

November 29, 2017

“Bezeq” - The Israel Telecommunication Corp. Ltd.

Quarterly report for period ended September 30, 2017

Update to Chapter A (Description of Company Operations) of the Periodic Report for 2016

Directors' Report on the State of the Company's Affairs for the period ended September 30, 2017

Interim Financial Statements as at September 30, 2017



Update to Chapter A (Description of Company Operations) of the Periodic Report for 2016



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

**Update to Chapter A (Description of Company Operations)¹
to the Periodic Report for 2016 ("Periodic Report")
of "Bezeq" - The Israel Telecommunication Corporation Ltd. ("the Company")**

1. General development of the Group's business

Section 1.1 - Group activities and business development (Merger of the Company and DBS) and on an event that deviates from the Company's business

On June 20, 2017, the Israel Securities Authority (ISA) launched a public investigation ("the Investigation") in which, among other things, the offices of the Company and DBS were searched and documents were seized. As the ISA informed the Company, the investigation addresses suspicions of crimes under the Securities Law and Penal Code in respect of transactions relating to the controlling shareholder. As far as the Company is aware, the investigation relates to the purchase of DBS shares by the Company from Eurocom D.B.S. Ltd., a company controlled by the Company's controlling shareholder. The investigation was later expanded to include transactions to provide satellite communications services between DBS and Spacecom Communications Ltd. ("Spacecom"), a company controlled by the Company's controlling shareholder, and with respect to dealings between the Ministry of Communications and the Company.

As part of the investigation, the Chairman of the Company's Board of Directors, CEO of the Company, the CEO and CFO of DBS were questioned, and as far as the Company is aware also other senior officers and functionaries in the Group ("Those Under Investigation").

In the course of the Investigation, some of Those Under Investigation were released with certain restrictions, which include partial restrictions on contact with employees and senior officers of Bezeq Group and Eurocom as well as other restrictions. As far as the Company is aware, on November 1, 2017, the restrictions imposed on Those Under Investigation, as noted above, expired, including the restrictions imposed on the Chairman of the Company's Board of Directors and CEO of the Company, as detailed below.

Notably, within the framework of the restrictions that were imposed and cancelled, restrictions were imposed on the Chairman of the Board of Directors which include, *inter alia*, dealing with matters relating to the Ministry of Communications and/or DBS. He is also barred from being in contact with members of the Board of Directors, senior officers and employees of the Group companies. Matters relating to Bezeq Group companies (excluding DBS) may only be handled by the CEOs of those companies (excluding the CEO of the Company and of DBS) and/or through the director David Granot, who was appointed Acting Chairman of the Board of Directors, and this pursuant to agreements reached between the Chairman of the Board of the Company and the ISA. Furthermore, restrictions were imposed on the CEO of the Company which include, *inter alia*, dealing with the Company's regulatory affairs exclusively with and through the Acting Chairman of the Board, engaging in transactions with the controlling shareholders and activity with the controlling shareholder, handling the affairs of DBS (except for marketing matters relating to DBS, with and through the Company's VP Marketing). She was also barred from making direct or indirect contact with members of the Company's Board of Directors (excluding the Acting Chairman of the Board).

At a meeting of the Company's Board of Directors held on November 15, 2017, the Board accepted Mr. Shaul Elovitch's proposal whereby until further notice he does not wish to resume the position of Chairman of the Board of Directors of Bezeq and Mr. David Granot will continue to serve as Acting Chairman of the Board of Directors. Mr. Shaul Elovitch resumed his position as Chairman of the Board of Directors of the Group's subsidiaries, with the exception of DBS.

On November 6, 2017, the Israel Securities Authority issued a press release regarding the conclusion of the Investigation and the transfer of the investigation file to the Tel Aviv District Attorney's Office (Taxation and Economics). According to the notice, the ISA has concluded that there is *prima facie* evidence establishing the involvement of the main suspects in the case on offenses of: (1) fraudulently receiving funds in connection with the entitlement of the Company's controlling shareholder to payment

¹ The update is further to Regulation 39A of the Securities Regulations (Periodic and Immediate Reports), 1970, and includes material changes or innovations that have occurred in the corporation in any matter which must be described in the periodic report. The update relates to the Company's periodic report for the year 2016 and refers to the section numbers in Chapter A (Description of Company Operations) in the said periodic report.

of NIS 170 million as part of the transaction for the purchase of DBS shares from the controlling shareholder of the Company by the Company, payment that was contingent upon DBS meetings certain targets; (2) leaking material from the independent committee of the Company's Board of Directors that was required to examine interested party transactions (the transaction for the acquisition of DBS shares by the Company and the transaction between DBS and Spacecom for the purchase of satellite segments for DBS) to the Company's controlling shareholder and his associates; and (3) promoting the Company's interests in the Ministry of Communications, in violation of the Penal Code and Securities Law. The notice also relates to the transfer of the investigation file to the District Attorney's Office and that the District Attorney's Office is authorized to decide on the continued handling of the case. Notably, in this context, on November 20, 2017, the Company and DBS received a letter informing them of the suspicions against them, whereby the investigation file relating to the investigation of the Company and DBS had been submitted to the District Attorney's Office for review.

Following the opening of the Investigation, in June-August 2017, several legal proceedings were initiated against the Company, its senior officers and companies in the group that hold the controlling interest in the Company, including motions to certify a class action and to disclose documents prior to the filing of a motion for certification of a derivative claim. For information about these proceedings, see the update to Section 2.18.

For information on this matter, see also immediate reports of the Company dated June 20, 22 and 23, 2017, and July 11, 14 and 23, 2017, September 18, 2017 and November 6, 2017, included here by way of reference.

On the Second Contingent Payment in accordance with the conditions of the Purchase Transaction

The Company revised the estimate of the Second Contingent Payment in view of its assessment that it is now unlikely that the merger of DBS with the Company will take place in 2017, and taking into account the revised forecast for the free cash flow of DBS for 2017. According to the agreement between the parties, and insofar as the final amount² of the contingent payment is deducted from the advance amounts that the Company paid Eurocom D.B.S. in respect of that payment (in the amount of NIS 119 million), Eurocom D.B.S. will have to return the difference to the Company. On this matter, see also Note 4.2 to the Company's consolidated financial statements for the period ended September 30, 2017.

In view of the updated estimate of the Second Contingent Payment, and in light of reports that discussions are underway between companies in the Eurocom Group and their creditors, in August 2017 the Company wrote to Eurocom D.B.S. (with a copy to the banks, who to the best of its knowledge are the principal creditors of Eurocom Group) asking for information about the ability of Eurocom D.B.S. to make the payment to the Company and with a request to be party to the discussions with Eurocom Group's creditors, and to any move that involves a change in the collaterals or assets of Eurocom Group. In response, Eurocom D.B.S. replied to the Company that discussions are in fact underway with bank creditors in an effort to settle Eurocom Group's debt package by consent, that it is working and intends to continue to work in full transparency on this matter, that as the discussions progress it will certainly wish to discuss the subject with the Company and that it will update the Company fully with the details of the evolving discussions, that are relevant to the Company, and in a manner that will provide the Company with a full picture. On November 24, 2017, the Company received a report from the indirect controlling shareholder in the Company, Eurocom Communications Ltd. ("Eurocom"), in which Eurocom announced that it has received written notification from banks ("the Bank") whereby Eurocom is required to repay a significant debt (including guaranteed debts) within a specified time frame - while the Bank reserves all its rights if the said debt is not paid. Eurocom advised that at the time of sending the report, it is negotiating intensively with the banking system to arrange and schedule its outstanding loans, and it intends to continue to expedite the discussions in an effort to reach agreement within a short time, with a real possibility, in its opinion, of achieving an arrangement. Subsequently, the Company discussed the subject again with the Eurocom representatives and it is monitoring developments on the subject.

Section 1.4 - Dividend distribution

For information about a dividend distribution in the amount of NIS 578 million in respect of profits in the second half of 2016 that was approved by a general meeting of the Company's shareholders on May 9, 2017, and distributed on May 29, 2017, and in connection with a dividend distribution in the amount of NIS 708 million in respect of profits in the first half of 2017 that was approved by a general meeting of

² The final settlement of accounts is expected to be soon after the signing of the Company's financial statements for 2017 (or at the date of the merger, whichever is earlier).

Update to Chapter A (Description of Company Operations) of the Periodic Report for 2016

the Company's shareholders on September 18, 2017 and distributed on October 16, 2017, see Note 10 to the Company's Financial Statements for the period ended September 30, 2017.

The outstanding, distributable profits at the report date amounted to NIS 322 million (surpluses accumulated over the last two years, after subtracting previous distributions).

Section 1.5.4 - Main results and operational data³
A. Bezeq Fixed Line (the Company's operations as a domestic carrier)

	Q3 2017	Q2 2017	Q1 2017	Q4 2016	Q3 2016	Q2 2016	Q1 2016
Revenues (NIS million)	1,061	1,058	1,078	1,082	1,089	1,100	1,112
Operating profit (NIS million)	492	496	513	481	519	540	536
Depreciation and amortization (NIS million)	186	177	180	161	188	185	183
EBITDA (Earnings before income taxes, depreciation and amortization) (NIS million) ⁽¹⁾	678	673	693	642	707	725	719
Net profit (NIS million)	276	317	319	235	343	326	328
Cash flow from operating activities (NIS million)	573	465	600	482	526	517	539
Payments for investments in property, plant & equipment, intangible assets and other investments (NIS million)	170	219	210	205	207	227	195
Proceeds from the sale of property, plant & equipment and intangible assets (NIS million)	46	16	10	15	22	54	41
Free cash flow (NIS million) ⁽²⁾	449	262	400	292	341	344	385
Number of active subscriber lines at the end of the period (in thousands) ⁽³⁾	2,061	2,077	2,100	2,119	2,137	2,151	2,167
Average monthly revenue per line (NIS) (ARPL) ⁽⁴⁾	56	55	57	56	58	58	59
Number of outgoing minutes (in millions)	1,134	1,100	1,180	1,139	1,297	1,257	1,316
Number of incoming minutes (in millions)	1,266	1,220	1,281	1,252	1,383	1,314	1,348
Number of active subscriber lines at the end of the period (in thousands) ⁽⁷⁾	1,608	1,593	1,580	1,558	1,539	1,521	1,503
Of which the number of active subscriber lines at the end of the period - retail (in thousands) ⁽⁷⁾	484	444	414	377	347	323	290
Average monthly revenue per Internet subscriber (NIS) - retail	91	91	91	90	89	90	91
Average bundle speed per Internet subscriber - retail (Mbps) ⁽⁵⁾	49.5	47.2	45.1	43.2	41.8	40.2	38.9
Churn rate ⁽⁶⁾	2.4%	2.4%	2.8%	2.4%	2.6%	2.4%	2.9%

(1) EBITDA (Earnings before income taxes, depreciation and amortization) is a financial index that is not based on generally accepted accounting principles. The Company presents this index as an additional index for assessing its business results since this index is generally accepted in the Company's area of operations which counteracts aspects arising from the modified capital structure, various taxation aspects and methods, and the depreciation period for fixed and intangible assets. This index is not a substitute for indices which are based on GAAP and it is not used as a sole index for estimating the results of the Company's activities or cash flows. Additionally, the index presented in this report is unlikely to be calculated in the same way as corresponding indices in other companies.

(2) Free cash flow is a financial index which is not based on GAAP. Free cash flow is defined as cash from operating activities less cash for the purchase/sale of property, plant and equipment, and intangible assets, net. The Company presents free cash flow as an additional index for assessing its business results and cash flows because the Company believes that free cash flow is an important liquidity index that reflects cash resulting from ongoing operations after cash investments in infrastructure and other fixed and intangible assets.

(3) Inactive subscribers are subscribers whose Bezeq lines have been physically disconnected (except for a subscriber during (roughly) the first three months of the collection process).

(4) Excluding revenues from transmission services and data communication, internet services, services to communications operators and contractor and other works. Calculated according to average lines for the period.

(5) For bundles with a range of speeds, the maximum speed per bundle is taken into account.

(6) The number of telephony subscribers (gross) who left Bezeq Fixed Line during the period divided by the average number of registered telephony subscribers in the period.

(7) Number of active Internet lines including retail and wholesale lines. Retail - Internet lines provided directly by the Company. Wholesale - Internet lines provided through a wholesale service to other communications providers.

³ On the initial application of IFRS 15 - Revenue from Contracts with Customers, commencing January 1, 2017, see Note 3.2 to the Company's Financial Statements for the period ended June 30, 2017.

Update to Chapter A (Description of Company Operations) of the Periodic Report for 2016

B. Pelephone

	Q3 2017	Q2 2017	Q1 2017	Q4 2016	Q3 2016	Q2 2016	Q1 2016
Revenue from services (NIS million)	461	449	435	439	468	456	455
Revenue from sale of terminal equipment (NIS million)	174	183	193	213	181	202	216
Total revenue (NIS million)	635	632	628	652	649	658	671
Operating profit (NIS million)	22	30	5	(4)	27	8	1
Depreciation and amortization (NIS million)	100	99	94	89	92	95	104
EBITDA (Earnings before income taxes, depreciation and amortization) (NIS million) ⁽¹⁾	122	129	99	85	119	103	105
Net profit (NIS million)	24	34	16	3	32	13	13
Cash flow from operating activities (NIS million)	209	193	117	65	152	180	185
Payments for investments in property, plant & equipment, intangible assets and other investments, net (NIS million)	78	82	73	63	64	63	51
Free cash flow (NIS million) ⁽¹⁾	131	111	44	2	88	117	134
Number of subscribers at the end of the period (thousands) ^{(2) (5)}	2,475	2,410	2,430	2,402	2,348	2,260	2,692
Average monthly revenue per subscriber (NIS) (ARPU) ⁽³⁾⁽⁶⁾	63	61	60	62	68	68	57
Churn rate ⁽⁴⁾	6.8%	6.1%	7.9%	6.3%	6.1%	6.2%	5.2%

- (1) Regarding the definition of EBITDA (earnings before income taxes, depreciation and amortization) and free cash flows, see comments (1) and (2) in the Bezeq Fixed Line table.
- (2) Subscriber data includes Pelephone subscribers (without subscribers from other operators hosted on the Pelephone network) and does not include subscribers connected to Pelephone services for six months or more but who are inactive. An inactive subscriber is one who in the past six months has not received at least one call, has not made one call / sent one SMS, performed no surfing activity on his phone or has not paid for Pelephone services. It is noted that a customer may have more than one subscriber number ("line").
- (3) Average monthly revenue per subscriber. The index is calculated by dividing the average total monthly revenues from cellular services, from Pelephone subscribers and other telecom operators, including revenues from cellular operators who use Pelephone's network, repair services and extended warranty in the period, by the average number of active subscribers in the same period.
- (4) The churn rate is calculated at the ratio of subscribers who disconnected from the company's services and subscribers who became inactive during the period, to the average number of active subscribers during the period. The churn rate in Q2 2017 does not include the effect of the writing off of 83,000 CDMA subscribers when the network was closed down, and in Q2 2016 it does not include the writing off of CDMA subscribers as noted in note 6.
- (5) Regarding the writing off of the CDMA subscribers, see Section 3.4 in the Description of Company Operations in the 2016 Financials ("Section 3.4"). On June 28, 2017, Pelephone discontinued operation of the CDMA network, as a result of which 83,000 subscribers ceased to receive service and were written off the subscriber listings.
- (6) In Q2 2016, Pelephone wrote off 499,000 CDMA subscribers. The effect of writing off the CDMA subscribers led to an increase of NIS 10 in Pelephone's ARPU in Q1 and Q2 2017, NIS 11 in Q3 2017, and an average of NIS 12 in Q2, Q3 and Q4 2016. The effect of writing off the subscribers on ARPU for the full year 2016 was NIS 9.

C. Bezeq International

	Q3 2017	Q2 2017	Q1 2017	Q4 2016	Q3 2016	Q2 2016	Q1 2016
Revenues (NIS million)	367	407	384	392	384	377	395
Operating profit (NIS million)	39	45	49	47	45	47	37
Depreciation and amortization (NIS million)	34	33	33	34	35	35	33
EBITDA (Earnings before income taxes, depreciation and amortization) (NIS million) ⁽¹⁾	73	78	82	81	80	82	70
Net profit (NIS million)	27	33	36	33	33	33	26
Cash flow from operating activities (NIS million)	74	69	52	86	65	69	49
Payments for investments in property, plant & equipment, intangible assets and other investments, net (NIS million) ⁽²⁾	29	46	29	25	24	33	37
Free cash flow (NIS million) ⁽¹⁾	45	23	23	61	41	36	12
Churn rate ⁽³⁾	6.3%	5.0%	5.3%	5.2%	5.5%	4.5%	5.2%

(1) On the definition of EBITDA (earnings before income taxes, depreciation and amortization) and cash flows, see comments (1) and (2) in the Bezeq Fixed Line table.

(2) The item also includes long term investments in assets.

(3) The number of Internet subscribers who left Bezeq International during the period, divided by the average number of registered Internet subscribers in the period.

D. DBS

	Q3 2017	Q2 2017	Q1 2017	Q4 2016	Q3 2016	Q2 2016	Q1 2016
Revenues (NIS million)	406	416	424	438	434	434	439
Operating profit (NIS million)	35	49	52	68	62	77	57
Depreciation and amortization (NIS million)	72	71	70	71	75	74	76
EBITDA (Earnings before income taxes, depreciation and amortization) (NIS million) ⁽¹⁾	107	120	122	139	137	151	133
Net profit (loss) (NIS million)	(123)	(151)	19	395	(142)	(114)	(71)
Cash flow from operating activities (NIS million)	115	169	51	207	154	110	158
Payments for investments in property, plant & equipment, intangible assets and other investments, net (NIS million)	69	52	60	41	50	58	59
Free cash flow (NIS million) ⁽¹⁾	46	117	(9)	166	104	52	99
Number of subscribers (at the end of the period, in thousands) ⁽²⁾	597	603	608	614	618	623	629
Average monthly revenue per subscriber (ARPU) (NIS) ⁽³⁾	226	229	232	237	233	231	231
Churn rate ⁽⁴⁾	4.8%	3.8%	4.3%	3.6%	4.5%	3.6%	4.2%

(1) On the definition of EBITDA (earnings before income taxes, depreciation and amortization) and cash flows, see comments (1) and (2) in the Bezeq Fixed Line table.

(2) Subscriber - a single household or small business customer. In the case of a business customer with multiple reception points or a large number of decoders (such as a hotel, kibbutz, or gym), the number of subscribers is calculated by dividing the total payment received from the business customer by the average revenue from a small business customer. The number of subscribers was corrected retrospectively due to an insignificant change in the counting of subscribers among large customers.

(3) Monthly ARPU is calculated by dividing total DBS revenues (from content and equipment, premium channels, advanced products, and other services) by the average number of customers. The average monthly revenue was corrected retrospectively due to an insignificant change in the counting of subscribers among large customers.

(4) Number of DBS subscribers who left DBS during the period, divided by the average number of DBS registered subscribers in the period.

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

State Comptroller's Report dated July 12, 2017

On July 12, 2017, the State Comptroller published a report regarding the Ministry of Communications' actions to regulate the fixed-line communication segment. By its very nature, the State Comptroller's report deals with criticism of government ministries (primarily with respect to issues pertaining to the Company) and its findings are directed at those entities.

It includes three reports on the following topics:

- Implementation of the wholesale market reform.
- The investment in infrastructures in the fixed-line communications segment, and structural aspects, including reference to the Ministry of Communications' actions in connection with the cancellation of the structural/corporate separation in the Company.
- The Prime Minister's conflicts of interests in his capacity as Minister of Communications.

The Company is unable to evaluate the impact of the aforementioned report on it, if at all.

Section 1.7.2 - Activities of Bezeq Group as a communications group and the structural separation restriction

Notably, Bezeq Group is conducting a preliminary review of certain synergetic aspects among its subsidiaries. This is a preliminary HQ study only as part of a review of a range of options. So far no recommendations have been made or discussed.

Section 1.7.2.1(B) - Cancellation of the structural separation and the announcement of the Director General of the Ministry of Communications from December 21, 2016 - to the best of the Company's knowledge, the Ministry of Communications appointed a team that includes a Ministry of Finance representative, who is charged with advancing the cancellation of the structural separation. The Company believes that the chances of concluding the hearing proceedings in 2017 are slim.

Section 1.7.3 - Regulatory oversight and changes in the regulatory environment - wholesale market

Section 1.7.3.2 BSA services - hearing on the subject of determining the format for reviewing a margin squeeze by fixed-line broadband network owners - on August 29, 2017, the Ministry of Communications published a secondary hearing, whereby it is considering allowing the infrastructure owners to conduct their own oversight proceeding to rule out margin squeeze, by means of inspection tools to be approved by the Ministry (in addition to the limited advance review track). As proposed, the effective tariff for the reviewed service or group of reviewed services will not be lower than the minimum price level set for marketing those services examined by the license holder. In the hearing, "license holder" includes the Company, Bezeq International, DBS, HOT Broadcasts, HOT Telecom and HOT Net. On November 14, 2017, the Company submitted its comments on the hearing whereby there is no reason to determine a format for examining margin squeeze, although if such format is determined, the independent inspection mechanism proposed in the hearing should be expanded. The Company believes that if the margin squeeze review format is applied, it could affect the ability of the Company and Group companies to market bundles with respect to the timing of the offers and the prices they will be able to offer.

Section 1.7.3.3 - Wholesale service use of physical infrastructures - On October 19, 2017 the Ministry of Communications informed the Company that it must allow certain contractors to enter Bezeq's infrastructures and carry out work connected with the physical infrastructure service portfolio for the service providers, instead of Bezeq employees, and not only in exceptional cases ("the Notice"). The Company disputes the information and reasons provided in the Notice, it views them as an infringement of its property and a security exposure, and it intends to contest the Notice with the legal tools available to it. Subsequently, on November 9, 2017, the Company filed a petition in the High Court of Justice to grant an order nisi against the Ministry of Communications and its Acting Director General to repeal the October 19, 2017 decision of the Acting Director General of the Ministry of Communications regarding the Ministry's decision as specified in the Notice. In the petition, the Company argues that the decision was made in breach of the Ministry of Communications' duty to hold a hearing and in serious violation of its right to present arguments, and that the decision is unreasonable and disproportionate given that it will lead to chaos in the communications infrastructures, exposing them to numerous risks and serious dangers, without any grounds or justification. On the day the petition was filed, the court ruled that the petition would be heard at the earliest opportunity and that the respondents to the petition must submit a preliminary response to the petition by January 9, 2018.

Further to sending the Notice, on October 21, 2017, the Company received a letter from the Chairman of the State Employees Union and holder of the Bezeq portfolio in the New Histadrut Labor Federation regarding "a labor dispute with respect to the entry of workers who are not Bezeq employees for core work". The letter states that the labor dispute declared by the New Histadrut Labor Federation in December 2016 is still in effect, and that if an attempt is made by external entities to carry out work in the normal course of the Company's activity, such that the work is performed by workers who are not Company employees (including contractor workers), the Histadrut will be forced to activate the aforementioned labor dispute. Subsequently, on October 25, 2017, the chairman of the Company's labor union informed the Company of a cessation of development work on the Company's infrastructures, whether for the Company or for other communications providers. The Company applied to the Labor Court to issue an order instructing the workers to refrain from the cessation of work and to immediately return to full, regular work. At a discussion which took place on November 2, 2017 (attended by the Acting Director General of the Ministry of Communications, who was summoned to the discussion by the court), the court ruled that the employees have the right to protest against the direct harm they foresee to their employment conditions, but may, nevertheless, take only short and limited organizational measures. Consequently, the court allowed the workers to take to take reasonable organizational measures for two days only, in the context of which the employees may refrain from cooperating with external contractors on infrastructure work related to the dispute, but will be precluded from taking

proactive steps to thwart or disrupt the performance of the work by a third party. An application for permission to appeal this decision, which was filed by the New Histadrut Labor Federation and workers' representatives, was dismissed on November 27, 2017.

Section 1.7.3.5 - Wholesale telephony market - on May 18, 2017, the then Acting Minister of Communications issued a decision regarding the "format for provision of telephony services for resale and setting the payment thereof on Bezeq's network". According to the decision, the Acting Minister of Communications adopted the recommendation of the Ministry's professional echelon, and determined the following:

A. A format was determined for provision of telephony services whereby the Company will allow another license holder to purchase telephony services from the Company to enable incoming and outgoing for customers of other license holders. The telephony service for resale will be provided for one year from July 31, 2017,⁴ after a two-month preparation period.

B. Maximum payments were set for the service, including a fixed monthly payment of NIS 16 per line and variable payment for outgoing calls of 1.6 agorot per minute of outgoing call.

The final maximum payments will be determined after a hearing has been held and if it becomes clear in the hearing that the payments must be adjusted, an appropriate amendment will be made to the payments and amounts will be offset (retroactively from the date of the decision) between the relevant operators.

C. The date of provision of wholesale telephony services (at wholesale prices) on the Company's network was postponed for the 14 months of the arrangement. Moreover, the decision stated that the option to extend the arrangement or turn it into a permanent arrangement will be reviewed (a recommendation on this matter will be put for a public hearing).

On June 28, 2017, the Company submitted its comments on the hearing in which context it argued, inter alia, that there were serious defects in the calculations on which the maximum payments recommended for the service are based, and that these tariffs are lower than they should be.

The Company is ready to provide the service from July 31, 2017.

The Company believes that implementation of the above service may have an adverse effect on its financial results. Nevertheless, at this stage, the Company is unable to estimate the extent of the effect since it depends on different variables, including the results of the late hearing, the marketing of the services by competitors, the volume of customer demand for calls and the price levels of alternative products currently available on the market (such as VoB services), etc. At the publication date of the report the number of customers who subscribe to the service is negligible.

On this matter, see also the Company's Immediate Report dated May 23, 2017 (to which the decision of the Acting Minister of Communications and recommendations of the professional echelon in the Ministry of Communications were attached), included here by way of reference.

On October 29, 2017, the Company received a letter from the Acting Director General of the Ministry of Communications according to which the obligation defined in the hearing regulations with respect to both wholesale telephony service and resale telephony service refers to the provision of telephony services by a domestic carrier as separate, stand-alone services (namely - an obligation to provide telephony service even if it is not part of the BSA service). According to the letter, the Ministry expects the Company to take immediate action to provide the service, and as requested by the Ministry the Company submitted a detailed time schedule for this. The Company believes that the Ministry's interpretation is erroneous, that it is inconsistent with the definitions in the regulations (which refer to the service portfolio) and that it contradicts explicit definitions included in the BSA + telephony service portfolio, according to which the telephony service will not be provided as a stand-alone service, not on the BSA service, and it expressed its position on the matter before the Ministry of Communications.

Regarding tariffs for HOT's wholesale services - it is noted that they were published on June 26, 2017.

On October 19, 2017, the Ministry of Communications sent the Company a final supervision report regarding implementation of a wholesale telephony service (the "Supervision Report") (after the Company responded to an initial supervision report in June 2015) together with notice of its intention to impose financial sanctions regarding the implementation of wholesale telephony services (the "Notice"). In accordance with the Supervision Report, after the Supervision and Enforcement Division at the

⁴ The original date set in the decision is July 17, 2017, however the relevant regulations were published on June 1, 2017 and they stipulate that the regulations will enter into force 60 days from their date of publication.

Ministry of Communications examined whether the Company had implemented the provisions detailed in the Minister of Communications' decision dated November 17, 2014, regarding the regulation of wholesale services, in the "Bitstream Access (BSA) and Wholesale Telephony" service portfolio, in the Communications Regulations (Telecommunications and Broadcasting) (Use of a Public Telecommunications Network of a Fixed-Line Operator), 2014, and in the Company's license, whereby the Company was required to provide wholesale telephony services as of May 17, 2015 (the "Directives"), and after examining and rejecting all of the Company's arguments in response to the initial supervision report in the matter, it was found that the Company was in breach of the Directives by failing to provide the wholesale telephony service. Concurrently with the Supervision Report, the Company was issued the Notice whereby, after the Company had been found to have violated the Directives and in accordance with the authority vested by the Communications Law (Telecommunications and Broadcasting), 1982, the Company was notified of the intention to impose a financial sanction on the Company in the amount of NIS 11,343,800. The Notice also stated that the Company must take affirmative action to comply with the instructions of the Ministry of Communications in the matter, since the MoC is considering initiating another proceeding in the same matter. The Company submitted its arguments in writing against the intention to impose a financial sanction and against the amount of the financial sanction, according to which, *inter alia*, the Company did not breach its obligations and the application of the financial sanction is out of place.

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

Subsection 1.7.4.5 – Consumer legislation

- A. On July 26, 2017, the Consumer Protection Bill, Amendment no. 55 (Professional human response on IVR systems), 2017, passed its first reading. Accordingly, the dealers listed in the Second Schedule to the Consumer Protection Law will be obligated to provide a human response after the option to choose a language on an IVR system, where the waiting time will not be more than the number of minutes that has yet to be defined and consumers will not be directed to a voice mail service. Insofar as the bill is approved in its current format, the costs of operating the call centers of the Group's companies are likely to increase significantly.
- B. On August 15, 2017, the Company received a request to produce documents from the Consumer Protection and Fair Trade Authority, whereby the Authority is conducting an investigation against the Company on suspicion of breaches of the Consumer Protection Law. Among other things, the request is for data and detailed information in relation to consumers of surfing packages and/or the Company's internet infrastructures. The Company provided the documents as requested.

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

Section 2.2.2 – Products and services - telephony

On an exemption from obtaining approval for a restrictive arrangement in relation to a "unified" information service (see Footnote 21 in the 2016 Periodic Report) - on November 6, 2017, the exemption was granted for a further six-year period.

Section 2.6.3 - Internet infrastructure segment

Competition from Partner - Partner announced the deployment of its optical fibers at an accelerated rate and the launching of commercial marketing of internet infrastructure to customers.

Section 2.6.5 – Other potentially competing infrastructures

On November 20, 2017, Cellcom and Partner announced that they are negotiating a potential long-term cooperation agreement for the deployment of fiber optic infrastructure by both companies, whereby each party will be entitled to purchase from time to time, as per its needs and at its sole discretion, fiber optic infrastructure services (including Indefeasible Right of Use - IRU) in the other party's present and/or future fiber optics infrastructure in order to connect residential buildings throughout Israel.

Section 2.7.2 – Domestic fixed-line communications infrastructure and equipment

On the expansion of the distribution of optical fiber infrastructures to the customer's premises as a basis for future provision of more advanced and broadband communication services than those currently provided - since by the end of 2016 the distribution of optical fibers was significant whereas advanced technologies that facilitate extensive high-speed provision of the service are still being tested and have not yet reached the necessary technological readiness, and in view of the prices resulting from these technologies, which at this stage are not economical, the Company slowed the pace of distribution of

the fibers significantly in 2017. The Company is focusing its efforts on examining the readiness of the new technologies, which will allow it to provide the service more extensively, and on investments in the existing network with the purpose of increasing the bandwidth, quality and survivability of the network.

Section 2.9 – Human resources

On a letter dated October 21, 2017 from the Chairman of the State Employees Union and holder of the Bezeq portfolio in the New Histadrut Labor Federation, regarding “the activation of a labor dispute with respect to the entry of workers who are not Bezeq employees for core work”, that was sent further to the Ministry of Communications notice of October 19, 2017, on the subject of work being performed by communications providers on the Company's infrastructures, and regarding the taking of union action and subsequent legal proceedings in the Labor Court, see the update to Section 1.7.3.3.

Section 2.9.5 - Officers and senior management in the Company

On the approval of an amended compensation policy for the Company – on April 5, 2017, a special general meeting of the Company's shareholders approved the amendments to the compensation policy according to the text attached as an addendum to the Report on Call for a General Meeting that was included in the 2016 Financials by way of reference.

Section 2.11 – Working capital

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

Section 2.13 - Financing

Section 2.13.1 – Average and effective interest rates on loans, Section 2.13.4 - Credit received during the Reporting Period / commitments to extend credit, and Section 2.13.5 - Company debentures

Debentures

In May and June 2017, the Company completed an issuance of debentures in the total amount of NIS 1.1 billion par value as follows:

1. Public issuance of NIS 384,467,000 par value debentures (Series 9) by way of an expansion of series, in accordance with a shelf prospectus from May 2014, as amended due to a clerical error in June 2014 (“the Shelf Prospectus”) and a shelf offering report dated May 25, 2017 (“the Shelf Offering Report”).
2. Issuance of traded Series 6 and 10 debentures of the Company to the bearers of Series B debentures of DBS, which are traded on the TASE's TACT (Tel Aviv Continuous Trading) Institutional System (“DBS Debentures”), in consideration of debentures of DBS that they own. The issuance took place in accordance with the shelf prospectus and the shelf offering report, as follows: NIS 125,000,000 par value DBS debentures were exchanged for NIS 125,750,000 par value debentures (Series 6), and NIS 436,307,797 par value DBS debentures were exchanged for NIS 481,683,808 par value debentures (Series 10).
3. Two private placements of Series 9 debentures of the Company to classified investors in the total amount of NIS 108,000,000 par value to which restrictions apply regarding resale, as defined in Section 15C of the Securities Law and under the Securities Regulations (Details Concerning Sections 15A - 15C of the Law), 2000.

With respect to all the foregoing, see also the Company's Immediate Reports dated May 25, 2017, May 29, 2017, June 4, 2017, June 11, 2017 and June 18, 2017, included here by way of reference and Note 8 to the Company's Financial Statements for the period ended September 30, 2017.

Exercising of commitment to extend credit

The Company completed the receipt of credit from financial institutions / banks in the total amount of NIS 900 million on June 15, 2017, and of NIS 500 million on September 26, 2017, all based on undertakings given to it as described in the 2016 Periodic Report.

On June 1, 2017, the Company repaid the last principal payment for Series 8 debentures thus securing final redemption of the debentures.

Update to Chapter A (Description of Company Operations) of the Periodic Report for 2016

The following is an up-to date table of the distribution of long-term loans (including current maturities), including information about the aforementioned issuances and credit:

Loan term	Source of financing	Principal amount (NIS million)	Currency or linkage	Type of interest and change mechanism	Average interest rate	Effective interest rate	Interest range in 2017
Long-term loans	Banks	738	Unlinked NIS	Variable, based on prime rate*	1.78%	1.79%	1.75%-1.80%
	Banks	2,115	Unlinked NIS	Fixed	4.36%	4.62%	2.40%-6.85%
	Non-bank sources	734	Unlinked NIS	Variable, based on annual STL rate**	1.51%	1.56%	1.51%-1.57%
	Non-bank sources	3,728	Unlinked NIS	Fixed	3.87%	3.98%	3.65%-6.65%
	Non-bank sources	3,961	CPI-linked NIS	Fixed	2.30%	2.35%	2.20%-3.70%

* Prime interest rate as at October 2017 – 1.6%.

** YSTL yield per year (828) – 0.092% (average for the last 5 days of trading in May 2017) for the interest period commencing September 1, 2017.

Section 2.13.6 - Credit rating

On April 24, 2017, Standard & Poor's Maalot Ltd. ("Maalot") affirmed a rating of ilAA/Stable for the Company and its debentures (Series 6-10) and for Telephone and DBS, as detailed in the full rating report published in an Immediate Report issued by the Company on April 24, 2017, which is included here by way of reference.

Furthermore, for the purpose of issuing the Company debentures as part of an expansion of series and exchange of the DBS debentures as noted in the above update, the following ratings were approved:

1. Approval from Midroog Ltd. for a rating of Aa2.il, outlook stable, for Series 6-10 debentures of the Company and for debentures of the Company in the amount of up to NIS 1.1 billion par value by means of an expansion of existing series of debentures and/or as part of an exchange of DBS debentures with debentures to be issued by the Company. On this, see immediate reports published by the Company on May 21, 2017, and May 25, 2017, which are included in this report by way of reference.
2. Maalot approval for an ilAA/Stable rating for debentures in the amount of up to NIS 1.1 billion par value to be issued by the Company by means of an expansion of one or more of the Series 6-10 for a cash payment and/or against an exchange for DBS debentures. On this, see immediate reports published by the Company on May 22, 2017, May 25, 2017, which are included in this report by way of reference.

On this matter, see also Section 4 of the Directors Report.

Section 2.14 - Taxation

For information about taxation, see Note 5 to the Company's Financial Statements for the period ended September 30, 2017.

Section 2.16 - Restrictions and control of the Company's operations

Section 2.16.1 - Control of Company tariffs

On June 27, 2017, the Company received a hearing letter from the Ministry of Communications. According to the hearing documents, the Ministry is considering two alternatives to the present tariff control mechanism for telephony services:

- A. To convert the existing supervisory method that sets fixed rates (FIX) to maximum rates; the main telephony services (telephone line - NIS 57.92 including VAT, and 1.87 agorot including VAT for calls) will be set in relation to the updated costs structure; for most of the additional services, the present tariff will become the maximum tariff and price control will be lifted for some of the services.

- B. To remove price control from the main telephony services - telephone line and calls, and from additional services that are currently supervised in the form of fixed tariffs, and to set a maximum price for a "supervised bundle" which will include a telephone line and call minutes which the Company will offer customers who wish to subscribe to this service, similar to the alternative payments package currently offered by the Company for which there is most demand.

Similarly, it is proposed that only existing subscribers of the alternative payments package for the "Kav Kal" (Light Line) service will be able to continue to receive it. The Ministry of Communications is also considering determining that price control will be lifted on PRI channels and the price control on their call components will be cancelled.

On August 13, 2017, the Company submitted its comments on the hearing, opposing the proposed tariffs. The Company believes that the change in the control mechanism being considered in the hearing, insofar as this change is implemented, will negatively affect its financial results. The Company believes that its retail tariffs will be affected in parallel also as a result of the setting of wholesale prices for telephony services (see Section 1.7.3).

The Company was summoned to an oral hearing on this matter on December 6, 2017.

On this, see also the Company's Immediate Report dated June 28, 2017, (to which the hearing letter is attached) included here by way of reference.

Section 2.17 – Significant agreements

Section 2.17.4 - Management agreement:

In view of the restrictions imposed on the activities of the Chairman of the Company's Board of Directors, Mr. Shaul Elovitch, and of other directors serving on the Boards of the Company and its subsidiaries on behalf of Eurocom Communications, due to the investigation being carried out by the Securities Authority (on this matter, see the update to Section 1.1), on September 25, 2017, the Company's Board of Directors adopted the Compensation Committee's recommendation and resolved that the amount to be paid to Eurocom Communications by the Company under the management agreement for the services of the Acting Chairman of the Board of the Company and the subsidiaries and affiliates for the period from June 20, 2017 (and for as long as no material change will be made to the restrictions currently imposed on Shaul Elovitch) will be 50% of the amount stipulated in this agreement for this period. This decision will remain in force until the end of 2017, at the latest. The Board of Directors also decided that in view of the difference between the amount paid as an advance payment at the beginning of 2017, as set out in the terms of the management agreement, for the service of directors in the Company and its subsidiaries and affiliates, and the amount calculated on the basis of actual participation so far, at this stage, payment of the reduced amounts for the services of the Chairman as set out above, as well as for consultation services as per the management agreement will be deferred, and the final calculation, offsetting the various amounts, will be made at the end of 2017. On this, see also the Company's Immediate Report dated September 26, 2017.

Section 2.18 – Legal proceedings

Pending proceedings

Subsection (B) - on a claim and motion for its certification as a derivative claim concerning an agreement for the purchase all the holdings and shareholders loans of Eurocom D.B.S. Ltd. in DBS by the Company - in view of the Israel Securities Authority investigation, *inter alia*, in connection with the agreement which is the subject of this claim (see update to Section 1.1) and the ISA's position that this move should be delayed, the court decided upon a stay of proceedings in this case, at this stage until March 5, 2018.

On a decision from October 24, 2017, concerning the striking out of three motions to disclose documents prior to filing a motion to certify a derivative claim given that these motions raise factual and legal questions that, in principle, are similar to the questions raised in this claim and motion, see subsection 4 in the New Proceedings section below.

Subsection (D) - on a motion for certification of a class action on the grounds of the Company abusing its position as a monopoly, including with respect to the wholesale market reform - on October 25, 2017, the plaintiffs filed a motion to include in the case an immediate report published by the Company on October 22, 2017, in which the Company reported on a final supervision report issued by the Ministry of Communications concerning implementation of the wholesale telephony service and notice of the Ministry's intention to impose a financial sanction in this matter (on these matters, see the update to Section 1.7.3.5) and to instruct the Company to include in the case also the two aforementioned documents.

Subsection (E) - on a claim and motion for its certification as a class action relating to a campaign by the Company to upgrade the internet surfing speed - on April 3, 2017, a ruling was handed down on this action certifying the plaintiff's application to abandon the motion to certify the claim as a class action and dismissing the plaintiff's personal claim, and this after, in its response, the Company drew attention to advertisements in which it had specified the exclusions to the campaign.

Subsection (H) - on two motions for the certification of class actions alleging that the Company charges a monthly payment, unlawfully and without consent, for support and/or warranty services as part of using its internet infrastructure, and a court ruling from March 26, 2017 to strike out the later motion in view of the similarity between the two motions - on May 14, 2017, the Company received notice of an appeal (that was filed in the Supreme Court on May 4, 2017) by the applicant in the later motion asking to strike out the earlier motion and continue the hearing in the later motion.

Subsection (F) - on a motion for certification of a class action on the grounds of charging internet subscribers twice when transferring them from one ISP to another - on September 13, 2017, a ruling was given approving the plaintiff's withdrawal from the motion.

Subsection (I) - on two motions for the certification of class actions in connection with the antivirus service - on July 4, 2017, the Central District Court resolved to strike out the later motion (the motion for the amount of NIS 11 million) in view of the similarity between the two motions.

Legal proceedings which ended during the Reporting Period or by the date of publication of the report

Subsection (B) - regarding a Supreme Court ruling which dismissed two appeals on a ruling of the Tel Aviv District Court (Economic Department) which dismissed two (consolidated) motions to certify derivative actions concerning the distribution of dividends and loans of the Company - on April 6, 2017, the Company received a copy of a petition to hold another hearing on the case that was filed by one of the appellants. On August 30, 2017 the petition was dismissed.

New proceedings added since the date of publication of the 2016 Periodic Report:

1. In April 2017, the Company received a class action certification motion which was filed in the Tel Aviv District Court against the Company and against its subsidiary, Walla! Communications Ltd., Yad2 and an advertising company owned by Walla (hereinafter collectively, the "Respondents"). The motion pertains to the Company's B144 service, which enables businesses to advertise on the Internet (the "Service"). According to the petitioner, the Respondents charged subscribers to the Service unlawful charges. The petitioner estimates the class action amount at NIS 1.11 billion (based on an estimate of 300,000 customers and compensation of NIS 3,700 per customer). Notably, in May 2017, the Company received another claim together with a class action certification motion (which was filed in the Tel Aviv District Court) the subject of which is similar to this claim and alleging that unlawful amounts had been charged for the Company's B144 service. According to the information in the motion, the amount of the class action cannot be estimated. The Company filed a motion to abandon the first motion in limine. Furthermore, a motion was filed to consolidate the two proceedings in view of shared questions and identity of some of the classes in both proceedings.
2. In June 2017, two motions for the certification of class actions were filed in the Tel Aviv District Court (Economics Department) by shareholders of the Company. The subject of the motions is a transaction from 2015 in which the Company acquired from Eurocom D.B.S. Ltd (a company controlled by the Company's controlling shareholders) the balance of shares of the subsidiary D.B.S that it held ("the Transaction"):

The first motion was filed against the Company, Chairman of the Company's Board of Directors, members of the Company's Board of Directors, CEO of the Company, the CEO and CFO of DBS and companies in the Eurocom Group (including companies that are controlling shareholders of the Company, whether directly or indirectly) in the name of all those who purchased Company shares between February 11, 2015, and June 19, 2017 (excluding the Respondents and/or those acting on their behalf and/or connected with them). In the motion it is argued that the report concerning the Transaction was misleading and/or deficient, and on account of which due to the opening of a public investigation into the Transaction by the ISA the public has become aware of details concerning the Transaction and its implementation, which led to a drop in the Company's share price in the days following the disclosure and analysis of the new information, such that the estimate of damage caused to the Company's shareholders as a result of the disclosure is approximately NIS 1.3 billion. The Petitioner argues that the Respondents acted contrary to the provisions of the Securities Law, 1969 and contrary to the provisions of additional laws, and caused holders of the Company's securities heavy financial losses, amounting to millions of shekels if not more.

The second motion was filed against the Company, Chairman of the Company's Board of Directors, members of the Company's Board of Directors, and companies that are controlling shareholders of the Company, B Communications Ltd. and Internet Gold - Golden Lines Ltd. in the name of three sub-groups - anyone who acquired (1) shares of the Company, (2) shares of B Communications Ltd, and (3) shares of Internet Gold - Golden Lines Ltd. on the Tel Aviv Stock Exchange between May 21, 2015 and June 19, 2017. The Petitioner argues that the public that invested in the aforementioned shares was seriously misled, which was uncovered following the opening of a public investigation into the Transaction by the ISA on June 20, 2017, whereby the increase in the cash flow of DBS as reported in the Company's financial statements was artificially inflated, according to their claim, thereby misleading reasonable investors who based themselves on DBS cash flow data to estimate its worth, which led to over-valuation of the above companies. The Petitioner estimates the damage caused to the sub-group of Company shareholders at NIS 568 million. The Petitioner also claims additional damage caused to the groups of shareholders in B Communications and Internet Gold-Golden Lines Ltd.

On October 25, 2017, a ruling was given ordering the striking out of another class action certification motion (mentioned in subsection 3 below), after the court ruled that the above motions should be preferred and after failing to find any added value in the other motion to advancing the class's interests or facilitating the hearing.

In accordance with a procedural arrangement approved earlier by the court, the petitioners agreed in the aforementioned motions to administer the motions jointly and they will file a consolidated motion.

Notably, on November 20, 2017, the Attorney General's attorney submitted his position whereby the hearing in this case should be delayed, at this stage for 4 months, to enable the evidence in connection with the ISA investigation (see update to Section 1.1) to be examined by the District Attorney's office, to allow the investigation to be completed to the extent that this is necessary, and so that the District Attorney's office can formulate its position. In accordance with the court's decision from that date, the Attorney General must clearly explain to the court the source of his authority to request a stay of proceedings.

3. In July 2017, the Company was served with a motion to certify a class action that was filed in the Tel Aviv District Court. The subject of the motion is a transaction for the purchase of DBS shares (in this section "DBS Transaction") as well as a transaction to continue the agreement between DBS and Spacecom (in this section "Spacecom Transaction"). The motion was filed against the Company and members of the Company's Board of Directors in the name of a group of people who are or had been Company shareholders, whether directly or indirectly, by various public or institutional bodies, all in the period between June 20, 2017 and June 29, 2017, and for the period relating to the publication of the failure in connection with the Spacecom Transaction from July 11, 2017. In the motion it is argued that in the circumstances described in the motion, there are four causes of action: breach of duty of care, breach of fiduciary duty, discrimination against the minority and the transfer of misleading information. According to the Petitioners, the damage caused is expressed as a decline in the value of the Company's share at the stage when the ISA summoned for investigation those involved acting for the Company and as a result, the alleged failures relating to the DBS Transaction were reported. The Petitioners estimate that the damage caused to the class as a result of the decline in the value of the Company's share is NIS 2 billion (including the damage caused after the publication of the affair relating to the continued contract with Spacecom).

On October 25, 2017, a ruling was given ordering the striking out of this motion after the court ruled that the two earlier class action certification motions (mentioned in subsection 2 above) should be preferred and after it did not find any added value in this motion to advancing the class's interests or facilitating the hearing.

4. In June - August 2017, Company shareholders filed several motions in the Tel Aviv District Court against the Company and DBS (not including two motions that were filed only against the Company). The motions were to disclose documents prior to filing a motion for certification of a derivative claim under Section 198A of the Companies law, where the background to these motions is the public investigation being conducted by the ISA, which began on June 20, 2017 and was expanded, as announced by the Company, on July 11, 2017 also with respect to the DBS - Spacecom transaction, as defined below (see update to Section 1.1).
 - A. In some of these motions (three in all), the court was moved to instruct the Company (and DBS, as applicable) to submit to the Petitioners documents and information in connection with the agreement for the Company's purchase of DBS, and specifically in connection with the Second Contingent Payment according to that agreement (payment of NIS 170 million which

is contingent on DBS meeting free cash flow targets in the period 2015-2017). On October 24, 2010, the court resolved to strike out the three motions after accepting the plaintiff's request in the motion to certify a derivative action in the matter of an agreement for the Company to purchase DBS (see above - Pending Proceedings subsection B) ("the Earlier Motion"), and this after concluding that these motions give rise to questions of fact and law that are essentially similar to the questions that arise in the Earlier Motion. In its decision, the court also noted that if the petitioner in the Earlier Motion does not submit a motion to amend the motion for certification (such that it also applies to the matters included in the Disclosure Motions) or, alternatively, it files such a motion and its motion is dismissed, the petitioners in the aforementioned three motions will have the right to initiate legal proceedings should they so determine.

- B. In some of the motions, the court was moved to instruct the Company (and DBS, as applicable) to submit to the Petitioners certain documents in connection with an interested party transaction between DBS and Spacecom from 2013, as amended early in 2017 (in this section: the "DBS - Spacecom Transaction"). The ISA expressed its position whereby in view of the investigation, there should be a stay of the proceedings in these cases, and that if the ISA's position on this matter is accepted, it wishes to submit a revised notice with respect to further conducting of the proceedings no later than March 5, 2018. The court instructed the ISA to submit a revised notice by January 3, 2018, as a court hearing on this case is scheduled for January 8, 2018.
- C. In an additional motion, the court was moved to instruct the Company and DBS to submit to the Petitioner documents and information also in connection with the agreement for the Company's purchase of DBS and in connection with the DBS - Spacecom Transaction. In this motion, the Petitioner wishes to explore the filing of a motion to certify a derivative claim against officers in the Company and DBS who were in breach of their fiduciary duty against the Company in these transactions, according to the Petitioner, where the relief requested is to return all the benefits they received for the positions they held in the Company or DBS (salary, bonuses, management fees, etc.). The court consolidated the preliminary hearing in this case with the preliminary hearing on the motions to disclose documents prior to filing the motion for certification of a derivative claim, detailed in subsection (B) above.

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

Section 3.1 - General information about the area of operations

Section 3.1.5.1 - on April 20, 2017, permission was received from the Ministry of Communications to operate the LTE Advanced technology (LTEA).

Section 3.2 - Services and Products

Section 3.2.2 - in April 2017, the Finance Minister announced an economic plan that includes, inter alia, the elimination of import duties and purchase taxes. As part of this plan, the Finance Ministry decided to abolish purchase tax on imported cellular devices, which had been 15% of the value of the device.

Section 3.7 - Property, plant and equipment

Section 3.7.1.1 - in April 2017, Pelephone received approval to close down the CDMA network on July 30, 2017, or earlier with the Ministry's approval. On June 28, 2017, Pelephone discontinued operation of the CDMA network, in accordance with the amendment to its license on this matter.

Section 3.8 - Intangible assets

Pelephone returned to the national pool of frequencies two frequency bands, both on the 1 mega bandwidth, in the 850 Mhz spectrum and towards the end of April 2017 Pelephone received a temporary allocation of 5 mega bandwidth on the 1800 Mhz spectrum. This allocation is for limited use and for a limited period and it will expire at the end of 2019 or earlier, according to the conditions specified in the allocation.

Section 3.9 – Human resources

Sections 3.9.2 and 3.9.5 - on April 27, 2017, a new collective labor agreement was signed by Pelephone and the New Histadrut Labor Federation ("the Histadrut") and Pelephone's workers' committee, replacing the collective agreement that expired on December 31, 2016. The main points of this agreement are:

1. The agreement applies retroactively from January 1, 2017 and up to December 31, 2019. After this date, the agreement will be extended automatically for 18-month periods, unless one of the parties gives notice that it wishes to change it.
2. The inclusion of mechanisms which include the Committee in decisions concerning the termination of permanent employees, the implementation of disciplinary measures against them and restructuring of the organization, while allowing for administrative flexibility which would make it possible to operate in a competitive and dynamic market.
3. The determination of quotas for streamlining-related dismissals and annual salary increments, various financial benefits and annual bonuses based on Pelephone's business results to be given to employees during the term of the Agreement. The ongoing costs of the agreement are not materially different from the previous collective agreement.
4. The open labor dispute declarations are cancelled.

Section 3.16 – Legal proceedings

Section 3.16.1(A) - On an appeal filed in the Supreme Court against a decision by the District Court to dismiss a claim and a motion for its certification as a class action that was filed against cellular operators, including Pelephone, for the collection of VAT from customers who use cellular services while they are outside Israel - on July 3, 2017, the Supreme Court issued a ruling accepting the Petitioners' appeal against the decision to dismiss the claim and the hearing will be returned to the District Court to rule on the question of whether monies were collected unlawfully for cellular services abroad. According to the Supreme Court ruling, if the District Court will rule in favor of the issue and Pelephone will be required to refund the collected VAT to its customers, a claim for indemnification against the Tax Authority will be possible for these amounts that it will be required to refund. Furthermore, it was determined that in the context of prepaid service bundles for use overseas, the VAT rate is zero. According to Pelephone's initial estimate, the implication of the Supreme Court ruling is that the results of the aforementioned process will have no significant repercussions for Pelephone.

Section 3.16.1(G) - On a claim and motion for its certification as a class action against Pelephone, in which it is argued that Pelephone is in breach of the portability plan / rules, so that when attempting to move to another operator (the receiving operator), the Plaintiff discovered that Pelephone (the deserted operator) had deliberately blocked her from moving to a competitor. When contacting Pelephone to clarify the matter, the unacceptable motive for the blockage, the attempt to retain her as a customer and prevent her moving to a competitor, were discovered. Furthermore, injunctions are sought to prevent such blocking. On March 28, 2017, the court approved abandonment of the motion, striking out of the motion for certification and dismissal of the Plaintiff's personal claim.

Section 3.16.1(H) - on a claim and class action certification motion against Pelephone which alleges that Pelephone opted customers to the Smart Call service (a service that blocks incoming calls from various call centers, including the call centers of Pelephone's competitors), without their consent or knowledge - on May 7, 2017, the court authorized the applicant to abandon the motion for certification of the class action against Pelephone and it dismissed his personal claim against Pelephone.

Section 3.16.1(I) - On a claim and motion for its certification as a class action against Pelephone alleging that Pelephone overcharges for calls made to Israel from abroad on the Travel track, and that it charges a higher tariff instead of a call on the savings plan, due to the fact that the calls were made using the prefix 972 - on June 4, 2017, a ruling was issued dismissing the motion for certification and the Plaintiff's personal claim without ordering costs.

On September 12, 2017, Pelephone received a claim and a motion for its certification as a class action, which was filed in the Nazareth District Court. The plaintiff argues that Pelephone is in breach of the provisions of its operating license, by not blocking access to foreign internet browsing services for its subscribers who did not purchase a package for web-browsing abroad or who asked for voluntary access to the surfing services, and that it charges these subscribers retroactively when they purchase a web-browsing package and after accumulating a debt for the surfing services. The plaintiff argues that Pelephone therefore practices unjust enrichment. The total amount of the claim is estimated at NIS 262.5 million.

On October 29, 2017, Pelephone received a claim and a motion for its certification as a class action, which was filed against Pelephone and against another cellular company ("the Respondents") in the Central District Court. The subject of the action is the allegation that the Respondents make unlawful use of their customers' location data, thus violating the agreements with them, the operating licenses and various laws, including the Protection of Privacy Law, 1981. The plaintiffs ask the Respondents to compensate each of the class members with a one-time payment of NIS 500 for all the violations performed in 2017, plus NIS 2 for each day of further infringement of privacy from 2018 onwards. The plaintiffs estimate that the total loss caused to members of the class from Pelephone is NIS 850 million.

4. Bezeq International – international communications, Internet and NEP services

Section 4.13 – Legal proceedings

Section 4.13.1(D) - a financial claim with a motion to certify it as a class action, alleging that Bezeq misleads its customers with respect to internet surfing speed by NIS 187 million - the claim was struck out after the court ruled that a similar claim together with a motion for its certification as a class action which had been filed earlier (in March 2016) ("the Earlier Claim") would be the one to be heard. The hearing on the Earlier Motion was consolidated with a similar claim which had also been filed against the Company. The amount of the Earlier Claim cannot be estimated.

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

Section 5.1 - General information about the area of operations

Recently, competition has increased as new players are beginning to launch low-priced television services over the internet and existing players become more firmly established. In April 2017, Triple C Cloud Computing Ltd. launched an internet-based television service. In July 2017, Netflix launched a Hebrew interface and Partner also launched an internet-based television service. Furthermore, in March 2017, HOT launched a new internet-based television service and in September 2017 it began to cooperate with the Rami Levy Group, such that HOT converters will be available for purchase in Rami Levy chain stores and can also be used for viewing internet-based content.

DBS believes that this intensification of the competition could have a significant adverse effect on its operations and results.

DBS's opinion in this instance is forward-looking information, as defined in the Securities Law, based in part on the announcements of the new players. This assessment may not materialize, or it may materialize differently than expected, depending, inter alia on the dependence, manner in which these television services develop and become established, the entry of additional players, as well as the question of the application of regulations with respect to these television services.

Section 5.1.2.6 - at the date of this report, the Knesset is discussing a government bill to amend the Communications Law. Among other things, the bill addresses issues that are similar to the must-sell regulations in the area of sports content that were also discussed by the Filber Committee, including the granting of a license for broadcasting a sports channel or a significant sports operator by their producers. At the date of the report, DBS is unable to estimate whether the aforementioned bill will be implemented in legislation and in what format, and it is also unable to estimate what effect it will have on DBS's business.

Section 5.2 – Products and services

In November 2017, DBS launched an internet-based television service called "StingTV", which includes linear television channels, VOD service and other content of DBS, including original Israeli productions, children's content, documentaries, imported series and other content. The service is based on the Android TV operating system which allows content to be viewed by streaming, smart TV and on other terminal devices such as tablets, smartphones and PCs.

Section 5.6.1 - Competitors in the market

On the entry of new competitors to the television market, see the update to Section 5.1.

Section 5.11 – Human resources

Declaration of a labor dispute - on November 12, 2017, DBS was notified by the National Federation of Labor that a labor dispute had been declared in accordance with the Settlement of Labor Disputes Law, 1957, and a strike commencing on November 27, 2017 onwards (the "Notice"). According to the Notice, the issues in dispute are the intention to implement reforms and structural changes in DBS, including the intention to dismiss employees. At this stage, DBS is unable to assess the implications of the Notice.

Section 5.13.2 - Institutional financing

In July 2017, DBS repaid the balance of the Series A debentures, as a result of which the liens registered in favor of Trustee A were removed.

On the purchase of Series B debentures of DBS by the Company (while at the same time issuing debentures of the Company), see the update to Section 2.13.

Section 5.15.1 - S&P Maalot ratings for DBS and its debentures

On the affirmation of an iIAA/Stable rating by Standard & Poor's Maalot Ltd. for DBS (as part of the affirmation of the rating for the Company), see the update to Section 2.13.6.

Section 5.16.1 - Space segment leasing agreement

In April 2017, the Company's general meeting and the general meeting of Spacecom approved the engagement in the 2017 Agreement (see the Company's Immediate Report dated April 3, 2017, which is included in this report by way of reference).

At the beginning of April 2017, the Amos 2 satellite reached the end of its commercial life and ceased providing services to DBS. At the date of this report, DBS uses the space segments on the Amos 3 and Amos 7 satellites.

Section 5.17 – Legal proceedings

New legal proceedings

For information about a public investigation that was launched by the ISA in June 2017, in which context the CEO and CFO of DBS, among others, were questioned, see the update to Section 1.1.

For information about a motion to certify a class action that was filed, *inter alia*, against the CEO and CFO of DBS in connection with a transaction from 2015, in which the Company acquired from Eurocom D.B.S. Ltd (a company controlled by the Company's controlling shareholders) the balance of shares of the subsidiary DBS that it held in connection with a transaction to acquire shares of the Company held by Eurocom, see the update to Section 2.18.

For information about motions filed in the Tel Aviv District Court (Economics Division) to disclose documents prior to filing a motion for certification of a derivative claim under Section 198A of the Companies Law, that were filed by shareholders in the Company against the Company and DBS, to submit documents and information in connection with an agreement to purchase DBS shares by the Company, and specifically in connection with the Second Contingent Payment under that agreement, see the update to Section 2.18.

For information about motions filed by Company shareholders in the Tel Aviv District Court (Economics Division) in July 2017, to disclose documents prior to filing a motion for certification of a derivative claim under Section 198A of the Companies Law, against the Company and DBS, and to disclose certain documents in connection with an interested party transaction between DBS and Spacecom from 2013, as amended in 2017, see the update to Section 2.18.

For information about a motion to disclose documents prior to filing a motion for certification of a derivative action under Section 198A of the Companies Law, which was filed in July 2017 by a shareholder against the Company and DBS in the Tel Aviv District Court (Economics Division), in connection with benefits received by senior officers of the Company and DBS, in the context of the transaction to acquire shares of DBS by the Company and the transaction with Spacecom, see the update to Section 2.18.

Section 5.17.1 - Pending legal proceedings

Subsection (C) - on a claim and motion for its certification as a class action in connection with alleged discrimination of new DBS customers over existing customers - in August 2017, the court ruled that it does not see fit to separate the cases being litigated against DBS and HOT to parallel cases against the

Update to Chapter A (Description of Company Operations) of the Periodic Report for 2016

cellular companies. In the same month, DBS submitted notice whereby in proceedings against DBS the stage of submitting the arguments had not been concluded and that unlike the cellular sector, in the multi-channel television sector the regulator had conducted an in-depth review of the tariff-setting policy and had made a final, exhaustive decision which addresses the issues at the heart of the motions for certification against the Company. The court is expected to decide on the manner of continuing the proceeding after the plaintiffs submit their responses to DBS' response and an amended response will be submitted by HOT.

November 29, 2017

Date

Bezeq The Israel Telecommunication Corporation Ltd.

Names and titles of signatories:

David Granot, Acting Chairman of the Board of Directors

Stella Handler, CEO

Chapter B -

Board of Directors' Report on the State of the Company's Affairs for the Period Ended September 30, 2017



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

Board of Directors' Report on the State of the Company's Affairs for the Period Ended September 30, 2017

We hereby present the Board of Directors' report on the state of affairs of "Bezeq" - The Israel Telecommunication Corporation Ltd. ("the Company") and the consolidated Group companies (the Company and the consolidated companies, jointly - "the Group"), for the nine months ended September 30, 2017 ("the Period") and the three months then ended ("the Quarter").

The Board of Directors' report includes a condensed review of its subject-matter, and was prepared assuming the Board of Directors' report of December 31, 2016 is also available to the reader.

For information concerning a public investigation by the Israel Securities Authority which began on June 20, 2017, and the case's submission to the State Attorney's Office on November 6, 2017, see Note 1.2 to the financial statements.

At this time, the Company cannot assess the implications, if any, of the Israel Securities Authority's investigation and the case's submission to the State Attorney's Office. The auditors have drawn attention to the matter in their opinion of the financial statements.

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

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

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

The Group's results were as follows:

	1-9.2017	1-9.2016	Increase (decrease)		7-9.2017	7-9.2016	Increase (decrease)	
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%
Profit	1,030	1,059	(29)	(2.7)	322	394	(72)	(18.3)
EBITDA (operating profit before depreciation and amortization)	2,971	3,120	(149)	(4.8)	980	1,041	(61)	(5.9)

Operating profit was down in the Period and the Quarter, due to lower revenues. This decrease was partially offset, mainly by early adoption of IFRS 15 - Revenue from Contracts with Customers, whereby sales commissions are recognized as subscriber acquisition assets. See Note 3.2 to the financial statements.

Furthermore, during the Period, the decrease was also partially offset by a reduction in taxes on income, as compared to an increase in the same period last year. The reduction in the corresponding period was due to the effects of lower corporate tax rates on deferred tax assets.

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

1.1 Financial position

	September 30, 2017	September 30, 2016	Increase (decrease)	
	NIS millions	NIS millions	NIS millions	%
Cash and current investments	2,565	1,846	719	38.9
Eurocom D.B.S. Ltd.	43	29	14	48.3
Inventory	101	96	5	5.2
Current and non-current trade and other receivables	2,762	2,830	(68)	(2.4)
Broadcasting rights	457	450	7	1.6
Property, plant and equipment	6,817	6,840	(23)	(0.3)
Intangible assets	2,894	3,121	(227)	(7.3)
Deferred tax assets	1,014	1,103	(89)	(8.1)
Deferred costs and non-current investments	489	388	101	26.0
Total assets	17,142	16,703	439	2.6

Explanation
The increase was mainly attributable to higher cash balances in the Domestic Fixed-Line Communications segment, including receipt of loans and the issue of debentures. For more information, see Section 1.3 - Cash Flows, below.
The increase was due to adjusted estimates for the second contingent consideration and the fair value of the advanced payments for DBS's acquisition. See Note 4.2.1 to the financial statements.
The decrease was mainly due to a reduction in trade receivables in the Cellular Communications segment, due to lower revenues from handset sales and services. The decrease was partially offset, by an increase in overall receivables from real estate sales in the Domestic Fixed-Line Communications segment.
The decrease was mainly due to write-downs of excess acquisition costs attributed to intangible assets upon assuming control of DBS, and a decrease in investment (net of depreciation) in the Cellular Communications and Domestic Fixed-Line Communications segments.
Tax assets were reduced, mainly due to the reduction in the corporate tax rate starting 2017.
The increase was due to early adoption of IFRS 15 - Revenues from Contracts with Customers, whereby sales commissions are recognized as subscriber acquisition assets. See Note 3.2 to the financial statements.

1.1. Financial Position (Contd.)

	September 30, 2017	September 30, 2016	Increase (decrease)	
	NIS millions	NIS millions	NIS millions	%
Debt to financial institutions and debenture holders	11,533	11,246	287	2.6
Trade and other payables	1,807	1,599	208	13.0
Current and deferred tax liabilities	222	252	(30)	(11.9)
Liabilities towards Eurocom D.B.S. Ltd.	-	6	(6)	(100)
Employee benefits	511	517	(6)	(1.2)
Dividend payable	708	665	43	6.5
Other liabilities	434	391	43	11.0
Total liabilities	15,215	14,676	539	3.7
Total equity	1,927	2,027	(100)	(4.9)

Explanation
Receipt of loans and debenture issues were mostly offset by loan and debenture repayments.
An increase was seen across all Group segments, mainly due to payment deferrals as the end of the month fell on a Saturday (not a business day).
See Note 4.2.1 to the financial statements.
For more information, see Note 10 to the financial statements.
Equity comprises 11.2% of the balance sheet total, as compared to 12.1% of the balance sheet total on September 30, 2016.

1.2 Results of operations

1.2.1 Highlights

	1-9.2017	1-9.2016	Increase (decrease)		7-9.2017	7-9.2016	Increase (decrease)	
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%
Revenues	7,331	7,580	(249)	(3.3)	2,415	2,510	(95)	(3)
Depreciation and amortization	1,288	1,331	(43)	(3.2)	436	442	(6)	(14)
Salaries	1,500	1,509	(9)	(0.6)	502	501	1	0
General and operating expenses	2,888	2,984	(96)	(3.2)	956	994	(38)	(3)
Other operating income, net	28	33	(5)	(15.2)	23	26	(3)	(11)
Operating profit	1,683	1,789	(106)	(5.9)	544	599	(55)	(9)
Finance expenses, net	297	311	(14)	(4.5)	94	104	(10)	(9)
Share in losses of investees	4	4	-	-	-	2	(2)	(100)
Taxes on income	352	415	(63)	(15.2)	128	99	29	23
Profit for the period	1,030	1,059	(29)	(2.7)	322	394	(72)	(18)

Explanation
Revenues were down in the Group's primary segments.
The decrease was mainly attributable to the Domestic Fixed-Line Communications and Multi-Channel Television segments. There was also a decrease in the write-down of excess acquisition costs created upon assuming control of DBS.
The decrease in the Group's depreciation costs was partially offset by increased depreciation costs, mainly in the Cellular Communications segment, following amortization of a subscriber acquisition asset after early adoption of IFRS 15. See Note 3.2 to the financial statements.
The decrease was mainly attributable to lower expenses in the Cellular Communications segment. The decrease in the Group's expenses was affected, among other things, by early adoption of IFRS 15 - Revenue from Contracts with Customers, whereby distributor fees are recognized as subscriber acquisition assets. See Note 3.2 to the financial statements.
The decrease in net finance expenses in the Period was attributable to the Domestic Fixed-Line Communications segment. In the Quarter, the decrease was attributable to the Multi-Channel Television segment, and was partially offset, mainly by higher net finance expenses in Domestic Fixed-Line Communications operations.
Taxes were down in the Period, mainly due to a reduction in the tax asset and recognition of NIS 64 million in deferred tax expenses in the last-year period, following a reduction in the corporate tax rate.
In the Quarter, the increase in taxes was attributable to the Domestic Fixed-Line Communications segment.

1.2.2 Operating segments

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

	1-9.2017		1-9.2016		7-9.2017		7-9.2016	
	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues	NIS millions	% of total revenues
Revenues by operating segment								
Domestic Fixed-Line Communications	3,197	43.6	3,301	43.5	1,061	43.9	1,089	43.4
Cellular Communications	1,895	25.9	1,978	26.1	635	26.3	649	25.8
International Communications, Internet and NEP Services	1,158	15.8	1,156	15.3	367	15.2	384	15.3
Multi-Channel Television	1,246	17.0	1,307	17.2	406	16.8	434	17.3
Other and offsets	(165)	(2.3)	(162)	(2.1)	(54)	(2.2)	(46)	(1.8)
Total	7,331	100.0	7,580	100.0	2,415	100.0	2,510	100.0

	1-9.2017		1-9.2016		7-9.2017		7-9.2016	
	NIS millions	% of segment revenues	NIS millions	% of segment revenues	NIS millions	% of segment revenues	NIS millions	% of segment revenues
Operating profit by segment								
Domestic Fixed-Line Communications	1,501	47.0	1,595	48.3	492	46.4	519	47.7
Cellular Communications	57	3.0	36	1.8	22	3.5	27	4.2
International Communications, Internet and NEP Services	133	11.5	129	11.2	39	10.6	45	11.7
Multi-Channel Television	136	10.9	196	15.0	35	8.6	62	14.3
Other and offsets	(144)	-	(167)	-	(44)	-	(54)	-
Consolidated operating profit/ % of Group revenues	1,683	23.0	1,789	23.6	544	22.5	599	23.9

1.2.2. Operating segments

B. Domestic Fixed-Line Communications Segment

	1-9.2017	1-9.2016	Increase (decrease)		7-9.2017	7-9.2016	Increase (decrease)		
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	Explanation
Fixed-line telephony	1,053	1,133	(80)	(7.1)	345	375	(30)	(8.0)	The decrease was due to lower average revenues per phone line and a decrease in the number of lines.
Internet - infrastructure	1,229	1,191	38	3.2	413	399	14	3.5	The increase was mainly due to growth in the number of internet subscribers through the wholesale service and higher ARPU (retail), offset by a decline in the number of retail internet subscribers.
Transmission, data communications and others	915	977	(62)	(6.3)	303	315	(12)	(3.8)	The decrease was mainly due to lower transmission revenues from telecom operators.
Total revenues	3,197	3,301	(104)	(3.2)	1,061	1,089	(28)	(2.6)	
Depreciation and amortization	543	556	(13)	(2.3)	186	188	(2)	(1.1)	
Salaries	668	672	(4)	(0.6)	224	225	(1)	(0.4)	
General and operating expenses	514	525	(11)	(2.1)	183	183	-	-	The change was mainly due to a reduction in distributor fee costs, recognized as an asset following early adoption of IFRS 15, and a reduction in interconnect fees to telecom operators. These were partially offset, mainly by higher advertising costs.
Other operating income, net	29	47	(18)	(38.3)	24	26	(2)	(7.7)	Net income was down due to a NIS 11 million fine, imposed by the Ministry of Communications, and increased expenses on legal actions. These were partially offset (in the Quarter - completely offset) by higher capital gains on real estate sales.
Operating profit	1,501	1,595	(94)	(5.9)	492	519	(27)	(5.2)	
Finance expenses, net	281	299	(18)	(6.0)	107	93	14	15.1	The change in net finance expenses in the Period and the Quarter was affected by adjusted estimates for the second contingent consideration and update to the fair value estimate for advanced payments on DBS's acquisition (see Note 4.2.1 to the financial statements).
Taxes on income	308	299	9	3.0	109	83	26	31.3	Tax expenses were up due to a decrease in the last-year period and quarter following an update of previous-year taxes, and an increase in non-deductible expenses in the present Period and Quarter.
Segment profit	912	997	(85)	(8.5)	276	343	(67)	(19.5)	

1.2.2. Operating segments

C. Cellular Communications segment

	1-9.2017	1-9.2016	Increase (decrease)		7-9.2017	7-9.2016	Increase (decrease)		
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	Explanation
Services	1,345	1,379	(34)	(2.5)	461	468	(7)	(1.5)	The decrease was due to migration of existing customers to cheaper plans offering greater data volumes at current market prices. The decrease was offset by growth in the Company's subscriber base. This growth significantly slowed down the erosion in revenues seen in recent years.
Equipment sales	550	599	(49)	(8.1)	174	181	(7)	(3.9)	The decrease was mainly due to cancellation of purchase tax on imported cellular handsets which lowered prices. The decrease was further affected by lower sales volumes of cellular handsets.
Total revenues	1,895	1,978	(83)	(4.2)	635	649	(14)	(2.2)	
Depreciation and amortization	293	290	3	1.0	100	92	8	8.7	The increase was mainly due to depreciation costs on a subscriber acquisition asset, following early adoption of IFRS 15, and was offset in the Period by a decrease in current depreciation costs.
Salaries	286	284	2	0.7	94	94	-	-	
General and operating expenses	1,259	1,368	(111)	(8.0)	419	436	(17)	(3.9)	The decrease was mainly due to a reduction in distributor fees, recognized as an asset following early adoption of IFRS 15, and a reduction in the cost of handset sales as aforesaid. Results were also affected by a decrease in engineering expenses, updates to site leasing estimates, and continued cost-cutting efforts by the Company.
Operating profit	57	36	21	58.3	22	27	(5)	(18.5)	
Finance income, net	37	37	-	-	9	14	(5)	(35.7)	
Taxes on income	20	15	5	33.3	7	9	(2)	(22.2)	
Segment profit	74	58	16	27.6	24	32	(8)	(25.0)	

1.2.2 Operating segments

D. International Communications, Internet and NEP Services

	1-9.2017	1-9.2016	Increase (decrease)		7-9.2017	7-9.2016	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Revenues	1,158	1,156	2	0.2	367	384	(17)	(4.4)	In the Period, the increase was due to increased revenues from telecom solution equipment sales to businesses. The increase was offset by a decrease in revenues from call transfers between global operators (hubbing), lower revenues from international calls due to a decrease in call minutes driven by continued competition with cellular operators and increasing use of substitute software products, and lower revenues from data transfer. In the Quarter, the decrease was mainly due to lower revenues from international calls and call transfers between global operators, as aforesaid.
Depreciation and amortization	100	103	(3)	(2.9)	34	35	(1)	(2.8)	
Salaries	246	248	(2)	(0.8)	81	83	(2)	(2.4)	
General and operating expenses	679	662	17	2.6	214	221	(7)	(3.2)	In the Period and Quarter, cost of sales was up for telecom solution equipment for businesses. Internet service expenses were also up. The increase in the Period was partially offset (in the Quarter - completely offset) by lower expenses on call transfers between global operators, expenses on international calls, and data transfer expenses, corresponding with the aforesaid decrease in revenues, plus a decrease in customer recruitment commission expenses which were recognized as an asset following early adoption of IFRS 15.
Other expenses (income)	-	14	(14)	(100)	(1)	-	(1)	-	
Operating profit	133	129	4	3.1	39	45	(6)	(13.3)	
Finance expenses, net	6	7	(1)	(14.3)	3	2	1	50.0	Expenses in the last-year period were attributable to the collective labor agreement signed in the first quarter of 2016.
Share in the earnings of associates	-	1	(1)	(100)	-	1	(1)	(100)	
Tax expenses	31	31	-	-	9	11	(2)	(18.2)	
Segment profit	96	92	4	4.3	27	33	(6)	(18.2)	

1.2.2 Operating segments

E. Multi-Channel Television

	1-9.2017	1-9.2016	Increase (decrease)		7-9.2017	7-9.2016	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Revenues	1,246	1,307	(61)	(4.7)	406	434	(28)	(6.5)	The decrease was mostly due to a decrease in the average trade payables balance and a decrease in ARPU.
Depreciation and amortization	213	225	(12)	(5.3)	72	75	(3)	(4.0)	The decrease was mainly due to a reduction in investments.
Salaries	180	186	(6)	(3.2)	62	64	(2)	(3.1)	
General and operating expenses	717	700	17	2.4	237	233	4	1.7	The increase in the Period was mainly due to increased content expenses and advertising and marketing expenses. This increase was partially offset by a decrease in distribution fee costs, which were recognized as an asset following the early adoption of IFRS 15.
Operating profit	136	196	(60)	(30.6)	35	62	(27)	(43.5)	
Finance expenses (income), net	58	57	1	1.8	(1)	26	(27)	-	The change in the Quarter was mainly due to a change in the fair value of financial assets, and income from linkage differences on debentures.
Finance expenses for shareholder loans	-	465	(465)	(100)	-	178	(178)	(100)	No finance expenses were recognized in the present Period and Quarter, following conversion of the shareholder loans to equity at the end of the third quarter of 2016.
Tax expenses	333	1	332	-	159	-	159	-	The increase in tax expenses was mainly due to the tax asset being fully written-off following the change in expected profitability as a result of changes in Management expectations concerning the scope and severity of competition in the television market.
Segment loss	(255)	(327)	72	(22.0)	(123)	(142)	19	(13.4)	

1.3 Cash flow

	1-9.2017	1-9.2016	Increase (decrease)		7-9.2017	7-9.2016	Increase (decrease)		Explanation
	NIS millions	NIS millions	NIS millions	%	NIS millions	NIS millions	NIS millions	%	
Net cash from operating activities	2,683	2,694	(11)	(0.4)	982	902	80	8.9	The change in net cash from operating activities was mainly due to an increase in net cash in Domestic Fixed-Line Communications operations, and in the Quarter was also due to an increase in net cash in the Cellular Communications segment, due to changes in working capital, mainly attributable to trade and other payables. In the Quarter, the increase was partially offset (in the Period - fully offset) by a decrease in net cash in the Multi-Channel Television segment, due to a decrease in cash profits.
Net cash used in investing activities	(587)	(1,575)	988	(62.7)	(388)	(784)	396	(50.5)	Net cash used in investing activities was down, mainly due to taxes paid on finance income from shareholder loans to DBS to the amount of NIS 461 million in the last-year quarter, and net proceeds from disposal of bank and other deposits in the Domestic Fixed-Line Communications segment in the present Period, as compared to net investment in the last-year period.
Net cash from (used in) financing activities	(273)	(736)	463	(62.9)	23	(518)	541	-	The decrease in net cash used in financing activities was due to the receipt of additional loans to the amount of NIS 500 million in the present Quarter in the Domestic Fixed-Line Communications segment, as compared to payments to Eurocom D.B.S. for the purchase of DBS's loans and shares in the last-year period and quarter. Furthermore, in the present Period, there was a decrease in overall dividend payments, as compared to the same period last year. The decrease was partially offset by an increase in loan repayments in the Domestic Fixed-Line Communications segment.
Net increase (decrease) in cash	1,823	383	1,440	617	(400)	1,017	-		

Average volume in the reporting Period:

Long-term liabilities (including current maturities) to financial institutions and debenture holders: NIS 11,155 million.

Supplier credit: NIS 920 million.

Short-term credit to customers: NIS 1,980 million. Long-term credit to customers: NIS 422 million.

1.3. Cash Flows (contd.)

As of September 30, 2017, the Group had a working capital surplus of NIS 1,418 million, as compared to a working capital deficit of NIS 783 million on September 30, 2016.

According to its separate financial statements, the Company had a working capital surplus of NIS 921 million as of September 30, 2017, as compared to a working capital deficit of NIS 1,163 million on September 30, 2016.

The change from a working capital deficit to a surplus at the Group and Company level was mainly due to a decrease in current liabilities to financial institutions and debenture-holders, and an increase in cash balances.

2. Market Risk - Exposure and Management

Surplus liabilities exposed to changes in the nominal NIS-based interest rate were up NIS 1.3 billion, mainly following receipt of unlinked loans and expansion of Debentures (Series 9) (see Note 8 to the financial statements). This increase was partially offset, mainly by repayment of Debentures (Series 8) and scheduled loan payments in the Domestic Fixed-Line Communications segment (see Section 4 below). Other than the above, fair value sensitivity analysis data in accordance with changes in market factors as of September 30, 2017 do not differ materially from sensitivity analysis data as of December 31, 2016.

3. Disclosure Concerning the Company's Financial Reporting

3.1 Disclosure on the early adoption of IFRS 15 - Revenues from Contracts with Customers

Following publication of IFRS 15 - Revenues from Contracts with Customers ("the Standard"), the Company reviewed the Standard's possible impact on its financial statements, including by consultation with its auditing accountants and additional consultants. This review was conducted across all Group companies. As a result, the Company decided on the early adoption of the Standard, starting from the Company's financial statements as of March 31, 2017.

For information concerning the Standard's guidelines, its application, and adjustments to the Group's financial statements following the Standard's first-time application, see Note 3.2 to the financial statements.

Actions taken by the Group in preparation for adopting the Standard, and measures for reducing risk of errors in its financial statements:

1. The Group studied the possible impact of the Standard on its financial statements. This process included a review of the Standard's provisions, a review of professional information issued by international accounting firms and by the International Accounting Standards Board (IASB), and internal discussions with Group companies. Meetings were also held with the auditing accountants and additional accounting consultants. These meetings included a thorough discussion of issues raised by the Standard's application, and a review of its impact on the Group's companies. Each company documented the relevant issues and their impact on the financial statements.
2. The Group studied the Israel Securities Authorities' response to a pre-ruling request on the early adoption of the Standard, and Accounting Staff Position 11-4 - Disclosure on the Effects of Applying IFRS 15.
3. The Group has reviewed the necessary adjustments to the Group's information systems supporting the Standard's application.
4. The Group has studied its internal controls and adaptations needed to achieve effective control over proper first-time application of the Standard, in particular concerning the plausibility of significant judgments and estimates made in such application.

3.2 Disclosure of material valuations

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

	DBS
Subject of valuation	Value in use of D.B.S Satellite Services (1988) Ltd. in order to assess impairment of goodwill attributed in the Company's financial statements under IAS 36.
Date of valuation	September 30, 2017; valuation signed on November 27, 2017.
Value prior to the valuation	NIS 1,482 million carrying amount of the net operating assets of D.B.S. Satellite Services (1988) Ltd. (NIS 120 million - balance of goodwill).
Value set in the valuation	NIS 1,761 million. The Company concluded that there is no impairment requiring a write-down of goodwill recognized in the Company's books(*).
Assessor's identity and profile	Giza Singer Even Ltd. The work was done by a team headed by Mr. Nir Harush, CPA a partner in Giza Singer Even, who holds a BA in Business Administration and Accounting, and an MBA from the College of Management Academic Studies, and has extensive experience in economics and finance. The assessor has no dependence on the Company.
Valuation model	Discounted Cash Flow method (DCF).
Assumptions used in the valuation	Discount rate - 8.5% (post-tax). Permanent growth rate - 1%. Scrap value of total value set in valuation - 91%.

For more information, see Notes 4.2 and 7 to the financial statements.

(*) DBS was last valued as of June 30, 2017, at NIS 1,947 million, and as of December 31, 2016, at NIS 2,551 million.

- 3.3** Due to legal actions brought against the Group, which cannot yet be assessed or for which the Group cannot yet estimate its exposure, the auditors drew attention to these actions in their opinion concerning the financial statements.

4. Details of debt certificate series

4.1 Debentures (Series 8)

On June 1, 2017, a total of NIS 434,209,624 par value in bonds were repaid - final settlement.

4.2 Issuance of debentures

In May and June 2017, the Company completed the issue of NIS 1.1 billion par value in debentures, as follows:

- A. Public offering of NIS 384,467,000 par value Debentures (Series 9) issued as a series expansion, pursuant to the Company's shelf prospectus of May 2014, as amended in the clerical error amendment of June 2014 ("the Shelf Prospectus"), and the shelf offering report of May 25, 2017 ("the Shelf Offering Report"), for a total consideration of NIS 408 million.
- B. Issue of the Company's listed Debentures (Series 6 and 10) to holders of DBS's Debentures (Series B), traded on the TASE 'TACT Institutional' system ("DBS Debentures") in consideration for their holdings in DBS Debentures. The issue was conducted under the Shelf Prospectus and the Shelf Offering Report, as follows:

NIS 125,000,000 par value in DBS Debentures were exchanged for NIS 125,750,000 par value in Debentures (Series 6), and NIS 436,307,797 par value in DBS Debentures were exchanged for NIS 481,683,808 par value in Debentures (Series 10).

Following this issue, total liabilities for Debentures (Series 10) became material compared to the Company's overall liabilities balance.

- C. Two private placements of the Company's Debentures (Series 9) were made to classified investors, at a total value of NIS 108,000,000 par value. These placements are subject to the resale restrictions set forth in Section 15C to the Securities Law and the Securities Regulations (Details Concerning Sections 15A to 15C to the Law), 2000. The placements were made for a total consideration of NIS 114 million.

For more information, see Note 8.2 to the financial statements.

4.3 Debenture ratings

On April 24, 2017, Standard & Poor's Maalot Ltd. ("Maalot") affirmed its ilAA/Stable rating for the Company and its Debentures (Series 6-10), as detailed in the ratings report published in the Company's immediate report of April 24, 2017 (ref. no. 2017-01-034792), included herein by way of reference.

Furthermore, as part of the issuance of Company debentures through an expansion of existing series and a swap of DBS's debentures as aforesaid, the following ratings were approved:

- A. Midroog Ltd. approved an Aa2.il-Stable rating for the Company's Debentures (Series 6-10), and for up to NIS 1.1 billion par value in Company debentures issued through an expansion of existing series of debentures and/or through a swap of DBS debentures for debentures issued by the Company. For more information, see the Company's immediate reports of May 21, 2017 (ref. no. 2017-01-042550), and May 25, 2017 (ref. no. 2017-01-043915), included herein by way of reference.
- B. Maalot approved an ilAA/Stable rating for up to NIS 1.1 billion in debentures to be issued by the Company through an expansion of one or more of Series 6-10, for cash and/or against a swap for DBS debentures. For more information, see the Company's immediate reports of May 22, 2017 (ref. no. 2017-01-042862), and May 25, 2017 (ref. no. 2017-01-043918), included herein by way of reference.

5. Miscellaneous

For information concerning the liabilities balances of the reporting corporation and those companies consolidated in its financial statements as of September 30, 2017, see the Company's reporting form on the MAGNA system, dated November 30, 2017.

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

David Granot

Acting Chairman of the Board of
Directors

Stella Handler

CEO

Signed: November 29, 2017

A collage of financial data visualization elements. It includes a silver calculator, a magnifying glass over a document with a table and bar chart, and several line and bar charts. The table lists metals and their prices: Gold (\$1879.21), Silver (\$455.59), Steel (\$507.74), Manganese (\$284.48), Chrome (\$192.11), Bauxite (\$116.43), Flax, Wool, and Sateen. The bar chart shows prices for various metals. The line charts show price trends over time, with one chart dated 26 Feb 2009 and 27 Feb 1.

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

Contents	Page
Review Report	1
Condensed Consolidated Interim Financial Statements as of September 30, 2017 (Unaudited)	
Condensed Consolidated Interim Statements of Financial Position	2
Condensed Consolidated Interim Statements of Income	4
Condensed Consolidated Interim Statements of Comprehensive Income	5
Condensed Consolidated Interim Statements of Changes in Equity	6
Condensed Consolidated Interim Statements of Cash Flows	8
Notes to the Condensed Consolidated Interim Financial Statements	
1 General	10
2 Basis of Preparation	10
3 Reporting Principles and Accounting Policy	10
4 Group Entities	13
5 Income Tax	14
6 Fixed Assets	14
7 Analysis of Impairment of the Multi-Channel Television Sector	14
8 Debentures, Loans and Borrowings	15
9 Contingent Liabilities	16
10 Equity	18
11 Revenues	18
12 General and Operating Expenses	19
13 Other Operating Income, Net	19
14 Financial Instruments	20
15 Segment Reporting	21
16 Condensed Financial Statements of Pelephone, Bezeq International, and DBS Satellite Services (1998) Ltd.	27



Somekh Chaikin
KPMG Millennium Tower
17 Ha-Arbaa Street, PO Box 609
Tel Aviv 6100601, Israel
800068403

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

Introduction

We have reviewed the accompanying financial information of “Bezeq” -The Israel Telecommunication Corporation Ltd. and its subsidiaries (hereinafter – “the Group”) comprising of the condensed consolidated interim statement of financial position as of September 30, 2017 and the related condensed consolidated interim statements of income, comprehensive income, changes in equity and cash flows for the nine and three-month periods then ended. The Board of Directors and Management are responsible for the preparation and presentation of this interim financial information in accordance with IAS 34 “Interim Financial Reporting”, and are also responsible for the preparation of financial information for this interim period in accordance with Section D of the Securities Regulations (Periodic and Immediate Reports), 1970. Our responsibility is to express a conclusion on this interim financial information based on our review.

We did not review the condensed interim financial information of a certain consolidated subsidiary whose assets constitute 1% of the total consolidated assets as of September 30 2017, and whose revenues constitute 1% of the total consolidated revenues for the nine and three month periods then ended. The condensed interim financial information of that company was reviewed by other auditors whose review report thereon was furnished to us, and our conclusion, insofar as it relates to amounts emanating from the financial information of that company, is based solely on the said review report of the other auditors.

Scope of Review

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

Conclusion

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

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

Without qualifying our abovementioned conclusion, we draw attention to Note 1.2 regarding the Israel Securities Authority's (ISA) investigation of the suspicion of committing offenses under the Israel Securities'



Somekh Chaikin
KPMG Millennium Tower
17 Ha-Arbaa Street, PO Box 609
Tel Aviv 6100601, Israel
800068403

Law and Penal Law, in respect to transactions related to the controlling shareholder, and the transfer of the investigation file to the District Attorney's Office. As stated in the abovementioned note, at this stage, the Company is unable to assess the implications of the ISA investigation and the transfer of the investigation to the District Attorney's Office, if any.

In addition, without qualifying our abovementioned conclusion, we draw attention to numerous lawsuits filed against the Group which cannot yet be assessed or the exposure in respect thereof cannot yet be estimated, as set forth in Note 9.

Somekh Chaikin
Certified Public Accountants (Isr.)

November 29, 2017

Condensed Consolidated Interim Statements of Financial Position

		September 30, 2017*	September 30, 2016	December 31, 2016
		(Unaudited)	(Unaudited)	(Audited)
Assets		NIS million	NIS million	NIS million
Cash and cash equivalents		2,471	938	648
Investments		94	908	586
Trade receivables		1,948	1,998	2,000
Other receivables		294	191	219
Eurocom DBS Ltd., related party	4.2.1	43	29	-
Inventory		101	96	106
Total current assets		4,951	4,160	3,559
Trade and other receivables		520	641	644
Broadcasting rights, net of rights exercised		457	450	432
Fixed assets	6	6,817	6,840	6,876
Intangible assets		2,894	3,121	3,047
Deferred tax assets		1,014	1,103	1,007
Deferred expenses and non-current investments		489	388	382
Total non-current assets		12,191	12,543	12,388
Total assets		17,142	16,703	15,947

Condensed Consolidated Interim Statements of Financial Position (Contd.)

	September 30, 2017*	September 30, 2016	December 31, 2016
	(Unaudited)	(Unaudited)	(Audited)
Liabilities and equity	NIS million	NIS million	NIS million
Debtures, loans and borrowings (Note 8)	555	2,135	1,825
Trade and other payables	1,807	1,599	1,610
Current tax liabilities	118	171	104
Liability to Eurocom DBS Ltd., related party 4.2.1	-	6	32
Employee benefits	251	280	315
Provisions	94	87	80
Dividend payable	708	665	-
Total current liabilities	3,533	4,943	3,966
Loans and debtures	10,978	9,111	9,128
Employee benefits	260	237	258
Derivatives and other liabilities	292	257	244
Deferred tax liabilities	104	81	101
Provisions	48	47	47
Total non-current liabilities	11,682	9,733	9,778
Total liabilities	15,215	14,676	13,744
Total equity	1,927	2,027	2,203
Total liabilities and equity	17,142	16,703	15,947

David Granot
Acting Chairman of the
Board of Directors

Stella Handler
CEO

Yali Rothenberg
CFO Bezeq Group

Date of approval of the financial statements: November 29, 2017

* See Note 3.2 for information about early adoption of IFRS 15, Revenue from Contracts with Customers.

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

Condensed Consolidated Interim Statements of Income

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017*	2016	2017*	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues (Note 11)	7,331	7,580	2,415	2,510	10,084
Costs of activity					
General and operating expenses (Note 12)	2,888	2,984	956	994	4,012
Salaries	1,500	1,509	502	501	2,012
Depreciation and amortization	1,288	1,331	436	442	1,739
Other operating income, net (Note 13)	(28)	(33)	(23)	(26)	-
	5,648	5,791	1,871	1,911	7,763
Operating income	1,683	1,789	544	599	2,321
Financing expenses (income)					
Financing expenses	358	360	112	119	508
Financing income	(61)	(49)	(18)	(15)	(61)
Financing expenses, net	297	311	94	104	447
Profit after financing expenses, net	1,386	1,478	450	495	1,874
Share in losses of equity-accounted investees	(4)	(4)	-	(2)	(5)
Profit before income tax	1,382	1,474	450	493	1,869
Income tax	352	415	128	99	625
Profit for the period	1,030	1,059	322	394	1,244
Basic and diluted earnings per share	0.37	0.38	0.12	0.14	0.45

* See Note 3.2 for information about early adoption of IFRS 15, Revenue from Contracts with Customers.

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

Condensed Consolidated Interim Statements of Comprehensive Income

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017*	2016	2017*	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Profit for the period	1,030	1,059	322	394	1,244
Items of other comprehensive loss (net of tax)	(20)	(6)	(12)	(1)	(15)
Total comprehensive income for the period	1,010	1,053	310	393	1,229

* See Note 3.2 for information about early adoption of IFRS 15, Revenue from Contracts with Customers.

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

Condensed Consolidated Interim Statements of Changes in Equity

	Share capital	Share premium	Capital reserve for employee options	Capital reserve for transactions between a corporation and a controlling shareholder	Other reserves	Deficit	Total
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Nine months ended September 30, 2017 (Unaudited)*							
Balance as of January 1, 2017	3,878	384	-	390	(88)	(2,361)	2,203
Profit for the period	-	-	-	-	-	1,030	1,030
Other comprehensive loss for the period, net of tax	-	-	-	-	(20)	-	(20)
Total comprehensive income for the period	-	-	-	-	(20)	1,030	1,010
Transactions with shareholders recognized directly in equity							
Dividends to Company shareholders (see Note 10)	-	-	-	-	-	(1,286)	(1,286)
Balance as of September 30, 2017	3,878	384	-	390	(108)	(2,617)	1,927
Nine months ended September 30, 2016 (Unaudited)							
Balance as of January 1, 2016	3,874	368	16	390	(98)	(2,139)	2,411
Profit for the period	-	-	-	-	-	1,059	1,059
Other comprehensive loss for the period, net of tax	-	-	-	-	(6)	-	(6)
Total comprehensive income for the period	-	-	-	-	(6)	1,059	1,053
Transactions with shareholders recognized directly in equity							
Dividend to Company shareholders	-	-	-	-	-	(1,441)	(1,441)
Exercise of options for shares	4	16	(16)	-	-	-	4
Balance as of September 30, 2016	3,878	384	-	390	(104)	(2,521)	2,027

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

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

	Share capital	Share premium	Capital reserve for employee options	Capital reserve for transactions between a corporation and a controlling shareholder	Other reserves	Deficit	Total
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Three months ended September 30, 2017 (Unaudited)*							
Balance as of July 1, 2017	3,878	384	-	390	(96)	(2,231)	2,325
Profit for the period	-	-	-	-	-	322	322
Other comprehensive loss for the period, net of tax	-	-	-	-	(12)	-	(12)
Total comprehensive income for the period	-	-	-	-	(12)	322	310
Transactions with shareholders recognized directly in equity							
Dividends to Company shareholders (see Note 10)	-	-	-	-	-	(708)	(708)
Balance as of September 30, 2017	3,878	384	-	390	(108)	(2,617)	1,927
Three months ended September 30, 2016 (Unaudited)							
Balance as of July 1, 2016	3,878	384	-	390	(103)	(2,250)	2,299
Profit for the period	-	-	-	-	-	394	394
Other comprehensive loss for the period, net of tax	-	-	-	-	(1)	-	(1)
Total comprehensive income for the period	-	-	-	-	(1)	394	393
Transactions with shareholders recognized directly in equity							
Dividend to Company shareholders	-	-	-	-	-	(665)	(665)
Balance as of September 30, 2016	3,878	384	-	390	(104)	(2,521)	2,027
Year ended December 31, 2016 (Audited)							
Balance as of January 1, 2016	3,874	368	16	390	(98)	(2,139)	2,411
Income in 2016	-	-	-	-	-	1,244	1,244
Other comprehensive income (loss) for the year, net of tax	-	-	-	-	10	(25)	(15)
Total comprehensive income for 2016	-	-	-	-	10	1,219	1,229
Transactions with shareholders recognized directly in equity							
Dividend to Company shareholders	-	-	-	-	-	(1,441)	(1,441)
Exercise of options for shares	4	16	(16)	-	-	-	4
Balance as of December 31, 2016	3,878	384	-	390	(88)	(2,361)	2,203

* See Note 3.2 for information about early adoption of IFRS 15, Revenue from Contracts with Customers.

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

Condensed Consolidated Interim Statements of Cash Flows

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017*	2016	2017*	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows from operating activities					
Profit for the period	1,030	1,059	322	394	1,244
Adjustments:					
Depreciation and amortization	1,288	1,331	436	442	1,739
Share in losses of equity-accounted investees	4	4	-	2	5
Financing expenses, net	321	335	94	115	474
Capital gain, net	(64)	(62)	(45)	(22)	(107)
Income tax expenses	352	415	128	99	625
Change in trade and other receivables	121	116	105	53	106
Change in inventory	(10)	7	2	2	(20)
Change in trade and other payables	64	(110)	103	(12)	(24)
Change in provisions	15	(12)	16	(3)	(19)
Change in employee benefits	(62)	(100)	(65)	(92)	(65)
Change in other liabilities	(30)	8	4	16	23
Net income tax paid	(346)	(297)	(118)	(92)	(455)
Net cash from operating activities	2,683	2,694	982	902	3,526
Cash flow used for investing activities					
Purchase of fixed assets	(835)	(901)	(255)	(290)	(1,193)
Investment in intangible assets and deferred expenses	(304)	(180)	(98)	(59)	(223)
Investment in deposits with banks and others	(76)	(867)	(76)	-	(917)
Disposal of deposits with banks and others	558	711	-	-	1,088
Proceeds from the sale of fixed assets	76	122	48	24	138
Tax payment for shareholder's loans	-	(461)	-	(461)	(461)
Miscellaneous	(6)	1	(7)	2	1
Net cash used in investing activities	(587)	(1,575)	(388)	(784)	(1,567)

Condensed Consolidated Interim Statements of Cash Flows

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017*	2016	2017*	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows used in financing activities					
Issue of debentures and receipt of loans (Note 8)	1,917	1,661	500	-	2,161
Repayment of debentures and loans	(1,325)	(1,085)	(456)	(279)	(1,841)
Dividend paid (Note 10)	(578)	(776)	-	-	(1,441)
Interest paid	(217)	(256)	(18)	(32)	(458)
Payment to Eurocom DBS for acquisition of DBS loans and shares (Note 4.2.1)	(61)	(256)	-	(198)	(256)
Miscellaneous	(9)	(24)	(3)	(9)	(31)
Net cash from (used in) financing activities	(273)	(736)	23	(518)	(1,866)
Increase (decrease) in cash and cash equivalents, net	1,823	383	617	(400)	93
Cash and cash equivalents at beginning of period	648	555	1,854	1,338	555
Cash and cash equivalents at end of period	2,471	938	2,471	938	648

* See Note 3.2 for information about early adoption of IFRS 15, Revenue from Contracts with Customers.

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

1. General

1.1 Reporting Entity

Bezeq – The Israel Telecommunication Corporation Limited (“the Company”) is a company registered in Israel whose shares are traded on the Tel Aviv Stock Exchange. The consolidated financial statements of the Company include those of the Company and its subsidiaries (together referred to as “the Group”). The Group is a principal provider of communication services in Israel (see also Note 15 – Segment Reporting).

1.2 Investigation of the Israel Securities Authority

On June 20, 2017, the Israel Securities Authority began an open investigation (“the Investigation”), which included searches at the offices of the Company and of DBS and seizure of documents.

On November 6, 2017, the Israel Securities Authority issued a press release regarding the conclusion of the Investigation and the transfer of the Investigation file to the Tel Aviv District Attorney (Taxation and Economics). In accordance with the notice, the Israel Securities Authority concluded that there is prima facie evidence establishing the involvement of the main suspects in the case, in offenses of (1) fraudulently receiving funds in connection with the entitlement of the Company’s controlling shareholder to a consideration of NIS 170 million as part of the transaction for the Company’s purchase of DBS shares from the Company’s controlling shareholder, a consideration contingent on certain targets to be met by DBS; (2) leaking the material of the independent committee of the Company’s Board of Directors that examined interested party transactions (the transaction for the acquisition of DBS shares by the Company and the transaction between DBS and Space Communications Ltd. for the purchase of satellite segments for DBS) to the Company’s controlling shareholder and associates ;(3) promoting the Company’s interests in the Ministry of Communications in violation of the Penal Law and the Israel Securities Law. The notice further stated that the Investigation file was transferred to the District Attorney’s Office and that the District Attorney’s Office is authorized to decide on how to continue with this case. It is noted that, in this context, on November 20, 2017 the Company and DBS received Notice to Suspect according to which the Investigation file under which the Company and DBS were investigated as suspects was sent to the District Attorney’s Office for review.

At this stage, the Company is unable to assess the implications of the ISA Investigation and the transfer of the Investigation to the District Attorney’s Office, if any.

2. Basis of Preparation

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

2.2 The condensed consolidated interim financial statements do not contain all the information required in full annual financial statements, and should be reviewed in the context of the annual financial statements of the Company and its subsidiaries as of December 31, 2016 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.

2.3 The condensed consolidated interim financial statements were approved by the Board of Directors on November 29, 2017.

2.4 Use of estimates and judgments

The preparation of the condensed consolidated interim financial statements in conformity 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, liabilities, income and expenses. Actual results may differ from these estimates.

The judgments made by management when applying the Group’s accounting policy and the principal assumptions underlying assessments that involve uncertainty, are consistent with those

used in the Annual Financial Statements, other than as set out in Note 3 regarding early application of IFRS 15.

3. Reporting Principles and Accounting Policy

3.1 The Group's accounting policy applied in these condensed consolidated interim financial statements is consistent with the policy applied in the Annual Financial Statements, except as described in section 3.2 below.

3.2 Initial application of new standards

3.2.1 As from January 1, 2017, the Group has early adopted IFRS 15, Revenue from Contracts with Customers ("IFRS 15"), which sets out guidelines for recognition of revenue.

IFRS 15 replaces IAS 18, Revenue and presents a new model for recognition of revenue from contracts with customers. The model includes five steps for analyzing transactions so as to determine when to recognize revenue and at what amount:

- A. Identifying the contract with the customer.
- B. Identifying separate performance obligations in the contract.
- C. Determining the transaction price.
- D. Allocating the transaction price to separate performance obligations.
- E. Recognizing revenue when the performance obligations are satisfied.

In accordance with the model, the Group recognizes revenue when the customer gains control over the goods or services. Revenue is based on the consideration that the Group expects to receive for the transfer of the goods or services promised to the customer. Revenue is recognized when it is expected that the economic benefits will flow to the Group and if the revenues and costs can be measured reliably.

Application of the model did not have a material effect on the measurement of the Group's revenue in the reporting period, compared to the provisions of the previous standard.

The main effect of the Group's application of IFRS 15 is the accounting treatment for the incremental costs of obtaining a contract with a customer ("Subscriber Acquisition"), which, in accordance with IFRS 15, are recognized as an asset when the costs are attributed directly to a contract that the Group can specifically identify, they produce or improve the Group's resources that will be used for its future performance obligation and it is probable that the Group will recover these costs, and not only where there is an obligation of the customer to acquire services from the Company for a defined period.

Accordingly, direct commissions paid to agents and sales employees of the Group for sales and upgrades under agreements that do not include an obligation period for the customer, are recognized as an asset for obtaining a contract instead of an expense in the statement of income, since the Group expects to recover these costs under the contracts.

An asset for obtaining a contract is amortized in accordance with the expected average churn rate of subscribers based on the type of subscriber and the service received (mainly over 3-4 years).

Contract acquisition costs that would arise regardless of whether the contract was obtained are recognized as an expense when incurred.

3.2.2 The Group applied IFRS 15 using the cumulative effect approach without a restatement of comparative figures.

As part of initial implementation of IFRS 15, the Group has chosen to apply the expedients in the transitional provisions, according to which the cumulative effect approach is applied only for contracts not yet complete at the transition date and the accounting treatment for the contracts completed at the transition date will not be amended.

The contracts that are renewed every month and that may be cancelled by the customer at any time, without any penalty, are contracts that ended at the date of initial application of IFRS 15. Therefore, Subscriber Acquisition costs incurred prior to January 1, 2017

and recognized in the statement of income as an expense were not accounted for retroactively.

- 3.2.3 Implementation of the accounting policy described above requires the Group companies to exercise their discretion to estimate the expected service period and the anticipated subscriber churn rate. Changes in such estimates may result in a change in depreciation and amortization expenses and changes in the Subscriber Acquisition asset.
- 3.2.4 Other than the accounting treatment of Subscriber Acquisition costs, implementation of IFRS 15 had no other material effects on the financial statements. In addition, implementation of IFRS 15 had no effect on retained earnings as of the transition date.
- 3.2.5 The tables below summarize the effects on the condensed consolidated interim statement of financial position as of September 30, 2017 and on the condensed consolidated interim statements of income and cash flows for the nine and three months then ended, assuming that the Group's previous policy regarding Subscriber Acquisition costs continued during that period.

Effect on the condensed consolidated interim statement of financial position as of September 30, 2017

	In accordance with the previous policy (Unaudited) NIS million	Change (Unaudited) NIS million	In accordance with IFRS 15 (Unaudited) NIS million
Net subscriber acquisition asset (stated as deferred expenses and non-current investments)	5	93	98
Equity	1,856	71	1,927

Effect on the consolidated interim statement of income for the nine and three months ended September 30, 2017:

	Nine months ended September 30, 2017			Three months ended September 30, 2017		
	In accordance with the previous policy (Unaudited) NIS million	Change (Unaudited) NIS million	In accordance with IFRS 15 (Unaudited) NIS million	In accordance with the previous policy (Unaudited) NIS million	Change (Unaudited) NIS million	In accordance with IFRS 15 (Unaudited) NIS million
General and operating expenses	2,989	(101)	2,888	993	(37)	956
Salaries	1,525	(25)	1,500	511	(9)	502
Depreciation and amortization expenses	1,255	33	1,288	419	17	436
Operating income	1,590	93	1,683	515	29	544
Profit after financing expenses	1,293	93	1,386	421	29	450
Profit before income tax	1,289	93	1,382	421	29	450
Income tax	330	22	352	121	7	128
Profit for the period	959	71	1,030	300	22	322

Effect on the consolidated interim statement of cash flow for the three months ended September 30, 2017:

	Nine months ended September 30, 2017			Three months ended September 30, 2017		
	In accordance with the previous policy	Change	In accordance with IFRS 15	In accordance with the previous policy	Change	In accordance with IFRS 15
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Net cash from operating activities	2,557	126	2,683	936	46	982
Net cash from (used in) investing activities	(461)	(126)	(587)	(342)	(46)	(388)

3.3 New standards and interpretations not yet adopted

A detailed description of the standards not yet adopted appears in Note 2.17 to the Annual Financial Statements. Following are details about the material changes since the publication of the Annual Financial Statements:

- 3.3.1 Further to Note 2.17.3 to the Annual Financial Statements, the Group companies are continuing to assess the anticipated effect of IFRS 16, "Leases", including an assessment of possible early implementation of IFRS 16 as from January 1, 2018. At this stage, the Group is unable to reliably assess the quantitative effect of implementation of IFRS 16 on its financial statements.
- 3.3.2 In June 2017, the IFRS Interpretations Committee issued IFRIC 23, Uncertainty over Income Tax Treatments ("IFRIC 23"). IFRIC 23 clarifies application of recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. IFRIC 23 will be effective for annual periods beginning on January 1, 2019, with early application being permitted. The Group believes that application of IFRIC 23 will not have a material effect on the financial statements.

4. Group Entities

- 4.1 A detailed description of the Group entities appears in Note 11 to the Annual Financial Statements. Below is a description of the material changes that occurred in connection with the Group entities since publication of the Annual Financial Statements.

4.2 DBS Satellite Services (1998) Ltd. ("DBS")

- 4.2.1 Further to Note 11.2.1 to the Annual Financial Statements regarding the additional consideration to be paid to Eurocom DBS based on the operating results of DBS in the three years as from the acquisition transaction, in March 2017 the Company paid the second advance payment of NIS 57 million (plus linkage differences) for the operating results of DBS in 2016. As of September 30, 2017, the cumulative advances paid to Eurocom DBS amounted to NIS 119 million (including interest).

As of June 30, 2017, the Company updated the estimated second contingent consideration in view of its assessment that it is highly unlikely that there will be a merger with DBS in 2017. Taking into consideration the revised free cash flow forecast of DBS for 2017, in the second quarter of 2017, the Company eliminated the liability of NIS 84 million to DBS in its financial statements. Elimination of the liability is recognized in the statement of income under financing income/expenses. As of September 30, 2017, the estimate remains the same.

As a result of the aforesaid, the advance payments received by Eurocom DBS from the Company as of September 30, 2017 amounts to NIS 113 million (after offsetting a liability of NIS 6 million for the first contingent consideration). In accordance with the agreement between the parties, if the final amount is less than the amount of advance payments, Eurocom DBS will return the difference to the Company immediately after the final settlement, which is expected to be shortly after the signing of the Company's financial statements for 2017 (or on the merger date, whichever is earlier). The repayment bears annual interest at a rate of 4%.

The Company estimated the fair value of the amount expected to be recovered from the excess of the advance payments, and taking into consideration the solvency of Eurocom DBS, the value of the debt at June 30, 2017 was estimated at NIS 56 million (representing 50% of the balance) and as at September 30, 2017 the estimated value was revised to NIS 43 million (representing 40% of the balance).

The revised value of NIS 57 million in the second quarter and NIS 13 million in the third quarter were included under financing expenses in the statement of income.

- 4.2.2 Further to Note 17.2 to the Annual Financial Statements regarding the agreement of DBS for space segment capacity, Space Communications Ltd. ("Space") notified DBS that the Amos 2 satellite had reached the end of its commercial life and is no longer fit to make television broadcasts for DBS. Accordingly, as from March 31, 2017, DBS no longer uses the Amos 2 satellite and is currently using the Amos 3 and Amos 7 satellites.

On April 3, 2017, the general meeting of the Company's shareholders approved the Company's vote at the general meeting of DBS in favor of the agreement between DBS and Space, with an amendment/addition to the existing agreement between the parties dated November 4, 2013 for the lease of satellite segments in space satellites, as described in Note 17.2 to the Annual Financial Statements, including implementation of the agreement.

- 4.2.3 Following the conversion of the shareholders loans and the investment in the equity of DBS in 2016 by the Company, the equity of DBS as of September 30, 2017 and December 31, 2016 amounted to NIS 337 million and NIS 592 million, respectively. As of September 30, 2017, its working capital deficit amounts to NIS 431 million.

The management of DBS believes that the financial resources at its disposal, which include the deficit in working capital, repayment of loans and receipt of loans from the Company, will be sufficient for the operations of DBS for the coming year.

- 4.2.4 See Note 8 below regarding the exchange of DBS Debentures (Series B) with Debentures (Series 6 and 10) issued by the Company.
- 4.2.5 Further to Note 12.4 to the Annual Financial Statements, in July 2017, DBS repaid the balance of Debentures (Series A), and as a result, the liens registered in favor of Trustee A of the Debentures were lifted.
- 4.2.6 For information about the investigation by the Israel Securities Authority that began on June 20, 2017, which involves suspicions of offenses under the Israel Securities Law and the Penal Law, see Note 1.2 above.

5. Income Tax

Further to Note 6.6.3 to the Annual Financial Statements, regarding the best-judgment assessment for 2011 received by the Company, the Company filed an objection against the position of the Tax Authority and is holding discussions with the Authority. In addition, assessment discussions are being held for 2012-2014, including discussions of the issues included in the 2011 assessment. Subsequent to the balance sheet date, the parties reached an agreement which has not yet been formally signed.

6. Fixed Assets

Further to Note 8.5 to the Annual Financial Statements regarding the installation of a fiber optic network that will reach the customer's home, in the reporting period, the fiber deployment reached the state required for their operation when it is decided which technology will be used, and the Company began to amortize the network over 25 years.

7. Analysis of Impairment of the Multi-Channel Television Sector

In view of the intensifying competition, DBS updated its forecasts and formulated a new business plan to address competition. Due to the above, the Company estimated the recoverable amount of the multi-channel television cash-generating unit as of September 30, 2017 (following the earlier estimate as of June 30, 2017, subsequent to which deduction for impairment of the unit as of the same date was not required).

The value in use of the multi-channel television cash-generating unit for Bezeq Group was calculated by discounting future cash flows (DCF) based on a five year cash flow forecast as of the end of the current period with the addition of the salvage value. The cash flow forecast is based on the results of DBS in recent years, so that the future growth and market share are affected by trends in the multi-channel television market, such as competition, regulation, and the entry of new players. The income forecast is based on assumptions regarding the number of users and the average revenue per user. A key assumption of the forecast is that competition in the market will continue in the mid-term, affecting the Company's operations by satellite TV subscriber churn and a decrease in the average revenue per user. At the same time, the launch of Sting TV is expected to lead to an increase in the number of subscribers at a slightly higher rate than this satellite TV subscriber churn.

The operating, sales, marketing and investment expenses were adjusted to the volume of DBS operations. The nominal capital price taken into account was 8.5% (after tax). In addition, a permanent growth rate of 1% was assumed. The valuation was prepared by an external appraiser. Based on the foregoing valuation, the Group was not required to amortize the impairment of the multi-channel television cash-generating unit.

8. **Debentures, Loans and Borrowings**

8.1 Further to Note 12.6 to the Annual Financial Statements regarding the undertakings received from banks and institutions to provide credit for the Company for 2017, on June 15, 2017, the Company received credit facilities from banks and financial institutions amounting to NIS 900 million, and on September 26, 2017, amounting to NIS 500 million, in accordance with the undertakings by the banks and financial institutions. The credit terms are set out in Note 12.6 to the Annual Financial Statements.

8.2 In May and June 2017, the Company completed the offering of the Company's debentures for a total par value of NIS 1.1 billion, par value as follows:

8.2.1 A public offering of NIS 384,467,000 par value Debentures (Series 9) by way of expansion of the series, under the Company's shelf prospectus of May 2014, as amended for a typographical error in June 2014 ("the Shelf Prospectus") and the shelf offering memorandum of May 25, 2017 ("the Shelf Offering Memorandum"). The total consideration (gross) that was received for this offering amounted to NIS 408 million.

8.2.2 An offering of Debentures (Series 6 and 10) that are traded by the Company, to the holders of Debentures (Series B) of DBS, which are listed on the TACT-Institutional system of the TASE ("the DBS Debentures") in return for the DBS Debentures that they hold. The offering was carried out in accordance with the Shelf Prospectus and the Shelf Offering Memorandum as follows: NIS 125,000,000 par value DBS Debentures were exchanged for NIS 125,750,000 par value Debentures (Series 6), and NIS 436,307,797 par value DBS Debentures were exchanged for NIS 481,683,808 par value Debentures (Series 10).

An exchange of debentures having substantially different terms was accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability at fair value. Accordingly, in the second quarter of 2017, the Group recognized financing expenses of NIS 13 million, for the difference between the amortized cost of the DBS Debentures and the fair value of Debentures (Series 6 and 10) issued by the Company.

In addition, in June 2017, the Company acquired NIS 17,401,997 par value DBS Debentures for NIS 20 million).

8.2.3 Two private offerings of Debentures (Series 9) of the Company to classified investors totaling NIS 108,000,000 par value which are subject to the resale restrictions set out in Section 15C of the Israel Securities Law and in accordance with the Israel Securities Regulations (Details in the Matter of Sections 15A to 15C of the Law), 2000.

The total consideration that was received for the private offerings amounted to NIS 114 million.

8.2.4 For information about the terms of the Debentures (Series 6, 9 and 10), see Note 12 to the Annual Financial Statements.

9. Contingent Liabilities

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

In the opinion of the managements of the Group companies, based, among other things, on legal opinions as to the likelihood of success of the Legal Claims, the financial statements include adequate provisions of NIS 88 million, where provisions are required to cover the exposure arising from such Legal Claims.

In the opinion of the managements of the Group companies, the additional exposure (beyond these provisions) as of September 30, 2017 for claims filed against Group companies on various matters and which are unlikely to be realized, amounted to NIS 5.9 billion. There is also additional exposure of NIS 5.6 billion for claims, the chances of which cannot yet be assessed.

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

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

For updates subsequent to the reporting date, see section 9.3 below.

- 9.1 Following is a detailed description of the Group's contingent liabilities as of September 30, 2017, classified into groups with similar characteristics:

Claims group	Nature of the claims	Provision	Additional exposure	Exposure for claims that cannot yet be assessed
		NIS million		
Customer claims	Mainly motions for certification of class actions concerning contentions of unlawful collection of payment and impairment of the service provided by the Group companies.	49	3,712	1,742 ⁽¹⁾
Claims by enterprises and companies	Claims alleging liability of the Group companies in respect of their activities and/or the investments made in various projects.	11	2,005 ⁽²⁾	3,808 ⁽³⁾
Claims of employees and former employees of Group companies	Mainly collective and individual claims filed by employees and former employees of the Group in respect of various payments and recognition of various salary components as components for calculation of payments to Group employees, some of which have wide ramifications.	8	47	1
Claims by the State and authorities	Various claims by the State of Israel, government institutions and authorities ("the Authorities"). These are mainly procedures related to regulations relevant to the Group companies and financial disputes concerning monies paid by the Group companies to the Authorities (including property taxes).	16	28	-
Supplier and communication provider claims	Legal claims for compensation for alleged damage as a result of the supply of the service and/or the product.	3	109	1
Claims for punitive damages, real estate and infrastructure	Claims for alleged physical damage or damage to property caused by Group companies and in relation to real estate and infrastructure. The additional amount of exposure for punitive damages does not include claims for which the insurance coverage is not disputed.	1	23	-
Total legal claims against the Company and subsidiaries		88	5,924	5,552

- (1) The amount includes exposure in the amount of NIS 1.11 billion for a claim against the Company, as well as against the subsidiary Walla! Communications Ltd., Yad 2 and an advertising company owned by Walla, which addresses with the Company's 144B service.
- (2) * Total exposure of NIS 2 billion for a claim filed by a shareholder against the Company and officers in the Company, referring to alleged reporting omissions by the Company regarding the wholesale market and the reduction of interconnect fees, which the plaintiff estimates at NIS 1.1 billion or NIS 2 billion (depending on the method used to calculate the damage).
- (3) Two motions for certification of a class action amounting to a total of NIS 1.8 billion, filed in June 2017 against the Company, officers in the Group and companies in the group of the Company's controlling shareholders regarding the transaction for the Company's acquisition of DBS shares from Eurocom DBS Ltd. Pursuant to the Court ruling, a motion to consolidate these two motions is expected to be filed.

In addition, a motion for certification of a class action amounting to NIS 2 billion, filed in July 2017 against the Company, the Chairman of the Board of Directors and other directors of the Company, regarding the acquisition of DBS shares and a transaction to continue the agreement between DBS and Spacecom. This motion was struck out subsequent to the reporting date in view of the foregoing two motions that were filed earlier and are concerned with a similar issue as that of this motion.

- 9.2 In June-August 2017, the Company's shareholders filed several motions against the Company and DBS for discovery of documents prior to filing a motion for certification of a derivative action in accordance with section 198A of the Companies Law. These motions were filed following a public investigation by the Israel Securities Authority concerning the transaction for the Company's acquisition of DBS shares from Eurocom DBS Ltd. and transactions for satellite communications services between DBS and Space Communications Ltd., as described in Note 1.2 above.

It should be noted that in addition to these motions, there is a pending claim from 2015 and motion for certification as a derivative action against the Company, its controlling shareholder and

directors, concerning the transaction for the Company's acquisition of the entire holdings and shareholder's loans of Eurocom DBS in DBS.

Subsequent to the reporting date, three motions for disclosure of documents relating to the agreement for acquisition of DBS shares by the Company were struck out, in view of the similarity of the motion from 2015, as described above.

- 9.3** Subsequent to the reporting date, claims amounting to NIS 938 million, as well as a claim without financial estimate, were filed against Group companies. At the approval date of the financial statements, the chances of these claims cannot yet be assessed. In addition, claims with exposure of NIS 2.1 billion (including the claim set out in section 9.1(3) above) came to an end.

10. Equity

- 10.1** On May 9, 2017, the general meeting of the Company's shareholders approved the recommendation of the Company's Board of Directors of March 29, 2017 to distribute a cash dividend of NIS 578 million (NIS 0.2090049 per share) to the Company's shareholders. The dividend was paid on May 29, 2017.
- 10.2** On September 18, 2017, the general meeting of the Company's shareholders approved the recommendation of the Company's Board of Directors of August 23, 2017 to distribute a cash dividend of NIS 708 million (NIS 0.2560129 per share) to the Company's shareholders. The dividend was paid on October 16, 2017.

11. Revenues

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Domestic fixed-line communication (Bezeq Fixed-Line)					
Fixed-line telephony	1,025	1,104	337	367	1,450
Internet - infrastructure	1,189	1,163	399	388	1,558
Transmission and data communication	591	630	193	208	843
Other services	164	168	55	53	213
	2,969	3,065	984	1,016	4,064
Cellular telephony - Pelephone					
Cellular services and terminal equipment	1,315	1,347	451	457	1,777
Sale of terminal equipment	544	598	172	180	811
	1,859	1,945	623	637	2,588
Multi-channel television - DBS					
	1,246	1,307	406	434	1,745
International communications, ISP, and NEP services - Bezeq International					
	1,097	1,106	345	369	1,480
Other					
	160	157	57	54	207
	7,331	7,580	2,415	2,510	10,084

12. General and Operating Expenses

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Terminal equipment and materials	613	594	181	177	831
Interconnectivity and payments to domestic and international operators	603	634	201	211	825
Maintenance of buildings and sites	437	450	152	151	605
Marketing and general	437*	525	159*	180	697
Content services	481	466	158	165	629
Services and maintenance by sub-contractors	198	192	67	68	261
Vehicle maintenance	119	123	38	42	164
	2,888	2,984	956	994	4,012

* See Note 3.2 for information about early implementation of IFRS 15, Revenue from Contracts with Customers.

13. Other Operating Income, Net

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Capital gain from the sale of fixed assets (mainly real estate)	(64)	(62)	(45)	(22)	(107)
Provision for severance pay in voluntary redundancy	15	18	3	3	96
Others	21	11	19	(7)	11
Total operating revenue, net	(28)	(33)	(23)	(26)	-

14. Financial Instruments

14.1 Fair value

14.1.1 Financial instruments at fair value for disclosure purposes only

The table below shows the differences between the carrying amount and the fair value of financial liabilities. The methods used to estimate the fair values of financial instruments are described in Note 29.8 to the Annual Financial Statements.

	September 30, 2017		September 30, 2016		December 31, 2016	
	Carrying amount (including accrued interest)	Fair value	Carrying amount (including accrued interest)	Fair value	Carrying amount (including accrued interest)	Fair value
	(Unaudited)		(Unaudited)		(Audited)	
	NIS million		NIS million		NIS million	
Loans from banks and institutions (unlinked)	4,022	4,294	2,782	2,889	2,947	3,089
Debentures issued to the public (CPI-linked)	4,135	4,355	3,519	3,707	3,473	3,656
Debentures issued to the public (unlinked)	1,680	1,758	1,610	1,645	1,592	1,602
Debentures issued to financial institutions (CPI-linked)	22	25	1,101	1,099	830	879
Debentures issued to financial institutions (unlinked)	359	388	410	451	403	440
	10,218	10,820	9,422	9,791	9,245	9,666

14.1.2 Fair value hierarchy

The table below presents an analysis of the financial instruments measured at fair value, with details of the evaluation method. The methods used to estimate the fair value are described in Note 29.7 to the Annual Financial Statements.

	September 30, 2017	September 30, 2016	December 31, 2016
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Level 1: investment in exchange-traded funds and financial funds	20	48	31
Level 2: forward contracts	(217)	(184)	(170)
Level 3: contingent consideration for a business combination	43	(35)	(84)

15. Segment Reporting**15.1 Operating segments**

Nine months ended September 30, 2017 (Unaudited):							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	2,969	1,859	1,097	1,246	160	-	7,331
Inter-segment revenues	228	36	61	-	13	(338)	-
Total revenues	3,197	1,895	1,158	1,246	173	(338)	7,331
Depreciation and amortization	543	293	100	213	15	124	1,288
Segment results – operating income (loss)	1,501	57	133	136	(18)	(126)	1,683
Financing expenses	305	3	7	73	-	(30)	358
Financing income	(24)	(40)	(1)	(15)	(6)	25	(61)
Total financing expenses (income), net	281	(37)	6	58	(6)	(5)	297
Segment profit (loss) after financing expenses, net	1,220	94	127	78	(12)	(121)	1,386
Share in losses of associates	-	-	-	-	(4)	-	(4)
Segment profit (loss) before income tax	1,220	94	127	78	(16)	(121)	1,382
Income tax	308	20	31	333	-	(340)	352
Segment results – net profit (loss)	912	74	96	(255)	(16)	219	1,030

15. Segment Reporting (Contd.)

15.1 Operating segments (contd.)

Nine months ended September 30, 2016 (Unaudited):							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	3,063	1,945	1,106	1,306	154	-	7,574
Inter-segment revenues	238	33	50	1	14	(330)	6
Total revenues	3,301	1,978	1,156	1,307	168	(330)	7,580
Depreciation and amortization	556	290	103	225	13	144	1,331
Segment results – operating income (loss)	1,595	36	129	196	(24)	(143)	1,789
Financing expenses	326	2	11	530	1	(510)	360
Financing income	(27)	(39)	(4)	(8)	(5)	34	(49)
Total financing expenses (income), net	299	(37)	7	522	(4)	(476)	311
Segment profit (loss) after financing expenses, net	1,296	73	122	(326)	(20)	333	1,478
Share in profits (losses) of associates	-	-	1	-	(3)	(2)	(4)
Segment profit (loss) before income tax	1,296	73	123	(326)	(23)	331	1,474
Income tax	299	15	31	1	-	69	415
Segment results – net profit (loss)	997	58	92	(327)	(23)	262	1,059

15. Segment Reporting (Contd.)**15.1 Operating segments (contd.)**

Three months ended September 30, 2017 (Unaudited):							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	983	623	345	406	58	-	2,415
Inter-segment revenues	78	12	22	-	4	(116)	-
Total revenues	1,061	635	367	406	62	(116)	2,415
Depreciation and amortization	186	100	34	72	5	39	436
Segment results – operating income (loss)	492	22	39	35	(4)	(40)	544
Financing expenses	119	3	3	1	(1)	(13)	112
Financing income	(12)	(12)	-	(2)	-	8	(18)
Total financing expenses (income), net	107	(9)	3	(1)	(1)	(5)	94
Segment profit (loss) before income tax	385	31	36	36	(3)	(35)	450
Income tax	109	7	9	159	-	(156)	128
Segment results – net profit (loss)	276	24	27	(123)	(3)	121	322

15. Segment Reporting (Contd.)

15.1 Operating segments (contd.)

Three months ended September 30, 2016 (Unaudited):							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	1,013	638	369	434	53	-	2,507
Inter-segment revenues	76	11	15	-	7	(106)	3
Total revenues	1,089	649	384	434	60	(106)	2,510
Depreciation and amortization	188	92	35	75	5	47	442
Segment results – operating income (loss)	519	27	45	62	(7)	(47)	599
Financing expenses	102	-	4	204	1	(192)	119
Financing income	(9)	(14)	(2)	-	-	10	(15)
Total financing expenses (income), net	93	(14)	2	204	1	(182)	104
Segment profit (loss) after financing expenses, net	426	41	43	(142)	(8)	135	495
Share in profits (losses) of associates	-	-	1	-	(1)	(2)	(2)
Segment profit (loss) before income tax	426	41	44	(142)	(9)	133	493
Income tax	83	9	11	-	-	(4)	99
Segment results – net profit (loss)	343	32	33	(142)	(9)	137	394

15. Segment Reporting (Contd.)

15.1 Operating segments (contd.)

Year ended December 31, 2016 (Audited)							
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	4,063	2,587	1,478	1,745	198	-	10,071
Inter-segment revenues	320	43	70	-	20	(440)	13
Total revenues	4,383	2,630	1,548	1,745	218	(440)	10,084
Depreciation and amortization	717	380	137	296	16	193	1,739
Segment results – operating income (loss)	2,076	32	176	264	(34)	(193)	2,321
Financing expenses	475	6	15	539	2	(529)	508
Financing income	(30)	(52)	(5)	(13)	(4)	43	(61)
Total financing expenses (income), net	445	(46)	10	526	(2)	(486)	447
Segment profit (loss) after financing expenses, net	1,631	78	166	(262)	(32)	293	1,874
Share in profits (losses) of associates	-	-	1	-	(5)	(1)	(5)
Segment profit (loss) before income tax	1,631	78	167	(262)	(37)	292	1,869
Income tax	399	17	42	(330)	-	497	625
Segment results – net profit (loss)	1,232	61	125	68	(37)	(205)	1,244

15.2 Adjustment of profit or loss for reporting segments

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Operating income for reporting segments	1,826	1,956	587	653	2,548
Financing expenses, net	(297)	(311)	(94)	(104)	(447)
Amortization of surplus cost for intangible assets	(120)	(140)	(35)	(47)	(193)
Share in losses of associates	(4)	(4)	-	(2)	(5)
Loss for operations classified in other categories and other adjustments	(23)	(27)	(8)	(7)	(34)
Income before income tax	1,382	1,474	450	493	1,869

16. Condensed Financial Statements of Pelephone, Bezeq International, and DBS**16.1 Pelephone Communications Ltd.**

Selected data from the statement of financial position

	September 30, 2017	September 30, 2016	December 31, 2016
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	1,310	1,251	1,275
Non-current assets	2,078	2,042	2,019
Total assets	3,388	3,293	3,294
Current liabilities	575	493	465
Long-term liabilities	98	78	104
Total liabilities	673	571	569
Equity	2,715	2,722	2,725
Total liabilities and equity	3,388	3,293	3,294

Selected data from the statement of income

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from services	1,345	1,379	461	468	1,818
Revenues from sales of terminal equipment	550	599	174	181	812
Total revenues from services and sales	1,895	1,978	635	649	2,630
Cost of services and sales	1,616	1,675	534	536	2,248
Gross profit	279	303	101	113	382
Selling and marketing expenses	158	198	58	65	260
General and administrative expenses	64	69	21	21	89
Other operating expenses	-	-	-	-	1
	222	267	79	86	350
Operating income	57	36	22	27	32
Financing expenses	3	2	3	-	6
Financing income	(40)	(39)	(12)	(14)	(52)
Financing income, net	(37)	(37)	(9)	(14)	(46)
Profit before income tax	94	73	31	41	78
Income tax	20	15	7	9	17
Profit for the period	74	58	24	32	61

16.2 Bezeq International Ltd.

Selected data from the statement of financial position

	September 30, 2017	September 30, 2016	December 31, 2016
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	517	521	497
Non-current assets	720	702	691
Total assets	1,237	1,223	1,188
Current liabilities	354	348	280
Long-term liabilities	112	98	100
Total liabilities	466	446	380
Equity	771	777	808
Total liabilities and equity	1,237	1,223	1,188

Selected data from the statement of income

	Nine months ended September 30		Three months ended September 30		Year ended December 31,
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from services	1,158	1,156	367	384	1,548
Operating expenses	799	760	253	256	1,015
Gross profit	359	396	114	128	533
Selling and marketing expenses	142	168	48	55	221
General and administrative expenses	84	85	28	28	118
Other expenses, net	-	14	(1)	-	18
	226	267	75	83	357
Operating income	133	129	39	45	176
Financing expenses	7	11	3	4	15
Financing income	(1)	(4)	-	(2)	(5)
Financing expenses, net	6	7	3	2	10
Share in the profits of equity-accounted investees	-	1	-	1	1
Profit before income tax	127	123	36	44	167
Income tax	31	31	9	11	42
Profit for the period	96	92	27	33	125

16.3 DBS Satellite Services (1998) Ltd.

Selected data from the statement of financial position

	September 30, 2017	September 30, 2016	December 31, 2016
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	358	313	440
Non-current assets	1,246	1,277	1,586
Total assets	1,604	1,590	2,026
Current liabilities	789	893	950
Long-term liabilities	478	696	484
Loans from shareholders	-	323	-
Total liabilities	1,267	1,912	1,434
Capital (capital deficit)	337	(322)	592
Total liabilities and equity deficit	1,604	1,590	2,026

Selected data from the statement of income

	Nine months ended September 30		Three months ended September 30		Year ended December 31,
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from services	1,246	1,307	406	434	1,745
Operating expenses	940	947	312	314	1,261
Gross profit	306	360	94	120	484
Selling and marketing expenses	98	97	34	35	128
General and administrative expenses	72	67	25	23	92
	170	164	59	58	220
Operating income	136	196	35	62	264
Financing expenses	73	65	1	26	71
Financing expenses (income) for loans from shareholders (to shareholders), net	(2)	465	-	178	468
Financing income	(13)	(8)	(2)	-	(13)
Financing expenses (income), net	58	522	(1)	204	526
Profit (loss) before income tax	78	(326)	36	(142)	(262)
Income tax	333*	1	159*	-	(330)
Profit (loss) for the period	(255)	(327)	(123)	(142)	68

* In the second quarter of 2017, as a result of the developments in the multi-channel television market, including the structure and intensity of the competition, DBS revised its projections and accordingly, reduced the tax asset in the amount of NIS 163 million against expenses in the statement of income. Due to the significant intensification of competition in the third quarter of 2017, DBS decided to reduce the tax asset in full.

Condensed Separate Interim Financial Information

September 30, 2017



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

Contents	Page
Auditors' Report	2
Condensed Separate Interim Financial Information as at September 30, 2017 (unaudited)	
Condensed Separate Interim Information of Financial Position	3
Condensed Separate Interim Information of Profit or Loss	5
Condensed Separate Interim Information of Comprehensive Income	5
Condensed Separate Interim Information of Cash Flows	6
Notes to the Condensed Separate Interim Financial Information	7



Somekh Chaikin
KPMG Millennium Tower
17 Ha-Arbaa Street, PO Box 609
Tel Aviv 6100601, Israel
800068403

To:
The Shareholders of "Bezeq"- The Israel Telecommunication Corporation Ltd.

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

Introduction

We have reviewed the separate interim financial information presented in accordance with Regulation 38D of the Securities Regulations (Periodic and Immediate Reports) – 1970 of "Bezeq"- The Israel Telecommunication Corporation Ltd. (hereinafter – "the Company") as of September 30, 2017 and for the nine and three month periods then ended. The separate interim financial information is the responsibility of the Company's Board of Directors and of its Management. Our responsibility is to express a conclusion on the separate interim financial information based on our review.

We did not review the separate interim financial information of an investee company the investment in which amounted to NIS 96 million as of September 30, 2017, and the loss from investee company amounted to NIS 17 million and NIS 6 million for the nine and three month periods then ended, respectively. The financial statements of that company were reviewed by other auditors whose review report thereon was furnished to us, and our conclusion, insofar as it relates to amounts emanating from the financial statements of that company, is based solely on the said review report of the other auditors.

Scope of Review

We conducted our review in accordance with Standard on Review Engagements 1, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" of the Institute of Certified Public Accountants in Israel. A review of separate interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards in Israel and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

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

Without qualifying our abovementioned conclusion, we draw attention to Note 6.1 regarding the Israel Securities Authority's (ISA) investigation of the suspicion of committing offenses under the Israel Securities' Law and Penal Law, in respect to transactions related to the controlling shareholder, and the transfer of the investigation file to the District Attorney's Office. As stated in the abovementioned note, at this stage, the Company is unable to assess the implications of the ISA investigation and the transfer of the investigation to the District Attorney's Office, if any. In addition, without qualifying our abovementioned conclusion, we draw attention to numerous lawsuits filed against the Company which cannot yet be assessed or the exposure in respect thereof cannot yet be estimated, as set forth in Note 4.

Somekh Chaikin
Certified Public Accountants (Isr.)
November 29, 2017

Condensed Separate Interim Information of Financial Position

	September 30, 2017 *	September 30, 2016	December 31, 2016
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Assets			
Cash and cash equivalents	1,802	412	182
Investments	75	859	549
Trade receivables	707	706	698
Other receivables	177	77	72
Eurocom DBS Ltd, an affiliate	43	29	-
Loans granted to investees	69	110	78
Investment in DBS debentures	202	-	-
Dividend receivable	152	85	-
Total current assets	3,227	2,278	1,579
Trade and other receivables	141	198	211
Property, plant and equipment	4,917	4,828	4,867
Intangible assets	220	234	229
Investment in investees	7,017	6,612	7,080
Loans granted to investees	101	443	120
Investment in DBS debentures	455	-	-
Non-current and other investments	140	104	105
Total non-current assets	12,991	12,419	12,612
Total assets	16,218	14,697	14,191

Condensed Separate Interim Information of Financial Position (Contd.)

	September 30, 2017 *	September 30, 2016	December 31, 2016
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Liabilities			
Debentures, loans and borrowings	526	1,711	1,405
Trade and other payables	690	613	679
Current tax liabilities	111	169	96
Employee benefits	193	226	263
Liability to Eurocom DBS Ltd, an affiliate	-	6	32
Provisions (Note 4)	63	51	48
Loan from an investee	15	-	-
Dividend payable	708	665	-
Total current liabilities	2,306	3,441	2,523
Debentures and loans	10,943	8,398	8,630
Loan from an investee	475	325	325
Employee benefits	222	200	220
Derivatives and other liabilities	276	242	231
Deferred tax liabilities	69	64	59
Total non-current liabilities	11,985	9,229	9,465
Total liabilities	14,291	12,670	11,988
Capital			
Share capital	3,878	3,878	3,878
Share premium	383	384	384
Reserves	283	286	302
Deficit	(2,617)	(2,521)	(2,361)
Total equity attributable to equity holders of the Company	1,927	2,027	2,203
Total liabilities and equity	16,218	14,697	14,191

David Granot
Acting Chairman of the Board of Directors

Stella Handler
CEO

Yali Rothenberg
CFO Bezeq Group

Date of approval of the financial statements: November 29, 2017

* See Note 1.3 concerning early application of IFRS 15 - Revenue from Contracts with Customers

The attached notes are an integral part of these condensed separate interim financial information.

Condensed Separate Interim Information of Profit or Loss

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017*	2016	2017*	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues (Note 2)	3,197	3,301	1,061	1,089	4,383
Costs of activity					
Salaries	668	672	224	225	898
Depreciation and amortization	543	556	186	188	717
Operating and general expenses (Note 3)	514	525	183	183	705
Other operating income, net	(29)	(47)	(24)	(26)	(13)
Cost of Activities	1,696	1,706	569	570	2,307
Operating profit	1,501	1,595	492	519	2,076
Financing expenses (income)					
Financing expenses	305	326	119	102	475
Financing income	(24)	(27)	(12)	(9)	(30)
Financing expenses, net	281	299	107	93	445
Profit after financing expenses, net	1,220	1,296	385	426	1,631
Share in earnings of investees, net	118	62	46	51	12
Profit before income tax	1,338	1,358	431	477	1,643
Income tax	308	299	109	83	399
Profit for the period attributable to the owners of the Company	1,030	1,059	322	394	1,244

Condensed Separate Interim Information of Comprehensive Income

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017*	2016	2017*	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Profit for the period	1,030	1,059	322	394	1,244
Items of other comprehensive income (loss) for the period including actuarial gains and hedging transactions, net of tax	(20)	(6)	(12)	(1)	(15)
Total comprehensive income for the period attributable to equity holders of the Company	1,010	1,053	310	393	1,229

* See Note 1.3 concerning early application of IFRS 15 - Revenue from Contracts with Customers

The attached notes are an integral part of these condensed separate interim financial information.

Condensed Separate Interim Information of Cash Flows

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017*	2016	2017*	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows from operating activities					
Profit for the period	1,030	1,059	322	394	1,244
Adjustments:					
Depreciation and amortization	543	556	186	188	717
Share in earnings of investees, net	(118)	(62)	(46)	(51)	(12)
Financing expenses, net	264	299	99	95	445
Capital gain, net	(64)	(62)	(45)	(22)	(107)
Income tax expenses	308	299	109	83	399
Change in trade and other receivables	27	(50)	17	(18)	(51)
Change in trade and other payables	22	(64)	84	15	(54)
Change in provisions	15	(10)	15	(4)	(12)
Change in employee benefits	(67)	(107)	(61)	(89)	(72)
Miscellaneous	4	(10)	3	(4)	(15)
Net cash (used in) from operating activities due to transactions with subsidiaries	(43)	(9)	(10)	21	27
Net income tax paid	(283)	(257)	(100)	(82)	(445)
Net cash from operating activities	1,638	1,582	573	526	2,064
Cash flows from investment activities					
Investment in intangible assets and other investments	(78)	(57)	(27)	(18)	(76)
Proceeds from the sale of property, plant and equipment	72	117	46	22	132
Investment in bank and other deposits	(76)	(855)	(76)	-	(905)
Exercise of bank and other deposits	547	644	-	-	1,003
Tax payment for shareholders loans	-	(461)	-	(461)	(461)
Purchase of property, plant and equipment	(521)	(572)	(143)	(189)	(758)
Miscellaneous	(34)	1	(7)	2	2
Net cash from investment activities due to transactions with subsidiaries	(70)	83	28	(2)	148
Net cash flows from (used in) investment activities	(160)	(1,100)	(179)	(646)	(915)
Cash flow from finance activities					
Issue of debentures and receipt of loans	1,918	1,661	500	-	2,161
Repayment of debentures and loans	(1,116)	(897)	(274)	(99)	(1,444)
Dividends paid	(578)	(776)	-	-	(1,441)
Payment to Eurocom DBS for acquisition of DBS shares and loans	(61)	(256)	-	(198)	(256)
Interest paid	(186)	(202)	(12)	(16)	(381)
Miscellaneous	-	(21)	-	-	(21)
Net cash from (used for) financing activities due to transactions with subsidiaries	165	311	(90)	-	305
Net cash from (used for) financing operations	142	(180)	124	(313)	(1,077)
Net increase (decrease) in cash and cash equivalents	1,620	302	518	(433)	72
Cash and cash equivalents at beginning of period	182	110	1,284	845	110
Cash and cash equivalents at the end of the period	1,802	412	1,802	412	182

* See Note 1.3 concerning early application of IFRS 15 - Revenue from Contracts with Customers

The attached notes are an integral part of these condensed separate interim financial information.

Notes to the Condensed Separate Interim Financial Information

1. Manner of preparing financial information**1.1 Definitions**

"The Company": Bezeq The Israel Telecommunication Corporation Limited

"Investee", the "Group", "Subsidiary": as these terms are defined in the Company's consolidated financial statements for 2016.

1.2 Principles used for preparing financial information

The condensed separate interim financial information is presented in accordance with Regulation 38(D) ("the Regulation") and the Tenth Addendum of the Securities Regulations (Periodic and Immediate Reports), 1970 ("the Tenth Addendum") with respect to the condensed interim financial information of the corporation. They should be read in conjunction with the separate financial information for the year ended December 31, 2016 and in conjunction with the condensed interim consolidated financial statements as at September 30, 2017 ("the Consolidated Financial Statements").

The accounting policies used in preparing this condensed separate interim financial information are in accordance with the accounting policies set out in the separate financial information as of and for the year ended December 31, 2016.

1.3 First-time Application of Accounting Standards

Commencing January 1, 2017, the Group applies early adoption of International Financial Reporting Standard - Revenues from Customer Contracts ("IFRS 15"), which sets out guidelines with respect to recognition of revenue. IFRS 15 replaces IAS 18 - Revenues and presents a new model for recognition of revenues from contracts with customers.

For further information concerning the first-time adoption of IFRS 15 see Note 3.2 to the Consolidated Financial Statements.

The tables below present a breakdown of the effects on the condensed consolidated interim statement of financial position as at September 30, 2017 and on the condensed consolidated statement of income and consolidated interim statement of cash flows for the nine and three months then ended, assuming that the Company's previous policy regarding subscriber acquisition costs was continued in this period.

Effect on the condensed consolidated interim statement of financial position as at September 30, 2017:

	Per previous policies	Change	Per IFRS 15
	(Unaudited)	(Unaudited)	(Unaudited)
	NIS million	NIS million	NIS million
Subscriber acquisition asset, net (presented as part of non-current deferred expenses and investments)	4	15	19
Capital	1,915	12	1,927

Effect on the Consolidated Interim Statement of Income for the nine and three-month periods ended September 30, 2017:

	Nine months ended September 30, 2017			Three months ended September 30, 2017		
	Per previous policies	Change	Per IFRS 15	Per previous policies	Change	Per IFRS 15
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
General and operating expenses	525	(11)	514	186	(5)	183
Salaries	674	(6)	668	226	(2)	224
Depreciation and amortization costs	541	2	543	184	2	186
Operating profit	1,486	15	1,501	487	5	492
Profit after financing expenses	1,205	15	1,220	380	5	385
Profit before income tax	1,323	15	1,338	426	5	431
Income tax	305	3	308	108	1	109
Profit for the period	1,018	12	1,030	318	4	322

Effect on the Consolidated Interim Statement of Cash Flows for the three months ended September 30, 2017:

	Nine months ended September 30, 2017			Three months ended September 30, 2017		
	Per previous policies	Change	Per IFRS 15	Per previous policies	Change	Per IFRS 15
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Net cash from operating activities	1,621	17	1,638	566	7	573
Net cash from investment activities	(143)	(17)	(160)	(172)	(7)	(179)

1.4 New standards and interpretations not yet adopted

With regard to new standards and interpretations that have not yet been adopted, see Note 3.3 to the Consolidated Financial Statements.

2. Revenues

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Fixed-line telephony	1,053	1,133	345	375	1,490
Internet - infrastructure	1,229	1,191	413	399	1,597
Transmission and data communication	747	804	247	261	1,077
Other services	168	173	56	54	219
	3,197	3,301	1,061	1,089	4,383

3. Operating and general expenses

	Nine months ended September 30		Three months ended September 30		Year ended December 31
	2017	2016	2017	2016	2016
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Maintenance of buildings and sites	141	144	49	49	189
Marketing and general	140	142	54	55	195
Interconnectivity and payments to communications operators	91	101	31	34	130
Services and maintenance by sub-contractors	55	50	19	16	72
Vehicle maintenance	53	53	18	18	72
Terminal equipment and materials	34	35	12	11	47
	514	525	183	183	705

4. Contingent Liabilities

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

In the opinion of the Company's management, based, inter alia, on legal opinions as to the likelihood of success of these litigations, the financial statements include appropriate provisions in the amount of NIS 63 million, where provisions are required to cover the exposure arising from such litigation.

In the Management's opinion, the additional exposure (exceeding the foregoing provisions), as of September 30, 2017 due to legal claims filed against the Company on various matters, which are unlikely to be realized, amounts to a total of NIS 3.1 billion. This amount includes exposure of NIS 2 billion for a claim by shareholders against the Company and officers of the Company which the plaintiff estimates to be NIS 1.1 billion or NIS 2 billion (based on the method to be fixed of calculating the damages) In addition, the Company has further exposure in the amount of NIS 5.1 billion* for claims, the success of which cannot be assessed at this stage. The foregoing amounts are linked to the consumer price index and are before the addition of interest.

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

- 4.2** From June through August 2017 shareholders of the Company filed several motions for discovery of documents against the Company and DBS prior to the filing of a motion for certification of a derivative action under section 198A of the Companies Law. These motions were filed due to the public investigation by the Securities Authority concerning the transaction for the Company's acquisition of DBS shares from Eurocom DBS Ltd. and transactions for satellite communications services between DBS and Space Communications Ltd., as described in Note 1.2 to the Consolidated Financial Statements.

It should be noted that in addition to these motions, there is a pending claim from 2015 and motion for certification as a derivative action against the Company, its controlling shareholder and directors, concerning the transaction for the Company's acquisition of the entire holdings and shareholder's loans of Eurocom DBS in DBS.

Subsequent to the reporting date, three motions for disclosure of documents relating to the agreement for acquisition of DBS shares by the Company were struck out, in view of the similarity of the motion from 2015, as described above.

- 4.3** Subsequent to Reporting Date, a claim in respect of which exposure was NIS 2 billion, as set out in section (2) below, ended. In addition, a claim without financial estimate was filed against the Company.

* This amount includes:

- (1) Exposure of NIS 1.11 billion with respect to a claim filed against the Company and its subsidiary, Walla Communications Ltd., Yad 2 and an advertising company owned by Walla, concerning the Company's 144 service.
- (2) Two motions for certification of class action suits for a total amount of NIS 1.8 billion, filed in June 2017 against the Company, officers of the Group and companies of the group that is the controlling shareholder of the Company, concerning the transaction for the Company's acquisition of DBS shares from Eurocom DBS Ltd. Pursuant to the Court ruling, a motion to consolidate these two motions is expected to be filed. In addition, a motion for certification of a class action for a total amount of NIS 2 billion was filed in July 2017 against the Company, the Chairman of the Board of Directors and other directors of the Company, in the matter of the acquisition of DBS shares and the transaction to continue the engagement between DBS and Space Communications. This motion was struck out subsequent to the Reporting Date in view of the foregoing two motions that were filed earlier and are concerned with a similar issue as that of this motion.

For further information concerning contingent liabilities see Note 9 to the Consolidated Financial Statements.

5. Dividends from investees

- 5.1 In May 2017, Bezeq International Ltd. paid a cash dividend to the Company, which was announced in March 2017, in the amount of NIS 65 million.
- 5.2 In October 2017, Pelephone Communications Ltd. paid a cash dividend to the Company, which was announced in July 2017, in the amount of NIS 84 million.
- 5.3 In October 2017, Bezeq International paid a cash dividend to the Company, which was announced in July 2017, in the amount of NIS 68 million.

6. Events in the reporting period

- 6.1 For further information concerning the Securities Authority investigation see Note 1.2 to the Consolidated Financial Statements.
- 6.2 On May 10, 2017, the Company provided Bezeq International a loan in the amount of NIS 50 million to be repaid in three equal annual installments commencing from May 2018. The loan bears annual interest of 2.56%.
- 6.3 On May 28, 2017, the Company received a loan from Pelephone in the amount of NIS 150 million. The loan bears annual interest of 3.41% and is repayable in four equal annual installments commencing from December 1, 2022.
- 6.4 With regard to receipt of credit in 2017 from institutional organizations and banks, on June 15, 2017 and September 29, 2017, see Note 8.1 to the Consolidated Financial Statements.
- 6.5 For information concerning the issue of debentures Series 6 and 10 of the Company replacing Debenture (Series B) of DBS, see Note 8.2.2 to the Consolidated Financial Statements.
- 6.6 For information concerning the Company's issue of debentures during the year, see Note 8.2 to the Consolidated Financial Statements.
- 6.7 For further information regarding the second contingent consideration to be paid to Eurocom DBS based on the business results of DBS, See Note 4.2 to the Consolidated Financial Statements and fair value estimate of the amount expected to be recovered from the surplus advance payments that were made.
- 6.8 On October 15, 2017, the Company provided a loan to Pelephone in the amount of NIS 95 million. The loan bears annual interest of 3.41% and is repayable in four equal annual installments commencing from December 1, 2022.
- 6.9 For further information concerning income tax see Note 5 to the Consolidated Financial Statements.