August 20, 2008

"Bezeq" The Israel Telecommunication Corp. Limited

Quarterly Report for the period ending 30.6.08

Update of Chapter A (Description of Company Operations) of the Periodic Report for 2007

Directors' Report on the State of the Company's Affairs for the period ended June 30, 2008

Condensed Interim Consolidated Financial Statements as at June 30, 2008

Update of Chapter A (Description of Company Operations) of the Periodic Report for 2007

UPDATE OF CHAPTER A (DESCRIPTION OF COMPANY OPERATIONS)[1]
OF THE PERIODIC REPORT FOR 2007 ("THE PERIODIC REPORT")
OF "BEZEQ" – THE ISRAEL TELECOMMUNICATIONS CORP. LTD. (HEREINAFTER: "the Company")

In this report, which contains an update of the chapter regarding the description of the Company's business in the 2007 periodic report, the Company has included forward-looking information, as defined in the Securities Law 5728-1968 (hereinafter: the "Securities Law") with respect to both itself and the market. Such information includes forecasts, goals, appraisals and assessments which apply to future events or matters the occurrence of which are not certain and are not within the Corporation's control. Forward-looking information in this report will usually be identified specifically, or by employing statements such as "the Company expects", "the Company estimates", "it is the Company's intention", and similar statements.

Forward-looking information is not a proven fact and is based only on the Corporation's subjective assessment, which relies on its assumptions based, inter alia, on a general analysis of the information available at the time of drafting of this report, including public announcements, research and surveys, which contain no undertakings as to the correctness or completeness of the information contained therein, and whose correctness has not been independently corrected by the Corporation. The Corporation's assessments vary from time to time in accordance with the circumstances.

In addition, the occurrence or non-occurrence of the forward-looking information will be affected by factors that cannot be assessed in advance, and which are not within the Corporation's control Corporation, including the risk factors that characterize its operations as set out in this report, and additionally, developments in the general environment, and external factors and the regulation that affects the Corporation'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

On March 12, 2008, the Gronau Committee appointed by the Minister of Communications to formulate detailed recommendations regarding policy and rules of competition in the field of communications in Israel (the "Gronau Committee") published its Report. Following are the principal summary recommendations:

Fixed-Line Sector

1. To act to develop the wholesale market in the fixed-line sector, centered around the local loop unbundling (hereinafter - "LLU") obligation. In this context, the owners of the universal infrastructure are to be required to sell services wholesale and to lease access segments to competitors. For reasons of technological applicability, at this stage the local loop unbundling obligation will only apply to the Company.

2. Within 15 months of the date of adoption of the recommendation by the Minister of Communications, the regulating body will publish maximum tariffs for the leasing of access segments and other services sold on the wholesale market (bitstream access services, resale, etc.) and the conditions for provision of such services. Such tariffs and conditions are to be determined subsequent to hearing the positions of the entities operating in the segment.

3. To grant a permit to the Company's subsidiaries to supply non-degradable service packages[2], including Bezeq Fixed-Line telephony and broadband services and IPTV, after implementation of the arrangement set out in section 1 above. On that date, the subsidiaries of the Company shall also be entitled to receive special licenses for the supply of domestic carrier services that are not VOB.

[1] The update is pursuant to Article 39A of the Securities Regulations (Periodic and Immediate Reports), 5730-1970, 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 2006 [sic] and relates to the section numbers in Chapter A (Description of Company Operations) in such periodic report.

[2] For which there is no obligation for any service included in such packages to be purchased individually under similar terms as provided in the service package.

4. So long as the Bezeq Group's market share is greater than 60%, supervision of the Company's tariffs shall continue in the format of fixing binding tariffs (fix); various restrictions (as set out in the recommendations) shall be set with respect to approval of alternative tariff bundles for the Company; with respect to supervised tariffs - up until the middle of 2009, cost-based tariffs will be prescribed for call completion on the fixed-line network; with respect to non-supervised tariffs, "loyalty discounts" will be prohibited so long as the Company is a monopoly: PRI lines - if there is no significant change in market share, the prices of these will come under supervision.

5. The structural separation in the Company is to remain so long as there are only two companies with nationally deployed fixed line infrastructure. Likewise, if the Minister of Communications finds, within a reasonable time of implementation of the local loop unbundling arrangement (no longer than two years), that the Company's actions are preventing expansion of competition in the domestic communications market, the recommendation is that he will exercise his powers under section 4(d2)(3) of the Communications Law regarding structural separation between operation of the infrastructure and operation of services at the Company.

<u>Cellular Sector</u>

It is necessary to accelerate the regulation processes required for the entry of virtual carriers, to accelerate the WiMAX tender in order to strengthen competition in the mobile sector and additionally, during 2009, to check the cost of call completion on mobile networks and to amend the tariff accordingly.

<u>International Call Sector</u>

International call tariffs via mobile telephones to be prescribed by the international calling company, and that company will make payments to the cellular company at the tariff determined in the Interconnect Regulations for call completion on mobile networks. Furthermore, new players controlled by the cellular companies shall be permitted entry into the international call sector.

<u>Multi-Channel Television</u>

1. Setting up of a "narrow basic channel package", including 5-10 channels (open channels and channels of special social or cultural value), with the possibility that the regulating body might determine the price of the package.

2. Enforcement of structural separation between Hot Broadcasts and Hot Telecom in the framework of their licenses, in accordance with the existing format in place in the Company.

<u>General</u>

<u>Consumer Issues</u> - The OECD recommendations are a guiding framework for handling consumer issues. It shall be prohibited to change fixed tariffs in a contract with customers during the contract term, the term of contracts shall be limited to 18-24 months and the prevention of transfer due to the tying of purchase of a handset to purchase of services will be removed.

<u>Royalties</u> - adoption of the position taken by the Carol Committee regarding the gradual reduction of the rate of royalties payable by licensees, up to cancellation of such royalties in the future. If there is a reduction of taxes during 2008-2012, the royalties will be cancelled. It is proper that cancellation of the royalties accompany a parallel reduction in tariffs.

On August 13, 2008, the Minister of Communications announced his decision to adopt the Committee’s recommendations, subject to changes and points of emphasis, which will become the Ministry’s guiding policy for the coming years. The Minister’s decision clarifies the regulatory situation to a certain extent. Hereunder, please find the principal changes and points of emphasis:

<u>Structure Changes in the Fixed Line Sector</u>

The Ministry of Communications will commence work on preparing the regulatory and pricing infrastructure required to establish a wholesale market, including arrangements for separation into segments (LLU). Nonetheless, in order to provide an incentive for the Company to implement the wholesale market arrangements as quickly as possible, the Company will be allowed to present the Ministry with a commercial agreement for the provision of wholesale services with any communications operator that is not a subsidiary of the Company.

The Minister agrees with the Committee regarding the importance of the fixed telephone infrastructure. Therefore, as long as the Minister thinks that it is appropriate to create incentives for the Company, which will advance rapid, universal deployment of the next generation network (NGN), he will work to do so.

Tariff Flexibility for Bezeq – Alternative Service Packages

In order to streamline the process for approving alternate payment packages and provide a higher level of certainty for the Company, the Minister decided to change the mechanism for approving alternate payment packages, such that the Company will not need to wait until the explicit approval of two Ministers is received but rather it will be able to offer a package 45 days subsequent to the detailed request being filed at the Ministry of Communications unless the Minister of Communications or the Minister of Finance informs it of their objection to the request. It should be noted that the Minister adopted the Committee's recommendation that as long as the Bezeq Group's market share is greater than 60%, regulation of the Company tariffs will continue in accordance with the current format of setting obligatory ("fix") tariffs. Regarding alternative payment packages, the maximum permitted discount rate will increase as the Group's market share for fixed telephony decreases (it will remain 15% as long as the market share is greater than 85%; 25% as long as the market share is between 75% and 85%; and 40% when as the market share is between 60% and 75%).

Competition in the Mobile Field

The Minister instructed the CEO of the Ministry of Communications to work towards advancing a licensing policy for virtual operators (MVNO).

Multi-Channel Television Sector – Basic Package of Channels

The Minister decided to conduct a more comprehensive examination of all aspects of the broadcast field. Therefore, in the near future, it is his intention to appoint a committee to provide recommendations regarding policy and terms of competition in the multi-channel and commercial television sector.

Structural Separation in the HOT Group

The Ministry will work in order to ensure that the companies in the Hot Group comply with the rules of structural separation established in their licenses, with the exception of the possibility available to the companies, of marketing packages of services that include services offered by the companies, on a regular basis as is currently permitted by their licenses, contrary to the committee's decision, which was that the terms of separation in the form applied to the Company, should be enforced.

The guidelines for structural separation must make it possible to implement the recommendations regarding the wholesale markets in general and its prices in particular.

International Call Sector – Entrance of Players Controlled by Mobile Companies to the International Call Sector

The Minister is of the opinion that the recommendations of the Committee regarding setting fees for outgoing international calls using a mobile network in the framework of the interconnect regulations should be advanced.

The Company is examining the decisions of the Minister and is unable to assess, at this stage, what their precise impact will be on its business results and those of its subsidiaries.

See also updates to sections 3.7, 4.1.2 and 5.1.3.5 below.

Section 1.1.4 - Holdings of the Company

The following are details of the current rate of holdings of the Company, fully diluted, assuming the exercise of all of the options actually allocated to employees of the Company as at the date of publication of this report (as set out in the Periodic Report for 2007 and in the update to section 1.3.2 below, including the allocation to the Chairman of the Board of Directors, made on June 1, 2008), and assuming the exercise of Ap. Sab. Ar.'s option to purchase approximately 10.66% of the State's shares in the Company.

Shareholders	Percentage holdings as at 20.08.08	Percentage holdings (fully diluted)
Ap. Sab. Ar.	30.00%	38.81%
State of Israel	15.63%	0.97%
Zeevi Group	17.75%	16.95%
The Public	36.62%	43.27%

Section 1.1.5A – Mergers and Acquisitions – DBS

During the hearing of an appeal filed by the Company against the decision of the Antitrust Commissioner to object to the Company's merger with DBS, the Antitrust Tribunal proposed that the parties try to reach an agreement regarding approval of the merger with conditions. At this stage the court proceedings are continuing.

Section 1.1.6 - Realizations

With respect to satellite operations - on March 26, 2008, an agreement regarding the sale of the Company's satellite communications operations ("Inmarsat" and "Bezeq Sat") and assets relating to such operations, including the satellite communications site at the Ella Valley, was executed between the Company and RRsat Global Communications Network Ltd., a company registered in Israel whose shares are traded on NASDAQ in the USA. According to the agreement, the operations are to be sold for a consideration of a total amount in NIS equal to US $ 15 million (at the representative rate on the date of payment) plus VAT, subject to price adjustments as a result of various stipulations and changes that might occur, if at all, to the operations during the period through the date of completion of the transaction. Completion of the transaction is subject, inter alia, to the regulatory consents of the Ministry of Defense, the Ministry of Communications and the Antitrust Commissioner. The Antitrust Commissioner gave his approval on June 4, 2008. If and when the transaction is completed at the maximum price as aforesaid, then the Company is expected to record a capital gain of approximately NIS 50 million (before tax)[3] in respect thereof, subject to changes in the dollar representative rate.

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

Section 1.3.2 - Employee Share Option Plans

Under the share option plan for senior managers and employees of the Group of November 2007 for the allocation of up to 65,000,000 options, since the date of publication of the 2007 periodic report, 17,200,000 additional options have been allotted (including the allotment of 9,000,000 options to the Chairman of the Board of Directors of the Company) such that as of the date of this update, a net total (less options that have been forfeited) of 56,200,000 options have been allotted through the plan.

Section 1.4 – Payment of Dividends

On April 28, 2008, a cash dividend for a total amount of NIS 679 million was distributed to the Company shareholders, representing, as at the date of the distribution NIS 0.260648 per share, this having been approved by the General Meeting of shareholders of the Company on April 3, 2008.

On August 20, 2008, the Board of Directors of the Company approved the distribution of a cash dividend for a total amount of NIS 835 million to the Company shareholders, representing, as at the date of the distribution NIS 0.3205318 per share, this to be approved by the General Meeting of shareholders of the Company on September 28, 2008.

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[3] Based on an exchange rate of NIS 3.576 = US$ 1.00.

Section 1.5 - Financial Information regarding the Group's Areas of Operations

Section 1.5.3 - Principal Results and Operational Data

A. Bezeq Fixed-Line (operations of the Company as domestic carrier)

	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	1,354	1,408	1,453	1,425	1,393	1,442
Operating Profit (NIS millions)	428	368	340	327	243	369
Depreciation and amortization (NIS millions)	211	218	232	236	236	237
EBITDA (NIS millions)	639	586	572	563	479	606
Payments for investments in property, plant and equipment and intangible assets (NIS millions)*	132	158	141	149	101	113
Proceeds received from sale of property, plant and equipment (NIS millions)*	25	60	23	16	96	18
Number of active subscriber lines at the end of the period (thousands)	2,682	2,713	2,761	2,767	2,778	2,797
Average monthly revenue per line (NIS)**	82.6	84.9	85.8	85.6	85.1	88.3
Number of outgoing call minutes used (millions)	3,413	3,594	3,738	3,849	3,753	3,914
Number of incoming call minutes used (millions)	1,191	1,182	1,164	1,149	1,069	1,045
Number of ADSL subscribers at the end of the period (thousands)	982	970	963	942	924	912
Average monthly revenue per ADSL subscriber (NIS).	57.7	58.1	58.1	58.5	58.1	57.4

* Data for Q1 2008 were updated retroactively, in order to reflect the timing of payments of investments in property, plant and equipment and receipts from sale of property, plant and equipment.

** Not including revenues from transmission and data communications services, services to communications providers, and other contractor work. In this item, insignificant adjustments were made to prior quarters in order to present nominal, non-standardized figures.

B. Pelephone

Pelephone	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	1,188	1,173	1,182	1,203	1,152	1,147
Operating Profit (NIS millions)	266	215	133	219	240	213
Depreciation and amortization (NIS millions)	130	129	126	121	115	117
EBITDA (NIS millions)	396	344	259	340	355	330
Net profit (NIS millions)	180	163	104	154	173	154
Cash flows from current operations (NIS millions)	351	264	252	392	246	359
Payments for investments in property, plant and equipment and intangible assets (NIS millions)	182	103	120	81	117	63
Proceeds received from sale of property, plant and equipment (NIS millions)	1	1	3	-	-	2
Number of subscribers at end of period (thousands)	2,636	2,595	2,622	2,560	2,513	2,478
Average minutes of use per subscriber (MOU) per month	358	355	358	363	350	344
Average monthly revenue per subscriber (NIS) (ARPU)	128	126	130	135	129	132
Number of 3G subscribers at end of period (thousands)	977	867	749	607	471	358
Revenues from value added services and content, as a percentage of total cellular service revenues	15.5%	15.0%	13.6%	12.8%	12.5%	12.0%

C. Bezeq International

	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	326	314	334	326	321	323
Operating Profit (NIS millions)	63	54	46	54	53	51
Depreciation and amortization (NIS millions)	20	20	21	21	22	23
EBITDA (NIS millions)	83	74	67	75	75	74
Net profit (NIS millions)	47	41	38	39	39	37
Cash flow from current operations (NIS millions)	51	8	30	34	32	(1)
Payments for investments in property, plant and equipment and intangible assets (in NIS millions)*	31	28	36	29	18	8
Proceeds received from sale of property, plant and equipment (in NIS millions)	-	-	2	2	-	-

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

D. DBS

	Q2 2008	Q1 2008	Q4 2007	Q3 2007	Q2 2007	Q1 2007
Revenues (NIS millions)	380	381	347	360	354	354
Operating Profit (NIS millions)	43	26	4	(4)	31	25
Depreciation and amortization (NIS millions)	60	65	70	66	69	68
EBITDA (NIS millions)	103	91	74	62	100	93
Net profit (loss) (NIS millions)	(99)	(66)	(75)	70	(65)	(48)
Cash flows from current operations (NIS millions)	32	84	76	56	25	93
Payments for investments in property, plant and equipment and intangible assets* (in NIS millions)	40	79	81	84	45	45
Proceeds received from sale of property, plant and equipment (in NIS millions)	-	-	-	-	-	-
Number of subscribers (as at the end of the period, thousands)	551	549	549	545	543	542
Average monthly revenue per subscriber (NIS).	230	231	212	220	218	218

* This item also includes investments in the cost of acquisition of subscribers

Section 1.7 – General Environment and Effect of External Factors on Group Operations

The acquisition of 15% of the share capital of HOT by Netvision, reported by Discount Investments, if and to the extent concluded, might strengthen the position of the IDB Group and HOT as a communications group in competition with the Group.

2. Fixed-Line Domestic Communications – "Bezeq" – The Israel Telecommunications Corp. Limited ("the Company")

Section 2.1 – General information on areas of operation

Section 2.1.2 – Limitations set by legislation and standards and special restrictions

Recently, on June 1, 2008, the Company's tariffs change. The interconnect charges to the Company were reduced, effective June 11, 2008.

Section 2.1.3 - Changes in volume of activity and profitability in the area

For changes in the volume of activity and profitability in this area, see update to section 1.5.3(a) above.

Section 2.1.5 – Technological changes that are necessary to significantly impact on the area of activity

Subsection A – Regarding the adaptation of company infrastructure to high broadband, see the updates to sections 2.6.7 and 2.7.2, below, regarding NGN.

Section 2.2 – Products and Services

Section 2.2.2 - Telephony

On April 7, 2008, a draft amendment to the license and service file of the toll free service (1-800) was received from the Ministry of Communications. The significance of the amendment is, inter alia, that the Company's 1-800 subscribers will pay the cellular companies a higher tariff for calls made to them from the cellular network. On May 6, 2008, the Company sent its comments on the aforementioned amendment.

In respect of the Company's request to the Antitrust Commission for an exemption from a cartel arrangement to an arrangement with the cellular operators and fixed, domestic licensees for information services –on August 13, 2008, the Commissioner decided to grant a conditional exemption as a response to the Company's request.

Section 2.2.3 – internet access services

For changes in the number of ADSL subscribers, and the average monthly revenue per ADSL subscriber during the first quarter of 2008, see the update to the table in section 1.5.3(a) above.

With respect to broadband access services via internet service providers without purchasing a basic telephone service (ADSL only) - the Company commenced provision of this service on May 15, 2008.

Section 2.2.5B - Satellite Services and Broadcasting

See update to section 1.1.6 above with respect to the agreement for sale of the Company's satellite communications operations.

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 June 30, 2008.

Section 2.6 – Competition

For an update regarding publication of the recommendations of the Gronau Committee, see the update to section 1.1 above.

Section 2.6.1

With respect to the Company's petition to the High Court of Justice with respect to the application to enforce the requirement of structural separation on HOT, on July 15, 2008, the Court decided that the petition will be corrected according to the Company's request, that a hearing will be set and the respondents will submit their responses prior to the hearing.

Regarding the policy for providing VOB services – on August 12, 2008, the Company applied to the Ministry and requested, for the sake of good order, to make an addition to the Services Addendum to the Company's license for broadband telephone service, if it reaches a market share of 85%.

Section 2.6.6A - Numbering and Number Portability

As at the end of June 2008, approximately 117,000 thousand lines have ported from the Company to competing companies (of these 45,000 in the second quarter) and approximately 10,000 lines ported to the Company (of these 4,000 in the second quarter) from competing companies.

On April 9, 2008, the Ministry of Communications gave notice to the Company and to other communications providers that it was considering amending the numbering plan and prescribing that with respect to the entitlement to number portability a "subscriber" would be deemed to include an NEP licensee to whom telephone numbers have been allocated and who pays for use thereof, and the end user will not be entitled to port such a number. On May 7, 2008, the Company submitted its comments to this amendment, claiming that it would amount to confiscation of the end user's right to decide whether to port the number or not.

On May 4, 2008, the Company received an Administrative Directive from the Ministry of Communications to the effect that a customer which has been allotted an abbreviated business dialing number (asterisk plus four digits) may port such a number.

Section 2.6.6.b – Other Potential Competitive Infrastructures

Regarding the hearing on the policy for allocating frequencies for wireless broadband access networks (WiMAX) – on July 30, 2008, the Ministry of Communications announced an additional hearing in which changes were made to the previous hearing. In this context, the Ministry announced that it is examining the possibility of amending the Communications Regulations (Telecommunications and Broadcast) (Frequencies for Wireless Access Devices) 5762-2002 which lists the devices that are exempt from permits pursuant to Chapter 5 of the Planning and Construction Law, so that it includes the *2.5* GHz and 3.7 GHz frequency ranges. The company is examining the draft policy to be presented at the hearing and will respond.

Section 2.6.7 – the Company's preparations for managing increased competition

Sub-section (i) regarding examination of the deployment of uniform infrastructure for the transmission of communications services – further to the decision of the Board of Directors of the Company to approve entry into detailed planning of an NGN (Next Generation Network) ("the **project**"), on June 26, 2008, the Board of the Directors of the Company decided to approve that the Company advance the project. In 2008, detailed plans will be made for the project, two areas will be set up as operational pilots and soft switches will be purchased. The project will be conducted in a modular fashion and the Company will examine regularly and at each stage, the feasibility of continuing the project, and the requirement to update the project's outline. The content, pace of implementation and amounts to be invested in the project will be determined annually, as part of the Company's annual budget. In addition to the purchase approved on June 26, 2008, the Board of Directors approved, on July 31, 2008, the purchase of management systems and other equipment required for deployment of the new system. In this respect, see also the update to section 2.7.2, below, and note 3(e) to the financial statements for the period ending June 30, 2008.

Section 2.7 – Fixed assets and Installations

Section 2.7.2 – Domestic, fixed-line communications infrastructure

NGN Network – The Company believes that the requirements of future communications services in the State of Israel, as in the entire world, will require increasing larger broad bands and an advanced IP platform. In order to provide a response to these needs, the Company intends to gradually establish, commencing in late 2008, an NGN network based on the core of the IP network and bringing fiber optic infrastructure to street switching cabinets (the topology of the network is referred to as "fiber to the curb" – FTTC). With this network, it is possible supply broadband technology up to 50 Mbit/s in the download channel and innovative added-value services. In addition, the NGN network will allow the Company to make the network more efficient. The project for establishing the new network will be implemented gradually with the pace of the deployment being tested annually. In this respect, see also the update of section 2.6.7, above, and note 3(e) to the financial statements for the period ending June 30, 2008.

The information in this section includes forward-looking information based on the Company's assessments. The actual results are likely to be significantly different from these estimations, when attention is paid to the changes that will occur in technology and in the communications market.

Section 2.7.4 – Land

Subsection d – In Q1 2008, the Company did not sell any real estate assets. During Q2 2008, the Company sold three real estate assets with a total area of approximately 40,500 sq. meters of land and approximately 7,800 sq. meters of building for a total sum of approximately $5.5 million.

Section 2.9 – Human Resources

Section 2.9.1 - Organizational structure and position of employees based on organizational structure

A. With respect to the organizational structure - the CFO and the VP Strategy and Business Development report only to the CEO.

B. In May 2008, execution of the amendment to the new collective agreement regarding advancing the completion of implementation of the organizational structure, and regarding advancing dates of retirement and changes in the mix of retirees who are supposed to retire under the new collective agreement before the end of 2008.

Section 2.9.2 – Personnel according to employment framework

During the first six months of 2008, the number of employees of the Company fell from 7,614 employees at December 31, 2007, to 7,425 at June 30, 2008 (a net reduction of 189 employees) as a result of retirements from the Company (in parallel with the recruitment of employees required, such as sales representatives).

Note that out of the 975 employees who are supposed to terminate their employment at the Company between 2006-2008 under early retirement tracks or increased severance pay tracks, under the collective agreement of December 5, 2006 (see section 2.17.4(f) of the Periodic Report for 2007), at June 30, 2008, 965 employees had retired.

Section 2.9.6 – Employee remuneration schemes

Section 2.9.6.3 - for the allotment of options to senior managers and employees of the Group, including to the Chairman of the Board of Directors, see update to section 1.3.2 above.

Section 2.9.7 – Company officers and senior executives

On April 17, 2008, the Board of Directors of the Company, after receiving the approvals of the Remunerations Committee and the Audit Committee of the Board of Directors, approved the conditions of employment of the Chairman of the Board of Directors as set out in the immediate report of the Company published on April 18, 2008. The conditions of employment of the Chairman of the Board of Directors were approved by the general meeting of shareholders of the Company on June 1, 2008.

Section 2.13 – Finance

Section 2.13.4 - Credit received after December 31, 2007

Commencing June 2008, the Company on occasion takes short-term, on-call loans, generally for insignificant amount. As of the date this update, the company does not have any such loans.

Section 2.13.6 – Credit Rating

On May 21, 2008, the Midroog Rating Company ("Midroog") gave notice that it had returned the Company's rating (which is Aa1) from negative to stable in light of the improvement in the Company's financial results, and the continued presentation of a strong financial profile, compensation for erosion in the fixed line communications segment via operations in the other segments and very low rates of financing despite the distribution of all of the net profit as dividend, after the transfer of the control core of the Company.

On August 12, 2008, Standard & Poor's ("S&P") gave notice that it is changing the Company's rating outlook (which is BBB+) from "negative" to "stable," on the basis of its re-examination of its operating performance and the leverage within the company. In its announcement, S&P noted that the company's rating relies, *inter alia*, on the Company's leadership as the national communications operator, its operational efficiency, the range of services it offers in the communications market and its adequate financial profile.

Section 2.13.7 – Assessment of funds raising in the coming year (2008) and sources of financing

In the Company's assessment, the Company is likely, from time to time, to raise short-term loans from banks and/or other credit providers to bridge gaps in cash flow as may arise, if at all, from time to time.

Section 2.15 – Environmental Protection

Following termination of the strike at the Ministry of the Environment, the process of obtaining operating permits was completed for most of the communications and broadcasting facilities.

Section 2.16 – Limitation and Regulation of Company Activities

Section 2.16.1 – Supervision of the Company's tariffs

Sub-section (a) (regarding the update of the Company's tariffs) – on March 20, 2008, a letter was received from the Ministry of Communications under which the next update (on June 1, 2008) would be based on the existing tariff outline prescribed by the Gronau Committee in 2003, in accordance with the formula set out in the Communications Regulations regarding calculation and linkage of payments for telecommunications services (the "Calculations Regulations"). According to the letter, after and to the effect that the Gronau Committee's recommendations are adopted regarding policy and rules of competition in the communications market, the path will be laid for the work of a commission to prescribe new tariff arrangements for the coming years. On June 1, 2008, the Company's tariffs were reduced in accordance with a formula fixed in the Calculation Regulations, at the average rate of approximately 2%, except for the fixed fee for a telephone line that was updated in accordance with the increase in the Cost-of-Living index (3.4%). The interconnect tariffs currently paid to domestic carriers by licensees were reduced by an average of approximately 2%, effective June 11, 2008. With respect to the update of the Company's tariffs, see also the update regarding publication of the recommendations of the Gronau Committee in section 1.1 above.

Section 2.16.2 – The Company's general license

On July 3, 2008, the Company received a draft amendment of the Company's license and the licenses of it subsidiary companies Pelephone, Bezeq International and D.B.S. regarding the marketing of joint packages of services. On July 27, 2008, the Company submitted its position to the Ministry of Communications, stating that the amendment of the licenses represents an intensification of regulation in comparison to the policy document of the Minister of Communications dated March 31, 2004, which is supposed to reflect relief for the Company, and it would be desirable to allow a model for marketing of joint packages of services that represents relief for the Company now that its market share has decreased to 85% or less, together with ministerial supervision using more moderate measures than those proposed in the draft amendment to the license. Regarding the positions of the subsidiary companies on this matter, see the updates to sections 3.18.3.1, 4.1.2 and 5.6.5, below.

Regarding the main points of the general license – subsection c regarding tariffs – on April 14, 2008, the Company's license was amended so as to permit it to require a subscriber to pay using a direct debit or a credit card, except for a private subscriber who does not have a bank account. It should be noted that the Economics Committee of the Knesset discussed a proposal to amend the Consumer Protection Law, by which a communications business would not be permitted to make a transaction conditional on payment using a direct debit or credit card. If the law is amended according to this proposal, the Company will be unable, despite the amendment to its license, to require a private subscriber to pay using a direct debit or credit card.

Main points of the general license – subsection 11 (miscellaneous issues) – on May 17, 2008, the Ministry published a hearing regarding its policies and amendment of the operators' licenses regarding fair disclosure on telephone bills. In this context, it is examining imposing new requirements on the operators regarding details and computation of bills. It should be noted that approximately three years ago, the licenses were amended so that a standard was adopted for telephone bills. The Company submitted its position on the matter on July 20, 2008, stating, *inter alia*, that there is no justification, neither from the consumers' perspective nor from an ethical perspective, to make changes in the Company's telephone bills. This would also be harmful to some of the Company's customers while being of no benefit to others. In its position, the Company claimed that since the demands being considered would require very extensive development and resources to implement and because of the technical issues involved, it would be worthwhile, before a decision is made, to discuss the matter with the Company.

Section 2.16.5 - Immunities

On May 19, 2008, the Company received a letter, dated May 18, 2008, from the Ministry of Communications, addressed to communications licensees, stating that the Ministry of Communications is of the opinion that following the adoption of the Civil Wrongs Ordinance Amendment (No. 10) Law, 5765-2005, under which the restrictions on the State's liability in tort were reduced, there might be grounds to consider reducing the existing immunity arrangement granted to general licensees and special general licensees. The licensees were requested to submit their positions to the Ministry of Communications by June 18, 2008. On July 31, 2008, the Company submitted its position to the Ministry of Communications stating that the said Amendment 10 does not change any of the arrangements regarding liability for torts to an extent that justifies reducing the existing immunity arrangement and assigning responsibility to the communications companies. Additionally, expansion of responsibility means placing a heavy burden on communications companies, including the Company, because of the potential extent of the indirect damages and the dimensions of the possible suits.

Section 2.16.7 - Antitrust laws

Subsection h.- with respect to the Antitrust Commissioner's ruling that the Company had abused its market status in handling an interconnection fault between the Company's network and that of HOT, against the backdrop of labor disruptions by the Company's employees - on March 16, 2008, the Company filed an appeal against the Commissioner's ruling. In this regard, see also Note 7C(1) to the financial statements of the Company for the period ended June 30, 2008.

Section 2.16.8 – Telegraph Regulations

Regarding the Company's use of radio frequencies – on October 25, 2007, the Ministry of Communications notified the Company that it is considering ordering it to cease using neighborhood radio and rural radio systems and the frequencies allocated to it for the purposes for which they are being used, including, in order to provide its services in areas where an infrastructure of telephone lines does not exist. On December 25, 2007, the Company submitted its response in which it clarified that the Ministry must allocate alternative frequencies and that the Ministry's requirement would create difficulties for the Company and require extensive deployment and operations that would entail significant expenses. Furthermore, the Company noted that it would be required, within a period of two years, to transfer subscribers from the existing systems to new systems and demanded that the State bear the cost of the migration from the systems that the Company would be required to evacuate.

Section 2.16.9 - Proposed Legislation to Amend the Consumer Protection Law

During April 2008, an amendment of the Consumer Protection Law regarding fixed transactions was approved by the Knesset (the "Amendment"). Under the Amendment, dealers will be required to inform consumers of the date of termination of a fixed transaction prior to termination of such, and of the conditions that will apply after the date of termination. In addition, dealers will be required to obtain the positive consent of the consumer to continue with the contract beyond the fixed period. If positive consent is not obtained, the consumer will be disconnected from the service to which the fixed transaction applied, apart from basic telephone services as defined in the Communications Law (voice services). This Amendment will come into force as of 2009. The Company's hearing regarding the amendment to the Company's license and those of other licensees in this regard, proposed by the Ministry of Communications, is also continuing. Furthermore, the Knesset approve an amendment to the Consumer Protection Law regarding disconnection from ongoing services (effective October 2008) allowing a private subscriber to disconnect from ongoing service by using mail, electronic mail or telephone. In addition, the Knesset approved the amendment to the Consumer Protection Law (effective September 2008) which imposes, in certain circumstances, fines if a technician is late and an amendment to the Communications Laws regarding junk mail (effective November 2008), according to which requires, among other provisions, as a general rule, a subscriber's explicit permission to receive advertising by way of mail, electronic mail, facsimile, automatic dialing systems and SMS.

The Company is examining the significance of the implementation of these amendments and is preparing to implement them.

Section 2.16.11 – Erection of communications installations – NOP 36

On April 17, 2008, the Company submitted its objections to the proposed wording of the National Communications Outline plan NOP/36A regarding small broadcast installations, and the National Communications Outline Plan NOP/36B regarding large broadcast installations. In summary, the objections are that the plans, as currently worded, particularly with respect to the changes in definitions of small and large broadcast installations, give rise to practical difficulties which might prevent the Company from providing the public with some of the varied services that it provides, and that it is required by law to provide.

Establishing communications facilities in the territories

On July 29, 2008, the Company received notification that in June 2008 National Master Plan 56, which regularizes construction and licensing of communications facilities in the territories, took effect. The plan includes transition instructions for facilities that were constructed prior to 1984 and for existing facilities. The Company is examining the subject and, as of the date this report, it is not able to evaluate the expected ramifications.

Section 2.17 – Significant Agreements

With respect to section 2.17.4(f) – the new collective agreement of December 5, 2006 – regarding the amendment to the agreement, see update to section 2.9.1 above.

Section 2.17.5 – Management Agreement

On July 31, 2008, the Board of Directors of the Company decided (subsequent to approval by the Audit Committee of the Board of Directors on June 26, 2008) to approve the extension of the relationship and management contract with AP. SB. AR. Cayman L.P., a related company to Ap.Sb.Ar., for a period of three additional years commencing January 1, 2009, through December 31, 2011, according to the conditions of the original agreement. The extension of the agreement requires the approval of the general meeting of the Company's shareholders which has been called for September 28, 2008.

Section 2.18 – Legal proceedings

For updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended June 30, 2008.

Section 2.19 – Goals and Business Strategy

Section 2.19.2 - Summary of Strategy and Directions for the Future

Regarding the Company's network – see sections 2.6.7 and 2.7.2, above, on the subject of NGN.

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

Section 3.2.1 – Services

At the end of March 2008, the Ministry of Communications published a document of a public hearing regarding the policy of regulating the provision of telephone trading services via a public telecommunications network. Telephone trading services including voice and visual information services, entertainment services, dating services, etc., provided to subscribers via terminal equipment connected to a network. It is important to note that the field of telephone trading services is a significant source of income in the content world of Pelephone and the other cellular carriers. Following the proposed regulation, the Regulator is seeking to dramatically change the conduct of the telephone trading services sector, in a way that it is also likely to harm Pelephone's revenues in this area. The Ministry of Communications has asked all relevant persons operating in the field of telephone trading for responses to the aforesaid hearing by May 29, 2008. Pelephone submitted its position in this regard, in which it, among others, requested that the Ministry of Communications hold frontal discussions on the subject of the hearing prior to making any decisions.

Section 3.7 – Competition

For an update regarding publication of the recommendations of the Gronau Committee, see the update to section 1.1 above.

On August 13, 2008, Minister of Communications published a document regarding adoption of the recommendations of the Gronau Committee. Following are the main points that relate to Pelephone:

1. The Minister instructed the CEO of the Ministry of Communications to work to promote the licensing of virtual operators (MVNO) while making it possible for the relevant parties to express their opinion on the subject to the Ministry of Communications. In the event that within a period of six months from the date that a virtual operator applies to a mobile operator, the parties do not reach an agreement regarding the provision of virtual services, the Minister will examine the reasons for this and, subsequent to a hearing with the relevant parties, consider issuing instructions on the matter in accordance with his authority.
2. It is the intention of the Minister to promote a change in the tariff structure for outgoing international calls using the mobile network, in the context of interconnect regulations so that the international carrier will determine the tariffs for these calls and, in the context of its accounting with the mobile operators, the international operator will transfer only interconnect charges to the mobile operator. A hearing with the relevant parties is to be held regarding the implementation of his policy.

   According to the Minister's position, international licenses should not be issued to existing mobile operators, at this stage.

Regarding Section 3.7.2

Recently the Minister of Communications expressed his position according to which he intends to promote the issuance of MVNO licenses in the near future. The Minister stated that the Ministry would examine a variety of possibilities for receiving MVNO licenses, ranging from a reseller model to full operation.

Section 3.10 – Intangible Assets

Regarding Section 3.10.2 – Right to use frequencies

During 2008, Pelephone asked the Ministry of Communications to execute its right for the allocation of frequencies in the 2100 MHZ range. In order to execute this right, Pelephone is required to pay approximately NIS 178 million in respect of retroactive licensing and frequency fees from the day it won the tender for the frequencies through the day that it executed its right for allocation of the frequencies.

Section 3.17 – Environment

Regarding Section 3.17.1

On July 17, 2008, a petition was filed on behalf of The Forum for Sane Cellular Consumption and the Israel Union for Environmental Defense with the High Court of Justice requesting an order nisi against the Minister for Environmental Protection, the Minister of Communications and others because of an alleged failure to reach an agreement on the wording of regulations by virtue of sections 25(a)(2) and 25(a)(5) of the Non-ionizing Radiation Law, 5766-2006, despite the obligation stated in the law to issue the said regulations by January 1, 2007. Furthermore, a declaration was requested that until these regulations are issued no construction permits or operating permit would be issued for sources of radiation intended for cellular communications. Simultaneously, a request was also filed for an interim order not to issue construction permits or operating permits for sources of radiation intended for cellular communications until a ruling is made on the petition.

Section 3.18 – Restriction and Control of Pelephone's Actions

Section 3.18.1.4 – the Consumer Protection law

During the month of April 2008, an amendment of the Consumer Protection Law regarding fixed transactions was approved by the Knesset. In this regard, see section 2.16.9 above. Pelephone is examining significance of implementing this regulation and is preparing to implement it.

Section 3.18.3 – Pelephone’s license

Regarding subsection 3.18.3.1(e), during June 2008, the Ministry of Communications published a hearing regarding proper disclosure on telephone bills. During this hearing, a variety of changes in the structure of the invoice were proposed. The hearing was based on the recommendations of the Subcommittee of the Knesset Economics Committee and recommendations of the professional committee of the Ministry of Communications regarding the structure of the invoice, which completed its work recently. Pelephone submitted its position to the Ministry of Communications. Implementation of the recommendations as proposed will require Pelephone to make appropriate operational arrangements.

Regarding subsection 3.18.3.1(f) – during the month of March 2008, the Ministry of Communications made a decision to implement the amendment of the MRT licenses under which the maximum obligation term for customers who are not business customers would be reduced to 18 months, and the carriers would be required to offer customers a reasonable no-obligation alternative. This resolution was passed following a hearing into this matter. Implementation of the amendment commenced on April 22, 2008.

Section 3.18.3.1(g) – during the first quarter of 2008, Pelephone submitted its response to a hearing regarding fixed-term transactions, with respect to the policy format presented. However, on April 14, a request was received from the Ministry of Communications for responses to a further hearing in this regard, under which the Ministry of Communications proposed a new ruling to the effect that a fixed tariff would apply during the obligation period, i.e., as different from the previous hearing: the current amendment proposes that during the obligation period, it will not be possible to amend tariffs. Pelephone submitted its response to the Ministry.

Following are additional changes that are being considered by the Ministry of Communications:

1) Further to the hearing held on the subject during July 2008, the Ministry of Communications published a legal opinion stating that it is prohibited to make the purchase of a Third Generation (3G) instrument conditional on the purchase of 3G services. According to this opinion, customers must be offered an economically effective alternative for purchasing a 3G instrument without a package of 3G services.

2) According to the policy document of the Ministry of Communications from 2004, the Company will be permitted to market joint packages of services with its subsidiary companies when its market share for fixed telephony services drops to 85%. In the very near future, the Company’s market share will reach 85%. Therefore, the Ministry of Communications recently announced the hearing including the proposed amendments to Pelephone’s license. According to the proposed amendment, the Company and Pelephone will be permitted to market combined packages (for fixed and mobile telephony) but only subsequent to approval being received from the Minister of Communications for marketing the package, on the condition that the package will be completely broken up, meaning that each component of the package will also be offered to customers, at the same price, outside of the package, and on the condition that can be proved that similar packages are available in the market. Pelephone submitted its response to the hearing, in which it expressed its objection to the proposed change.

Section 3.18.3.3 – License for Building Sites

On May 1, 2008, the Attorney General expressed his position regarding wireless access devices and stated that he accepts the opinion that the exemption, according to its wording and purpose, also applies to wireless communications devices for cellular communications and that the exemption represents the balance that the legislator created between the various interests. Despite this, and because of changes and developments in the law and the factual reality, the Attorney General asked that an inter-ministerial committee re-examine the significance and ramifications of continued application of the exemption for cellular devices, the purpose of developing an updated position regarding a worthy justification for the exemption for cellular telephone devices, by the end of 2008.

On May 22, 2008, Tel Aviv District Court, sitting as a Court of Appeals, handed down a ruling regarding the issue of wireless access devices. The main points of its determination were as follows:

a. The exemption from a building permit does not apply to access devices operating in a cellular network that were constructed on the roofs of buildings.

b. Wireless access devices, as defined by law, are fixed devices.

c. The antenna is not included the definition of an exception to the requirement for a building permit for an "internal change in an apartment."

Pelephone disagrees with the District Court's ruling and on June 10, 2008, it filed a request for permission to appeal to the Supreme Court.

On July 21, 2008, the Union of Local Authorities in Israel and others filed a petition with the High Court requesting an order nisi instructing the Attorney General to appear and explain, *inter alia,* why the enforcement guidelines he issued to municipal prosecutors stating that charges are not be filed and administrative demolition orders are not to be issued for the construction and operation of the cellular access devices without a permit should not be cancelled. Furthermore, the High Court was asked to determine, *inter alia*, that the position of the Attorney General (in a document dated May 1, 2008) suffers from an extreme lack of reasonableness. Furthermore, a request was made for an interim order to the Attorney General instructing him to defer or suspend the validity of the enforcement guidelines or, alternately, to forbid the construction of cellular access devices without a building permit, until the court meets and rules on the petition.

It is hereby clarified that Pelephone continues to construct wireless access devices. If Pelephone's position is rejected by the courts, in whole or in part, it will have an adverse impact on the possibility of deploying sites, the pace of deployment, etc. In the event that it is necessary to cease the operation of access devices, there will also be damage to service in the areas where these devices operate.

Section 3.21 – Legal proceedings

For updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended June 30, 2008.

4. International Communications, Internet Services and NEP – Bezeq International Ltd. ("Bezeq International")

Section 4.1.2 – Statutory and Standards Limitations on Bezeq International

On March 12, 2008, a report was published by the Committee to Formulate Detailed Recommendations on Policy and Rules of Competition in the field of Communications in Israel headed by Prof. Reuven Gronau. Inter alia, the report includes recommendations regarding the areas of operations of Bezeq International, which, if adopted by the Ministry of Communications in setting its policy, will affect the management of Bezeq International's business. Additionally, the Committee recommended: that a permit be given to the subsidiaries of the Company to supply unbundled service packages, including the Company's telephony and broadband services, after implementation of the local loop unbundling arrangement (see update to section 1.1 above); that on such date, the subsidiaries shall be granted special domestic carrier licenses for the provision of domestic carrier services that are not VOB; and that the entry of new players controlled by the mobile telephony companies shall be permitted into the international call sector, after the method of prescription of tariffs for international calls via mobile handsets is changed so that the international call tariff is set by the international calling company, which will pay the cellular carrier in accordance with the tariff set out in the Interconnect Regulations for call completion.

For an update regarding publication of the recommendations of the Gronau Committee, see also update to section 1.1 above.

On August 13, 2008, the Minister of Communications published his decision regarding setting policy and competition guidelines in the field of communications in Israel, on the basis of the conclusions of the Gronau Commission, which were published in March 2008. In the estimation of Bezeq International, the decisions of the Minister will not have an impact on its business operations in the near future and, in any case, it is currently unable to assess their possible long-term impact since the implementation of changes in its field of activity require, according to the Minister's decision, completion of an extended process of preparing regulatory infrastructure, whose nature is uncertain at this time, as well as the creation of new market arrangements, for which it is unclear when and if they will exist.

On July 3, 2008, Bezeq International received a letter from the Director-General of the Ministry of Communications on the subject of the amendment to its general license regarding the sale of packages of services that include both its services and the services of the Company, to which drafts of the amendment to the licenses of Bezeq International and the Company were appended. In the response written to the said letter and during the hearing on this matter that was held in the Ministry of Communications on July 30, 2008, Bezeq International notified the Ministry of Communications of its objections to the proposed wording of the amendment to its general license because, on one hand, the amendment will not alleviate the limitations that currently apply to it and the Company as regards the sale of joint packages of service and, on the other hand, the proposed amendment could change its current situation for the worse and discriminate against it in comparison to its competitors.

Section 4.9 – Intangible Assets

On March 23, 2008, Bezeq International signed an agreement with Gil A.R. Telecom Systems ("**Gil A.R.**") under which Bezeq International acquired all of the operations of Gil A.R. relating to the sale, leasing and service of communications products and switches manufactured by Avaya Office.

Section 4.14 - Investments

As at June 30, 2008, Bezeq International held 34.25% (32.42% under full dilution) of the share capital of Walla! Communications Ltd.

Section 4.19 – Legal proceedings

With respect to section 4.19.2 of the Periodic Report of the Company for 2007, regarding the claim filed against Bezeq International and against two other international carriers on grounds of breach of patent for a pre-paid telephone system by persons claiming to be the inventors and owners of such patent, on April 16, 2008, counsel for the plaintiffs filed a notice to the Court in which he gave notice that the settlement negotiations being conducted by the parties had not resulted in any agreement. According to the court's decision, the preliminary proceedings in the case will be completed by October 23, 2008, and the pretrial was scheduled for November 9, 2008.

For further updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended June 30, 2008.

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

Section 5.1.3 – Developments in markets in the area of operations

Section 5.1.3.3 – the private bill regarding the inclusion of two designated channels and the education television channel in the DTT system was approved in a preliminary reading by the Knesset Plenum. A number of private bills dealing with the addition of other channels to the cluster of channels intended for broadcast via the DTT system were also submitted to the Knesset and to the best of DBS's knowledge, they are currently in the initial processes of enactment.

Section 5.1.3.5 – in March 2008, the Minister of Communications published the recommendations of the Gronau Committee. The recommendations deal with the areas of telephony, internet and multi-channel broadcasts. Among other recommendations, the Committee recommended requiring multi-channel broadcasting companies to offer their subscribers a narrow channel package containing 5-10 channels, having the characteristics set out in the recommendations. The Committee also recommended not to remove the structural separation applying to the Company at this stage, due to its status in the field of fixed-line telephony, and recommended that subsidiaries of the Company, including DBS, not be allowed to supply "service packages" including the Company's services (including IPTV services) until its other recommendations regarding infrastructure and the Company's services are implemented. DBS expressed its opposition to and reservations regarding the recommendations to the Minister of Communications.

For an update regarding publication of the recommendations of the Gronau Committee and the decisions of the Minister, see also the update to section 1.1 above.

In June 2008, the Council published a hearing regarding a new policy relating to broadcast of sports on multi-channel television, effective January 2009. According to the hearing, the Council's intention is to expand the protection of content broadcast on the basic sports channel (Channel 5) and the channel known as Channel 5+ and to impose limitations on the broadcast of live sporting events on the pay sports channels. Furthermore, according to the hearing, the imposition of an obligation to broadcast certain sporting events using the PPV method for a defined payment is being considered. In July 2008, DBS submitted its response, in which it objected to implementation of the policy discussed at the hearing.

Section 5.6.5 – Principal methods for coping with competition

Section 5.6.5(g) – "package of services" – as of April 2008, DBS has ceased marketing a package of services to its subscribers containing broadcasts and high-speed internet connection infrastructure, and has commenced selling the Company's promotions of high-speed internet connection infrastructure such that subscriber contracts regarding such infrastructure are performed with the Company only. DBS has the option of contracting with a subscriber directly and transferring compensation from the subscriber to the Company.

On July 3, 2008, DBS received a letter from the Ministry of Communications stating that the Ministry is considering an amendment to the Company's license as a supplementary amendment to the amendment of the DBS license that would make it possible to offer a package of services according to the following principles:

The package of services will be unbundled so that it will be possible to purchase each of the services offered in the package of services separately for the same price it is offered in the package, a package of services may not be offered if is not also offered by the cable companies, marketing of the package of services must be approved by prior request by DBS to the Ministry of Communications. These instructions relate to any service offered by DBS together with services from the Company.

In its response to the letter of July 27, 2008, DBS objected to the proposed amendment to its license. In its response, DBS also claimed that offering the possibility of offering an unbundled package of services does not provide a true response to the package of services offered by its competitor and that the amendments must apply to marketing of the Company's telephony services only and not to other services, such as internet infrastructure services. Furthermore, DBS claims that it is necessary to change the supervisory mechanism for offering and services so that is not obliged to receive prior permission from the Ministry of Communications but rather required only to notify it and that offering packages of services should not be limited to offering services of the Company that are also offered by the cable companies.

Section 5.13 – Finance

Section 5.13.6 –at June 30, 2008, DBS is in compliance with the financial stipulations under the financing agreement (after the concession was received).

Section 5.13.8 – since debentures (series A) that were issued by DBS were not registered for trading until July 31, 2008, they will begin bearing annual interest at the rate of 8.4% from that date.

Section 5.15.1 – Subordination of Activity to Specific Laws

During April 2008, the Knesset approved an amendment to the Consumer Protection Law regarding group transactions. On this matter see the update to section 2.16.9, above.

Section 5.16.2 – Space segment lease agreements

Second space agreement – on April 28, 2008, the Amos 3 satellite, to be operated by HLL, and intended as a downstream satellite for Amos 1 and Amos 2, was successfully launched. In July 2008, its positioning in space was completed. Commencing June 30, 2008, DBS ceased using the satellite Amos 1 and it now uses the satellites Amos 2 and Amos 3 for its satellite segments.

On July 15, 2008, DBS and HLL signed an amendment to the second space agreement (subject to the approval of the authorized bodies of the two parties) stating, *inter alia*, that DBS will lease 13 space segments from HLL, instead of 14 and DBS will cease leasing the 13th segment until another agreement is made between the parties, according to the mechanism stated in the agreement.

Furthermore, a mechanism for back-up was set up using satellite Amos 3 in the event that space segments are not available on satellite Amos 2.

Section 5.17 – Joint Venture agreements

Section 5.17.1 – as set out in the update to section 5.6.5(g), this joint venture has ended.

Section 5.18 – Legal Proceedings

Regarding the claim against Pace and the counterclaim (section 5.18.1): on July 3, 2008, the registrar rejected the respondent's request to erase the suit, while determining that the nominal amount in the statement of claim is the maximum amount that DBS may receive if it wins the suit, including the amount of value added tax for which it was required to pay a fee. Similarly, the request of DBS to grant an order correcting the statement of defense and the statement of countersuit submitted by the respondent was rejected. A pretrial hearing was set for December 16, 2008.

The class action claim regarding the sports channel (section 5.18.6): on May 29, 2008, DBS, in cooperation with the cable company, submitted a summary of its claims regarding the primary appeal and also a summary of its claims regarding the counter-appeal. On June 23, 2008, appellants submitted summaries of their responses to the primary appeal and a summary of their response to the counter-appeal. On July 9, 2008, D.B.S., in cooperation with the cable company, filed summaries of their response to the counter-appeal. A court date for the hearing the appeal and counter-appeal has been set for November 25, 2008.

Re the deficit demand from the Customs Department (Section 5.18.7): In April 2008, the Taxation Authority stated that there is nothing preventing the VAT in the cash invoice from being paid by DBS, which shall be entitled to deduct the input tax contained therein. Therefore, DBS paid the value added tax. In July 2008, the parties signed a compromise agreement that brings to an end the dispute over the demand for deficit taxes, subject to the payment of approximately NIS 1.5 million by DBS.

For further updates on the subject of legal proceedings, see Note 7 to the financial statements of the Company for the period ended June 30, 2008.

Section 5.21.3 – Special risks to DBS

Section 5.21.3.5 - as set out in the update to section 5.16.2 above, commencing July 2008, DBS ceased using the Amos 1 satellite and it now uses the Amos 2 and Amos 3 satellites.

Section 5.21.3.6 as stated above, commencing July 2008 HLL is the only owner of rights with whom DBS has a contract for leasing space segments.

20.8.08	
Date	Bezeq – The Israel Telecommunication Corp. Ltd.

Names and titles of signatories:

Shlomo Rodav – Chairman of the Board

Avi Gabbay, CEO

Directors' Report on the State of the Company's Affairs for the period ended June 30, 2008

Chapter B of the Periodic Report

Directors' Report on the State of the Company's Affairs
For the six month period ended June 30, 2008

We respectfully present the Directors' Report on the state of affairs of Bezeq - The Israel Telecommunication Corp. Limited (hereinafter: "the Company") and the consolidated Group companies (the Company and the consolidated companies together are hereinafter collectively referred to as “The Group”), for the six month period ended June 30, 2008 (hereinafter: "the Directors' Report").

The Directors’ Report includes a condensed review of the Company’s affairs and it assumes that the Directors’ Report for December 31, 2007 is also available to the reader.

The Group operates in four main areas which are reported as business segments in the Company's consolidated reports as follows:

1. **Domestic fixed-line communications**
2. **Cellular**
3. **International communications, internet services and NEP**
4. **Multi-channel television**

The Company has an additional area of operations which is not material to the Group's operations, and which has been included in the financial statements of June 30, 2008 as another business segment, which mainly includes customer call center services and investment in a venture capital fund.

The net earnings in the six-month period amounted to NIS 798 million, compared to net earnings of NIS 725 million in the corresponding period in 2007. The increase in net earnings is due to an increase in earnings in all segments with the exception of the multi-channel television segment, where there was an increase in the loss. See below for further details.

1. Financial position

A. The financial statements are drafted in accordance with International Financial Reporting Standards (IFRSs).

B. The Group's assets on June 30, 2008, amounted to NIS 14.51 billion, compared to NIS 16.58 billion on June 30, 2007. Of these, NIS 5.97 billion (41%) are property, plant and equipment, compared to NIS 6.21 billion (37%) on June 30, 2007.

   The decrease is due to the domestic fixed-line communications segment. There was a decline in total assets in this segment, not including investment in subsidiaries, compared to the corresponding period in the prior year, in the amount of NIS 2.71 billion, mainly due to the decrease in cash and cash equivalents and the sale of financial assets held for trading which were used for financing and investment activities. In addition, there was a decrease in the net book value of property, plant and equipment resulting from the difference between the depreciation expense and investment made during the reporting period. The decrease in total assets was offset by an increase in trade receivables, mainly due to the transition from advanced billing of fixed user fees for telephone lines to retroactive billing.

   In the cellular segment, assets increased from NIS 4.13 billion on June 30, 2007 to NIS 4.57 billion on June 30, 2008. The increase was mainly due to an increase in the cash balances and frequency rights. Additionally, there was an increase in the trade receivables balance mainly due to the discounting of credit card payments. On the other hand, there was a reduction in the tax asset due to the sale of the asset recorded in the past for losses.

   In the international communications, internet and NEP services segment, there was an increase in total assets compared to June 30, 2007, mainly due to the increase in the trade receivables balance and advance expenses for user rights of capacities. The increase was offset by a reduction in the cash balances used for early payment of loans and advance tax payments.

In the multi-channel television segment, there was an increase in total assets compared to June 30, 2007, which was mainly due to an increase in broadcasting rights and an increase in the net investment balance in property, plant and equipment.

C. The equity attributable to the shareholders of the Company on June 30, 2008, amounted to NIS 4.72 billion, representing 32% of the total balance sheet, the same as the shareholders' equity on June 30, 2007, which represented 28% of the total balance sheet. During the period, a dividend was paid in the amount of NIS 1.44 billion, similar to the earnings in this period.

D. Group debt to financial institutions and debenture holders on June 30, 2008, amounted to NIS 6.28 billion, compared to NIS 8.06 billion on June 30, 2007.The decrease is mainly due to repayment of debentures in the amount of NIS 2.34 billion in the domestic fixed line communications segment. Total repayment of debentures and loans in the Group amounted to NIS 3.23 billion.

The decrease was offset mainly by the sale of debentures in the amount of NIS 443 million to institutions in the domestic fixed-line communications segment and issue of debentures in the amount of NIS 644 million in the multi-channel television segment in July 2007.

The Company's auditors have highlighted the financial position of DBS in the financial statements. As mentioned in Note 6, as of June 30, 2008, the subsidiary meets the financial criteria set for it, following the amended stipulations in respect of 2008 placed upon it by the banks on March 5, 2008, and June 25, 2008 as adapted to the subsidiary's 2008 annual budget and to certain prescribed operational data. The continuation of the operations of DBS is also conditional on compliance with conditions set for 2008 and/or further relief to be received during the year. The management of DBS believes that the financial resources available to it will be sufficient for its operational requirements in the coming year based on the forecasted cash flow approved by the board of directors of DBS.

E. The Group's cash and other current investment balances on June 30, 2008, amounted to approximately NIS 806 million compared to approximately NIS 3.071 billion on June 30, 2007. The decrease is mainly due to a decrease in the cash balances and the sale of securities held for trading in the domestic fixed-line communications segment, which were used for financing and investment activities. The decrease was offset by the positive cash flows from current operations in the principal segments of the Group's operations.

2. Results of operations

A. Principal results

Net earnings attributable to the shareholders of the Company for the first half of 2008 amounted to approximately NIS 835 million, compared to net earnings of approximately NIS 760 million in the corresponding period in the prior year.

Below are details of the changes in the results of the segments compared to the corresponding period in the prior year.

Segment	**Six months ended June 30, 2008 NIS millions Operating profit**	**Six months ended June 30, 2007 NIS millions Operating profit**
Domestic fixed-line communications	796	612
Cellular	481	453
International communications, internet services and NEP	117	104
Multi-channel television	69	56
Others	1	2
Total	1,464	1,227

Basic diluted earnings per share in the first half of 2008 amounted to NIS 0.32 per NIS 1.00 par value compared to NIS 0.29 per NIS 1 par value share in the corresponding period in the prior year.

B. Revenue

Group revenue in the first half of 2008 amounted to approximately NIS 6.19 billion compared to approximately NIS 6.14 billion in the corresponding period in the prior year.

Revenue from fixed-line domestic communications decreased from approximately NIS 2.84 billion in the first half of 2007 to approximately NIS 2.76 billion in the reporting period. The decrease in the segment's revenue is due to a decrease in interconnect fees to the cellular networks (as well as a decrease in expense). An additional decrease is due to a decrease in the number of lines (mainly due to number portability), a reduction in call traffic and a decrease in tariffs in June 2007 and June 2008. The decrease in revenue was moderated mainly by ongoing growth in revenues from high-speed internet service (ADSL) and by an increase in income from data communication services. The Company's auditors continue to draw attention to the growing competition, changes in the in the communications market and the impact of regulation on the financial situation of the Group and the results of its operations.

Revenues from the cellular telephone segment increased from approximately NIS 2.30 billion in the first half of 2007 to approximately NIS 2.36 billion in the reporting period. The increase is mainly due to an increase in the number of subscribers, which led to an increase in revenue from interconnect and revenue from content services, which was partially offset by a decrease in average revenue per user, mainly due to erosion of fees for outgoing calls and a decrease in interconnect fees.. There was also an increase in revenue from sale of terminal equipment, due to an increase in the number of handsets sold and upgraded.

Revenue in the international communications, internet and NEP services segment amounted to NIS 644 million in the first half of 2007, compared to approximately NIS 640 million in the reporting period. In this segment there was a decrease in operations relating to transfer of calls between communication operators around the world offset by an increase in revenue from internet broadband service and outgoing calls due to an increase in the market share.

Revenue from the multi-channel television segment increased from approximately NIS 708 million in the first half of 2007 to approximately NIS 761 million in the reporting period, mainly due to an increase in average revenue per user.

C. Depreciation and amortization

The Group's depreciation and amortization expenses decreased from approximately NIS 877 million in the first half of 2007 to approximately NIS 851 million in the reporting period, mainly due to a decrease in the depreciation expenses in the domestic fixed-line communication segment resulting from full depreciation of property plant and equipment and a decrease in investments in new assets. The decrease was partially offset by an increase in depreciation expenses in the cellular segment as a result of the accelerated depreciation of the 1X network due to the establishment of a UMTS network.

D. Salary

The Group's salary expenses increased from approximately NIS 1.16 billion in the first half of 2007 to approximately NIS 1.201 billion in the reporting period. In the domestic fixed line communications segment there was a decrease in salary expenses due to retirement of employees. This decrease was partially offset by an increase in salaries and share-based payments. In the other segments there was an increase in salary expenses mainly due to an increase in the number of employees in response to the increase in operational requirements.

E. General and operating expenses

The Group’s operating and general expenses in the first half of 2008 amounted to approximately NIS 2.68 billion, compared to approximately NIS 2.83 billion in the corresponding period in the prior year.

In the domestic fixed-line communications segment, operating and general expenses decreased from approximately NIS 1.067 billion in the first half of 2007 to NIS 934 million in the reporting period. The decrease is mainly due to a reduction in interconnect fees to cellular operators alongside a decrease in income, from the update of the provision for royalties and from implementation of streamlining steps that resulted in a decrease in operating expenses.

In the cellular segment, operating and general expenses decreased from approximately NIS 1.32 billion in the first half of 2007 to approximately NIS 1.292 billion in the reporting period. The decrease is mainly due to a decrease in prices of terminal equipment due to a decrease in the dollar exchange rate and advertising expenses which was partially offset by an increase in content expenses and connectivity as well as an increase in revenues.

In the international communications, internet services and NEP segment there was a decrease in general and operating expenses from approximately NIS 374 million in the first half of 2007 to approximately NIS 352 million in the reporting period. The decrease is mainly due to a reduction in operations relating to call transfers between communication operators around the world alongside a decrease in revenues.

In the multi-channel television segment, general and operating expenses increased from approximately NIS 433 million in the first half of 2007 to approximately NIS 470 million in the reporting period, due to an increase in consumption of content due to broadcasts of original productions and an increase in maintenance services by subcontractors.

F. Other operating expenses (income), net

The Group's other net operating revenue derived from the domestic fixed-line communications segment. These revenues amounted to approximately NIS 13 million in the reporting period, compared to expenses of approximately NIS 44 million in the corresponding period in the prior year. This is mainly due to provisions recorded for lawsuits in the corresponding period in the prior year compared to capital gain and a decrease of provisions in the reporting period.

G. Operating income

The Group's operating income in the first half of 2008 amounted to approximately NIS 1.464 billion, compared to approximately NIS 1.227 billion in the corresponding period in the prior year, an increase of approximately NIS 237 million. The increase in operating income is due to the changes in the results of the segments described above in the revenue and expenses sections.

H. Financing expenses, net

The Group's net financing expenses in the first half of 2008 amounted to approximately NIS 283 million compared to approximately NIS 131 million in the corresponding period in the prior year, an increase of NIS 152 million.

The Group's debt to financial institutions and debenture holders is mainly linked to the CPI and the financing expenses are affected by fluctuations in the index. In the reporting period there was a rise in the index, to which the debt balance is linked, compared to the corresponding period in the prior year and revaluation of liabilities led to an increase in the Group's financing expenses.

In the domestic fixed line communications segment, net finance expenses in the reporting period amounted to approximately NIS 41 million compared to net financing revenue amounting to approximately NIS 32 million in the corresponding period. The increase in net finance expenses compared to the corresponding period is mainly due to a decrease in revenues in the capital market and realization of deposits and securities and a decrease in their return. Additionally, in this segment there is an increase in expenses due to revaluation of CPI-linked liabilities, which was partially offset by hedging transactions.

In the cellular segment, there was an increase in net finance expenses, mainly due to the increase in expenses for revaluation of CPI-linked liabilities as a result of a rise in the index, which was partially offset by capitalized credit costs for qualified assets and a decrease in net debt.

In the multi-channel television segment, net financing expenses in the reporting period amounted to approximately NIS 234 million compared to approximately NIS 163 million in the corresponding period in the prior year. The increase in the CPI led to an increase in financing expenses due to the revaluation of CPI-linked liabilities and an increase in the Company's financial debt.

I. Income tax

The Group's tax expenses in the reporting period amounted to approximately NIS 385 million, representing approximately 33% of profit before taxes, compared to approximately NIS 373 million in the corresponding period in the prior year, representing 34% of profit before taxes. Most of the decrease in the tax expenses from profit before income taxes is due to a reduction in the tax rate and the cancellation of the Income Tax (Taxation under Conditions of Inflation) Law. The decrease was moderated by the increase in the losses of DBS that are not deductible for tax purposes.

3. Liquidity and sources of financing

Consolidated cash flows generated by operating activities in the first half of 2008 amounted to approximately NIS 1.413 billion, compared to NIS 1.562 billion in the corresponding period in the prior year, a decrease of approximately NIS 149 million. The decrease in cash flows generated by operating activities is mainly due to an increase in payments for early retirement, a decrease in the balance of liabilities to suppliers in the domestic fixed-line segment and an increase in the trade receivables balance, due to the abovementioned reasons. The decrease in cash flow from operating activities was moderated by the increase in operating income of the Group's segments.

Cash flows generated by operating activities are one of the sources of financing of the Group's investments, which during the reporting period included approximately NIS 617 million invested in development of communications infrastructures, compared to investments amounting to approximately NIS 413 million in the corresponding period.

During the reporting period, the Group repaid net debts and paid interest of approximately NIS 846 million, of which approximately NIS 627 million was on account of debentures, NIS 81 million in loans and approximately NIS 235 million in interest payments. On the other hand, the Company received approximately NIS 68 million in short-term credit and net consideration from realization of derivative financial instruments in the amount of approximately NIS 29 million compared to payment of net debt and interest payments in the amount of approximately NIS 481 million in the corresponding period in the prior year.

In the reporting period, cash dividends in the amount of NIS 679 million were paid, compared to NIS 2.1 billion paid in the corresponding period in the prior year.

The monthly average short-term credit average from banks in the first half of 2008 amounted to approximately NIS 105 million. The monthly average of long-term liabilities to financial institutions and debenture holders in the first half of 2008 amounted to approximately NIS 6.412 billion.

The working capital deficit on June 30, 2008, amounted to approximately NIS 426 million, compared to NIS 1.917 billion in the corresponding period in the prior year. The improvement in working capital is due to an increase in working capital in all the segments in which the Group operates, with the exception of the domestic fixed-line communications segment.

The improvement derives mainly from the multi-channel television segment, where there was a decrease in deficit of approximately NIS 1.257 billion, mainly from classification of bank loans as long-term loans, in view of compliance with the terms of the financing agreement with the banks.

4. Comparison: 2008 second quarter to the results of the corresponding quarter

Segment	Three months ended June 30, 2008 NIS millions Operating income	Three months ended June 30, 2007 NIS millions Operating income
Domestic fixed-line communications	428	243
Cellular	266	240
International communications, internet services and NEP	63	53
Multi-channel television	43	31
Others	-	4
Total	800	571

Revenue in the second quarter of 2008 increased by approximately NIS 33 million compared to the corresponding quarter in the prior year.

Total costs and expenses decreased by approximately NIS 196 million compared to the corresponding quarter in the prior year.

Net financing expenses increased by approximately NIS 109 million compared to the corresponding quarter in the prior year.

The income and expenses items and the reasons for the differences between the quarters are similar to the explanations in the half-year results. The abovementioned changes in the income statement items led to net earnings of approximately NIS 437 million in the second quarter, compared to net profit of approximately NIS 361 million in the corresponding quarter.

5. Group involvement in the community and donations

The Group is active in the community through contributions to recognized non-profit organizations that channel funds to education, welfare and other causes, and through development of direct volunteering of employees in the community. In the reporting period, Bezeq works with Matan - Your Way to Give, a non-profit organization that helps companies implement their philanthropic vision. In addition, the Company has become a member of Maale, Business for Social Responsibility, a non-profit membership organization that advocates corporate values. Additionally, Group employees volunteer in additional and diverse community activities.

During the reporting period the Group was involved in the community and donated approximately NIS 1,417 million. The principal recipients are listed below:

A. In the project Youth Employment at Bezeq, which has been ongoing for some 14 years, the Company's employees voluntarily mentor youth at risk with the aim of integrating them into normative life.

B. The Company initiated and established a photography exhibition of the country's leaders. The exhibition, which was free of charge, was open to the general public for one month. The cost of the exhibition amounted to approximately NIS 645,000.

C. The Yom Tov project – a special broadcast for contribution to youth at risk. The Company contributed approximately NIS 330,000.

D. Music Academy – the Company awarded scholarships amounting to NIS 40,000 to musicians from outlying areas.

E. The Company contributed approximately NIS 100,000 to the construction of a monument to commemorate victims of the Beit Lid terrorist attack, in which a graduate of the Bezeq school lost his life.

F. The Company continues to support the Dialogue in the Dark project at the Children's Museum in Holon, and many other activities.

G. Pelephone contributed approximately NIS 148,000 to various associations.

H. Bezeq International is involved in ongoing operations on behalf of underprivileged communities in Petach Tikva, it adopted "lone" soldiers and a combat division and participated in projects for children with special needs.

I. DBS donated NIS 50,000 to the Shirutrom telethon for soldiers.

6. Exposure to and management of market risks

A. Further to the description in the Directors' Report of 2007, hedging transactions against market risks connected to exposure to fluctuations in the exchange rate and the CPI partially reduced this exposure.

B. The sensitivity analyses for the fair value and the effect of the change in the market prices on the fair value of on- or off-balance sheet contractual agreements on June 30, 2008, are not substantially different from the December 31, 2007 statements. However, the total fair value of net liabilities that are sensitive to fluctuations in the dollar-shekel exchange rate on December 31, 2007 should amount to approximately NIS 1.148 billion. The sensitivity to changes in the dollar interest rate should amount to approximately NIS 622 million, due to the adjusted measuring of communications to space sections, which should amount to NIS 611 million instead of NIS 343 million.

C. The linkage basis report on June 30, 2008, is not substantially different from the December 31, 2007 statement.

The surplus monetary liabilities over monetary assets in or linked to foreign currency on June 30, 2008, amounted to approximately NIS 113 million in the Group. Forward currency transactions on June 30, 2008, amounted to approximately NIS 284 million. The transactions were also intended hedge against off-balance sheet liabilities in or linked to foreign currency.

The excess of liabilities over monetary assets linked to the CPI on June 30, 2008, amounted to approximately NIS 5.717 billion in the Group. As a result of hedging transactions, on June 30, 2008, the net CPI-linked liabilities, which are not hedged by forward transactions, amounted to NIS 4.418 billion.

7. Critical accounting estimates

Preparation of the financial statements according to international accounting standards requires the management to make estimates and assessments that influence the reported values of assets and liabilities, income and expenses, and disclosure relating to contingent assets and liabilities. Management bases its estimates and assessments on past experience and on additional factors, fair value assessments and opinions which it believes are relevant, taking into account the circumstances. The actual results can differ from those assessments based on various assumptions and conditions. Information on the principal matters of uncertainty in critical assessments and judgments in the application of the accounting policies is provided in the annual financial statements. We believe that these assessments and estimates are critical because every change in them and in the assumptions has the potential to materially affect the financial statements.

8. Disclosure regarding the process for approval of the Company's financial statements

The Company organ given the responsibility for oversight is the Board of Directors. The Board of Directors appointed a balance sheet committee whose duties and composition are described in the 2007 Directors' Report.

The financial statements were discussed at the balance sheet committee and submitted to the Board of Directors for approval. The following officers attended the board discussion: board members – Shlomo Rodav, Eyal Yaniv, Menachem Inbar, Michael Grabiner, Ran Gottfried, Yoav Rubenstein, Elon Shalev, Ki Kiarie, David Gilboa, Rami Nomkin, Yitzhak Idelman and Yehuda Porat. In addition, the following officers attended: Avi Gabbay – CEO, Alan Gelman – Deputy CEO and CFO, and Bosmat Chelouche – legal consultant. Representatives of the Company Auditors',,Somekh Chaikin, also participated in the discussion.

9. Sundry and events subsequent to the date of the financial statements

A. On June 1, 2008, the general shareholders meeting approved, this subsequent to the approval by the board of directors on April 17, 2008, the employment conditions for the chairman of the board as described in Note 8 to the financial statements., The directors examined each component in the compensation package and the package as a whole, and in their opinion the general compensation package is appropriate and reasonable under the circumstances and is compatible with the nature of the position and the challenges facing the chairman and the expectations of the board. The compensation package was also compared with other large companies in Israel and was found to be within the high range of the benchmarks.

B. On July 31, 2008, the Company's Board of Directors (after approval of the Board's audit committee) resolved to approve the extension of the Company's management agreement with a corporation connected to Ap.Sb.Ar. Holdings Ltd., the Company's controlling shareholder, for an additional three years subsequent to the expiry of the current agreement, under the same terms as the original agreement. Extension of the agreement is subject to approval of the general meeting of the Company's shareholders.

C. As of June 30, 2008, the Group's net dollar-linked contractual liabilities (including off-balance sheet) amounted to approximately NIS 894 million. The Group's net CPI-linked liabilities (including off-balance sheet) amounted to NIS 5.519 billion. The dollar exchange rate rose by 6.7% between June 30, 2008, and the date of approval of the financial statements. The CPI rose by 1.1% in July 2008.

The Company is exposed to changes in copper prices which leads to a change in the scrap value of the Company's copper cable infrastructure. The value of the Company's copper cables on June 30, 2008, amounts to NIS 591 million (based on an external assessment dated December 31, 2007, with adjustments, as required). A change in the price of copper could affect the Company's depreciation expenses and any consideration and capital gain from the sale of scrap.

On June 26, 2008, the Company's Board of Directors adopted a policy for management of financial exposure, which replaces former exposure policy. The primary aim of the new policy is to reduce material exposure to market risks that will affect the Group's cash flows and financial results. Based on this policy, the Company will enter into hedging transactions, in part, according to the circumstances and its judgment, primarily to reduce its exposure to changes in the foreign currency exchange rate and the CPI.

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

Shlomo Rodav	**Avi Gabbay**
Chairman of the Board	**CEO**

“BEZEQ” THE ISRAEL TELECOMMUNICATION CORP. LIMITED

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

JUNE 30, 2008

(UNAUDITED)

Contents

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The Board of Directors of
"Bezeq" - The Israel Telecommunication Corp. Limited

At your request, we have reviewed the condensed consolidated interim balance sheet of "Bezeq" - The Israel Telecommunication Corp. Limited (hereinafter "Company") at June 30, 2008, as well as the condensed consolidated interim statement of income, the condensed consolidated interim statement of recognised income and expense and the condensed consolidated interim statement of cash flows for the six-month and three-month periods then ended.

Our review was carried out in accordance with procedures prescribed by the Institute of Certified Public Accountants in Israel. The procedures included, inter alia, reading the said financial statements, reading the minutes of meetings of the shareholders and of the Board of Directors and its committees, as well as making inquiries of persons responsible for financial and accounting matters.

Reports of other auditors were furnished to us which relate to investments in associates in which the Company's investments amount to approximately NIS 30 million at June 30, 2008, and the Company's share in the profits in respect thereof amount to approximately NIS 2.3 million and approximately NIS 696,000 for the six-month and three-month periods then ended.

As the review is limited in scope and does not constitute an audit in accordance with generally accepted auditing standards, we do not express an opinion on the condensed consolidated interim financial statements.

In the course of our review, including reviewing the reports of other auditors as mentioned above, nothing came to our attention which would indicate the necessity of making material changes to the said interim financial statements in order for them to be in conformity with standard IAS 34 – Interim Financial Reporting and in accordance with the provisions of Section 4 of the Securities Regulations (Periodic and Immediate Reports), 5730-1970.

We draw attention to the uncertainties relating to the following matters, for which the maximum possible exposure is significant:

1. The continuing opening of the communications sector to competition, the changes in the communications market, and the effects of regulation on the Group's financial position and operating results, as described in Note 1.

2. Contingent claims made against the Group of which the exposure cannot yet be assessed or calculated, and other contingencies as described in Notes 7B and 7C.

3. The financial position of a subsidiary. As mentioned in Note 6A, as of June 30, 2008, the subsidiary meets the financial criteria set for it, following the amended stipulations in respect of 2008 placed upon it by the banks on March 5, 2008, and June 25, 2008 as adapted to the subsidiary's 2008 annual budget and to certain prescribed operational data. The continuation of the activity of the subsidiary is contingent on, *inter alia*, compliance with the conditions set for 2008 and/or further relief which may be received during the year. In the opinion of the management of the subsidiary, the financial resources at its disposal will be sufficient for the requirements of the subsidiary's operations in the coming year, based on the cash flow projections approved by the board of directors of the subsidiary.

Somekh Chaikin
Certified Public Accountants (Isr.)

August 20, 2008

Condensed Consolidated Interim Balance Sheets at

	June 30, 2008	June 30, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Assets			
Cash and cash equivalents	**740**	2,063	1,203
Investments and loans, including derivatives	**66**	1,008	389
Trade receivables	**2,497**	2,115*	2,403
Other receivables	**233**	231	247
Inventory	**186**	229	203
Current tax assets	**16**	12	11
Assets classified as available for sale	**23**	-	17
Total current assets	**3,761**	5,658	4,473
Trade and other receivables	**574**	498*	535
Investments and loans, including derivatives	**226**	279	233
Broadcasting rights	**278**	206*	243*
Property, plant and equipment	**5,971**	6,211	6,064
Intangible assets	**2,668**	2,541	2,526
Deferred and other expenses	**394**	363	367
Investments in associates accounted by the equity method	**30**	33	37
Deferred tax assets	**605**	789	678
Total non-current assets	**10,746**	10,920	10,683
Total assets	**14,507**	16,578	15,156

Condensed Consolidated Interim Balance Sheets at

	June 30, 2008 (Unaudited) NIS millions	June 30, 2007 (Unaudited) NIS millions	December 31, 2007 (Audited) NIS millions
Liabilities			
Loans and credit	**1,094**	4,187	1,913
Trade payables	**1,450**	1,333	1,533
Other payables, including derivatives	**742**	843*	745
Current tax liabilities	**75**	70	57
Deferred income	**32**	37	47
Provisions	**348**	332	392
Employee benefits	**446**	773*	705
Total current liabilities	**4,187**	7,575	5,392
Debentures	**3,941**	3,350	4,420
Obligations to banks	**1,102**	392	307
Loans from others	**147**	126	136
Loans provided by the minority in a subsidiary	**413**	599	375
Employee benefits	**259**	329	261
Deferred income and others	**13**	28	36
Provisions	**56**	54	57
Deferred taxes	**74**	-	-
Total non-current liabilities	**6,005**	4,878	5,592
Total liabilities	**10,192**	12,453	10,984
Shareholders' Equity			
Share capital	**6,132**	6,132	6,132
Reserves	**701**	681	681
Deficit	**(2,112)**	(2,089)	(2,268)
Total equity attributable to shareholders of the Company	**4,721**	4,724	4,545
Minority interest	**(406)**	(599)	(373)
Total shareholders' equity	**4,315**	4,125	4,172
Total shareholders' equity and liabilities	**14,507**	16,578	15,156

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

Date of approval of the financial statements: August 20, 2008.

* See Note 3C.

The notes to the interim financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Income

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues (Note 10)	**6,186**	6,141	**3,086**	3,053	12,400
Costs and expenses					
Depreciation and amortisation	**851**	877	**422**	436	1,769
Salary	**1,201**	1,160	**585**	584	2,375
Operating and general expenses (Note 11)	**2,683**	2,833	**1,313**	1,410	5,841
Other operating expenses (income), net	**(13)**	44	**(34)**	52	79
	4,722	4,914	**2,286**	2,482	10,064
Operating income	**1,464**	1,227	**800**	571	2,336
Financing costs					
Financing expenses	**392**	321	**231**	159	796
Financing income	**(109)**	(190)	**(48)**	(85)	(487)
Net financing expenses	**283**	131	**183**	74	309
Profit after financing expenses	**1,181**	1,096	**617**	497	2,027
Equity in profits of investees accounted by the equity method	**2**	2	**1**	1	6
Profits before income tax	**1,183**	1,098	**618**	498	2,033
Income tax	**385**	373	**205**	158	672
Profit for the period	**798**	725	**413**	340	1,361
Attributable to:					
The shareholders of the Company	**835**	760	**437**	361	1,330
Minority interest	**(37)**	(35)	**(24)**	(21)	31
Profit for the period	**798**	725	**413**	340	1,361
Earnings per share					
Basic earnings per share (in NIS)	**0.32**	0.29	**0.17**	0.14	0.51
Diluted earnings per share (in NIS)	**0.32**	0.29	**0.17**	0.14	0.50

The notes to the consolidated financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Recognised Income and Expense

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Net change in fair value of financial assets classified as available for sale	**-**	5	**-**	4	4
Net change in fair value of financial assets classified as available for sale transferred to profit and loss	**(5)**	-	**-**	-	-
Actuarial gains from a defined benefit plan (1)	**-**	-	**-**	-	14
Taxes in respect of income and expenses charged directly to equity	**1**	(2)	**-**	(1)	(4)
Foreign currency translation differences	**(11)**	-	**(11)**	-	-
Income and expenses recognised directly to equity	**(15)**	3	**(11)**	3	14
Profit for the period	**798**	725	**413**	340	1,361
Total recognised income and expenses for the period	**783**	728	**402**	343	1,375
Attributable to:					
The shareholders of the Company	**820**	763	**426**	364	1,344
Minority interest	**(37)**	(35)	**(24)**	(21)	31
Total recognised income and expenses for the period	**783**	728	**402**	343	1,375

(1) The Group does not recalculate its actuarial provisions in each interim reporting period unless there are significant changes in the benefit plan or fundamental changes in market terms during the interim period. As a result, there are no actuarial earnings or losses in the reporting period.

The notes to the consolidated financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Cash Flows

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flows from operating activities					
Profit for the period	**798**	725	**413**	340	1,361
Adjustments:					
Depreciation	**707**	741	**356**	365	1,482
Amortisation of intangible assets	**124**	126	**56**	66	270
Amortisation of deferred and other charges	**20**	10	**10**	5	17
Gain from decrease in holding in companies accounted by the equity method	**-**	-	**-**	-	1
Equity in earnings of associates accounted by the equity method	**(2)**	(2)	**(1)**	(1)	(6)
Net financing expenses	**320**	179*	**191**	161*	372
Net capital (gain) loss	**(19)**	(5)	**(18)**	11	(88)
Share-based payment transactions	**35**	-	**22**	-	-
Payments to a former senior officer	**-**	6	**-**	6	6
Income tax expenses	**385**	373	**205**	158	672
Payment in respect of clearance of derivative financial instruments, net	**(14)**	(4)*	**(4)**	(9)*	(9)
Change in inventory	**15**	(25)	**52**	22	(6)
Change in trade receivables	**(132)**	(109)	**(28)**	(96)	(437)
Change in other receivables	**(14)**	(25)	**39**	27	4
Change in other payables	**4**	38*	**(69)**	(18)*	(18)
Change in suppliers	**(277)**	(129)	**(134)**	(162)	36
Change in provisions	**(46)**	45	**(42)**	30	105
Change in broadcasting rights	**(35)**	(36)	**(7)**	(5)	(74)
Change in employee benefits	**(262)**	(192)	**(179)**	(107)	(300)
Change in deferred and other income	**(2)**	(3)*	**(3)**	(40)*	(11)
	1,605	1,713	**859**	753	3,377
Interest received	**34**	70	**15**	27	116
Dividend received	**2**	3	**2**	3	3
Income tax paid	**(228)**	(224)	**(100)**	(86)	(430)
Net cash from operating activities	**1,413**	1,562	**776**	697	3,066

* See Note 3C.

The notes to the consolidated financial statements are an integral part thereof.

Condensed Consolidated Interim Statements of Cash Flows (Contd.)

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	**2007**	**2008**	**2007**	**2007**
	(Unaudited)	**(Unaudited)**	**(Unaudited)**	**(Unaudited)**	**(Audited)**
	NIS millions	**NIS millions**	**NIS millions**	**NIS millions**	**NIS millions**
Cash flows from investing activities					
Investment in intangible assets and deferred expenses	**(135)**	(105)	**(76)**	(43)	(273)
Proceeds from sale of property, plant and equipment and deferred expenses	**87**	121	**26**	97	177
Financial assets held for trade, net	**314**	7	**257**	(108)	647
Purchase of property, plant and equipment	**(617)**	(413)	**(310)**	(235)	(973)
Proceeds from sale of investments and long-term loans	**11**	33	**5**	26	66
Purchase of investments and long-term loans	**(4)**	-	**(4)**	-	(8)
Investment in an associated company	**(1)**	-	**-**	-	-
Net cash used for investment activities	**(345)**	(357)	**(102)**	(263)	(364)
Cash flows from financing activities					
Issue of debentures	**-**	757	**-**	757	1,814
Receipt of loans	**-**	50	**-**	50	50
Repayment of debentures	**(627)**	(97)	**(398)**	(15)	(1,927)
Repayment of loans	**(81)**	(149)	**(41)**	(80)	(840)
Short-term credit, net	**68**	(23)	**56**	9	(37)
Dividends paid	**(679)**	(2,100)	**(679)**	-	(2,860)
Interest paid	**(235)**	(198)	**(179)**	(123)	(389)
Receipt (payment) in respect of clearance of derivative financial instruments, net	**29**	(14)*	**25**	(2)*	77
Injections of a minority in a subsidiary	**4**	-	**4**	-	-
Net cash from (used for) financing activities	**(1,521)**	(1,774)	**(1,212)**	596	(4,112)
Net increase (decrease) in cash and cash equivalents	**(453)**	(569)	**(538)**	1,030	(1,410)
Cash and cash equivalents at the beginning of the period	**1,203**	2,632	**1,283**	1,033	2,632
Effect of fluctuations in the rate of exchange on cash balances	**(10)**	-	**(5)**	-	(19)
Cash and cash equivalents at the end of the period	**740**	2,063	**740**	2,063	1,203

* See Note 3C.

The notes to the consolidated financial statements are an integral part thereof.

NOTE 1 – REPORTING ENTITY

A. Bezeq – The Israel Telecommunication Corp. Ltd. ("the Company") is a company domiciled in Israel whose shares are traded on the Tel Aviv Stock Exchange. The official address of the Company is 132 Menachem Begin Road, Tel Aviv. The condensed consolidated interim financial statements of the Company comprise those of the Company and its subsidiaries (jointly referred to as the "Group"), and the Group's interests in associates. The Group is a principal provider of communications services in Israel (see also Note 13 – Segment Reporting).

B. On October 11, 2005, control in the Company was transferred from the State to Ap.Sb.Ar. Holdings Ltd. and the Company ceased to be a government company. The Company was declared a monopoly in the main areas in which it operates. An appeal filed by the Company was pending in the Antitrust Court against the non-revocation of its monopoly status in the basic telephony field; however, at the suggestion of the court (in view of the time elapsed since it was filed), the Company consented to withdraw the appeal. All the segments of operation of the Group are subject to competition. The activities of the Group are, in general, subject to government regulation and control.

C. The Company is subject to various systems of laws that regulate and limit its business operations, including its tariffs, which are controlled by Sections 15 to 17 of the Communications Law. The tariffs of the Company's controlled services, which are set in regulations, are updated according to a linkage formula less a reduction factor, as laid down in the regulations and pursuant to the recommendations of public committees with a mandate to examine those tariffs. In March 2008 the Committee for Examining the Policy and Rules of Competition in Communications in Israel, submitted its recommendations to the Minister of Communications. On August 13, 2008, the Minister of Communications announced his decision to adopt the conclusions of the committee, subject to a number of changes and emphases, and they will become the policy guiding the Ministry in the years to come. The Minister's decision improves the level of regulatory clarity to some extent.

The intensifying competition and numerous changes in the communications market are expected to have an adverse effect on the business results of the Group, an effect that the Group is unable to estimate.

NOTE 2 – BASIS OF PRESENTATION

A. The condensed interim consolidated financial statements were prepared in accordance with the International Accounting Standard 34 – Interim Financial Reporting, and in accordance with Chapter 4 of the Securities (Periodic and immediate reports) Regulations, 5730-1970.

B. These reports do not contain all the information required in full annual financial statements, and should be reviewed in the context of the annual financial statements of the Company and its subsidiaries at December 31, 2007 and the year then ended, and their accompanying notes ("the annual financial statements"). The Group states in the notes to the interim financial statements only the material changes that have occurred in its business and legal environment from the date of the most recent annual financial statements until the date of these interim financial statements.

C. The condensed consolidated interim financial statements were approved by the Board of Directors on August 20, 2008.

NOTE 3 – REPORTING PRINCIPLES AND ACCOUNTING POLICIES

The significant accounting policies applied in these condensed consolidated interim financial statements are consistent with those applied in the annual financial statements for the year ended December 31, 2007, except as mentioned in this note.

A. Initial application of accounting standards

Commencing January 1, 2008, the following international financial reporting standards came into force:

(1) Interpretation 11 of the International Financial Reporting Interpretations Committee (IFRIC 11) for *IFRS 2 – Group and Treasury Share Transactions*. The interpretation requires that a share-based payment in which the entity receives goods and services as consideration for its own equity instruments, be accounted for as equity-settled share-based payment, irrespective of the question of how the equity instruments were obtained. This interpretation did not materially affect the results of the Group's operations and its financial position.

(2) IFRIC 14 for IAS 19 – *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*. The interpretation clarifies when refunds and reductions in future contributions in connection with defined benefit assets must be seen as available, and provides instruction about the influence of minimum contribution requirements on those assets. The Interpretation relates to the question of when a minimum deposit requirement establishes a liability. This interpretation did not materially affect the results of the Group's operations and its financial position.

(3) The Group opted for early application of IAS 2 – *Share-Based Payment – Vesting and Cancellation*. The standard states that vesting terms are terms that determine whether the group receives the services for which the other part is entitled to share-based payment, and they are limited to terms of service and performance. Non-vesting terms will be reflected in the fair value of the grant on the grant date, and after the grant date the group will not revise the fair value in respect of those terms. In addition, the standard describes the treatment of non-compliance with non-vesting terms. The early application did not materially affect the results of the Group's operations and its financial position.

B. New standards prior to their application

A number of new standards, amendments to existing standards and interpretations have not yet come into force on June 30, 2008, and therefore were not applied in the preparation of these consolidated financial statements

Since publication of the last annual report, the following standards have been published:

(1) IAS 32 – *Financial Instruments: Presentation*, IAS1 – *Presentation of Financial Statements – Redeemable Financial Instruments and Obligations Arising on Liquidation.* According to these amendments, certain financial instruments and obligations arising on liquidation are to be classified as redeemable equity if certain criteria exist. In addition, appropriate disclosure is required for redeemable instruments classified as equity. The amendments will apply to annual periods commencing January 1, 2009, or thereafter. The amendments are not expected to have a material effect on the activities and financial position of the Group.

(2) IFRIC 13 – *Customer Loyalty Programs* – The interpretation deals with the accounting treatment of companies that grant benefits in customer loyalty programs (such as points or frequent flyer plans) at the time of purchase of goods or services. IFRIC 13 explains how companies should treat liabilities to supply goods or services in the future, free of charge or at a discount (benefits) to customers who expect to utilise the benefits. The interpretation applies to annual periods commencing July 1, 2008 or thereafter. The Group is considering the effects of the interpretation on its financial statements.

NOTE 3 – REPORTING PRINCIPLES AND ACCOUNTING POLICIES (CONTD.)

B. New standards prior to their application (contd.)

(3) IFRIC 15 – *Agreements for the Construction of Real Estate* (in this sub-section – "the Interpretation"). The Interpretation provides guidelines for ascertaining whether real estate construction transactions are covered by IAS 18 – *Revenue*, whereby revenue from the construction of real estate will be recognized similarly, from the aspects of timing and character, to revenue from the sale of a product or service, or are covered by IAS 11 – *Construction Contracts*, whereby the revenue will be recognized according to the completion stage of the real estate asset. The Interpretation will apply to annual periods commencing January 1, 2009, or thereafter, and will be applied retrospectively. Early application is permissible, with disclosure. The Interpretation is not expected to affect the financial statements of the Group.

(4) IFRIC 16 – *Hedges of a Net Investment in a Foreign Operation* (in this sub-section – "the Interpretation"). The Interpretation relates to instances in which an investment is made in a foreign operation, and provides guidelines for hedging such an investment. The Interpretation relates, *inter alia*, to the nature of the hedged risk and the amount of the hedged item for which the hedging is designated, to the location of the hedging item in the group of companies, and to the accounting treatment of the capital fund on the date of disposal of the foreign operation. This Interpretation applies to annual periods commencing October 1, 2008, or thereafter. Early application is permitted, with disclosure. Adoption of the interpretation is not expected to influence the financial statements of the Group.

(5) IAS 27 – *Consolidated and Separate Financial Statements* and IFRS 1 – *First-time Adoption of International Financial Reporting Standards*, Amended ("the Standards"). Under the Standards, after their amendment, a company that chooses the method of measuring the cost of its investments in subsidiaries, jointly-controlled companies and associates in separate (solo) financial statements, can measure those investments on the date of transition to IFRSs at the fair value according to IAS 39 or at their book value according to prior accepted accounting principles. In addition, a dividend received from subsidiaries, jointly-controlled companies and associates will be recognized as income in the separate financial statements of the investor company. Also, in certain cases, receipt of a dividend constitutes a sign of impairment of the investment in the investee company. The new Standards will apply to annual periods commencing January 1, 2009, or thereafter. Early application is permitted, for each standard separately, with disclosure. The changes attributed to IAS 27 will be applied prospectively. Adoption of the Standard is not expected to affect the consolidated financial statements.

(6) Improvements to IFRSs – As part of a project for amending the international standards, the IASB published and approved, in May 2008, 35 amendments to various international standards on a wide range of accounting issues. The importance of the amendments lies in their indicating the position of the IASB on those issues, and therefore they could affect the accounting treatment even prior to the date of their application. Most of the amendments will come into force for periods commencing January 1, 2009, or thereafter, with early adoption permitted, subject to the terms set out for each amendment and subject to the transition provisions relating to initial adoption of IFRSs. The Group is considering the effects of the aforementioned on its financial statements.

(7) Hedgeable items, Amendment to IAS 39 – *Financial Instruments: Recognition and Measurement* ("the Amendment"). The Amendment clarifies that changes in cash flows or changes in the fair value of a one-sided risk can be designated as a hedged item, i.e. a risk defined as a risk of exposure to fluctuations above or below a certain price or a defined variable. The Amendment also clarifies that an inflationary component can be designated as a separate risk, provided it is contractually specified in the cash flow of Index-linked debentures so that it can be identified separately and measured reliably, and if the other cash flows of the instrument are not affected by the inflationary component, the amendment should be retroactively applied to annual periods commencing on July 1, 2009, or thereafter. Early application is permitted, with disclosure. The Group is considering the effects on its financial statements.

NOTE 3 – REPORTING PRINCIPLES AND ACCOUNTING POLICIES (CONTD.)

C. Classified amounts

The condensed consolidated interim financial statements include reclassification of certain amounts of the comparative figures of the relevant sections,, including the classification of broadcasting rights to non-current assets

D. Index-linked assets and liabilities not measured at fair value

Further to Note 3C(1) to the financial statements at December 31, 2007, concerning index-linked financial instruments – discussion of the matter by IFRIC resulted in the committee's decision that the provisions of IAS 39 (Financial Instruments: Recognition and Measurement) should be applied with discretion as to the most appropriate application of the standard's guidelines, and furthermore, the committee saw no justification for continuing its discussions of the matter. Nevertheless, the committee will refer the question to the IASB for review of the clarification or a broadening of the application guidelines of IAS 39. In light of the aforesaid, the value of index-linked financial assets and liabilities that are not measured at fair value, is revalued in each period according to the actual rate of rise in the Index.

E. Property, plant and equipment

On June 26, 2008, the Board of Directors of the Company resolved to approve Company implementation of the NGN project. At that date, the Board approved detailed planning of the project, setting-up of two areas as operational pilots, and the purchase of soft switches. The project will be implemented in modules with Company assessments on a regular basis, and after each stage of implementation it will reconsider the viability of continuing the project, looking at all the variable factors that could influence its viability and therefore the need to revise the project outline. The content, pace of performance and the amounts to be invested in the project, will be determined each year in the framework of the annual budget of the Company. Subsequent to the balance sheet date, an additional investment budget, in excess of the above, was approved for implementation in 2008, which includes, *inter alia*, management systems, equipment cabinets, MSAG systems, optical equipment and other items. The estimated life of part of the communications infrastructure that will be replaced in the project, will vary, and as a result, the Company's depreciation expenses for that part can be expected to be accelerated, and despite the pace of performance of the entire project, the lifetime could still change. It is expected that commencing in the second half of 2008, the Company's depreciation expense will increase by an average of about NIS 55 million per year up to and including 2010, and in 2011 – 2013 it will decrease by about NIS 20 million per year on average. The effect of the aforementioned is subject to changes in the pace of deployment of the new network and the scrap value of the copper cables, if any.

NOTE 4 – ESTIMATES

The preparation of interim financial statements requires Management to make judgments and use estimates, assessments and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

The significant estimations applied in these interim statements do not differ significantly from those applied to the annual financial statements.

NOTE 5 – RATES OF CHANGES IN THE CONSUMER PRICE INDEX AND FOREIGN CURRENCY EXCHANGE RATES

The changes that occurred in the consumer price index and in the exchange rates of the US dollar and the euro in the accounting period are as follows:

	Consumer Price Index	Rate of exchange of the US dollar	Rate of exchange of the euro
	%	%	%
For the six-month period ended on:			
June 30, 2008	**2.25**	**(12.8)**	**(6.6)**
June 30, 2007	0.97	0.57	2.68
For the three-month period ended on:			
June 30, 2008	**2.24**	**(5.66)**	**(5.9)**
June 30, 2007	1.21	2.26	3.23
For the year ended December 31, 2007	3.40	(8.97)	1.71

NOTE 6 – GROUP ENTITIES

A detailed description of the Group entities appears in Note 33 to the annual financial statements of the Group at December 31, 2007. Below are details of the material changes that occurred in connection with the Group entities since publication of the last annual report.

A. D.B.S. Satellite Services (1998) Ltd. ("DBS")

(1) Since commencing its operations, DBS has accumulated considerable losses. Its losses in 2007 amounted to approximately NIS 118 million and the loss during the six-month period ended June 30, 2008, amounted to approximately NIS 165 million. As a result of these losses, its capital deficit and its working capital deficit at June 30, 2008, amounted to approximately NIS 2,794 million and approximately NIS 543 million, respectively.

(2) The Company's investment in DBS (primarily through shareholders' loans) at the balance sheet date amounts to approximately NIS 1,562 million (without interest and linkage). The balance of DBS's current debt to the Company and its subsidiaries amounts to approximately NIS 133 million, of which approximately NIS 100 million is owed to the Company. The Company has come to an arrangement with DBS for the collection of a debt balance of approximately NIS 55.6 million in arrears. Under the arrangement, the debt will be paid in 60 equal monthly instalments plus interest at prime + 1.5%. At the balance sheet date, the debt balance in the arrangement is approximately NIS 36 million. The remainder of the debt to the Company, beyond the arrangement, is a current debt for which the agreed terms of payment are the regular credit terms in effect between the Company and its customers. At the date of approval of the financial statements, DBS is not in compliance with the arrangement and credit terms noted above. The Company and its subsidiaries are working to collect DBS's debts in arrears.

(3) During 2005, the banks completed the provision of the entire credit facility to which DBS was entitled under the financing agreements.

The terms of the loans and the credit facility that DBS received from the banks, the balance of which at June 30, 2008, is NIS 974 million, impose various restrictions on DBS that include, *inter alia*, restrictions on providing a lien on or sale of certain assets, a restriction on receipt of credit from other banks without prior approval, a restriction concerning repayment of shareholders' loans, and a requirement for compliance with financial criteria ("the Conditions").

NOTE 6 – GROUP ENTITIES (CONTD.)

A. D.B.S. Satellite Services (1998) Ltd. ("DBS") (contd.)

(3) (contd.)

a. DBS applied to the banks requesting revision of the stipulations for 2008 so as to adapt them to its budget, and on March 5, 2008 the banks consented to amend the stipulations. DBS also requested a further revision of a particular operational stipulation, and on June 25, 2008, the banks consented to amend that stipulation.

b. At June 30, 2008, DBS is in compliance with the financial criteria set for it.

c. The management of DBS believes that the sources of financing available to it will be sufficient for the needs of its operations in the coming year, based on the projected cash flow approved by the board of directors of DBS. If additional resources are required to meet operational needs during the year, DBS will adapt its operations to preclude the need for additional resources beyond those available to it.

B. Pelephone Communications Ltd. ("Pelephone")

Further to Pelephone's right to purchase frequencies from the Ministry of Communications as described in Note 18G to the financial statements at December 31, 2007, Pelephone has applied to the Ministry of Communications requesting exercise of its right to allocation of the frequencies. In exercising its right, Pelephone will pay an additional sum of approximately NIS 178 million in frequency fees and license fees.

NOTE 7 – CONTINGENT LIABILITIES

A. Claims

During the normal course of business, legal claims are filed against the companies in the Group, including applications for certification as class action lawsuits.

In the opinion of the managements of the Group companies, based, *inter alia*, on legal opinions regarding the probability of success of the claims, including the applications for certification of the class action lawsuits, appropriate provisions in the amount of approximately NIS 330 million were included in the financial statements where such provisions were required to cover the exposure resulting from such claims.

In the opinion of the managements of the Group's companies, the additional exposure (in addition to the above provisions) at June 30, 2008, due to claims filed against the companies in the Group on various matters and the probability of realisation of which is likely, amounts to approximately NIS 12.9 billion, of which approximately NIS 3.4 billion relates to claims filed by groups of employees or by individual employees which could have far-reaching implications. The above amounts are stated before the addition of interest.

Concerning applications for certification as class actions of lawsuits in respect to which the Group has exposure beyond the aforesaid (since the claims do not state a specific amount), see claims in Note 17A(4), (5), (7) and (20) to the financial statements at December 31, 2007, and significant changes as described below.

For a detailed description of these claims, see Note 17A to the Group's annual financial statements at December 31, 2007. Details of the significant changes in the status of the material contingent liabilities of the Group since December 31, 2007 are provided below:

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

A. Claims (contd.)

(1) Further to Note 17A(1) to the financial statements at December 31, 2007, concerning a claim and application for its certification as a class action, which alleges a cartel in public switching, a proceeding for certification the claim, the amount of which is estimated by the plaintiff at approximately NIS 1,750 million, is still in its preliminary stages. In April 2008 the plaintiff filed another application, for discovery of documents, as well as a motion to call witnesses. The plaintiffs' motions were dismissed.

(2) Further to Note 17A(2)(a) to the financial statements at December 31, 2007, concerning a claim filed by 2,343 retired employees who were transferred from the Ministry of Communications to the Company upon its establishment – on February 12, 2008 the plaintiffs filed a written summation of their allegations. The plaintiffs narrowed their claim to an incentive pay salary component and withdrew their claims relating to grossing up of tax and to clothing.

The claim from January 2007, which was filed by another 85 retired employees, was consolidated with the above claim.

(3) Further to Note 17A(3) to the financial statements at December 31, 2007, concerning a class action alleging unlawful collection of collection expenses – on July 20, 2008, in a court hearing , the parties were requested to respond to a proposal of the court whereby the decision on certification of the claim as a class action would be reversed and the group of plaintiffs would be widened as requested by the plaintiff. The parties were unable to agree on the proposal. In the matter of another class action mentioned in the same Note, in the amount of NIS 21 million in respect of unlawful debiting of collection fees – on July 2, 2008, the court ruled, following the request of the plaintiff's lawyer (after the death of the plaintiff) and the Company's consent, to strike out the claim and the application for its certification as a class action. It is noted that the causes of the two above claims are similar, and the first class action is still pending.

(4) Further to Note 17A(8) to the financial statements at December 31, 2007, concerning a claim and application for its certification as a class action, which alleges unlawful collection by the Company for surfing the internet at the promised speed – on April 7, 2008, the Company filed a motion for leave to appeal the decision of the District Court. The Supreme Court ruled that the motion for leave to appeal warrants a reply, and instructed the respondents to reply to it. The reply was filed on May 19, 2008.

(5) Further to Note 17A(17) to the financial statements at December 31, 2007, concerning a claim and application for its certification as a class action against the Company in the matter of collection of a regular monthly payment for a fixed telephone line through which high-speed internet infrastructure services are also provided – on June 27, 2008, a decision was given in which the application for certification of the class action and the action itself were struck out without an order to pay costs, with the consent of the parties.

(6) Further to Note 17A(19) to the financial statements at December 31, 2007, concerning a claim and application for its certification as a class action against the Company (the Company was later deleted from the statement of claim), Bezeq International, the Chairman of the Board of Bezeq International and the then CEO of Bezeq International – a hearing was held on April 14, 2008, in which the Court proposed the settlement described in the aforementioned Note 19A(17). Bezeq International rejected the settlement proposal and is awaiting the ruling of the Supreme Court on the merits of the appeal, i.e. whether the decision of the District Court to dismiss the application for certification as a class action should be reversed or not.

(7) Further to Note 17A(30) to the financial statements at December 31, 2007, concerning the class action filed against DBS and against the cable companies in connection with the broadcasting of commercials during the World Cup telecasts – on March 17, 2008, the applicants filed an agreed abandonment motion in the court, without an order to pay costs. On March 18, 2008, the court decided to allow the motion to abandon the claim.

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

A. Claims (contd.)

(8) Further to Note 17A(31) to the financial statements at December 31, 2007, concerning class actions against DBS and against the Sports channel relating to the broadcasts of Channel 5+ - on July 9, 2008, the Cable and Satellite Broadcasting Council announced that it will not appear at the proceeding, while reserving the right to review its position should the need arise later in the proceedings.

(9) Further to Note 17A(32) to the financial statements at December 31, 2007, concerning claims filed against DBS in the matter of interrupted broadcasts – on April 13, 2008, DBS filed its response to the application for certification, in which it denied the plaintiffs' allegations outright.

B. Claims which cannot yet be assessed or for which the exposure cannot be calculated

For a detailed description of the claims which cannot yet be assessed or for which the exposure cannot be calculated, see Note 17B to the Group's annual financial statements at December 31, 2007. Details of significant changes since December 31, 2007, are provided below:

Claims for which the exposure cannot be calculated

(1) Further to Note 17B(1) to the financial statements at December 31, 2007, concerning a claim against the Company and against Makefet Fund which was filed by Company employees who retired under a retirement agreement from November 2007 – in March 2008 an identical claim was filed in the Tel Aviv District Labour Court by another 17 retired Company employees.

Claims which cannot yet be assessed

(2) Further to Note 17B(2) to the financial statements at December 31, 2007, concerning a claim against the Company, Makefet Fund and the State of Israel, which was filed by the Organization of Bezeq Retirees and six of its retirees, alleging violation of arrangements which were agreed when the employees transferred from the civil service to the Company – on June 5, 2008 the court decided to strike out the claim.

(3) During the second quarter of 2008, four claims were filed in the Tel Aviv District Court against Bezeq International, concerning Bezeq International's conduct relating to the use of international phone cards for calling destinations in the Philippines, Thailand and Nepal. The claims were filed together with application for their recognition as class actions. The plaintiffs estimate the loss incurred by all the members of the group at approximately NIS 200 million in the Philippine citizens' claim, approximately NIS 150 million in the Thai citizens' claim, approximately NIS 58 million in the Nepal citizens' claim, and approximately NIS 332 million in the additional group of Thai citizens.

(4) In April 2008, a claim was filed in the Tel Aviv District Court against Pelephone, together with an application for its certification as a class action, in a total amount of approximately NIS 60 million. The claim is for restitution of amounts allegedly over-collected from Pelephone's subscribers in respect of "Call Continue" service from a voice-mail box and debiting for 1-800 destinations.

(5) In May 2008, a financial claim was filed in the Tel Aviv District Court against Pelephone and another defendant. The total amount of the claim is not defined in the claim. The claim is for restitution of amounts by the other defendant, which the plaintiff alleges it collected, through Pelephone, from the members of its "customer club" for services provided to those customers.

(6) In May 2008, a claim was filed in the Tel Aviv District Court against Pelephone, Cellcom and Partner, together with an application for certification as a class action in a total amount of NIS 50 million. The claim is for the restitution of amounts which the plaintiffs allege were over-collected from the subscribers of the defendants for "Callback" service (calls made from abroad to Israel by means of a service which Pelephone calls "Saver Service").

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

B. Claims which cannot yet be assessed or for which the exposure cannot be calculated (contd.)

Claims which cannot yet be assessed (contd.)

(7) In June 2008, a claim was filed in the Tel Aviv District Court against Pelephone., together with an application for its certification as a class action in the amount of NIS 64 million. The claim is for restitution of amounts which the plaintiff alleges were collected by Pelephone unlawfully, in contravention of its license, as a commission for payment made by means of a voucher (a commission collected from a customer who does not pay the monthly charge by direct debit, but by individual payment each month).

(8) In July 2008, a claim was filed in the Tel Aviv District Court against Pelephone., together with an application for its certification as a class action, in the amount of approximately NIS 240 million. The claim is for restitution of amounts which the plaintiff alleges were over-collected from the defendant's subscribers in respect of "Continue Call" from the 144 information service, for the collection of arrearage interest from a subscriber who is late in making payment, and for direct debits and payments in respect of voucher payment at a service center.

(9) In July 2008, Bezeq International received a claim that was filed in the Tel Aviv District Court together with an application for its certification as a class action, concerning charging customers at a dollar exchange rate higher than the representative rate. The amount of the claim is not stated, but is estimated by the plaintiff in the tens of millions of shekels.
Bezeq International has filed a motion to order the plaintiff to deposit a guarantee to secure its expenses if the claim is dismissed. The plaintiff has not yet filed its response to the motion.

On July 13, 2008, Bezeq International received another claim in the same matter, together with an application for its certification as a class action, filed in the Tel Aviv District Court by another of its business customers. The application for certification is for the business customers of Bezeq International from whom payment was collected for Bezeq International's services at a dollar exchange rate higher than the representative rate, from September 2007 to the date of filing the claim. The plaintiff estimates the amount of the claim at approximately NIS 93 million. Bezeq International intends to file a motion to order the plaintiff to deposit a guarantee to secure Bezeq International's expenses if the claim is dismissed.

C. Other contingencies

For a detailed description of other contingencies, see Note 17C to the Group's annual financial statements at December 31, 2007. Details of material changes since December 31, 2007 are provided below:

(1) Further to Note 17C(1) to the financial statements at December 31, 2007, in the matter of the Antitrust Commissioner's determination that the Company abused its status in the market when it disconnected its network from the HOT network – on March 16, 2008, the Company filed an appeal against the Commissioner's determination.

(2) Further to Note 17C(2)(b) to the financial statements at December 31, 2007, in the matter of a shareholder's letter pursuant to Section 194 of the Companies Law, on the matter of approval of transfer of funds from the Company to DBS despite the decisions of the Ministers of Communications – on April 6, 2008, the shareholder filed an application for leave to file a derivative action against the Company and a statement of claim against directors who were party to the decision, which led to the Company incurring losses of NIS 10 million (the amount called in by the Ministry of Communications from the Company's guarantee after the Minister of Communications denied the Company's appeal on March 25, 2008). The Company's response was filed on August 7, 2008.

NOTE 7 – CONTINGENT LIABILITIES (CONTD.)

C. Other contingencies

(3) Further to Note 17C(6) to the financial statements at December 31, 2007, in connection with a claim filed by the cable companies ("HOT") against DBS – on July 9, 2008, the parties filed an application for approval of a settlement agreement, part of which is a request to strike out the claim without an order to pay costs. On the same date, the court validated the settlement decision between the parties.

In addition and further to the same Note, in the matter of a claim filed against Pelephone concerning the solicitation of information about the plaintiff's business – in May 2008, the claim was dismissed due to the plaintiff's failure to appear before the court.

(4) Further to Note 17C(7) to the financial statements at December 31, 2007, concerning the operation of facilities that emit electromagnetic radiation – after termination of the strike at the Ministry for Protection of the Environment, the proceedings for issue of operating permits for communications and broadcasting installations by the Supervisor of Radiation were completed. In addition, on April 17, 2008, the Company submitted its reservations concerning the proposed draft of National Outline Plan for Communications – NOP/36A Small Broadcasting Installations, and NOP/36B Large Broadcasting Installations. In brief, the reservations are that the plans as proposed, and in particular as they relate to changing the definitions of large and small broadcasting installations, create practical difficulties which could prevent the Company from granting the public some of the varied services it provides and is obligated by law to provide.

On July 29, 2008, the Company received notice that in June 2008, National Outline Plan 56 came into force, which regulates the manner of erection and registration of communications installations in the Administrated Territories. The plan includes transition directives for installations erected before 1984 and for existing installations. The Company is studying the subject, and at the date of publication of this report is unable to assess its expected implications.

(5) Further to Note 17C(9) to the financial statements at December 31, 2007, concerning an application for certification of a class action against Pelephone in the amount of NIS 12 billion – the action was struck out without an order to pay costs.

(6) Further to Note 17C(10) to the financial statements at December 31, 2007 – on February 28, 2008 the DBS shareholder, holding an insignificant number of shares, applied to the Tel Aviv District Court for the appointment of an arbitrator. The Companies filed a response to the application in which it explained that there is no cause for the appointment of an arbitrator. On May 4, 2008, the Court ruled that in view of the difficulty in understanding the essence of the claim that the shareholder wishes to put to the arbitrator, she must file such a draft claim, which she did and in which the claimed amount is NIS 160 million. On July 13, 2008, the Court ruled to allow the application for appointment of an arbitrator. An introductory meeting with the arbitrator is scheduled for September 9, 2008.

(7) In February 2008, the Ministry of Industry, Trade and Employment (in this sub-section – "the Ministry"), instituted an investigation of DBS relating to the terms of employment of a certain group of DBS employees, and DBS was required to submit various documents to the Ministry, which it did. The investigation is still in its initial stages, and its full extent is not yet known.
Furthermore, in December 2007, DBS received a letter from 19 of its employees (18 of whom are no longer employed by DBS), regarding various periods between 2001 and 2007 in which they allege that during the period of their employment at DBS they were not paid all the monies due to them. On April 21, 2008, DBS sent its reply to those employees, rejecting all their allegations. At this stage, the extent of the Ministry's investigation is unknown, and no action has been filed by the employees.

NOTE 8 – TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES

A. On June 1, 2008, the general meeting of the shareholders of the Company approved the terms of employment of the Chairman of the Board of the Company. Below are the main points of the engagement of the Chairman of the Board:

(1) The Chairman is employed under a personal employment agreement as acting Chairman of the Board of Directors of the Company, in a full-time position, effective from September 4, 2007, the date on which the Chairman actually started working in the Company.

(2) The salary of the Chairman is NIS 175,000 per month, linked to the CPI. In addition, Chairman in entitled to contributions to senior employees insurance, study fund and loss of earning capacity insurance. The Company will provide the Chairman with a company car, and will bear all the car maintenance expenses.

(3) The Chairman will be granted 9,000,000 options, as described in Section 9B below.

(4) A decision on the award of an annual bonus will be made at the discretion of the Board of Directors and subject to the approval of the Audit Committee and the general meeting. The amount of the annual bonus, if awarded, will be between six and eighteen monthly salaries.

(5) Immediately after approval of the agreement by the general meeting, the Company will pay the Chairman a special "signature bonus" of NIS 1.2 million.

(6) The Company will insure the Chairman with directors and officers insurance, and will indemnify him from time to time as is customary with regard to other directors in the Company.

(7) The engagement between the Company and the Chairman is for an unlimited period, where each party is entitled to bring it to an end at any time and for any reason by giving 12 months' notice (the Company) or 6 months' notice (the Chairman).

B. On July 31, 2008, the Board of Directors of the Company resolved to approve extension of the Company's engagement in the management agreement with a corporation related to Ap.Sb.Ar Holdings Ltd., the controlling shareholder in the Company, for a period of three years subsequent to the end of the term of the current agreement, on the same terms as the original agreement. Extension of the engagement is subject to the approval of the general meeting.

C. For the matter of stock options for senior officers who are key personnel in the Group, see Note 9 below.

NOTE 9 – SHARE-BASED PAYMENTS

A. On November 20, 2007, the Board of Directors of the Company resolved to adopt a new stock options plan for managers and senior employees in the Company and/or in associates, which would allocate up to 65,000,000 non-negotiable options exercisable for up to 65,000,000 shares of the Company and representing approximately 2.5% of the issued capital of the Company, and at full dilution – 2.37% of the share capital.

On December 25, 2007, the Company published an outline for the allocation of up to 65,000,000 options in accordance with the Securities (Details of an outline offer of securities to employees) regulations, 5760-2000, which described, *inter alia*, the terms of the plan, as well as a private placement report in accordance with the Securities (Private placement of securities in a listed company) Regulations 5760-2000.

The options plan and the allocation of all the options in accordance with it, were approved by the general meeting of the Company on January 31, 2008, in accordance with the Company's Articles of Association (since in certain cases, there is also a requirement in law for the further approval of the general meeting).

NOTE 9 – SHARE-BASED PAYMENTS (CONTD.)

A. (contd.)

Exercise of the options under the plan is contingent upon receipt of the appropriate approvals in accordance with the provisions of the Communications (Telecommunications and Broadcasts) (Determination of an essential service provided by Bezeq, The Israel Telecommunications Corp. Ltd.) Order, 5757-1997 ("the Telecommunications Order"), and it is possible that such exercise will necessitate amendment of the Telecommunications Order or a different solution. It is noted that on March 30, 2008, a letter was received from the Ministry of Communications, dismissing the possibility of amendment of the Telecommunications Order. Nevertheless, the Company believes a solution will be found that enables allocation of the Company's shares while complying with the Telecommunications Order.

The options will vest in three equal annual portions. The vesting dates of each portion will fall at the end of each of the first, second and third years from the grant date, respectively, and the expense for each portion will be spread according to its vesting period. In addition, the plan sets terms which, if met, bring forward the vesting dates.

Exercise of the options for shares will be by using a cashless exercise mechanism, unless the Board of Directors decides otherwise.

The exercise price set for the grant of up to 41,350,000 options is NIS 5.50 (adjusted for distribution of a dividend in cash or in kind). On June 26, 2008, the Board of Directors of the Company resolved that the exercise price for future grants of options, as will be approved by the Board of Directors from time to time, will be the same as the average closing price of the Company's share on the stock exchange in the 30 days' trading prior to the date of the Board's decision to grant options to those offerees.

B. Of the options, 54,700,000 were actually allocated at the date of the financial statements, as follows:

(1) 45,700,000 options whose theoretical economic value is approximately NIS 131 million (of which 13,500,000 were allocated to the CEO of the Company and to senior officers who are key persons in the Group, the theoretical economic value of which is approximately NIS 35 million), based, *inter alia*, on the share price on the grant date, a risk-free annual interest rate between 5.09% and 5.68%, a weighted average of expected life of between 4.5 and 5.5 years, the exercise price noted above, an annual standard deviation between 22.7% and 24.3%. The limitation described above by virtue of the Telecommunications Order was taken into account in calculating the theoretical economic value of the options, on the assumption that the limitation is resolvable. The grant date was set as the later of the date of the general meeting and the date of the notice to the employees.

(2) On April 17, 2008, the Board of Directors of the Company resolved to allocate 9,000,000 options to the Chairman of the Board in accordance with the plan described in Section A above, subject to a number of changes relating to the terms of his options. The allocation to the Chairman was approved by the general meeting of the shareholders of the Company on June 1, 2008.

The options will vest in 12 equal quarterly portions. The vesting dates of each portion will fall at the end of each quarter from the grant date, and the expense will be spread for each portion in accordance with its vesting period. In addition, the plan sets terms which, if met, will bring the vesting date forward.

The exercise price of the each option is NIS 6.4405 per share. The price was set according to the share price on the date on which the Chairman took up his post – September 4, 2007 (which was NIS 6.649 per share) and after adjustment for distribution of a net dividend in the amount of NIS 0.26 per share, for which the X-day was April 14, 2008. The closing price of the Company's share on June 1, 2008, the date of approval by the Audit Committee, was NIS 6.494 per share.

The theoretical economic value of the options granted to the Chairman as described above, according to a weighted Black and Scholes model, is approximately NIS 16 million, based, *inter alia,* on the share price on the grant date, a risk-free annual interest rate of 5.1%, a weighted average expected life of 4 years, the exercise price noted above, and an annual standard deviation of 23.11%, as well as resolution of the limitation described in Section A above pursuant to the Telecommunications Order.

NOTE 9 – SHARE-BASED PAYMENTS (CONTD.)

C. On June 26, 2008, the Board of Directors of the Company resolved to grant an additional 2,600,000 options to senior employees of the Group, in accordance with the outline dated December 25, 2007, and mentioned in Section A above. The grant date was set for July 17, 2008, as the later of the date of the general meeting and the date of the notice to the employees.

The theoretical economic value of the options granted, according to a weighted Black and Scholes model, is approximately NIS 5 million, based, *inter alia,* on the share price on the grant date, which was NIS 6.55, a risk-free annual interest rate of 5.3%– 5.5%, a weighted average expected life of 4.5 – 5.5 years, an exercise price of NIS 6.35 determine as aforesaid, an annual standard deviation of between 23.07% and 24.07%. The limitation described in Section A above pursuant to the Telecommunications Order was taken into account in calculating the theoretical economic value of the options, assuming that the limitation is resolvable.

D. On July 3, 2008, the board of directors of DBS resolved to approve in principle an allocation of 4,250,000 options of the Company to the CEO of DBS, exercisable for Company shares at an exercise price of NIS 5.5 per option (as will be adjusted according to dividend distributions starting from October 25, 2007). This was after approval of the grant by the Board of Directors of the Company. The options will vest in three equal annual portions, and those that vest will be exercisable through the end of five years from the vesting date of the third portion. The board of directors of DBS also resolved that after the allocation is approved by the Antitrust Commissioner, it will be brought to the organs of DBS for approval. The theoretical economic value of these options, which was calculated shortly before the date of approval by DBS's board of directors, is approximately NIS 11.4 million.
On the same date, the board of directors of DBS approved an annual bonus plan for the CEO of DBS for the years 2009-2010, which is contingent upon the approval of the Antitrust Commissioner and approval of the allocation by DBS's organs as aforesaid. The plan is based on attaining an aggregate percentage of certain goals as defined in the plan. On July 29, 2008, the Antitrust Commissioner notified DBS that it has no objection to the allocation, and the board of directors of DBS approved the allocation on August 11, 2008.

E. The terms of the options are as shown below:

Grant date / eligible employees	No. of instruments in thousands	Vesting terms	Contractual life of options
A. Grant of options from the State to employees on October 11, 2005	122,698	Immediate (subject to lock-up, commencing at the end of 2 years, to 3 years – one third each year)	4 years
B. Grant of options to employees on February 22, 2007 (1)	78,151	Immediate (subject to lock-up for two years)	5 years
C. Grant to the Chairman of the Board	9,000	12 quarterly portions	4 years
D. Approval and/or grant of options to managers, senior employees and officers up to the date of approval of the financial statements	48,300	Three equal annual portions	8 years
Total stock options granted	258,149		

(1) The expenses in respect of this grant were recorded in 2006 as a promise was made to the employees in 2006, along with the conditions of the grant.
Remark: The options referred to in A and B are settled by way of physical delivery of shares. The options referred to in C and D are settled in a cashless exercise mechanism.

NOTE 9 – SHARE-BASED PAYMENTS (CONTD.)

E. (contd.)

Changes in the number of options:

	Number of options For the six-month period ended June 30 2008 (in thousands)	For the six-month period ended June 30 2007 (in thousands)	For the year ended December 31 2007 (in thousands)
Balance in circulation at January 1	**200,849**	200,849	200,849
Options granted during the period	**54,700**	-	-
Options forfeited during the period	**(1,100)**	-	-
Options exercised during the period	**(18,830)**	-	-
Balance in circulation at the end of the period	**235,619**	200,849	200,849
Exercisable at the end of the period, subject to lock-up terms	**159,950**	200,849	200,849
Exercisable at the end of the period not subject to lock-up	**22,069**	--	--

Subsequent to the balance sheet date, approximately 736,000 options granted by the State to employees on October 11, 2005, were exercised.

The weighted average exercise price in the six-month period ended June 30, 2008 and in 2007, was NIS 3.09 per share and NIS 2.852 per share, respectively.

The average share price in the six-month period ended June 30, 2008 and in 2007, is NIS 6.66 per share and NIS 6.82 per share, respectively.

The range of the exercise price of the balance of the issued options at June 30, 2008, is between NIS 2.22 and NIS 6.44, and the weighted average of the remaining contractual life is 3.309 years.

The fair value of the services received in consideration of the options for shares granted, is based on the fair value of the options granted, which was measured according to the Black and Scholes model on the basis of the following parameters:

	For the six-month period ended June 30 2008	For the six-month period ended June 30 2007	For the year ended December 31 2007
Weighted average of the fair value on the grant date	**NIS 2.69**	-	-
Share price	**NIS 6.49 - 7.049**	-	-
Exercise price	**NIS 5.5 - 6.44**	-	-
Expected volatility (weighted average)	**22.7% - 24.3%**	-	-
Life of the option (expected weighted average)	**4 - 5.5 years**	-	-
Risk-free interest rate (based on government bonds)	**5.09% - 5.68%**	-	-

Salary expense

	For the six-month period ended June 30, 2008 NIS millions	For the six-month period ended June 30, 2007 NIS millions	For the year ended December 31, 2007 NIS millions
Stock options granted in the reporting period (1)	**35**	-	-

(1) In calculating the salary expense, a discount of 5% was taken into account in respect of forfeiture, for each year.

NOTE 10 – REVENUES

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Fixed-line domestic communications					
Landline telephony	**1,772**	1,921	**857**	936	3,798
Internet – infrastructure	**391**	336	**193**	172	711
Transmission, data communication and others	**470**	447	**241**	217	935
	2,633	2,704	**1,291**	1,325	5,444
Cellular telephones					
Cellular services and terminal equipment	**1,702**	1,630	**860**	817	3,669
Sale of terminal equipment	**522**	514	**264**	260	711
	2,224	2,144	**1,124**	1,077	4,380
International communications, internet services and network end point	**606**	625	**312**	319	1,226
Multi-channel television	**710**	659	**352**	327	1,331
Others	**13**	9	**7**	5	19
	6,186	6,141	**3,086**	3,053	12,400

NOTE 11 – OPERATING AND GENERAL EXPENSES

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cellular telephone expenses	**865**	891	**423**	439	1,828
General expenses	**524**	565*	**248**	308*	1,187
Materials and spare parts	**427**	430	**210**	210	924
Consumption of satellite services content	**232**	202	**117**	98	426
Services and maintenance by sub-contractors	**170**	192	**86**	90	381
Building maintenance	**156**	166	**78**	84	332
International communication expenses	**133**	172*	**65**	73*	338
Motor vehicle maintenance expenses	**94**	93	**48**	47	183
Royalties to the Government of Israel	**58**	96	**26**	48	194
Collection fees	**24**	26	**12**	13	48
	2,683	2,833	**1,313**	1,410	5,841

* See Note 3C.

NOTE 12 – CONDENSED DATA FROM THE INTERIM SEPARATE FINANCIAL STATEMENTS OF THE COMPANY

A. Income statement

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues (see B below)	**2,762**	2,835	**1,354**	1,393	5,713
Costs and expenses					
Depreciation and amortisation	**429**	473	**211**	236	941
Salary	**616**	636	**300**	326	1,293
General and operating expenses	**934**	1,067	**449**	534	2,121
Other operating expenses (income), net	**(13)**	47	**(34)**	54	79
	1,966	2,223	**926**	1,150	4,434
Operating income for the period	**796**	612	**428**	243	1,279

B. Revenue segmentation

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007*	2008	2007*	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Telephony	**1,809**	1,967	**876**	959	3,905
Internet	**391**	338	**193**	174	712
Transmission and data communication	**396**	367	**204**	184	754
Other services	**166**	163	**81**	76	342
	2,762	2,835	**1,354**	1,393	5,713

* See Note 3C.

NOTE 13 –SEGMENT REPORTING

The Company and the investee companies operate in various segments of the communications sector. Data on activities by segment are stated by the segments of operation of these companies.

	For the six-month period ended June 30, 2008 (unaudited)						
	Domestic fixed–line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues							
Revenues from external sources	**2,587**	**2,224**	**606**	**756**	**13**	**-**	**6,186**
Inter-segment revenues	**175**	**137**	**34**	**5**	**24**	**(375)**	**-**
Total revenues	**2,762**	**2,361**	**640**	**761**	**37**	**(375)**	**6,186**
Segment results	**796**	**481**	**117**	**69**	**1**	**-**	**1,464**

	For the six-month period ended June 30, 2007 (unaudited)						
	Domestic fixed–line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues							
Revenues from external sources	2,674	2,144	625	689	9	-	6,141
Inter-segment revenues	161	155	19	19	21	(375)	-
Total revenues	2,835	2,299	644	708	30	(375)	6,141
Segment results	612	453	104	56	2	-	1,227

NOTE 13 –SEGMENT REPORTING (CONTD.)

	For the three-month period ended June 30, 2008 (unaudited)						
	Domestic fixed–line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues							
Revenues from external sources	**1,264**	**1,124**	**312**	**379**	**7**	**-**	**3,086**
Inter-segment revenues	**90**	**64**	**14**	**1**	**11**	**(180)**	**-**
Total revenues	**1,354**	**1,188**	**326**	**380**	**18**	**(180)**	**3,086**
Segment results	**428**	**266**	**63**	**43**	**-***	**-**	**800**

	For the three-month period ended June 30, 2007 (unaudited)						
	Domestic fixed–line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues							
Revenue from external sources	1,312	1,077	319	340	5	-	3,053
Inter-segment revenue	81	75	2	14	10	(182)	-
Total revenues	1,393	1,152	321	354	15	(182)	3,053
Segment results	243	240	53	31	4	-	571

* Less than NIS 500,000.

Notes to the Financial Statements as at June 30, 2008

NOTE 13 –SEGMENT REPORTING (Contd.)

	For the year ended December 31, 2007 (audited)						
	Domestic fixed–line communications	Cellular telephone	International communications, internet and NEP services	Multi-channel television	Others	Adjustments	Consolidated
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues							
Revenues from external sources	5,373	4,380	1,226	1,402	19	-	12,400
Inter-segment revenues	340	304	78	12	46	(780)	-
Total revenues	5,713	4,684	1,304	1,414	65	(780)	12,400
Segment results	1,279	805	204	48	-*	-	2,336

* Less than NIS 500,000.

NOTE 14 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD. D.B.S. SATELLITE SERVICES (1998) LTD., AND BEZEQ INTERNATIONAL LTD.

1. Pelephone Communications Ltd.

A. Balance sheet

	June 30, 2008	June 30, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**1,983**	1,681*	1,976
Non-current assets	**2,585**	2,447*	2,363
	4,568	4,128	4,339
Current liabilities	**1,195**	1,053	1,106
Long-term liabilities	**1,140**	1,251	1,154
Total liabilities	**2,335**	2,304	2,260
Shareholders' equity	**2,233**	1,824	2,079
	4,568	4,128	4,339

* See Note 3C

B. Income statement

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues from services and sales	**2,361**	2,299	**1,188**	1,152	4,684
Cost of services and sales	**1,626**	1,603	**796**	795	3,347
Gross profit	**735**	696	**392**	357	1,337
Sales and marketing expenses	**191**	197	**94**	94	430
General and administrative expenses	**63**	46	**32**	23	102
	254	243	**126**	117	532
Operating income	**481**	453	**266**	240	805
Financing expenses	**72**	44	**46**	24	114
Financing income	**(64)**	(44)	**(29)**	(16)	(109)
Financing expenses, net	**8**	-	**17**	8	5
Earnings before income tax	**473**	453	**249**	232	800
Income tax	**130**	126	**69**	59	215
Net earnings for the period	**343**	327	**180**	173	585

NOTE 14 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., D.B.S. SATELLITE SERVICES (1998) LTD., AND BEZEQ INTERNATIONAL LTD. (CONTD.)

2. D.B.S. Satellite Services (1998) Ltd.

A. Balance sheet

	June 30, 2008	June 30, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**172**	172*	157*
Non-current assets	**978**	867*	943*
	1,150	1,039	1,100
Current liabilities	**715**	1,973	1,483
Long-term liabilities	**3,229**	2,040	2,246
Total liabilities	**3,944**	4,013	3,729
Equity deficit	**(2,794)**	(2,974)	(2,629)
	1,150	1,039	1,100

* See Note 3C.

B. Income statement

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues	**761**	708	**380**	354	1,415
Cost of sales	**564**	535	**278**	265	1,117
Gross profit	**197**	173	**102**	89	298
Sales and marketing expenses	**71**	67	**31**	33	138
General and administrative expenses	**57**	50	**28**	25	104
	128	117	**59**	58	242
Operating income	**69**	56	**43**	31	56
Financing expenses	**264**	183	**154**	97	394
Financing income	**(30)**	(20)	**(12)**	(6)	(226)
Financing expenses, net	**234**	163	**142**	91	168
Loss before income tax	**(165)**	(107)	**(99)**	(60)	(112)
Income tax	**-**	6	**-**	5	6
Net loss for the period	**(165)**	(113)	**(99)**	(65)	(118)

NOTE 14 – CONDENSED FINANCIAL STATEMENTS OF PELEPHONE COMMUNICATIONS LTD., D.B.S. SATELLITE SERVICES (1998) LTD., AND BEZEQ INTERNATIONAL LTD. (CONTD.)

3. Bezeq International Ltd.*

A. Balance sheet

	June 30, 2008	June 30, 2007	December 31, 2007
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets	**487**	429	431
Non-current assets	**475**	427	456
	962	856	887
Current liabilities	**297**	338	312
Long-term liabilities	**22**	46	26
Total liabilities	**319**	384	338
Shareholders' equity	**643**	472	549
	962	856	887

B. Income statement

	For the six-month period ended June 30		For the three-month period ended June 30		For the year ended December 31
	2008	2007	2008	2007	2007
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Revenues	**640**	644	**326**	321	1,304
Cost of sales	**382**	427	**192**	211	859
Gross profit	**258**	217	**134**	110	445
Sales and marketing expenses	**89**	68	**45**	33	147
General and administrative expenses	**52**	46	**26**	25	94
Other income, net	**-**	(1)	**-**	(1)	-
	141	113	**71**	57	241
Operating income	**117**	104	**63**	53	204
Financing expenses	**8**	7	**4**	3	13
Financing income	**(11)**	(8)	**(5)**	(5)	(14)
Financing income	**(3)**	(1)	**(1)**	(2)	(1)
Equity in earnings of an associate accounted for by the equity method	**2**	2	**1**	1	6
Earnings before income tax	**122**	107	**65**	56	211
Income tax	**(34)**	31	**18**	17	58
Net earnings for the period	**88**	76	**47**	39	153

* The above financial statements are presented solely in accordance with International Financial Reporting Standards (IFRSs).

NOTE 15 – MATERIAL EVENTS DURING THE REPORTING PERIOD AND EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

A. On March 10, 2008, the Board of Directors of the Company resolved to recommend to the general meeting of the shareholders of the Company to distribute a cash dividend to the shareholders in the amount of NIS 679 million (approximately NIS 0.26 per share). On April 3, 2008 the general meting approved payment of the dividend and it was paid on April 28, 2008.

B. On March 26, 2008, the Company signed an agreement for the sale of its satellite communications operations (Inmarsat and Bezeq Sat) and related assets, including the satellite communications site in Emek Ha'Ela. Under the agreement, the operation will be sold in consideration of USD 15 million plus VAT, subject to price adjustments resulting from various stipulations and from changes that will apply, if they apply, in the operation during the period until the date of closing the transaction. Closing the transaction is subject to various approvals in addition to the regulatory approvals of the Ministry of Defence, the Ministry of Communications and the Antitrust Commissioner. The Antitrust Commissioner's approval was given on June 4, 2008. If the transaction is closed at the maximum price noted above, the Company expects to record a capital gain of approximately NIS 50 million (before tax).

C. In May 2008, the amendment to the new collective labour agreement was completed, concerning bringing forward completion of the implementation of the organizational structure and concerning bringing forward the retirement dates and changing the mix of those scheduled to retire under the new collective agreement by the end of 2008.

D. On July 31, 2008, the Board of Directors of the Company resolved to recommend to the general meeting of the shareholders of the Company to increase the registered capital of the Company by 251,000,000 shares of NIS 1 par value each.

E. On July 31, 2008, the Board of Directors of the Company resolved to recommend to the general meeting of the shareholders of the Company the distribution of a cash dividend to the shareholders in a total amount of NIS 835 million (which is approximately NIS 0.32 per share).

NOTE 16 – DETAILS OF ADDITIONAL MOVEMENTS IN THE SHAREHOLDERS' EQUITY

	Share capital	Premium on shares	Translation fund	Capital reserve in respect of a transaction between a corporation and a controlling shareholder	Capital reserve in respect of assets available for sale	Capital reserve in respect of options for employees	Deficit	Total	Minority rights	Total shareholders' equity
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
	Relates to holders of the Company's equity									
Six-month period ended June 30, 2008										
Balance at January 1, 2008 (audited)	**6,132**			**390**	**4**	**287**	**(2,268)**	**4,545**	**(373)**	**4,172**
Total revenues and expenses recognized in the period (unaudited)	**-**	**-**	**(11)**	**-**	**(4)**	**-**	**835**	**820**	**(37)**	**783**
Dividends to Company shareholders (unaudited)	**-**	**-**	**-**	**-**	**-**	**-**	**(679)**	**(679)**	**-**	**(679)**
Share-based payments (unaudited)	**-**	**-**	**-**	**-**	**-**	**35**	**-**	**35**	**-**	**35**
Minority injection in a subsidiary (unaudited)	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**4**	**4**
Balance at June 30, 2008 (unaudited)	**6,132**	**-**	**(11)**	**390**	**-**	**322**	**(2,112)**	**4,721**	**(406)**	**4,315**
Six-month period ended June 30, 2007										
Balance at January 1, 2007 (audited)	6,309	1,623	-	384	1	287	(2,849)	5,755	(564)	5,191
Total revenues and expenses recognized in the period (unaudited)	-	-	-	-	3	-	760	763	(35)	728
Dividends to shareholders – distribution that does not pass the earnings test (unaudited)	(177)	(1,623)	-	-	-	-	-	(1,800)	-	(1,800)
Payments to a former senior officer (unaudited)	-	-	-	6	-	-	-	6	-	6
Balance at June 30, 2007 (unaudited)	6,132	-	-	390	4	287	(2,089)	4,724	(599)	4,125

NOTE 16 – DETAILS OF ADDITIONAL MOVEMENTS IN THE SHAREHOLDERS' EQUITY (CONTD.)

	Share capital	Premium on shares	Translation fund	Capital reserve in respect of a transaction between a corporation and a controlling shareholder	Capital reserve in respect of assets available for sale	Capital reserve in respect of options for employees	Deficit	Total	Minority rights	Total shareholders' equity
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
	Relates to holders of the Company's equity									
Three-month period ended June 30, 2008										
Balance at April 1, 2008 (unaudited)	**6,132**	**-**	**-**	**390**	**-**	**300**	**(1,870)**	**4,952**	**(386)**	**4,566**
Total revenues and expenses recognized in the period (unaudited)	**-**	**-**	**(11)**	**-**	**-**	**-**	**437**	**426**	**(24)**	**402**
Dividends to company shareholders (unaudited	**-**	**-**	**-**	**-**	**-**	**-**	**(679)**	**(679)**	**-**	**(679)**
Share-based payments (unaudited)	**-**	**-**	**-**	**-**	**-**	**22**	**-**	**22**	**-**	**22**
Minority injection in a subsidiary (unaudited)	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**4**	**4**
Balance at June 30, 2008 (unaudited)	**6,132**	**-**	**(11)**	**390**	**-**	**322**	**(2,112)**	**4,721**	**(406)**	**4,315**
Three-month period ended June 30, 2007										
Balance at April 1, 2007 (audited)	6,132	-	-	384	1	287	(2,450)	4,354	(578)	3,776
Total revenues and expenses recognized in the period (unaudited)	-	-	-	-	3	-	361	364	(21)	343
Payments to a former senior officer (unaudited)	-	-	-	6	-	-	-	6	-	6
Balance at June 30 2007 (unaudited)	6,132	-	-	390	4	287	(2,089)	4,724	(599)	4,125

Notes to the Financial Statements as at June 30, 2008

NOTE 16 – DETAILS OF ADDITIONAL MOVEMENTS IN THE SHAREHOLDERS' EQUITY (CONTD.)

	Share capital	Premium on shares	Capital reserve in respect of a transaction between a corporation and a controlling shareholder	Capital reserve in respect of assets available for sale	Capital reserve in respect of options for employees	Deficit	Total	Minority rights	Total shareholders' equity
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Year ended December 31, 2007									
Balance at January 1, 2007 (audited)	6,309	1,623	384	1	287	(2,849)	5,755	(564)	5,191
Total revenues and expenses recognized (audited)	-	-	-	3	-	1,341	1,344	31	1,375
Dividends to Company shareholders (audited)	-	-	-	-	-	(760)	(760)	-	(760)
Dividend to Company shareholders – dividend that does not pass the profit test (audited)	(177)	(1,623)	-	-	-	-	(1,800)	-	(1,800)
Change in due date of a loan provided by the minority in a subsidiary (audited)	-	-	-	-	-	-	-	160	160
Payments to a former senior officer (audited)	-	-	6	-	-	-	6	-	6
Balance at December 31, 2007 (audited))	6,132	-	390	4	287	(2,268)	4,545	(373)	4,172