UPDATE OF CHAPTER A (DESCRIPTION OF COMPANY OPERATIONS)[1]
OF THE PERIODIC REPORT FOR 2008 ("THE PERIODIC REPORT")
OF "BEZEQ" – THE ISRAEL TELECOMMUNICATIONS CORP. LTD. ("the Company")

In this report, which contains an update of the chapter regarding the description of the Company's business from the periodic report for 2008, the Company has included forward-looking information, as defined in the Securities Law 5728-1968 ("the Securities Law") with respect to both itself and the market. Such information includes forecasts, targets, appraisals and assessments which apply to future events or matters the realization of which is not certain and is not under the Company's control. Forward-looking information in this report will usually be identified specifically, or by employing statements such as "the Company expects", "the Company assesses", "it is the Company's intention", and similar statements.

Forward-looking information is not a proven fact and is based only on the Company's subjective assessment, based, inter alia, on a general analysis of the information available at the time of drafting of this report, including public announcements, studies and surveys, and they contain no undertakings as to the correctness or completeness of the information contained therein, and the Company does not independently check their correctness. The Company's assessments vary from time to time in accordance with the circumstances.

In addition, the realization and/or otherwise of the forward-looking information will be affected by factors that cannot be assessed in advance, and which are beyond the Company's control, including the risk factors that are characteristic of its operations as set out in this report, developments in the general environment, and external factors and the regulation that affects the Company's operations, as set out in this report.

1. DESCRIPTION OF GENERAL DEVELOPMENT OF GROUP OPERATIONS

Section 1.1 – Group activity and description of its business development

Section 1.1.4 - Holdings of the Company

The following are details of the current rate of the Company's holdings, fully diluted, assuming exercise of all of the options actually allotted to employees of the Company at September 30, 2009 and November 3, 2009 (as set out in the Periodic Report for 2008 and in the update to section 1.3.2 below):

Shareholders	Percentage of holdings		
	At Sept. 30, 2009	At November 3, 2009	Fully diluted at Sept. 30, 2009
Ap.Sb.Ar.	30.68%	30.64%	29.69%
State of Israel	2.98%	2.79%	0.96%
Zeevi Group	11.58%	7.05%	11.21%
Public	54.76%	59.51%	56.73%

For details regarding the sale of shares in the Company by Ap.Sb.Ar. Holdings, Ltd. ("Ap.Sb.Ar.") and by the Ze'evi Group, see section 1.3, below.

Section 1.1.5 – Mergers and Acquisitions – DBS

On August 20, 2009, the Supreme Court handed down its ruling on the appeals filed by the Antitrust Authority and Eurocom DBS Ltd. against the ruling of the Antitrust Tribunal on February 3, 2009 that approved the merger of the Company and DBS Satellite Services (1998) Ltd. ("DBS") subject to conditions. The Supreme Court accepted the appeal of the Antitrust Authority and decided not to approve the merger.

[1] The update is pursuant to Article 39A of the Securities (Periodic and Immediate Reports) Regulations, 5730-1970, and includes material changes or innovations that have occurred in the Company in any matter which must be described in the Periodic Report. The update relates to the Company's periodic report for 2008 and relates to the section numbers in Chapter A (Description of Company Operations) in that periodic report.

In consideration of the decision of the Supreme Court, the Company no longer controls DBS. Accordingly, as of August 21, 2009, the company ceased consolidating its financial reports with the reports of DBS and the investment in shares of DBS is presented according to the equity value method as at that date. As at the date on which the consolidation was discontinued, the Company placed the investment in the shares and options in DBS and the loans the Company made to DBS according to their fair value, based on an assessment of value conducted by an external appraiser, according to which the value of the Company's investment in DBS is valued at approximately NIS 1,145-1,234 million. The company placed the investment of NIS 1,175 million and recognized profit of approximately NIS 1,538 million. For additional information on this matter, see Note 4 of the Financial Statements of the Company as at September 30, 2009.

It should be noted that on September 29, 2009, Polar Communications Ltd. ("Polar"), which owns shares in DBS gave notice that it had signed an agreement with a third party to sell approximately 2.54% of the shares in DBS that it holds and approximately 32% of all the loans it gave to DBS in return for consideration of NIS 40 million. Pursuant to this, on the same day, Polar sent notification to the other shareholders in DBS, including the Company, informing them of the transaction and of their right, in accordance with the DBS shareholders agreement and the articles of organization of DBS to realize within 45 days their right of first refusal for acquiring the shares sold, in accordance with their relative holdings in YES.

Section 1.3 – Investments in equity and stock transactions

Section 1.3.1 – Transactions in shares of Bezeq

A. Sale of the Controlling Stake

On October 25, 2009, the controlling shareholder in the Company, Ap.Sb.Ar., informed the Company that it concluded an agreement with 012 Smile Communications, Ltd. for an off floor sale of 814,211,545 ordinary shares of the Company, worth NIS 1 par value each, which are 30.6% of the issued and paid up share capital of the Company listed on the of Poalim (Romema) Trustees, Ltd. in consideration of the sum NIS 6,513,692,360. In accordance with the said notification, the share price set in the context of the transaction is NIS 8. Completion of the transaction is conditional of receiving the regulatory approvals required by law no later than April 25, 2010, including the following approvals: approval of the Ministry of Communications for the transaction (including granting control permits); approval of the Antitrust Commissioner for the transaction, approval of the Prime Minister and the Minister of the Communications, pursuant to provisions of the Communications Law (Telecommunications and Transmissions) 5742-1982 and provisions of the Communications Order (Telecommunications and Transmissions) (Determination of Critical Services Provided by Bezeq, the Israel Telecommunications Company, Ltd.) 5757-1997; any other approval or agreement required by law. After completion of the transaction, it is not expected that AP.SB.AR. will hold any more shares in the Company. For additional information see notes 1B and 15E of the financial statements for the period ending on September 30, 2009.

B. Other Transactions in Shares of Bezeq

1. On August 10, 2009, a transaction for the sale of 155,000,000 shares of Bezeq worth NIS 1 par value each, which were held by Ze'evi Communications Holdings, Ltd. (in receivership) was completed through the investment bank UBS Limited in consideration of NIS 1,151,650,000 (the sales was made in two stages, so that the value of the shares held by the purchaser would not exceed 4.99% of the Company's share capital.)

2. On August 11, 2009, a transaction for the sale of 149,376,642 shares of Bezeq worth NIS 1 par value each, which were held by AR.SB.AR. was completed through Citigroup Global Markets, Ltd. in consideration of NIS 1,120,324,815, so that after completion of the purchase no purchaser held more than 5% of the Company's share capital.

3. On September 17, 2009, a transaction for the distribution of 95,623,358 shares of Bezeq worth NIS 1 par value each, which were held by AR.SB.AR. was completed through Citigroup Global Markets, Ltd. in consideration of NIS 748,730,893, so that after completion of the purchase no purchaser held more than 5% of the Company's share capital.

4. On October 19, 2009, a transaction for the sale of 120,000,000 shares of Bezeq worth NIS 1 par value each, which were held by Ze'evi Communications Holdings, Ltd. (in

receivership) was completed through the investment bank UBS Limited in consideration of NIS 976,800,000.

Upon completion of the aforementioned sales of shares listed in section B, above, the holdings of AR.SB.AR. in the Company were reduced to approximately 30.68% (approximately 29.69% at full dilution) and the holdings of the Ze'evi Group in the Company were reduced to approximately 7.06% (approximately 6.84% at full dilution).

Section 1.3.2 - Employee option schemes

Further to an option scheme for managers and senior employees of the Group of November 2007, to allot up to 65,000,000 options, since the date of publication of the Periodic Report for 2008 and until November 3, 2009, 600,000 additional options were allotted and 1,133,334 options expired, so that as at September 30, 2009 and as at November 3, 2009, 59,016,666 options, net (less expired options), have been allotted under the scheme.

Section 1.4 – Distribution of dividends

Section 1.4.1 – Dividend distribution policy

On August 4, 2009, the Board of Directors of the Company has also adopted a dividend distribution policy, whereby the Company will distribute to its shareholders on a semi-annual basis, cash dividends amounting to 100% of the net profit (attributable to the shareholders of the Company) recorded for the previous six-month period, based on the consolidated financial statements of the Company.

The implementation of this dividend policy is subject to Israeli law, including the distribution tests set forth in the Companies Law (1999), and is also subject to the Board of Directors' assessment of the Company's ability to meet its current and expected obligations, in consideration of its projected cash flows, activities and commitments, cash balances, future plans and financial position, as they may be from time to time. Each dividend distribution will be subject to the approval of the general meeting of shareholders of the Company, pursuant to the Company's bylaws.

Section 1.4.2 – Distribution of dividends

On May 3, 2009, the general meeting of shareholders of the Company, following the recommendation of the Board of Directors of the Company on March 23, 2009, approved the distribution of a cash dividend to the shareholders of the Company in the amount of NIS 792 million, constituting, at the effective date for the distribution (May 11, 2009), the sum of NIS 0.3013025 per share and 30.13025% of the issued and paid up share capital of the Company. The dividend was paid to the shareholders of the Company on May 24, 2009.

On September 2, 2009, the general meeting of shareholders of the Company, following the recommendation of the Board of Directors of the Company of August 4, 2009, approved the distribution of a cash dividend to the shareholders of the Company in the amount of NIS 1,149 million, constituting, at the effective date for the distribution (September 22, 2009), the sum of NIS 0.4329743 per share and 43.29743% of the issued and paid up share capital of the Company. The dividend was paid to the shareholders of the Company on October 5, 2009.

Section 1.5 - Financial information regarding the Group's areas of operation

Section 1.5.3 Principal results and operational data

A. <u>Bezeq Fixed line (the Company's activity as domestic operator)</u>

(NIS millions except where stated otherwise)

	Q3 2009	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008
Revenues	1,343	1,318	1,326	1,348	1,388	1,354	1,408
Operating profit	491	434	437	232**	428**	442**	373**
Depreciation and amortization	184	205	211	209	214	211	218
Earnings before interest, taxes, depreciation and amortization (EBITDA)	675	639	648	441**	642**	653**	591**
Payments for investment in property, plant and equipment and intangible assets	224	191	238	170	156	132	158
Proceeds from sale of property, plant and equipment and intangible assets	40	8	50	47	12	25	60
No. of active subscriber lines at end of period (in thousands)	2,518	2,547	2,579	2,615	2,645	2,681	2,711
Average monthly revenue per line (NIS) *	83	81	81	82	85	82	84
No. of outgoing minutes (in millions)	3,095	3,014	3,123	3,154	3,428	3,346	3,511
No. of incoming minutes (in millions)	1,737	1,664	1,654	1,648	1,719	1,651	1,673
No. of ADSL subscribers at end of period (in thousands)	1,026	1,016	1,011	1,005	994	982	970
Average monthly revenue per ADSL subscriber (NIS)	72	69	68	67	68	66	68

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

** Reclassification of the sum of approximately NIS 26 million, spread over the four quarters of 2008, for financing costs for provisions for termination of labor relations under early retirement, presented in the past under the item of operating expenses (income) net.

B. Pelephone

(NIS millions except where stated otherwise)

	Q3 2009	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008
Revenue	1,372	1,346	1,265	1,138	1,214	1,188	1,173
Operating profit	316	321	302	159	293	266	215
Depreciation and amortization	155	151	139	135	129	130	129
Earnings before interest, taxes, depreciation and amortization (EBITDA)	471	472	441	294	422	396	344
Net profit	231	233	230	128	211	180	163
Cash flow from current operations	395	290	375	298	379	344	256
Payments for investment in property, plant and equipment and intangible assets	146	163	149	163	350	182	103
Proceeds from sale of property, plant and equipment and intangible assets	-	4	-	1	-	1	1
No. of subscribers at end of period (in thousands)	2,721	2,694	2,669	2,649	2,698	2,636	2,595
Average monthly minutes of use (MOU) per subscriber*	339	329	323	335	359	358	355
Average monthly revenue per subscriber (ARPU) (in NIS)*	136	131	128	122	129	128	126
No. of subscribers at end of period (in thousands)	1,407	1,307	1,217	1,151	1,068	977	867
Revenues from value added services and content as % of revenues from cellular services	20.3%	19.2%	18.5%	18.4%	16.2%	15.5%	15.0%

* On December 31, 2008, Pelephone adopted a stricter policy for counting subscribers, by which subscribers who only receive SMS messages are not counted as subscribers. This change in policy led to the deduction of approximately 92,000 subscribers, the number of subscribers as at September 30, 2008 is prior to the deduction of those subscribers.

The decrease in MOU is the result of the transition to charging according to segments of one second that went into effect on January 1, 2009, which led to a reduction in the number of minutes billed.

C. Bezeq International

(NIS millions except where stated otherwise)

	Q3 2009	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008
Revenue	332	327	324	337	329	326	314
Operating profit	66	68	60	65	59	63	55
Depreciation and amortization	21	21	20	20	20	20	20
Earnings before interest, taxes, depreciation and amortization (EBITDA)	88	88	80	85	79	83	75
Net profit	51	56	44	46	44	47	42
Cash flow from current operations	82	83	84	72	32	51	8
Payments for investment in property, plant and equipment and intangible assets	33	26	21	26	33	31	28
Proceeds from sale of property, plant and equipment and intangible assets	-	-	-	1	-	-	-

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

D. DBS

(NIS millions except where stated otherwise)

	Q3 2009	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008
Revenue	380	376	384	377	375	380	381
Operating profit	61	59	66	55	52	43	27
Depreciation and amortization	59	56	57	66	59	60	65
Earnings before interest, taxes, depreciation and amortization (EBITDA)	120	115	122	122	111	103	92
Net profit (loss)	(88)	(95)	(1)	(18)	(82)	(99)	(66)
Cash flow from current operations	135	93	91	134	97	32	84
Payments for investment in property, plant and equipment and intangible assets*	87	60	61	63	56	40	79
Proceeds from sale of property, plant and equipment and intangible assets	-	-	-	-	-	-	-
No. of subscribers at end of period (in thousands)	567	562	560	560	556	551	549
Average monthly revenue per subscriber (in NIS)*	224	224	228	225	226	230	231

* This item also includes investments in the cost of acquiring subscribers.

Section 1.6 - Group forecast

Based upon the Bezeq Group's financial performance for the first nine months of 2009, which was materially stronger than the corresponding nine-month period in 2008, the Bezeq Group reiterates its outlook for 2009 and continues to anticipate achieving full-year revenue, net profit, EBITDA and operating cash flows above those for the full-year 2008 results. The Bezeq Group is maintaining its outlook for full-year 2009 gross capital expenditures, which are still expected to be close to the 2008 level.

The aforementioned guidance for the full-year 2009 is based on the anticipated Bezeq Group consolidated performance, which following the deconsolidation of yes financials as of August 21st, 2009, excludes the financial contribution of yes from both the 2009 and 2008 full-year periods.

The information in this section contains forward-looking information, based on the Company's assessments. Actual results might be substantially different from these assessments, taking into account the changes that might occur in commercial conditions, and the possible impact of regulatory decisions.

Section 1.8 - Group strategy

* **Frontrunner status** – reinforcement and strengthening of the Bezeq Group's status as the leading communications group in Israel.
* **Presence in central arenas in the communications market and availability for the end user** – the mobile market, the customer's home, the business sector, internet, television and content.
* **Total client solution** – provision of an inclusive communications solution for private and business customers based on a variety of services and products.
* **Substantial presence in all components of the value chain** – provision and reinforcement of the connection with the customer by maintaining quality service and innovation throughout the value chain: infrastructure, services and content.
* **Tailoring of service to customer** – focusing on the provision of tailored services to customers, with the services being provided at a high level, and full response to the needs of both private and business customers.
* **Innovation and technology** – the relative advantage of the companies in the Group will be based, inter alia, on leading and up-to-date technology in the market, such as technology that has matured sufficiently in order to enable deployment and provision of such services to a large scale, and with the requisite level of reliability.
* **Commercial focusing** – focusing on the core areas of the communications market and related areas, and focusing on the local market in Israel.
* Retention and reinforcement of the concept of quality, goodwill and assetization of the Group's brands.

Naturally, a review of the Group's strategy involves assessments regarding future developments in customer conduct and needs, rate of adoption of new services, technological developments, regulatory policy and the marketing strategy of competitors. However, there is no certainty that this strategy will in fact eventuate, or will eventuate in the manner set out above. The circumstances that might lead to failure of the strategy to eventuate, or to its absolute failure, depend, *inter alia*, on frequent technological changes and on regulatory compulsions.

2. FIXED-LINE DOMESTIC SERVICES – BEZEQ, THE ISRAEL TELECOMMUNICATION CORP. LTD. ("THE COMPANY")

Section 2.1.2 – General information on area of operations – statutory restrictions and special constraints

Tariffs were updated on June 1, 2009, and interconnect tariffs to the Company were reduced as of the same date. See update to section 2.16.1 below.

Section 2.3 - Breakdown of revenues and profitability of products and services

For updates of data regarding the breakdown of the Company's revenues based on products and services, see Note 12B to the financial statements of the Company for the period ended on September 30, 2009.

Section 2.6 – Competition

On May 10, 2009, HOT announced the establishment of a UFI (Ultra Fast Internet) network using Docsis3 technology. According to its announcement, the network will offer speeds of up to 100 mega. In accordance with its announcement, HOT launched the mentioned network in October 2009.

Section 2.6.1 – Telephony

With regard to the Company's petition to the High Court of Justice concerning enforcement of the structural separation rules on HOT – on June 4, 2009, the Ministry of Communications gave notice of an amendment of HOT Telecom's license with respect to structural separation between HOT Telecom and HOT Communications Systems Ltd. ("HOT Broadcasts") setting out restrictions on the structural separation obligation that had been part of HOT Telecom's license. Under these circumstances, and pursuant to supplementary notices by the Respondents (the State and HOT), on July 16, 2009, the Company filed a supplementary notice in which it requested that the Court set aside the petition. On July 19, 2009, the ruling of the Supreme Court was handed down stating that the petition should be set aside, in accordance with the petitioners' request, with no order being made as to costs.

On July 30, 2009, the Ministry of Communications issued a hearing for HOT Telecom after HOT Net, a limited partnership wholly owned by HOT Broadcasts, submitted a petition to receive a special license to provide Internet access services. The hearing relates to the amendment of the HOT Telecom's license prior to issuing a license to HOT Net, in order to set out the mechanisms that will make it possible for them to market a joint basket of services, while maintaining the limitations regarding the structure separation between HOT Telecom and HOT Broadcasts, and as a result thereof, between HOT Telecom and HOT Net.

Regarding the hearing on the issue of tariffs for PRI services (which are mainly fines for exiting the PRI service), on August 8, 2009, the Ministry of Communications decided to accept the manner of operation that the Company proposed for changes in this matter.

Section 2.6.2 – Broad Band Access to the Internet

On August 31, 2009, the Ministry of Communications published a request to receive public opinions regarding the organizing the structure of the market for broadband service over the cellular telephone network. Regarding this issue, please see the updates to Sections 3.7 and 4.1.2, below.

Section 2.6.7

Section H – NGN: In September 2009, the Company launched the NGN network and as of the date this report was published, approximately 270,000 of the Company's subscribers are connected to the network.

Section 2.7 – Property, plant and equipment

Section 2.7.4 – Real estate

During the course of the first nine months of 2009, the Company sold seven real estate assets in a total area of approximately 41,400 m^2 in land and approximately 20,000 m^2 built-up, for a total sum of NIS 93 million (approximately NIS 65 million of which in the third quarter of 2009). Additionally, under the settlement agreement between the Company and the Israel Lands Administration, an agreement was signed in June 2009 between the parties to the effect that the Company undertook to return the Bayit VaGan installation to the State within 18 months of the date of execution of the agreement and to waive receipt of a substitute property for such property, in consideration for the sum of approximately NIS 6 million. The Company invested the above consideration in the purchase of offices for the purpose of providing services to the Israel Broadcast Authority.

Section 2.9 – Human resources

On May 27, 2009, the Company's Board of Directors decided to the change the organizational structure so that the Company's Internal Auditor no longer reports to the Chairman of the Board but rather to the CEO.

Pursuant to a resolution of the Company's Board of Directors in 2008 to approve the retirement of 245 employees during 2009 in accordance with the conditions of the Collective Agreement of December 2006, 176 employees retired from the Company in this context as at November 3, 2009 (of whom 171 retired prior to September 30, 2009).

On November 4, 2009, the Company's Board of Directors approved an early retirement plan for employees for 2010, in which approximately 171 employees will retire from the Company at an overall cost of approximately NIS 225 million, in accordance with the conditions of the Collective Agreement of December 2006. Furthermore, the Company's Board of Directors decided at the same time to approve an additional expense of approximately NIS 41 million for the purpose of completing the 2009 early retirement plan. In consideration thereof, the Company is expected to record a provision of NIS 266 million for this purpose in its financial statements for Q4 2009.

Section 2.13 – Finance

Section 2.13.6 – Credit rating

On September 3, 2009, Moody's which rates the Company, gave notice that the Company's rating would remain Baa1 (stable).

On October 28, 2009, S&P which rates the Company, and Standard & Poor's Maalot which rates the Company's debentures, gave notice that it placed a Credit Watch with negative consequences on the rating of the international company which is BBB+ (BBB plus) and the rating of the Company's local debentures which are rated AA+ (AA plus) following the notification regarding that the Company's controlling shareholder AP.SB.AR. Holdings, Ltd. concluded a contract for the sale of its entire holdings in Bezeq (approximately, 30.6%) to Smile 012, Communications Ltd, and the possible impact of the change of control on the capital structure of the Company.

Section 2.14 – Taxation

See Note 15(b) to the financial statements of the Company for the period ended on September 30, 2009.

Section 2.16 – Limitation and regulation of Company activities

Section 2.16.1 – Control of the Company's tariffs

Sub-section (a), regarding update of the Company's tariffs – According to the Communications (Telecommunications and Broadcasts) (Calculation of Payments and Linkage for Telecommunications Services) Announcement, 5769-2009, the Company's tariffs were updated as of June 1, 2009, based on the regular update formula in the Communications (Telecommunications and Broadcasts) (Calculation of Payments and Linkage for Telecommunications Services) (Amendment) Regulations 5767-2007, so that the monthly payment for a telephone line and for a basic ISDN (Integrated Services Digital Network) line rose by 3.8% and the other controlled services provided by the Company declined by 0.3183%.

Furthermore, pursuant to the amendment of the Communications (Telecommunications and Broadcasting) (Payments for Interconnect) (Amendment) Regulations, 5769-2009, the interconnect fee paid by cellular and domestic operators in respect of termination of a call on the domestic operator's network, and the interconnect fee the international operators pay in respect of an international call that begins or ends on the domestic operator's network, was reduced as of June 1, 2009 by 0.3183%.

Section 2.16.2 – The Company's general license

Concerning the letter of the Director General of the Ministry of Communications of March 9, 2009, in which he gave notice that he was considering imposing a monetary sanction on the Company for alleged breach of the provisions of its license with respect to structural separation, on April 26, 2009, the Company submitted its detailed remarks to the effect that the Company had not breached the provisions of its license with respect to structural separation, and no such breach can be attributed to it, and that in these circumstances and those described in the Company's document, a monetary sanction cannot be imposed on the Company. The Company also requested a hearing.

Concerning baskets of common services – According to the notice of the Ministry of Communications on July 8, 2009, the market share of the Company has fallen, in terms of normative revenue for June 2009, to 78.5% in fixed-line telephony in the private sector and to 86.3% in the business sector. In addition, the Ministry is employing another method of measurement intended for determining the discount brackets permitted to the Company with approvals of alternative tariff baskets as prescribed in the Gronau Report. By this measurement, the Company's market share in June 2009, in terms of regular (individual) lines based on normative revenue, declined to 77.2%, and in terms of access lines based on normative revenue, declined to 81.6%.

Section 2.16.3 – Royalties

On October 27, 2009, the Economic Committee of the Knesset approved the amendment to the regulations regarding royalties as described in the Company's periodic report for 2008.

Section 2.16.6 – Rules and regulations under the Communications Law

With respect to the Exceptions Committee – according to the Ministry of Communications notice dated June 16, 2009, the Ministry of Communications submitted draft regulations relating to the Exemption Advisory Committee for the approval of the Economic Committee of the Knesset.

Section 2.16.11 – Establishment of Communications Installations

Section D – The Company's reservations regarding the proposed wording of National Outline Plans for Communications, NOP 36A and NOP 36B was accepted in part by the investigator appointed in accordance with the Planning and Construction Law for hearing reservations regarding NOP 36A and NOP 36B but they were not included in the text submitted for the approval of the Subcommittee for Principles of Planning of the National Planning and Construction Committee in July 2009. The Company is working to change the proposed wording of the provisions of NOP 36A and NOP 36B

Section 2.18 – Legal proceedings

For updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2009.

3. CELLULAR – PELEPHONE COMMUNICATIONS LTD. ("PELEPHONE")

Section 3.1.9 – General Information on the Field of Activity

In September 2009, Pelephone submitted an offer to acquire Mirs Communications, Ltd. in accordance the conditions set therein. It is emphasized that the offer is still in the stage of a proposal and it is not certain that the offer will be accepted. Similarly, the final conditions and limitations on which the transaction is based are yet to be determined. The transaction, if it is to occur, is conditional on various regulatory permits and it is also not certain that these will be received. According to information published in the media, other organizations are competing for the acquisition of Mirs and negotiations are being conducted with another competitor.

In September 2009, Netvision reported that, in the context of various works it is undertaking as a result of changes occurring and likely to occur in the communications market, it is in the very earliest preliminary stages of examining a business combination with Cellcom Israel, Ltd. According to the report, current regulations do not allow the aforementioned business combination and this move would be possible only if the relevant legislation is amended and would be conditional on receiving various permits as required by any law.

Section 3.4 – New Products

In May 2009, Pelephone signed an agreement with Apple Sales International ("the manufacturer") for the acquisition and distribution of iPhone handsets in Israel. Under the agreement, Pelephone undertakes to acquire a minimum number of handsets every year for three years. These quantities are a significant part of the number of handsets expected to be sold by Pelephone during the agreement period and represent approximately 5% of the cost of Pelephone's annual services and sales. Under the agreement, the cost of the handsets for Pelephone depends on the prices that are in effect at the actual acquisition date.

The information in this section contains forward-looking information, based on the Company's assessments and forecasts. Actual results might be substantially different from these assessments, taking into account the changes that might occur in commercial conditions.

Section 3.7 – Competition

In August 2009, the Ministry of Communications issued a request to receive the public's positions regarding organizing the structure of the market for broadband service over the cellular telephone network. In the context of the hearing the Ministry of Communications wanted to examine the possibility of separating the provision of access to the broadband network from the connection to the Internet (ISP), similar to the division that exists on the fixed line network. In this context, the Ministry will examine the following topics:

1. The mobile communications market, the market for providing infrastructure for accessing the Internet, the market for providing connection to the Internet (ISP) and the market for fixed line communications.
2. The welfare of the consumer as regards the price, quality and the variety of Internet services.

Pelephone submitted its position stating that it opposed the proposal.

Section 3.7.1

In March 2009, upon the recommendation of the Gronau Committee, the Ministry of Communications published a hearing on the issue of a change in the tariff structure and the method of billing for international calls via a cellular network. In May 2009, Pelephone submitted its response to the hearing and its objection to the proposed change.

According to government publications and pursuant to the government's resolution to set up an inter-ministerial team regarding examination of interconnect tariffs, a joint team was set up between the Ministry of Communications and the Ministry of Finance which has recently completed a tender to select an international consultancy company to look into this matter. The company that was chosen was Nera. The issues defined for examination are examination of interconnect tariffs and examination of conditions of entry of new competitors onto the cellular market. During September 2009, representatives of Pelephone, the Ministry of Communications and Nera began working together.

Under the Ministry of Communications' work plan, the team is expected to submit recommendations at the beginning of 2010.

According to government publications, in government discussions regarding the State budget for 2009-2010, a recommendation was made to publish a frequency tender for an additional infrastructure-owning cellular carrier. Following this, the Ministry of Communications set up a tender committee which was supposed to publish a frequency tender as aforesaid by the end of the third quarter of 2009. The tender was expected to include various benefits aimed at removing obstacles and significantly facilitating the entry of another infrastructure-owning carrier. During October 2009, the Ministry of Communications published the main points of the planned tender, which were developed by the Tender Committee, while noting that they are subject to change in the final tender documents that will be published in the future.

1. The tender will offer two frequency bands to two operators.
2. Only Mirs and new operators who are not connected to existing cellular operators and comply with the threshold conditions will be permitted to participate in the tender.
3. The minimum price for acquiring a frequency band will be NIS 180 million per operator.
4. A mechanism for returning the cost of the license and the frequency fee to the winner of the tender during the first five years of operation in connection with an increase in the market share in the private sector.
5. The winner of the tender will be exempt from paying royalties to the State for the first five years of operation.
6. A period of seven years will be set for the winner of the tender to deploy the new network.
7. If a decision is made to reduce the interconnect charges, the winner of the tender will be required to pay according to the minimum tariff set.
8. In order to allow the winner of the tender to operate the network before it is fully deployed, the possibility of arranging cooperative use of the sites/domestic migratory services using the networks of existing cellular operators.

The committee is expected to issue the tender before the end of 2009.

Section 3.7.2 – Mobile Virtual Network Operator (MVNO)

In the context of discussions surrounding the Budget Law and the Arrangements Law for 2009 and 2010 conducted during the months of June – July 2009, an amendment to the Communications Law was approved to the effect that the Minister of Communications is expected to complete all of the proceedings required in order to grant licenses by October 1, 2009. Likewise, the amendment to the law also provided that should an MVNO license be awarded and in the event that such licensee has conducted negotiations with the existing operators which did not give rise to a positive result within a period of 6 – 9 months, and it is proven that this stemmed from anti-competitive conduct by the existing operators, the Minister of Communications shall intervene in the commercial conditions in accordance with the jurisdiction vested in him by law.

Section 3.7.5 – WIMAX

Further to the hearings held on the subject of the tenders for operating a network using WIMAX technology, the Ministry of Communications issued, in March 2009, a policy document regarding the allocation of frequencies for establishing a network using WIMAX technology. According to this policy document, the frequencies will be allocated through two separate tenders. In the first tender, frequencies will be allocated only to new operators and the second tender, issued after clearing another frequency in the aforementioned range, will be open to additional participants including existing cellular operators. As of the date of this report, neither of these tenders has been issued.

Section 3.9.2 – Premises Used by Pelephone

Regarding section 3.9.2.2 – In October 2009, the Court approved the compromise agreement between the parties. According to this agreement, the claim that Pelephone filed against the Israel Lands Administration et al. will be erased and the parties will negotiate the issue until December 31, 2009 for the purpose of resolving the issue out of court.

Section 3.15.6 – Credit rating

On July 9, 2009, Maalot gave notice of increase of the rating of Pelephone's debentures from AA minus to AA plus. The rating forecast is stable and reflects Maalot's assessment that Pelephone will continue to be strategically important to Bezeq and will maintain a strong level of profitability, and will create significant cash flows in the future.

On October 28, 2009, Standard & Poor's Maalot, which rates the Pelephone's debentures, gave notice that it placed a Credit Watch with negative consequences on the rating of the Pelephone's local debentures which are rated AA+ (AA plus) following the notification regarding the Company's controlling shareholder AP.SB.AR. Holdings, Ltd. conclusion of a contract for the sale of its entire holdings in Bezeq (approximately, 30.6%) to Smile 012, Communications Ltd, and the possible impact of the change of control on the capital structure of the Company (and therefore of Pelephone as well).

Section 3.16 – Taxation

See Note 15(b) to the financial statements of the Company for the period ended on June 30, 2009.

Section 3.18.2 – Control of tariffs

Regarding section 3.18.2, see also section 3.7.1, above.

Section 3.18.3.1 – Main changes in Pelephone's license

Section A – further to hearings on the question of disconnecting the link between a terminal MRT equipment purchase transaction and the giving of benefits, the Ministry of Communications ruled that the MRT license of the cellular companies would be amended such that as of November 1, 2009, the licensee would not create any link between any benefit for MRT services granted to the subscriber and the fact that MRT terminal equipment in the subscriber's possession was purchased, rented or received from a licensee or other reseller acting for such licensee.

Section C – The changes in terms of the invoice structure will take effect in December 2009.

Section 3.18.3.3 – Site construction licenses

The team set up by the Attorney General to research the question of access facilities completed its work and submitted a report during the course of June 2009. The team's report was published on the websites of the Ministry for the Environment and the Ministry of Communications. In some of the team's conclusions, the representatives of the various ministries were in disagreement. The Ministry of Communications supported continuation of the exemption arrangement for a period of one to two years following the approval of NOP 36A1, in light of licensing difficulties mainly in urban areas, and an examination of the need for continuing the exemption in light of the quality of response that the NOP gives to the matter. The Ministries of the Interior and the Environment concluded that there was no justification for the exemption arrangement regarding cellular communications facilities to continue to exist. If the position of those ministries is accepted and the exemption arrangement is terminated, this will adversely affect deployment capabilities and the quality of the service that Pelephone will be able to provide to its customers, particularly in high-density areas. Prior to publication of the team's report, a further petition was filed with the High Court of Justice against the Attorney General, the inter-ministerial team and other persons, requesting remedies relating to the Attorney General's position supporting the continuation of the exemption from a building permit for wireless access facilities.

Following the report of the team and discussion of the subject held in September 2009, the Attorney General stated his position in a document dated September 9, 2009, according to which the Communications Regulations (Telecommunications and Transmissions) (Frequencies for Wireless Access Installations) 5762-2002 that includes the exemption from the requirement for a building permit according to Section 266c of the Construction and Planning Law, 5725-1965 for wireless access installations was enacted legally and properly. Despite this the Attorney General stated that in light of changes in law and in fact that have occurred in the intervening years and in light of their consequences, which became clear in the discussion and report of the team, the arrangement in its current form does strike a proper balance between the interests of the efficiency and competition and the interests expressed in the Planning and Construction Law. Furthermore, the Attorney General determined that the Ministries of the Interior and Communications would submit by the end of October 2009 regulations setting conditions that would limit and reduce application of the exemption from the requirement of building and use permit.

As for the private bills dealing with cancellation of the exemption from a permit for cellular wireless access facilities, the government decided to formulate its position in respect thereto only after publication of the inter-ministerial team's report. This position has not yet been formulated.

Section 3.21 – Legal proceedings

For updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2009.

4. INTERNATIONAL COMMUNICATIONS, INTERNET SERVICES AND NEP – BEZEQ INTERNATIONAL LTD. ("BEZEQ INTERNATIONAL")

Section 4.1.2 – Legislative and statutory restrictions applicable to Bezeq International

Special License for providing Internet access services – On August 10, 2009. Bezeq International received a special license for providing Internet access services. The services that Bezeq International is allowed to provide under terms of this license were previously supplied under the provisions of the General License for providing international telecommunications services of Bezeq International. Issuing this license is supposed to make the situation of Bezeq International equivalent to that of the other all other Internet providers who operate under a similar license. The license is valid until August 29, 2014.

Hearing regarding organization of the market structure for providing broadband service over the cellular telephone network – On August 31, 2009, the Ministry of Communications issued a request to receive the public's positions regarding organizing the structure of the market for broadband service over the cellular telephone network. In its request, the Ministry asked to examine the desirable structure for these services. The possible decision of the Ministry of Communications on this issue, which would change the current structure to one similar to the current structure for fixed line internet access could have substantive impact on the business of Bezeq International.

Section 4.1.2.2 – General Special Domestic License

On August 2, 2009, Bezeq International began to supply broadband domestic telephony services (VOB) to its private customers.

Section 4.1.2.5 – Gronau Committee Report.

In March 2009, the Ministry of Communications, upon the recommendation of the Gronau Committee, published a hearing regarding a change in the tariff structure and method of billing for international calls via cellular networks. In Bezeq International's response to the Ministry of Communications in the aforesaid hearing, Bezeq International expressed its objection to the proposed format for changing the tariff structure in overseas calls by cellular subscribers, pointed to possible faults as a result of its implementation, proposed reservations and limitations on its application and again warned the Ministry of Communications of the problems existing in the market for international telephony and internet access services provided by cellular operators.

Section 4.4 – New products

In October 2009, Bezeq International launched the Private NGN service, which offers private customers who surf at high speeds (10 MB and higher) a separate internet network.

Section 4.9.1 – Licenses to supply telecommunications services

Beginning on August 10, 2009, the internet access services of Bezeq International are provided under a Special License for providing internet services, which is valid until August 29, 2014. For additional details, see section 4.1.2, above.

Section 4.15.3 – Bank Guarantees

In accordance with the requirements of the Ministry of Communications, Bezeq International provided a bank guarantee of NIS 10 million for compliance with all of the requirements of the Special License for providing fixed line domestic telephone services that was issued to BIP Communications Solutions (Limited Partnership), which is controlled by Bezeq International.

Section 4.16 – Taxation

See Note 15(b) to the financial statements of the Company for the period ended on June 30, 2009.

Section 4.17.2 – Interconnect charges

In the context of the Special License for providing fixed line domestic telephone services, BIP Communications Solutions (Limited Partnership) is entitled to receive interconnect charges, in accordance with regulations, for completing calls on the network that it operates and for outgoing international calls and is obligated to pay interconnect charges for completing cellular calls to the cellular operator's network or for completing fixed line domestic calls on the network of another license holder.

Section 4.19 – Legal proceedings

For updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2009.

5. MULTI-CHANNEL TELEVISION – D.B.S. SATELLITE SERVICES (1998) LTD. ("DBS")

Section 5.1.3 – Developments in markets in the area of operation

Section 5.1.3 – In May 2009, the Government made a decision in which it determined, *inter alia,* that some of the provisions included in the Arrangements in the State Economy (Legislative amendments for attaining budget targets and economic policy for the 2009 fiscal year) Bill, 5769-2008, published in October 2008 ("the Arrangements Bill") would be amended. The decision determined, among other things, that the date on which license-holders for broadcasting would be able to broadcast advertising will be postponed to January 1, 2012 (with an option to postpone the date of the permit for a period not exceeding three years); that the date on which the broadcasting licenses would be required to offer the basic package to their subscribers will be postponed to August 1, 2012 (with an option to postpone that date for no more than one year); that the broadcasting licensees will distribute to all their subscribers the broadcasts of a special license-holder for cable broadcasts without collecting payment from the subscriber beyond the access fee. The Government also decided that if the Communications Law is amended as proposed in the relevant sections of the Arrangements Bill, to direct the Minister of Communications and the Minister of Finance to request approval from the Knesset Finance Committee for regulations granting exemption from payment of royalties to broadcasting licensees commencing on the date on which the broadcasting licensees are required to offer the basic package. The decision also states that the date for completing set-up of the DTT array will be postponed to August 2009. In addition, the Government decision adopted the recommendations of the Mordechai Committee in everything relating to the transition of the Second Authority franchisees from a regimen of franchises to one of licenses for the establishment of a National Communications Authority. The decision also provides that a committee is to be set up to examine the advertising fees paid by advertisers and bodies that sell advertisements to advertising companies. In June 2009, it was resolved to split the remedies regarding the matters described above from the Arrangements Bill and the discussion of them was transferred to the Economics Committee in order to prepare for first reading.

Section 5.1.3.1 – On August 2, 2009 the DTT system commenced broadcasting. In February 2009, the Minister of Finance made an order stating that DTT broadcast reception decoders will be exempt from purchase tax (as distinct from the decoders used by DBS which are subject to a 10% purchase tax).

Section 5.1.3.4 – In May 2009, the Council resolved to defer commencement of the new policy until the end of September 2009 in order to reexamine other models for regulating sports broadcasts on the paid sports broadcasts. In September 2009, the Council issued an invitation to present positions regarding the proposed model and therefore announced that it is again considering a new policy, however unless another decision is made before the end of October 2009, the policy is expected to become effective on November 1, 2009. In October 2009, the Council decided, *inter alia*, to reinforce the sports offerings on the basic sports channel (Sport 5), to establish a broadcast format for the pay sports broadcasts "5+" and to prohibit live sports broadcasts on other pay sports channels, unless the conditions stated in the decision are met.

Section 5.1.3.5 – In September 2009, the Council published a hearing, according to which:

a. The Council decided to amend the previous decision regarding the way in which special licenses are granted for movie channels and to examine, within six months from the day of the decision, the possibility of also canceling the Council's current policy that prohibits issuing special licenses to channels broadcasting series.

b. The Council will examine, within six months from the day of the decision, canceling the limitation in the current policy on the number special licenses that can be issued to a single organization.

c. The Council decided on certain leniencies in the production obligations holders of special licenses.

Section 5.1.3.7 – For the merger of the Company and DBS, see section 1.1.5 above.

Section 5.1.3.8 – In March 2009, the Ministry of Communications and the Council published a hearing on the question of the regulation of broadcasts over new broadcasting platforms and technologies. The hearing sought comments, *inter alia*, on the question of the characterization of the new services in respect of which the need for arrangement is being examined, including the nature and purpose of content, the method of distribution of such content, the handset that will enable its viewing, the need to distinguish linear broadcasts from VOD broadcasts, the method of offering services, the identity of the offerors, the extent to which the service providers are to be involved in various aspects of the service and the expectations of the reasonable consumer for regulatory protection. Comments were also requested regarding the scope of regulation necessary, including restrictions on adult broadcasts, protection of minors, classification and marking of broadcasts, original production obligations, a prohibition against broadcasting advertisements, and ethics in broadcasts. In addition, comments were also called for on the question of the need to protect new competitors and the impact that the regulation would have on the currently existing regulation. DBS presented its position in this hearing in May 2009.

Section 5.2 – Products and Services

In April 2009, DBS began marketing PVR decoders capable of receiving HDTV broadcasts (as well as the other services that PVR decoders permit), at the same time as it expanded the supply of channels that it broadcasts using HD technology.

Section 5.8 – Intangible assets

Section 5.8.1.2 – On May 4, 2009, a representative of the Civil Administration gave notice to DBS that the Civil Administration intended to extend the broadcast license in Judea and Samaria until 2014, overlapping the license in Israel, although the extension still requires a final resolution by the head of the Civil Administration.

Section 5.11.1.B – Space segments

In June 2009, a letter was received from Aviation Industries containing a demand for immediate repayment of the debt still owed by DBS for use of the Amos 1 satellite, as well as payments of interest and additional sums allegedly owing to Aviation Industries by virtue of an agreement between the Parties. DBS has arguments against some of the sums alleged by Aviation Industries. In September 2009, the Company and Aviation Industries signed an agreement resolving the financial disputes between them.

Section 5.14 – Taxation

See Note 15(b) to the financial statements of the Company for the period ended on September 30, 2009.

Section 5.15.1 – Specific legal restrictions on operations

In March 2009, the Ministry of Communications gave notice to DBS that in the opinion of the legal counsel, and in the opinion of the Legal Department of the Ministry of Communications, the split of the deeds of pledge of shares of DBS charged to the consortium of banks into individual charges for each bank will not, in and of itself, affect Bank Leumi's status as a "holder" of DBS with respect to the qualification restriction set out in the License Regulations, in the absence of an amendment of the financing agreement. The Ministry of Communications gave further notice that it intends to take the necessary steps to ensure compliance with the conditions of the Regulations. Although DBS is of the opinion that the current state of affairs does not amount to a breach of the aforesaid qualification restriction, it is negotiating with the Ministry of Communications to arrive at an arrangement that will satisfy the Ministry in order to resolve the issue within such fixed period of time as may be agreed upon. In September 2009, Bank Leumi gave notice that its subsidiary concluded an agreement to sell its entire holding in Keshet Broadcasting, Ltd. conditional on compliance with the stipulated conditions, to Bank Leumi. In the opinion of DBS, if this transaction is completed, the subordination of shares in DBS will not be a breach of the aforementioned qualification restriction, even in the opinion of the Ministry of Communications.

Regarding the obligation to invest in local productions – In October 2009, the Council informed DBS, *inter alia*, that there is a deficit in its investment in local productions of the external production channels and that DBS must complete it during 2010 and 2011. Therefore, the chairperson of the Council imposed a financial sanction on DBS. Furthermore, the Council informed DBS that it had not met its obligation to invest in the television movie, cinema movie, complex drama and mini-series genres in 2008 (*inter alia*, because of deficiencies from the past) and that it must also complete this lack in during 2010 and 2011. A financial sanction was also imposed on DBS for not meeting this obligation. As of this report, DBS is studying the Council's notifications and the decision to impose the said financial sanctions on it.

Section 5.15.3 – Principal restrictions by virtue of the law and broadcasting license

With respect to transfer fees – In March 2009, the Ministry of Communications published a hearing regarding the setting of transfer fees that the producer of an independent channel, including the broadcaster of a designated channel, must pay DBS for use of its channels, noting that the outcome would constitute the basis for a resolution of the dispute between DBS and the designated channels, the sum of the payment set in the hearing being applicable as of 2007 and until the end of 2013 and the method of its calculation serving the parties as an outline for calculating the amount of the payment until 2006. The Ministry of Communications noted that the economic opinion that it attached to the hearing may be used as a basis for ruling in other disputes, if such arise between DBS and other independent channel operators. Under the aforesaid economic opinion, the usage fee will include a fixed component of an annual payment of approximately NIS 1.2 million, plus variable payment components amounting to approximately NIS 1 million with respect to an independent channel producer not financed by way of subscription fees. In June 2009, DBS submitted its position in the hearing. As at the date of this report, the Ministry of Communications' decision on this hearing has not yet been handed down. In July 2009, a bill was approved in preliminary reading to the effect that the designated channels would be exempt from payment of transition fees to the cable company. To the best of DBS's knowledge, this bill was approved by the Ministerial Committee on Legislation however the Minister of Communications has submitted an appeal against this decision.

Section 5.18 – Legal proceedings

In April 2009, two claims were filed against DBS in the Regional Labor Court on behalf of 21 technicians (20 of whom are former employees of the Company previously and the other is still employed by the Company) in a total sum of NIS 1.3 million. The claim alleges that DBS owes the technicians for various salary components that the plaintiffs claim were not paid to them, and that DBS held over some of their salaries. A statement of defense was filed in July 2009.

Section 5.18.1 – In June 2009, a settlement agreement was signed to the effect that without admitting to any of the claims DBS would compensate subscribers from whose deposits depreciation was alleged to have been unlawfully collected such that existing subscribers of DBS would be entitled to view 3 DVDbox movies without payment and subscribers who had left YES would be entitled to monetary compensation of NIS 25 or NIS 50 as set out in the Agreement or to 5 DVDbox movies without payment should they choose to return to DBS's broadcasts. It was further held that the lead plaintiff would be entitled to payment of the sum of NIS 50,000 and her attorneys would be entitled to the sum of NIS 450,000. The Court at which the agreement was submitted for approval held that this was an appropriate and reasonable arrangement and allowed DBS to publish an initial notice in this regard, which was published on June 18, 2009. On September 1, 2009, a request was submitted for approval of the compromise agreement and on September 2, 2009, the agreement was approved as a court ruling. On September 14, 2009, a second notice to the public was published.

Section 5.18.2 – In April 2009, the Special Manager in the debt claim handed down a decision in which the debt claim that DBS filed was accepted in part, such that the sum of the debt to DBS was assessed in the sum of approximately NIS 180,000.

<u>Section 5.18.3</u> – On June 17, 2009, a hearing took place in the Supreme Court on the appeal and the counter appeal. At the recommendation of the Court, it was agreed that the appeal and the counter-appeal be struck out without any award as to costs, without the Court expressing any opinion as to the essence of the ruling of the District Court regarding remuneration and fees.

For updates on the subject of legal proceedings, see Note 6 to the financial statements of the Company for the period ended September 30, 2009.

November 4, 2009	
Date	Bezeq – The Israel Telecommunication Corp. Ltd.

Names and titles of signatories:

Shlomo Rodav – Chairman of the Board

Abraham Gabbay – CEO