under the arrangement, DBS will repay the debt to the Company in 36 equal monthly payments of NIS 875,000 each plus VAT and interest at prime + 1.5% plus VAT for the interest. On May 20, 2010, the general meeting of the Company's shareholders approved the debt arrangement. As at the approval date, the agreement has yet to be signed and implemented.

(3) Pursuant to the immediate report issued by Hot Communication Services ("the cable company"), in July 2010 a ruling was provided in the arbitration between the cable company and ACUM, the composers, lyricists, poets and music publishers society for royalties to which ACUM has rights. The arbitrator accepted in principle ACUM's formula for calculating royalties, with the exception of certain changes, and determined that this formula would also apply to the difference in royalties as from 2003 onwards, to be calculated by the parties in a settlement.

NOTE 5 – GROUP ENTITIES (CONTD.)

A. Equity-accounted associates (contd.)

DBS Satellite Services (1998) Ltd. (contd.)

(3) (contd.)
The cable company noted that it intends to appeal the arbitration ruling. Since DBS does not have access to the arbitration ruling and the other arbitration documents, the model that was adopted and the reasons for the arbitration ruling are unknown to DBS. However, pursuant to the agreements between DBS and ACUM, the royalties paid to ACUM as from 2003 are liable to be adjusted, inter alia, subject to the settlement between the cable company and ACUM, and according to ACUM, also subject to the ruling of the arbitrator. Therefore, the management of DBS believes that following the arbitration ruling, DBS will be required to pay material amounts retrospectively. In view of the aforesaid, DBS adjusted the estimated amount of royalties as from 2003. The adjustment was based on the formula for calculating royalties furnished by ACUM shortly after the arbitration ruling, with adjustments according to the estimation of the management of DBS. On this basis, DBS recorded a significant provision in its financial statements as at June 30, 2010.

DBS is in compliance with the financial covenants set out in the finance agreement of June 30, 2010, after receiving relief from the banks in August 2010 in respect of one of the covenants at June 30, 2010, which was required in view of the significant provision recorded by DBS as aforesaid. As this relief was received subsequent to the reporting date, DBS's bank loan of NIS 816.520 million is stated as a short-term liability. The covenant is measured on an annual basis, therefore the management of DBS believes that the company will require additional relief in respect of the purposes of the financial covenant for September 30, 2010 and December 31, 2010, which DBS is attempting to obtain from the banks.

The management of DBS believes that the financing resources available to the company will be sufficient for its operational requirements for the coming year, based on the projected cash flow approved by the board of directors of DBS. If additional resources are required to meet its operational requirements in the coming year, DBS will adapt its operations to preclude the need for additional resources beyond those available to it.
For additional details see Note 4 to the financial statements of DBS as at June 30, 2010, which are attached to these financial statements.

B. Subsidiaries

Walla! Communications Ltd.

(1) On April 25, 2010, Bezeq International acquired 14,807,939 ordinary shares of Walla, representing 32.55% of the issued and paid up share capital of Walla, in an exchange transaction, for NIS 89 million. Upon receipt of the acquired shares, Bezeq International transferred 21.77% of the issued and paid up share capital of Walla to a trustee that will hold them in a blind trust. Following the transfer, Bezeq International directly holds 44.99% of the issued and paid up share capital of Walla and is the controlling shareholder in Walla. As from April 25, 2010, Bezeq International consolidates Walla in its financial statements.
The contribution of Walla to profit and revenue as from the beginning of the consolidation and through to June 30, 2010 amounted to NIS 3 million and NIS 31 million, respectively. Had the acquisition taken place on January 1, 2010, the revenue in the consolidated statement of income and the consolidated profit in the period would not have been materially different. Management assumes that the fair value adjustments at the acquisition date, which were determined, are the same as the adjustments that would have been received had the acquisition taken place on January 1, 2010. As from the date of consolidation, the operations of Walla are included under other segments (see Note 11). In accordance with IFRS, the holdings in Walla prior to the acquisition were estimated at the share price which was included in the acquisition transaction. As a result, a profit of NIS 57 million was included in the consolidated financial statements.

NOTE 5 – GROUP ENTITIES (CONTD.)

B. Subsidiaries (contd.)

Walla! Communications Ltd. (contd.)

(1) (contd.)
Bezeq International carried out temporary attribution of the acquisition cost in relation to the fair value of the assets and liabilities that were acquired in the context of a business combination. The fair value of the acquired assets and liabilities is adjustable up to twelve months from the acquisition date.

Acquisition of the Group's assets and liabilities at the acquisition date had the following effect:

	Values recognized at the acquisition date
	(Unaudited)
	NIS millions
Identifiable assets and liabilities, net	105
Prior equity rights in an acquiree	(94)
Goodwill upon acquisition	73
Non-controlling interests	(54)
Cost of business combination	30
Proceeds paid in cash	(89)
Cash acquired	59
Cash paid, net	(30)

(2) On July 8, 2010, Walla entered into an agreement with the shareholders of Coral-Tell Ltd. ("Yad2"), which is the operator of the classified ads site Yad2. Under the agreement, Walla will acquire 75% of the share capital of Yad2 for NIS 117.5 million, and will also pay additional amounts to some of the sellers, based on the total working capital of Yad2 and subject to adjustments. At the approval date of these financial statements, the transaction has yet to be finalized. Finalization of the transaction is subject to preconditions.

NOTE 6 – CONTINGENT LIABILITIES

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

In the opinion of the managements of the Group companies, based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions of NIS 355 million, where provisions are required to cover the exposure resulting from such claims.
In the opinion of the managements of the Group companies, the additional exposure at June 30, 2010, due to claims filed against the Group companies on various matters and which are unlikely to be realized, amounts to NIS 13 billion (for updates in this matter subsequent to the reporting date, see section B below). This amount and all the amounts of the additional exposure in this note are linked to the CPI and before the addition of interest.

For applications for certification as class action of lawsuits to which the Group has exposure beyond the aforesaid (since the claims do not state an exact amount), see sections B and D below.

The contingent liabilities of the Group are described in detail in Note 18 to the financial statements of the Group as at December 31, 2009. Following is a detailed description of the Group's contingent liabilities as at June 30, 2010, classified into groups with similar characteristics.

NOTE 6 – CONTINGENT LIABILITIES

A. Employee claims

At June 30, 2010, the additional exposure (beyond the provisions included in these financial statements) for employee claims amounts to NIS 1.4 billion and relates mainly to claims filed by groups of employees or individual claims with wide ramifications. In the opinion of the management of the Company, based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions of NIS 117 million, where provisions are required to cover the exposure resulting from such claims.

B. Customer claims

At June 30, 2010, the amount of the additional exposure for customer claims (beyond the provisions included in these financial statements) amounted to NIS 5 billion. There are other claims for which the Group has additional exposure beyond the aforesaid, which cannot be quantified, as the exact amount of the claim is not stated in the claim. In the opinion of the managements of the Group companies, based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions of NIS 56 million, where provisions are required to cover the exposure resulting from such claims. Of these claims, there are claims amounting to NIS 34 million, which, at this stage, cannot yet be estimated. Subsequent to the reporting date, another two claims were filed against the company, together with application for certification as class actions, which at this stage cannot be assessed. The plaintiff estimates the first claim at tens of millions of shekels and the second claim is estimated at NIS 250 million. On the other hand, a class action against Pelephone amounting to NIS 239 million was dismissed.

C. Supplier and communication provider claims

At June 30, 2010, the amount of the additional exposure for claims filed by suppliers and communication providers (beyond the provisions included in these financial statements) amounts to NIS 970 million. In the opinion of the managements of the Group companies, which is based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions amounting to NIS 11 million, where provisions are required to cover the exposure resulting from such claims.

D. Claims for punitive damages

At June 30, 2010, the amount of the additional exposure (beyond the provisions included in these financial statements) for punitive damages amounts to NIS 4.9 billion. This amount does not include claims for which the insurance coverage is not disputed. There are other claims for which the Group has additional exposure beyond the aforesaid, which cannot be quantified, as the exact amount of the claim is not stated in the claim.

In the opinion of the managements of the Group companies, based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions of NIS 2.4 million, where provisions are required to cover the exposure resulting from such claims. In addition, of these claims, there are claims amounting to NIS 3.7 billion, which, at this stage, cannot yet be estimated.

E. Claims by entrepreneurs and companies

At June 30, 2010, the amount of the additional exposure for claims filed by entrepreneurs and companies (beyond the provisions included in these financial statements) amounts to NIS 315 million. In the opinion of the managements of the Group companies, which is based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions amounting to NIS 10 million, where provisions are required to cover the exposure resulting from such claims.

F. Claims by the State and authorities

At June 30, 2010, the amount of the additional exposure for claims filed by the State of Israel and various authorities ((beyond the provisions included in these financial statements) amounts to NIS 588 million. In the opinion of the managements of the Group companies, which is based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions amounting to NIS 159 million, where provisions are required to cover the exposure resulting from such claims.

For claims against DBS, see Note 5 to the financial statements of DBS as at June 30, 2010, which are attached to these financial statements.

NOTE 7 – EQUITY AND SHARE-BASED PAYMENTS

A. Share capital

Registered			Issued and paid up		
June 30, 2010	June 30, 2009	December 31, 2009	June 30, 2010	June 30, 2009	December 31, 2009
(Unaudited)	(Unaudited)	(Audited)	(Unaudited)	(Unaudited)	(Audited)
Number of shares	Number of shares	Number of shares	Number of shares	Number of shares	Number of shares
2,749,000,000	2,749,000,000	2,749,000,000	**2,675,835,682**	2,645,988,758	2,659,727,630

B. In January and March 2010, the board of directors of the Company approved the allotment of 1,000,000 options to senior employees in the Group, under the plan set out in Note 27(A)(3) to the financial statements as at December 31, 2009. The theoretical economic value of the allotted options, calculated at the date of approval of the allotment by the board of directors, according to a weighted Black and Scholes model, is NIS 3.2 million.

C. Following the exercise of options by employees in accordance with the options plans described in Note 27 to the financial statements as at December 31, 2009, in the six months ended June 30, 2010, the Company issued 16,108,052 ordinary shares of NIS 1 par value each.

D. Subsequent to the reporting date and through August 1, 2010, following the exercise of options by the employees, in accordance with the options plans set out in Note 27 to the financial statements as at December 31, 2009, the Company issued 340,033 ordinary shares of NIS 1 par value each.

E. The Company paid dividends as follows:

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash dividend paid in May 2010 (NIS 0.917 per share)	**2,453**	-	**2,453**	-	-
Cash dividend paid in May 2009 (NIS 0.3 per share)	-	792	-	792	792
Cash dividend paid in October 2009 (NIS 0.43 per share)	-	-	-	-	1,149
	2,453	792	**2,453**	792	1,941

F. On August 2, 2010, the board of directors of the Company resolved to recommend to the general meeting the distribution of a dividend to the shareholders in the amount of NIS 1.280 billion, representing NIS 0.4782944 per share at the resolution date. The percentage of the dividend actually paid will be determined according to the Company's issued and paid up capital at the end of the business day on September 20, 2010. The distribution is subject to the approval of the general meeting of the Company.

NOTE 8 – TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES

A. Further to Note 30(B) to the financial statements as at December 31, 2009, in respect of the management and consultation services agreement with Ap.Sb.Ar. and the subsequent sale of the controlling stake in the Company by Ap.Sb.Ar., on April 14, 2010, the management agreement between the Company and a company owned and controlled by the shareholders in Ap.Sb. Ar was terminated.
In addition, in May 2010, the general meeting of the shareholders of the Company approved a new agreement between the Company and Eurocom Communications Ltd. Under the agreement, Eurocom will provide the Company ongoing management and consultation services for an annual fee of $1.2 million. The term of the agreement is for three years as from June 1, 2010.

B. Subsequent to the transfer of control in the Company, the certified bodies of the Company approved a series of agreements between the Company and its subsidiaries and DBS with the B Communications Group, including extraordinary transactions. The transactions are approved from time to time according to the requirements of the Company and its subsidiaries and are reported to the public according to the law.

Material transactions with interested and related parties

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue:					
Associates	**73**	107	**51**	67	224
Related parties	**5**	-	**5**	-	-
Expenses:					
Associates	**-**	1	**-**	1	3
Related parties	**86**	-	**86**	-	-
Investments:					
Related parties	**29**	-	**29**	-	-

Material balances with interested and related parties

	June 30	December 31,
	2010	2009
	(Unaudited)	(Audited)
	NIS millions	NIS millions
Associates, net	**60**	70
Loans to an associate	**1,136**	1,165
Related parties, net	**(115)**	-
Loan from related parties to an associate	**(888)**	-

NOTE 8 – TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES (CONTD.)

C. Further to Note 30(E) to the financial statements as at December 31, 2009, on April 8, 2010, the general meeting of the Company's shareholders approved a maximum bonus for 2009 for the chairman of the Company's board of directors, under the terms of his employment agreement, as approved by the general meeting on June 1, 2008, of 18 monthly salaries, amounting to NIS 3.44 million.

D. Further to Note 30 (G)(11) to the financial statements as at December 31, 2009 regarding the conversion of the D&O insurance policy to a runoff policy, in March 2010, the general meeting of the Company's shareholders approved the agreement for acquisition of the runoff policy. In addition, further to the transfer of control in the Company and the appointment of new directors, in May 2010, the general meeting of the Company's shareholders approved a letter of indemnity for the directors, in the format that is accepted by the Company as approved by the general meeting.

E. In May 2010, the general meeting of the Company's shareholders approved the settlement agreement between the Company and the former CEO of the Company, in which all of the mutual claims of the parties are dismissed, including claims against other Group companies and their representatives. Under the agreement, the Company will pay the former CEO a lump sum of NIS 9 million (gross). These financial statements include provisions for this settlement agreement.

NOTE 9 – REVENUE

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009*	2010	2009*	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Domestic fixed-line communications					
Fixed line telephony	**1,537**	1,630	**774**	815	3,247
Internet - infrastructure	**471**	408	**235**	201	862
Transmission, data communication and other	**468**	478	**231**	242	940
	2,476	2,516	**1,240**	1,258	5,049
Cellular					
Cellular services and terminal equipment	**2,122**	1,948	**1,080**	989	4,013
Sale of terminal equipment	**574**	542	**288**	297	1,119
	2,696	2,490	**1,368**	1,286	5,132
International communications, internet services and NEP	**667**	629	**332**	314	1,276
Other	**57**	28	**41**	14	62
	5,896	5,663	**2,981**	2,872	11,519

* Restatement due to discontinued operations, see Note 4

NOTE 10 – OPERATING AND GENERAL EXPENSES

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	**2009***	**2010**	**2009***	**2009**
	(Unaudited)	**(Unaudited)**	**(Unaudited)**	**(Unaudited)**	**(Audited)**
	NIS millions	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**
Cellular telephone expenses	**912**	852	**476**	437	1,750
General expenses	**563**	491	**280**	241	1,140
Materials and spare parts	**520**	482	**257**	264	1,003
Services and maintenance by sub-contractors	**60**	73	**27**	34	146
Building maintenance	**121**	141	**57**	72	295
International communication expenses	**158**	161	**73**	80	313
Vehicle maintenance expenses	**64**	61	**33**	30	124
Royalties to the State of Israel	**33**	48	**17**	24	66
Collection fees	**11**	16	**4**	7	34
	2,442	2,325	**1,224**	1,189	4,871

* Restatement due to discontinued operations, see Note 4

NOTE 11 – SEGMENT REPORTING

A. Operating segments

	Six months ended June 30, 2010 (unaudited)						
	Domestic fixed-line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue from external sources	2,474	2,695	667	787	54	(789)	5,888
Inter-segment revenue	137	127	18	-	16	(290)	8
Total revenue	2,611	2,822	685	787	70	(1,079)	5,896
Depreciation and amortization	341	298	49	132	3	(132)	691
Segment results – operating profit	993	684	182	66	5	(66)	1,864
Finance income	78	45	4	4	2	(9)	124
Finance expenses	(106)	(30)	(6)	(221)	-	226	(137)
Total finance income (expenses), net	(28)	15	(2)	(217)	2	217	(13)
Segment profit (loss) after finance expenses, net	965	699	180	(151)	7	151	1,851
Share in the (profits) losses of equity-accounted investees	-	-	3	-	-	(112)	(109)
Segment profit (loss) before income tax	965	699	183	(151)	7	39	1,742
Income tax	(256)	(173)	(31)	-	(2)	-	(462)
Segment results – net profit (loss)	**709**	**526**	**152**	**(151)**	**5**	**39**	**1,280**

NOTE 11 – SEGMENT REPORTING (CONTD.)

A. Operating segments (contd.)

	Six months ended June 30, 2009 (unaudited)*						
	Domestic fixed-line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue from external sources	2,509	2,490	626	759	23	(759)	5,648
Inter-segment revenue	135	121	25	1	12	(279)	15
Total revenue	2,644	2,611	651	760	35	(1,038)	5,663
Depreciation and amortization	416	290	40	112	2	(112)	748
Segment results – operating profit	871	623	128	125	1	(131)	1,617
Finance income	145	45	9	12	-	(19)	192
Finance expenses	(120)	(39)	(6)	(233)	(5)	240	(163)
Total finance income (expenses), net	25	6	3	(221)	(5)	221	29
Segment profit (loss) after finance expenses, net	896	629	131	(96)	(4)	90	1,646
Share in the profits of equity-accounted investees	-	-	4	-	-	-	4
Segment profit (loss) before income tax	896	629	135	(96)	(4)	90	1,650
Loss from discontinued operations	-	-	-	-	-	(96)	(96)
Income tax	(244)	(166)	(35)	-	-	2	(443)
Segment results – net profit (loss)	652	463	100	(96)	(4)	(4)	1,111

* Restatement due to discontinued operations, see Note 4

Notes to the Financial Statements as at June 30, 2010

NOTE 11 – SEGMENT REPORTING (CONTD.)

A. Operating segments (contd.)

	Three months ended June 30, 2010 (unaudited)						
	Domestic fixed-line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue from external sources	**1,239**	**1,367**	**332**	**396**	**41**	**(398)**	**2,977**
Inter-segment revenue	**68**	**62**	**10**	**-**	**10**	**(146)**	**4**
Total revenue	**1,307**	**1,429**	**342**	**396**	**51**	**(544)**	**2,981**
Depreciation and amortization	**171**	**149**	**26**	**68**	**2**	**(68)**	**348**
Segment results – operating profit	**503**	**362**	**121**	**7**	**4**	**(7)**	**990**
Finance income	**50**	**11**	**2**	**4**	**2**	**(3)**	**66**
Finance expenses	**(79)**	**(18)**	**(3)**	**(154)**	**-**	**153**	**(101)**
Total finance income (expenses), net	**(29)**	**(7)**	**(1)**	**(150)**	**2**	**150**	**(35)**
Segment profit (loss) after finance expenses, net	**474**	**355**	**120**	**(143)**	**6**	**143**	**955**
Share in the profits of equity-accounted investees	**-**	**-**	**2**	**-**	**-**	**(88)**	**(86)**
Segment profit (loss) before income tax	**474**	**355**	**122**	**(143)**	**6**	**55**	**869**
Income tax	**(125)**	**(88)**	**(16)**	**-**	**(2)**	**-**	**(231)**
Segment results – net profit (loss)	**349**	**267**	**106**	**(143)**	**4**	**55**	**638**

Notes to the Financial Statements as at June 30, 2010

NOTE 11 – SEGMENT REPORTING (Contd.)

A. Operating segments (contd.)

	Three months ended June 30, 2009 (unaudited)*						
	Domestic fixed-line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue from external sources	1,256	1,286	316	375	10	(375)	2,868
Inter-segment revenue	62	60	11	1	8	(138)	4
Total revenue	1,318	1,346	327	376	18	(513)	2,872
Depreciation and amortization	205	151	20	55	1	(55)	377
Segment results – operating profit	434	321	68	59	1	(65)	818
Finance income	87	6	6	3	-	8	110
Finance expenses	(83)	(11)	(2)	(157)	(5)	147	(111)
Total finance income (expenses), net	4	(5)	4	(154)	(5)	155	(1)
Segment profit (loss) after finance expenses, net	438	316	72	(95)	(4)	90	817
Share in the profits of equity-accounted investees	-	-	2	-	-	-	2
Segment profit (loss) before income tax	438	316	74	(95)	(4)	90	819
Loss from discontinued operations	-	-	-	-	-	(95)	(95)
Income tax	(122)	(83)	(18)	-	-	1	(222)
Segment results – net profit (loss)	316	233	56	(95)	(4)	(4)	502

* Restatement due to discontinued operations, see Note 4

NOTE 11 – SEGMENT REPORTING (Contd.)

A. Operating segments (contd.)

	Year ended December 31, 2009						
	Domestic fixed-line communications	**Cellular telephone**	**International communications, internet and NEP services**	**Multi-channel television**	**Others**	**Adjustments**	**Consolidated**
	NIS millions	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**
Revenue from external sources	5,039	5,130	1,273	1,529	54	(1,529)	11,496
Inter-segment revenue	264	246	45	1	20	(553)	23
Total revenue	5,303	5,376	1,318	1,530	74	(2,082)	11,519
Depreciation and amortization	794	603	84	234	4	(234)	1,485
Segment results – operating profit	1,523	1,190	261	248	4	(254)	2,972
Finance income	310	90	**15**	8	23	(17)	429
Finance expenses	(295)	(100)	(12)	(478)	-	487	(398)
Total finance income (expenses), net	15	(10)	3	(470)	23	470	31
Segment profit (loss) after finance expenses, net	1,538	1,180	264	(222)	27	216	3,003
Share in the profits of equity-accounted investees	-	-	7	-	-	(41)	(34)
Segment profit (loss) before income tax							
Loss from discontinued operations	1,538	1,180	271	(222)	27	175	2,969
Income tax	-	-	-	-	-	1,379	1,379
	(431)	(305)	(71)	(1)	(2)	3	(807)
Segment results – net profit (loss)	1,107	875	200	(223)	25	1,557	3,541

Notes to the Financial Statements as at June 30, 2010

NOTE 11 – SEGMENT REPORTING (CONTD.)

B. Adjustments for segment reporting of revenue, profit or loss

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009*	2010	2009*	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue					
Revenue from reporting segments	**6,903**	6,666	**3,472**	3,367	13,527
Revenue from other segments	**70**	35	**51**	18	74
Cancellation of revenue from inter-segment sales, except for revenue from sales to an associate reporting as a segment	**(290)**	(279)	**(146)**	(138)	(553)
Cancellation of revenue for a segment classified as an associate (up to August 20, 2009 - discontinued operations)	**(787)**	(759)	**(396)**	(375)	(1,529)
Consolidated revenue	**5,896**	5,663	**2,981**	2,872	11,519

* Restatement due to discontinued operations, see Note 4

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009*	2010	2009*	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Profit or loss					
Operating profit or loss for reporting segments	**1,925**	1,741	**993**	876	3,216
Profit or loss for other categories	**5**	1	**4**	1	4
Cancellation of expenses from a segment classified as an associate (up to August 20, 2009 - discontinued operations)	**(66)**	(125)	**(7)**	(59)	(248)
Finance income (expenses), net	**(13)**	29	**(35)**	(1)	31
Share in the profits (losses) of equity-accounted investees	**(109)**	4	**(86)**	2	(34)
Consolidated profit before income tax	**1,742**	1,650	**869**	819	2,969

* Restatement due to discontinued operations, see Note 4

NOTE 12 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD. AND BEZEQ INTERNATIONAL LTD.

1. Pelephone Communications Ltd.

A. Statement of financial position

	June 30, 2010	June 30, 2009	December 31, 2009
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**1,983**	1,881	2,102
Non-current assets	**2,868**	2,887	2,888
	4,851	4,768	4,990
Current liabilities	**1,155**	1,236	1,519
Long term liabilities	**820**	972	921
Total liabilities	**1,975**	2,208	2,440
Equity	**2,876**	2,560	2,550
	4,851	4,768	4,990

B. Statement of income

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009*	2010	2009*	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue from services	**2,246**	2,069	**1,140**	1,050	4,256
Revenue from sale of terminal equipment	**576**	542	**289**	296	1,120
Revenue from services and sales	**2,822**	2,611	**1,429**	1,346	5,376
Cost of services and sales	**1,843**	1,717	**920**	899	3,592
Gross profit	**979**	894	**509**	447	1,784
Selling and marketing expenses	**236**	209	**117**	96	461
General and administrative expenses	**59**	62	**30**	30	133
	295	271	**147**	126	594
Operating profit	**684**	623	**362**	321	1,190
Finance expenses	**30**	39	**18**	11	100
Finance income	**(45)**	(45)	**(11)**	(6)	(90)
Net finance expenses (income)	**(15)**	(6)	**7**	5	10
Profit before income tax	**699**	629	**355**	316	1,180
Income tax	**173**	166	**88**	83	305
Profit for the period	**526**	463	**267**	233	875

NOTE 12 - CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD. AND BEZEQ INTERNATIONAL LTD. (CONTD.)

2. Bezeq International Ltd.

A. Statement of financial position

	June 30, 2010	June 30, 2009	December 31, 2009
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**621**	553	547
Non-current assets	**724**	540	559
	1,345	1,093	1,106
Current liabilities	**370**	278	367
Long term liabilities	**63**	34	37
Total liabilities	**433**	312	404
Equity	**912**	781	702
	1,345	1,093	1,106

B. Statement of income

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009*	2010	2009*	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue	**714**	651	**371**	327	1,318
Operating expenses	**430**	389	**220**	190	777
Gross profit	**284**	262	**151**	137	541
Selling, marketing and development expenses	**99**	84	**55**	43	175
General and administrative expenses	**56**	50	**28**	26	105
Other income, net – see Note 5	**(57)**	-	**(57)**	-	-
	98	134	**26**	69	280
Operating profit	**186**	128	**125**	68	261
Finance expenses	**6**	6	**3**	2	12
Finance income	**(4)**	(9)	**(2)**	(6)	(15)
Net finance expenses (income)	**2**	(3)	**1**	(4)	(3)
Share in earnings of equity-accounted associates	**3**	4	**2**	2	7
Profit before income tax	**187**	135	**126**	74	271
Income tax	**32**	35	**18**	18	71
Profit for the period	**155**	100	**108**	56	200
Attributable to:					
Owners of Bezeq International	**155**	100	**108**	56	200
Non-controlling interests	**-****	-	**-****	-	-
Profit for the period	**155**	100	**108**	56	200

** Less than NIS 500,000

NOTE 13 – MATERIAL EVENTS DURING THE REPORTING PERIOD AND SUBSEQUENT EVENTS

A. On March 25, 2010, the Company received notice of a strike, in accordance with the Settlement of Labor Disputes Law, 5719-1957, which was declared by the Histadrut Labor Union, as from April 11, 2010. According to the notice, the dispute relates to the Company's disregard of the demand of the workers' union to negotiate for a collective agreement to regulate the rights of employees following transfer of the controlling stake in the Company, before taking steps to transfer control. Consequently, negotiations between the Company's management and the workers' union are underway. It is noted that on May 2, 2010, the workers' union began limited sanctions.

B. In April-May 2010, the Company completed debt financing amounting to NIS 1.9 billion, through loans from banks in Israel. Of this amount, NIS 400 million is against early repayment of bank loans from March 2009. The loans were received for 80 months and are repayable in four equal annual payments of the principal between 2013 and 2016. The interest on the loans are payable twice a year. Loans of NIS 800 million are unlinked and bear fixed interest of 5.56%. The balance of the loans of NIS 1.1 billion are unlinked and bear variable interest at an average of prime minus 0.21%. To secure the repayment of the loans, the Company created a negative pledge in favor of the banks.

C. On June 24, 2010, the Company entered into agreements to sell its title to two properties in Tel Aviv. The total consideration for the Company's title to the two properties amounts to NIS 100 million. The capital gain for the Company from the two transactions is NIS 70 million, after tax. At the reporting date, all the conditions required for recognition of the gain have yet to be fulfilled, therefore these financial statements do not include the gain.

D. Subsequent to the reporting date, Bezeq International submitted specifications for a special tender offer to acquire 5% of Walla shares. If the tender offer is accepted, Bezeq International will hold 49.99% of the shares of Walla. In accordance with the terms of the tender offer, Bezeq International proposes purchasing Walla shares from the public at a price of NIS 6 per share, which is the price at which Bezeq International purchased Walla shares from Haaretz Newspaper Publishing Ltd. as set out in Note 5(B)(1) above. The total consideration for the shares in the tender offer amounts to NIS 13.6 million. Subject to completion of the special tender offer, Bezeq International intends to submit to the Antitrust Commissioner notice of a merger by way of transfer of the additional Walla shares to Bezeq International, such that subsequent to the transfer, Bezeq International will hold 71.8% of Walla shares.

In addition, shortly after transfer of Walla shares from the trustee to Bezeq International, the Company intends to purchase all the shares of Walla held by Bezeq International at the same price that Bezeq International acquired the shares from Haaretz.

DBS SATELLITE SERVICES (1998) LTD.

CONDENSED INTERIM FINANCIAL STATEMENTS
JUNE 30, 2010
(UNAUDITED)

Condensed Interim Financial Statements as at June 30, 2010

Contents

Somekh Chaikin
8 Hartum Street, Har Hotzvim
PO Box 212, Jerusalem 91001
Israel

Telephone 972 2 531 2000
Fax 972 2 531 2044
Internet www.kpmg.co.il

Review Report to the Shareholders of
DBS Satellite Services (1998) Ltd.

Introduction
We have reviewed the accompanying financial information of DBS Satellite Services (1998) Ltd ("the Company"), comprising of the condensed interim statement of financial position as of June 30, 2010 and the related condensed interim statements of income, comprehensive income, changes in equity and cash flows for the six 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.

Review scope
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 accepted accounting principles 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, 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, 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 above conclusion, we draw attention to Note 4 regarding the financial condition of the Company. As stated in the aforementioned Note, as of the date of financial position, the Company is in compliance with the financial covenants set out in the finance agreement, after receiving relief from the banks subsequent to the balance sheet date. The Company intends to apply to the banks for relief of the financial covenants with respect to the remainder of the year. In the opinion of management of the Company, the financing resources available to the Company will be sufficient for its operational requirements for the coming year, based on the cash flow forecast approved by the board of directors of the Company.

Additionally, we draw attention to Note 22B to the Company's annual financial statements as at December 31, 2009, regarding the class action filed against the Company in respect of disruptions to the Company's broadcasts. In accordance with the assessment of the Company's management, which is based on the opinion of its legal counsels, the Company has included an appropriate provision in its financial statements.

Somekh Chaikin
Certified Public Accountants

August 1, 2010

Condensed Interim Statements of Financial Position

	June 30 2010 (Unaudited) NIS thousands	June 30 2009 (Unaudited) NIS thousands	December 31 2009 (Audited) NIS thousands
Assets			
Short-term deposits	**-**	3,000	3,020
Trade receivables	**160,294**	154,759	160,152
Other receivables	**12,645**	6,999	8,177
Total current assets	**172,939**	164,758	171,349
Property, plant and equipment, net	**688,893**	676,059	682,473
Intangible assets, net	**75,830**	55,284	67,043
Broadcasting rights, net of rights exercised	**306,886**	316,914	284,766
Total non-current assets	**1,071,609**	1,048,257	1,034,282
Total assets	**1,244,548**	1,213,015	1,205,631

Condensed Interim Statements of Financial Position

	June 30 2010 (Unaudited) NIS thousands	June 30 2009 (Unaudited) NIS thousands	December 31 2009 (Audited) NIS thousands
Liabilities			
Borrowings from banks	**843,219**	188,918	283,698
Current maturities for debentures	**55,020**	-	54,812
Trade payables	**432,886**	434,467	406,389
Other payables	**210,760**	165,623	143,343
Provisions	**7,515**	9,579	8,079
Total current liabilities	**1,549,400**	798,587	896,321
Debentures	**628,441**	662,690	625,741
Loans from institutions	**192,109**	167,990	181,729
Loans from banks	**-**	728,907	607,036
Loans from shareholders	**2,118,101**	1,812,211	1,981,887
Other liabilities	**7,402**	20,943	14,288
Employee benefits	**7,461**	7,079	7,389
Total non-current liabilities	**2,953,514**	3,399,820	3,418,070
Total liabilities	**4,502,914**	4,198,407	4,314,391
Capital deficit			
Equity	**29**	29	29
Share premium	**85,557**	85,557	85,557
Option warrants	**48,219**	48,219	48,219
Capital reserves	**1,537,271**	1,537,271	1,537,271
Capital reserve for share-based payments	**8,376**	4,689	6,931
Accumulated deficit	**(4,937,818)**	(4,661,157)	(4,786,767)
Total capital deficit	**(3,258,366)**	(2,985,392)	(3,108,760)
Total liabilities and capital	**1,244,548**	1,213,015	1,205,631

David Efrati **(Authorized to sign as chairman of the board)***	**Ron Eilon** **CEO**	**Katriel Moriah** **CFO**

* See Note 8.

Date of approval of the financial statements: August 1, 2010

The accompanying notes are an integral part of the financial statements.

Condensed Interim Income Statements

	Six months ended		Three months ended		Year ended
	June 30	June 30	June 30	June 30	December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Revenue	**787,363**	759,880	**395,947**	376,098	1,530,435
Cost of revenue	**583,664**	514,069	**322,111**	255,615	1,042,101
Gross profit	**203,699**	245,811	**73,836**	120,483	488,334
Selling and marketing expenses	**71,978**	61,438	**33,042**	33,017	122,312
General and administrative expenses	**65,745**	59,369	**33,509**	28,412	117,805
	137,723	120,807	**66,551**	61,429	240,117
Operating profit	**65,976**	125,004	**7,285**	59,054	248,217
Finance expenses	**84,296**	102,489*	**60,650**	66,935*	177,900
Finance income	**(3,657)**	(12,463)*	**(3,601)**	(2,515)*	(8,347)
Shareholders' finance expenses	**136,214**	130,696	**92,928**	89,398	300,373
Finance expenses, net	**216,853**	220,722	**149,977**	153,818	469,926
Loss before income tax	**(150,877)**	(95,718)	**(142,692)**	(94,764)	(221,709)
Income tax	**174**	589	**92**	390	745
Loss for the period	**(151,051)**	(96,307)	**(142,784)**	(95,154)	(222,454)
Basic and diluted loss per share (NIS)	**5,053**	3,221	**4,776**	3,183	7,441

* Reclassified (see Note 2C)

The accompanying notes are an integral part of the financial statements.

Condensed Interim Statements of Comprehensive Income

	Six months ended		Three months ended		Year ended
	June 30	June 30	June 30	June 30	December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Loss for the period	**(151,051)**	(96,307)	**(142,784)**	(95,154)	(222,454)
Other items of comprehensive income:					
Actuarial gains from a defined benefit plan	**-**	-	**-**	-	537
Other comprehensive income for the period	**-**	-	**-**	-	537
Total comprehensive loss for the period	**(151,051)**	(96,307)	**(142,784)**	(95,154)	(221,917)

The accompanying notes are an integral part of the financial statements.

Condensed Interim Statements of Changes in Equity

	Share capital	Share premium	Share options	Capital reserve	Capital reserve for share-based payments	Accumulated deficit	Total
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Six months ended June 30, 2010 (unaudited)							
Balance at January 1, 2010 (audited)	**29**	**85,557**	**48,219**	**1,537,271**	**6,931**	**(4,786,767)**	**(3,108,760)**
Movement in the period (unaudited):							
Comprehensive loss for the period	**-**	**-**	**-**	**-**	**-**	**(151,051)**	**(151,051)**
Share-based payments	**-**	**-**	**-**	**-**	**1,445**	**-**	**1,445**
Balance at June 30, 2010 (unaudited)	**29**	**85,557**	**48,219**	**1,537,271**	**8,376**	**(4,937,818)**	**(3,258,366)**
Six months ended June 30, 2009 (unaudited)							
Balance at January 1, 2009 (audited)	29	85,557	48,219	1,537,271	1,636	(4,564,850)	(2,892,138)
Movement in the period (unaudited):							
Comprehensive loss for the period	-	-	-	-	-	(96,307)	(96,307)
Share-based payments	-	-	-	-	3,053	-	3,053
Balance at June 30, 2009 (unaudited)	29	85,557	48,219	1,537,271	4,689	(4,661,157)	(2,985,392)

The accompanying notes are an integral part of the financial statements.

Condensed Interim Statements of Changes in Equity

	Share capital	Share premium	Share options	Capital reserve	Capital reserve for share-based payments	Accumulated deficit	Total
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Three months ended June 30, 2010 (unaudited)							
Balance at April 1, 2010 (unaudited)	**29**	**85,557**	**48,219**	**1,537,271**	**7,650**	**(4,795,034)**	**(3,116,308)**
Movement in the period (unaudited):							
Comprehensive loss for the period	**-**	**-**	**-**	**-**	**-**	**(142,784)**	**(142,784)**
Share-based payments	**-**	**-**	**-**	**-**	**726**	**-**	**726**
Balance at June 30, 2010 (unaudited)	**29**	**85,557**	**48,219**	**1,537,271**	**8,376**	**(4,937,818)**	**(3,258,366)**
Three months ended June 30, 2009 (unaudited)							
Balance at April 1, 2009 (unaudited)	29	85,557	48,219	1,537,271	3,154	(4,566,003)	(2,891,773)
Movement in the period (unaudited):							
Comprehensive loss for the period						(95,154)	(95,154)
Share-based payments	-	-	-	-	1,535	-	1,535
Balance at June 30, 2009 (unaudited)	29	85,557	48,219	1,537,271	4,689	(4,661,157)	(2,985,392)

The accompanying notes are an integral part of the financial statements.

Condensed Interim Statements of Changes in Shareholders Equity (Contd.)

	Share capital	Share premium	Share options	Capital reserve	Capital reserve for share-based payments	Accumulated deficit	Total
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Year ended December 31, 2009 (audited)							
Balance at January 1, 2009 (audited)	29	85,557	48,219	1,537,271	1,636	(4,564,850)	(2,892,138)
Movement in 2009							
Comprehensive loss for the period (audited)	-	-	-	-	-	(221,917)	(221,917)
Share-based payments (audited)	-	-	-	-	5,295	-	5,295
Balance at December 31, 2009 (audited)	29	85,557	48,219	1,537,271	6,931	(4,786,767)	(3,108,760)

The accompanying notes are an integral part of the financial statements.

Condensed Interim Statements of Cash Flows

	Six months ended		Three months ended		Year ended
	June 30	June 30	June 30	June 30	December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Cash flows from operating activities					
Loss for the period	**(151,051)**	(96,307)	**(142,784)**	(95,154)	(222,454)
Adjustments					
Depreciation and amortization	**131,930**	112,107	**68,176**	55,562	234,203
Finance costs, net	**202,520**	200,581	**137,391**	135,386	455,232
Loss (profit) from the sale of property, plant and equipment	**(29)**	(192)	**(14)**	58	(236)
Share-based payments	**1,445**	3,053	**726**	1,535	5,295
Income tax expenses	**174**	589	**92**	390	745
Change in trade receivables	**(142)**	(1,883)	**(5,479)**	742	(7,277)
Change in other receivables	**(4,468)**	1,262	**(2,021)**	9,017	84
Change in trade payables	**12,330**	27,403	**(21,118)**	9,924	5,466
Change in other payables and provisions	**67,500**	6,775	**73,115**	11,518	(15,231)
Change in broadcasting rights, net of rights exercised	**(22,120)**	(63,582)	**6,836**	(29,334)	(31,433)
Change in employee benefits	**72**	2,028	**24**	968	(82)
Change in other liabilities	**(7,166)**	(6,869)	**(5,396)**	(6,846)	(13,524)
	230,995	184,965	**109,548**	93,766	410,788
Income tax paid	**(174)**	(904)	**(92)**	(390)	(1,060)
Net cash from operating activities	**230,821**	184,061	**109,456**	93,376	409,728
Cash flows for investment activities					
Repayment of short-term deposits	**3,020**	-	**89**	-	-
Proceeds from sale of property, plant and equipment	**437**	-	**253**	-	949
Purchase of property, plant and equipment	**(99,020)**	(101,850)	**(50,599)**	(49,758)	(214,368)
Acquisition of intangible assets	**(7,721)**	(5,187)	**(4,089)**	(2,798)	(9,262)
Payments for subscriber acquisition	**(17,528)**	(14,311)	**(8,547)**	(7,356)	(37,931)
Net cash used for investment activities	**(120,812)**	(121,348)	**(62,893)**	(59,912)	(260,612)

The accompanying notes are an integral part of the financial statements.

Condensed Interim Statements of Cash Flows (contd.)

	Six months ended		Three months ended		Year ended
	June 30	June 30	June 30	June 30	December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Cash flows for finance activities					
Bank loans received	**255,000**	-	**-**	-	-
Repayment of bank loans	**(283,105)**	-	**(37,187)**	-	-
Short-term credit from banks, net	**(17,804)**	40,623	**5,376**	(21,341)	13,532
Interest paid	**(64,100)**	(103,336)	**(14,752)**	(12,123)	(162,648)
Net cash used for finance activities	**(110,009)**	(62,713)	**(46,563)**	(33,464)	(149,116)
Change in cash and cash equivalents	**-**	-	**-**	-	-
Cash and cash equivalents for beginning of period	**-**	-	**-**	-	-
Cash and cash equivalents for end of period	**-**	-	**-**	-	-

The accompanying notes are an integral part of the financial statements.

NOTE 1 – REPORTING ENTITY

DBS Satellite Services (1998) Ltd. ("the Company") was incorporated in Israel on December 2, 1998. The Company's head office is at 6, Hayozma St., Kfar Saba, Israel.

In January 1999, the Company received a license from the Ministry of Communications to broadcast satellite television ("the license"). The Company's broadcasting license is valid until January 2017 and can be extended for a further six years under certain conditions. The Company's operations are subject, inter alia, to the Communications (Telecommunications and Broadcasts) Law 5742-1982 ("the Communications Law") and the regulations and rules promulgated thereunder and to the license terms.

Under the license of Bezeq The Israel Telecommunication Corporation Limited ("Bezeq"), Bezeq is required to maintain full structural separation between it and its subsidiaries, including the Company. In May and June 2010, the license of Bezeq and the Company were amended, permitting them, under certain circumstances, to market joint service packages.

In August 2009, the Supreme Court accepted the Antitrust Commissioner's appeal of the ruling of the Antitrust Tribunal approving the merger (as defined in the Restrictive Trade Practices Law, 5748-1988) between the Company and Bezeq by exercising the share options held by Bezeq in the Company, subject to certain conditions, and ruled against the merger.

NOTE 2 - BASIS OF PREPARATION

A. Statement of compliance

The condensed interim financial statements have been prepared in accordance with IAS 34, Interim Financial Reporting, and do not include all of the information required for full annual financial statements. They should be read in conjunction with the financial statements for the year ended December 31, 2009 ("the Annual Report"). Additionally, these statements were prepared in accordance with Chapter D of the Securities Regulations (Periodic and Immediate Reports), 5730-1970.

The condensed interim financial statements were approved by the board of directors of the Company on August 1, 2010.

B. Use of estimates and judgments

The preparation of the condensed financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

The judgment of the management when applying the Company's accounting policy and the principal assumptions used in assessments that involve uncertainty are consistent with those applied in the annual financial statements.

C. Reclassified

The comparative figures were reclassified, such that NIS 33.991 million and NIS 24.307 million were reclassified from finance income to finance expenses, for the six and three months ended June 30, 2009, respectively.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

The Company's accounting policy in these condensed interim statements is the same policy applied in the annual statements. The Company does not recalculate its actuarial commitments in each interim reporting period, unless there are significant changes in the benefit plans or fundamental changes in market conditions during the interim period, which affect the Company's commitments. As a result, actuarial gains or losses in the reporting period are not recognized.

A. Changes in the CPI and foreign currency exchange rate

Changes in the CPI and the dollar exchange rates in the accounting periods:

	US$ exchange rate	CPI
	%	%
Six months ended 30 June:		
2010	2.65	0.67
2009	3.08	2.14
Three months ended June 30		
2010	4.36	1.53
2009	(6.42)	2.28
Year ended December 31, 2009	(0.71)	3.91

NOTE 4 – FINANCIAL POSITION OF THE COMPANY

A. Since the beginning of its operations, the Company has accumulated substantial losses. The Company's loss in 2009 amounted to NIS 222 million and the loss in the six months ended June 30, 2010 amounted to NIS 151 million. As a result of these losses, the capital deficit and working capital deficit at June 30, 2010 amounted to NIS 3.258 billion and NIS 1.376 billion, respectively.

B. 1. In March 2010, an amendment to the Company's bank finance agreement was signed and came into effect ("the amendment agreement"). Under the amendment agreement, another Israeli bank ("the additional bank") joined the current syndicate of banks ("the present banks"). The additional bank provided the Company with its proportionate share in the Company's current credit line and extended a long-term loan of NIS 255 million to the Company, most of which was used for its addition (in its proportionate share) to the Company's long-term loans as well as repayment and early repayment of the Company's debts to the present banks. The balance of NIS 46 million will be used for the Company's ongoing needs.

Under the amendment agreement, a floating lien was created in favor of the additional bank, similar to the floating liens in favor of the present banks. The additional bank also became party to the fixed lien in favor of the present banks. The shareholders of the Company signed the amendments to the bonds, mortgage deeds and letter of guarantee, as the case may be, that they had previously signed in favor of the present banks, in respect of the addition of the additional bank.

Under the amendment agreement, the term of the bank loan repayment (the long-term loans as well as the credit line) was extended to the end of 2015, after receiving the consent of the banks for repayment of the loans provided by institutional entities at the repayment date (December 31, 2013).

Under the amendment agreement, the financial covenants set out in the finance agreement were replaced by the following new covenants, which apply up to 2015 and are compatible with the Company's business plan:

A. Minimum solvency
B. Minimum EBITDA
C. Maximum and minimum supplier credit

The values for compliance with the financial covenants vary and are measured each quarter. Under the terms of the finance agreement, the banks are entitled to call for early repayment of the loans in the event of failure to comply with the covenants.

NOTE 4 – FINANCIAL POSITION OF THE COMPANY (CONTD.)

B. (contd.)

2. The Company is in compliance with the financial covenants under the finance agreement of June 30, 2010, after receiving relief from the banks for August 2010 in respect of the purpose of one of the covenants, which was required in view of the material provision made by the Company as set out in section 7(C). As this relief was given subsequent to the reporting date, the bank loan of NIS 816.52 million is stated as a short-term liability. As the covenants are incremental on an annual basis, the management of the Company believes that the Company will require additional relief in respect of the purposes of the financial covenants for September 30, 2010 and December 31, 2010 and the Company is taking steps to achieve this from the banks.

3. In the opinion of the management of the Company, the sources of financing available to it will be sufficient for the Company's operating requirements for the forthcoming year, based on the cash flow forecast approved by the Company's board of directors. If additional resources are required to meet its operational requirements during the year, the Company will adapt its operations to preclude the need for additional resources beyond those available to it.

NOTE 5 – CONTINGENT LIABILITIES

Lawsuits

A. Employee claims

During the normal course of business, employees and former employees filed group and individual claims against the Company. Most of the claims are for alleged non-payment of salary items and delay in wages. At June 30, 2010, the total amount of these claims amounted to NIS 1.688 million. In the opinion of the management of the Company, which is based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions amounting to NIS 736,000, where provisions are required to cover the exposure resulting from such claims.

B. Customer claims

During the normal course of business, the Company's customers filed claims against the Company. These are mainly applications for certification as class actions (and the ensuing claims) concerning alleged unlawful collection of payment and impairment of the service provided by the Company. At June 30, 2010, the total amount of these claims amounted to NIS 275.557 billion. In the opinion of the management of the Company, which is based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions amounting to NIS 6.554 million, where provisions are required to cover the exposure resulting from such claims

Of these claims, there are claims amounting to NIS 118.259 million, which cannot yet be estimated.
The aforementioned claims include the following:

In March 2010 a claim and application for certification as a class action were filed at the Tel Aviv District Court against HOT Communication Systems Ltd. (HOT) and the Company, alleging that the Company interrupted broadcasts during the second and third seasons of the Big Brother program on channel 20, despite its commitment to round the clock broadcasts. The applicant further claims that the Company undertook to broadcast the channel directly and live, however it breached this commitment by broadcasting a recording. According to the applicant, by doing so, the Company breached the Contracts Law and the Torts Ordinance (New Version), 5728-1968. In the application for certification, the applicant defined the group he seeks to represent ("the group") as any person who purchased the Big Brother channel from HOT and from the Company, "which is a pay-per-view channel of the Big Brother reality program, in the second and third season of the program broadcasts". The applicant estimates the damage caused to the group members due to the acts or omissions of HOT and the Company at NIS 19.240 million.

NOTE 5 – CONTINGENT LIABILITIES (CONTD.)

Lawsuits (contd.)

B. Customer claims (contd.)

The court allowed the applicant, who is not a subscriber of the Company, to add another class action applicant to his application, who acquired the channel from the Company in the third season of Big Brother. On March 25, 2010, the applicant filed an amended application for certification as a class action ("the amended application"), together with an amended statement of claim. At the reporting date, the Company has yet to file a response to the amended application, which is expected to be filed by August 9, 2010.

In June 2010, a claim and application for certification as a class action was filed at the district court in Tel Aviv against the Company ("the claim" and "the application for certification", respectively), alleging that when the Company refunded monies that were over-collected, these monies were refunded at their nominal values, without interest and linkage, contrary to the agreements and the law. The plaintiff alleges that by doing so, the Company unjustly enriched itself at the expense of its customers, was negligent, caused damages to customers in the amount of the interest and linkage differences and allegedly breached its duty to act in good faith and its fiduciary duty towards them.
The plaintiff defined the group he seeks to represent as "any person or other legal entity that was overcharged by the respondent, whether in contravention of the law or contrary to the agreement, and that received a refund in the amount of the principal only, without linkage differences and interest by law" ("the group"). The plaintiff estimated the size of the group at 2.8 million customers, and the damage caused to the group members as NIS 44.680 million. The date for submitting the Company's response to the application for certification is September 1, 2010.

See also Note 7 A.

C. Supplier and communication provider claims

During the normal course of business, suppliers of goods and/or services to the Company filed claims against the Company. The main claim was filed for alleged damage to a supplier as a result of the Company's negligence. At June 30, 2010, these claims amounted to NIS 51.822 million. In the opinion of the management of the Company, based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions amounting to NIS 224,000, where provisions are required to cover the exposure resulting from such claims.

NOTE 6 – MATERIAL EVENTS IN THE REPORTING PERIOD

A. In April 2010, in the framework of the approvals of the Ministry of Communications for the Company's request, under its licenses, to approve the transfer of control (directly or indirectly) in respect of the acquisition of control in the Company and transfer of the holdings of Eurocom DBS Ltd. in the Company to a trustee, the Ministry of Communications decided that the following main terms would apply to the Company:

1. Any change, direct or indirect, in the trustee's holding of the controlling stake in the Company is subject to the prior written approval of the Minister of Communications, after having consulted with the council.
2. The trustee will not act under the instructions received from any entity that relates, directly or indirectly, to the regulations of the Ministry of Communications, without the approval of the Ministry of Communications.
3. The transaction between the Company and the Eurocom Group relating to satellite terminal equipment will be considered, as well as the approval procedure in the Company's organs, as an extraordinary transaction, as defined in section 270(4) of the Companies Law and as such, the transaction is subject to the approval of the Company's bodies under section 275 of the Companies Law.
4. The discussions of the Company's board of directors meetings on these transactions will be recorded in full and detailed minutes, signed by the chairman of the meeting and submitted to the director general of the Ministry of Communications for review.

NOTE 6 – MATERIAL EVENTS IN THE REPORTING PERIOD (CONTD.)

B. In April 2010, S&P Maalot rating company announced that it was raising the rating of the Company's Debentures (Series A) from ilBBB- to ilBBB, inter alia, due to its assessment of the material improvement in the Company's liquidity following the new loan received from the additional bank and the continuing improvement in the Company's debt coverage ratio, ability to generate cash flows and liquidity since the last rating. The rating company also placed the Company's rating on the Credit Watch list with positive outlook, noting that it plans to complete the assessment of possible raising of the rating within three months, following a more comprehensive evaluation of the Company's business plan and the implications on its financial profile.

C. In June 2010, S&P Maalot rating company announced that it was raising the rating of the Company's Debentures (Series A) from ilBBB- to ilBBB+, inter alia, due to its assessment of the material improvement in the Company's liquidity following the new loan received from the additional bank and the continuing improvement in the Company's debt coverage ratio, ability to generate cash flows and liquidity since the last rating. The rating company also placed the Company's rating on the Credit Watch list with positive outlook.

D. The Company and Bezeq The Israel Telecommunication Corporation Ltd. ("Bezeq") formulated an arrangement for the Company's debt to Bezeq for communication services, amounting to NIS 31.5 million at July 31, 2009 (reflecting a compromise between the Company's position and that of Bezeq). Under the arrangement, the Company will repay the debt to Bezeq in 36 equal monthly payments of NIS 875,000 each plus VAT and interest at prime + 1.5% plus VAT for the interest. The debt arrangement was approved by the general meeting of the Company on November 1, 2009 and by the general meeting of Bezeq of Bezeq on May 20, 2010. The agreement has yet to be signed.

NOTE 7 – MATERIAL EVENTS SUBSEQUENT TO THE REPORTING DATE

A. In July 2010, a claim was filed against the Company in the Tel Aviv District Court together with an application for certification as a class action. According to the plaintiff, the Company is in breach of the consumer protection regulations ("the regulations") in that the text size and line spacing in the agreements with its customers does not comply with the provisions of the regulations. The plaintiff claims that she has grounds for a claim for breach of statutory duty and grounds for a claim under the consumer protection regulations for misleading information and exploitation of distress.
The plaintiff defined the group she seeks to represent as "any subscriber with agreements that do not comply with the provisions of the consumer protection regulations (print size in a standard contract) in respect of the small print and line spacing ("the group"). The plaintiff estimates that the group includes approximately one million customers.
The amount of the personal claim is NIS 50 and the amount of the total claim is estimated at NIS 50 million. The plaintiff is also claiming for declaratory relief to determine that these amounts do not comply with the consumer protection regulations and to issue a mandatory injunction that instructs the Company to amend them and send them to its customers.

B. In March 2010, the Knesset passed the first reading of a bill to exempt designated channels from transfer payment to the cable company and the Company. In July 2010, the Knesset passed the second and third reading of the bill.

NOTE 7 – MATERIAL EVENTS SUBSEQUENT TO THE REPORTING DATE (CONTD.)

C. Pursuant to the immediate report issued by Hot Communication Services ("the cable company"), in July 2010, a ruling in the arbitration between the cable company and the composers, lyricists, poets and music publishers society (ACUM), accepted in principle ACUM's formula for calculating annual royalties for broadcasting music to which ACUM has rights, with the exception of certain changes, and determined that this formula would also apply to the difference in royalties as from 2003 onwards, to be calculated by the parties in a settlement. The cable company noted that it intends to appeal the arbitration ruling. Since the Company does not have access to the arbitration ruling and the other arbitration documents, the model that was adopted and the reasons for the arbitration ruling are unknown to the Company. However, pursuant to the agreements between the Company and ACUM, the royalties paid to ACUM as from 2003 are liable to be adjusted, inter alia, subject to the settlement between the cable company and ACUM, and according to ACUM, also subject to the ruling of the arbitrator. Therefore, the management of the Company believes that following the arbitration ruling, the Company will be required to pay material amounts retrospectively. In view of the aforesaid, the Company adjusted the estimated amount of royalties as from 2003. The adjustment was based on the formula for calculating royalties furnished by ACUM shortly after the arbitration ruling, with adjustments according to the estimation of the management of the Company. On this basis, the Company recorded a significant provision in its financial statements as at June 30, 2010.

NOTE 8 – APPOINTMENT OF THE CHAIRMAN OF THE BOARD FOR THE APPROVAL MEETING

At the date of approval of the financial statements, the Company's board of directors does not have an incumbent chairman. Consequently, the Company's board of directors authorized David Efrati, a director in the Company, to serve as chairman of the board of directors' meeting convened to approve the financial statements and to sign the Company's financial statements as at June 30, 2010.

BEZEQ THE ISRAEL TELECOMMUNICATION CORP. LIMITED

SEPARATE CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION
JUNE 30, 2010
(UNAUDITED)

Separate condensed interim financial information as at June 30, 2010 (unaudited)

Contents

Somekh Chaikin
8 Hartum Street, Har Hotzvim
PO Box 212, Jerusalem 91001
Israel

Telephone 972 2 531 2000
Fax 972 2 531 2044
Internet www.kpmg.co.il

Special review report to the Shareholders of "Bezeq" The Israel Telecommunication Corp. Limited, 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 Corp. Limited (hereinafter – the Company), as at June 30, 2010 and for the six 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.

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, 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 above conclusion, we draw attention to the claims made against the Company of which the exposure cannot yet be assessed or calculated, as described in Note 4.

Somekh Chaikin
Certified Public Accountants (Isr.)

August 2, 2010

Condensed interim information on financial position

	June 30, 2010	June 30, 2009	December 31, 2009
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Assets			
Cash and cash equivalents	**6**	268	360
Investments, including derivatives	**191**	12	10
Trade receivables	**865**	867	845
Receivables	**134**	89	555
Inventory	**9**	15	9
Current tax assets	**-**	2	-
Assets held for sale	**38**	64	40
Total current assets	**1,243**	1,317	1,819
Investments, including derivatives	**96**	106	100
Trade and other receivables	**96**	60	102
Property, plant and equipment	**3,888**	3,762*	3,771*
Intangible assets	**221**	147	193
Investments in investees	**6,828**	5,049	6,566
Deferred tax assets	**327**	448	383
Total non-current assets	**11,456**	9,572	11,115
Total assets	**12,699**	10,889	12,934

	June 30, 2010	June 30, 2009	December 31, 2009
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Liabilities			
Debentures, loans and borrowings	**1,163**	662	685
Trade payables	**228**	298	263
Other payables, including derivatives	**433**	421	537
Loans from subsidiaries	**201**	-	250
Current tax liabilities	**80**	-	86
Deferred income	**18**	21	19
Provisions (Note 4)	**270**	262	279
Employee benefits	**414**	301	469
Total current liabilities	**2,807**	1,965	2,588
Debentures	**2,340**	3,098	3,166
Bank loans	**1,900**	400	383
Employee benefits	**248**	222	247
Deferred income and others	**4**	6	6
Total non-current liabilities	**4,492**	3,726	3,802
Total liabilities	**7,299**	5,691	6,390
Equity			
Share capital	**6,203**	6,172	6,187
Share premium	**345**	203	275
Reserves	**538**	631	595
Retained earnings (deficit)	**(1,686)**	(1,808)	(513)
Total equity	**5,400**	5,198	6,544
Total equity and liabilities	**12,699**	10,889	12,934

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

Date of approval of the financial statements: August 2, 2010

* Retrospective application by restatement, see Note 3 to the condensed consolidated interim financial statements as at June 30, 2010

The accompanying notes are an integral part of the condensed interim financial information.

Condensed interim information on income

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenue (Note 2)	**2,611**	2,644	**1,307**	1,318	5,303
Costs and expenses					
Depreciation and amortization	**341**	416	**171**	205	794
Salaries	**527**	542	**250**	264	1,094
General and operating expenses (Note 3)	**788**	831	**396**	411	1,690
Other operating expenses (income), net	**(38)**	(16)	**(13)**	4	202
	1,618	1,773	**804**	884	3,780
Operating profit	**993**	871	**503**	434	1,523
Finance income					
Finance income	**78**	145	**50**	87	310
Finance expenses	**(106)**	(120)	**(79)**	(83)	(295)
Finance income (expenses), net	**(28)**	25	**(29)**	4	15
Profit after finance income, net	**965**	896	**474**	438	1,538
Share in profits of investees	**571**	497	**289**	225	958
Profit before income tax	**1,536**	1,393	**763**	663	2,496
Income tax	**256**	244	**125**	122	431
Profit after income tax	**1,280**	1,149	**638**	541	2,065
Profit from deconsolidation of a subsidiary	**-**	-	-	-	1,538
Profit for the period	**1,280**	1,149	**638**	541	3,603

The accompanying notes are an integral part of the condensed interim financial information.

Condensed interim information on comprehensive income

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Profit for the period	**1,280**	1,149	**638**	541	3,603
Other comprehensive income (loss) for the period, net of tax	**-**	1	**1**	(2)	(11)
Total comprehensive income for the period	**1,280**	1,150	**639**	539	3,592

The accompanying notes are an integral part of the condensed interim financial information.

Condensed interim information on cash flows

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flows from operating activities					
Profit for the year	**1,280**	1,149	**638**	541	3,603
Adjustments:					
Depreciation	**304**	363*	**153**	183*	715*
Amortization of intangible assets	**37**	53	**18**	22	79
Profit from deconsolidation of a subsidiary	**-**	-	**-**	-	(1,538)
Share in profits of equity-accounted investees	**(571)**	(497)	**(289)**	(225)	(958)
Finance expenses, net	**12**	(22)	**16**	(1)	(44)
Capital gain, net	**(29)**	(20)	**(2)**	-	(64)
Share-based payments	**6**	13	**2**	6	25
Income tax expenses	**256**	244	**125**	122	431
Change in inventory	**-**	(5)	**2**	(5)	1
Change in trade receivables	**(12)**	20	**2**	(12)	(20)
Change in other receivables	**(23)**	9	**29**	67	46
Change in other payables	**(38)**	(29)	**(37)**	(140)	20
Change in trade payables	**(37)**	18	**5**	(44)	(19)
Change in provisions	**(9)**	9	**(5)**	7	25
Change in employee benefits	**(55)**	(73)	**(28)**	(16)	118
Net cash from (used for) operating activities for transactions with investees	**(6)**	(13)	**3**	(7)	2
Income tax paid, net	**(199)**	(176)	**(109)**	(90)	(202)
Net cash flows from operating activities	**916**	1,043	**523**	408	2,220
Cash flows from investment activities					
Investment in intangible assets	**(65)**	(61)	**(32)**	(39)	(133)
Proceeds from sale of property, plant and equipment	**41**	58	**26**	9	86
Change in current investments, net	**-**	6	**-**	-	6
Purchase of property, plant and equipment	**(420)**	(368)	**(215)**	(152)	(720)
Proceeds from disposal of investments and long-term loans	**4**	40	**3**	35	46
Interest received	**6**	10	**6**	7	25
Net cash flows from investment for transactions with investees	**634**	430	**214**	30	578
Net cash flows from (used for) investment activities	**200**	115	**2**	(110)	(112)

* Retrospective application by restatement, see Note 3 to the condensed consolidated interim financial statements as at June 30, 2010

The accompanying notes are an integral part of the condensed interim financial information.

Condensed Interim Statements of Cash Flows (Contd.)

	Six months ended June 30		Three months ended June 30		Year ended December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flow from finance activities					
Bank loans received	**1,900**	400	**1,900**	-	400
Repayment of bank loans	**(400)**	-	**(400)**	-	-
Short-term borrowing, net	**226**	-	**226**	-	-
Repayment of debentures	**(558)**	(547)	**(416)**	(403)	(556)
Dividend paid	**(2,453)**	(792)	**(2,453)**	(792)	(1,941)
Interest paid	**(153)**	(152)	**(142)**	(152)	(167)
Proceeds for derivatives, net	**-**	11	**-**	21	44
Proceeds from exercise of options into shares	**18**	97	**3**	61	129
Net cash from (used for) finance activities for transactions with investees	**(50)**	-	**200**	-	250
Net cash from (used for) finance activities	**(1,470)**	(983)	**(1,082)**	(1,265)	(1,841)
Increase (decrease) in cash flow and cash equivalents	**(354)**	175	**(557)**	(967)	267
Cash and cash equivalents at beginning of period	**360**	93	**563**	1,235	93
Cash and cash equivalents at end of period	**6**	268	**6**	268	360

The accompanying notes are an integral part of the condensed interim financial information.

NOTE 1 – METHOD FOR PREPARING THE FINANCIAL INFORMATION

A. Definitions

“The Company”: Bezeq The Israel Telecommunication Corporation Ltd.

“Associate”, "the Group", “Investee”, “Interested Party”: as defined in the consolidated financial statements of the Company for 2009.

B. Main points of the method for preparing of the financial information

The separate interim financial information is stated in accordance with Article 38(D) of the Securities Regulations (Periodic and Interim Reports), 5730-1970 and does not include the information required under the provisions of Article 9(C) and the Tenth Addendum of the Securities Regulations (Periodic and Interim Reports), 5730-1970 in respect of separate financial information of the corporation. The report should be read together with the separate financial information as at December 31, 2009 and for the year then ended and together with the condensed consolidated interim statements as at June 30, 2010 (“the consolidated reports”).

NOTE 2 – REVENUE

	Six months ended		Three months ended		Year ended
	June 30		June 30		December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Telephony	**1,580**	1,667	**795**	828	3,333
Internet	**471**	417	**235**	210	863
Transmission and data communications	**444**	420	**221**	213	851
Other services	**116**	140	**56**	67	256
	2,611	2,644	**1,307**	1,318	5,303

NOTE 3 – OPERATING AND GENERAL EXPENSES

	Six months ended		Three months ended		Year ended
	June 30		June 30		December 31
	2010	2009	2010	2009	2009
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cellular telephone expenses	**401**	410	**211**	206	823
General expenses	**116**	110	**56**	51	266
Materials and spare parts	**39**	41	**16**	19	80
Building maintenance	**119**	132	**58**	68	278
Services and maintenance by sub-contractors	**39**	48	**18**	23	96
Vehicle maintenance expenses	**48**	47	**25**	22	96
Royalties to the State of Israel	**16**	25	**8**	13	18
Collection fees and sundry	**10**	18	**4**	9	33
	788	831	**396**	411	1,690

NOTE 4 – CONTINGENT LIABILITIES

During the normal course of business, legal claims were filed or are pending against the Company ("hereinafter in this section: "claims").

The financial statements of the Company include provisions of NIS 270 million for the claims.
The additional exposure beyond these provisions for the claims amounts to approximately NIS 3 billion.
In addition, subsequent to the reporting date, another two claims were filed against the company, together with application for certification as class actions, which at this stage cannot be assessed. The plaintiff estimates the first claim at "tens of millions of shekels" and the second claim is estimated at NIS 250 million.
There are other claims for which the Company has additional exposure beyond the aforesaid, as the exact amount of the claim is not stated in the claim.

For further information about contingent liabilities, see Note 6 to the consolidated financial statements - Contingent Liabilities.

NOTE 5 - SUBSTANTIAL AGREEMENTS AND TRANSACTIONS WITH INVESTEES

A. Loans

1) On March 21, 2010, the Company provided a loan of NIS 45 million to Bezeq International Ltd. ("Bezeq International"), subject to the terms of the framework loan agreement between the companies. The loan, which bears annual interest of 4% and is linked to the CPI, will be repaid in four equal monthly payments (principal and interest), commencing on June 1, 2010.

2) On May 31, 2010, the Company took out a loan of NIS 90 million from Pelephone Communications Ltd. ("Pelephone"), subject to the terms of the framework loan agreement between the companies. The loan, which bears annual interest of 4% and is linked to the CPI, will be repaid on January 6, 2011.
In addition, on June 15, 2010, Pelephone provided the Company with another loan of NIS 110 million. The loan, which is linked to the CPI and bears annual interest of 4%, was repayable on July 6, 2010. Pursuant to the aforesaid terms, the loan was repaid on July 6, 2010.

3) In respect of the loan provided by the Company to Bezeq Online Ltd. ("Bezeq Online"), after repayment of NIS 2.5 million on June 30, 2010, the balance of the loan amounted to NIS 8 million.

B. Dividends

On May 2, 2010, the Company received a dividend of NIS 200 million from Pelephone.

NOTE 6 – SUBSEQUENT EVENTS

A. On August 1, 2010, the board of directors of Pelephone approved the distribution of a dividend amounting to NIS 210 million.

B. On August 1, 2010, the board of directors of Bezeq International approved the distribution of a dividend of NIS 196 million (this distribution is subject to the acquisition of Walla shares by Bezeq International and their sale to the Company as set out in Note 13 (D) to the consolidated financial statements).