# "Bezeq" The Israel Telecommunication Corporation Limited

# Part C:

# Consolidated Financial Statements for the Year Ended

# December 31, 2015

bezeq

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## Auditors' Report to the Shareholders of

## "Bezeq "the Israeli Telecommunication Corporation Ltd.

We have audited the accompanying consolidated statements of financial position of "Bezeq "the Israeli Telecommunication Corporation Ltd. (hereinafter "the Company") as of December 31, 2015 and 2014 and the consolidated income statements, statements of comprehensive income, statements of changes in shareholders' equity and statements of cash flows, for each of the three years, in the period ended December 31, 2015. These financial statements are the responsibility of the Company's Board of Directors and of its Management. Our responsibility is to express an opinion on these financial statements based on our audit.

We did not audit the financial statements of certain consolidated subsidiaries whose assets constitute approximately 1.2% of the total consolidated assets as of December 31, 2015 and 2014, and whose revenues constitute approximately 1%, 1.2% and 1.6% of the total consolidated revenues for the years ended December 31, 2015, 2014 and 2013, respectively. The financial statements of those companies were audited by other auditors whose reports thereon were furnished to us, and our opinion, insofar as it relates to amounts emanating from the financial statements of such companies, is based solely on the reports of the other auditors.

We conducted our audit in accordance with generally accepted auditing standards in Israel, including standards prescribed by the Auditors Regulations (Manner of Auditor's Performance) - 1973. Such standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors and by Management of the Company, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and on the reports of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company and its consolidated subsidiaries as of December 31, 2015 and 2014 and their results of operations, changes in equity and cash flows, for each of the three years in the period ended December 31, 2015, in accordance with International Financial Reporting Standards (IFRS) and in accordance with the Securities Regulations (Annual Financial Statements) - 2010.

We have audited, in accordance with Auditing Standards of the Public Company Accounting Oversight Board (United States) the Internal Control over Financial Reporting of "Bezeq" the Israeli Telecommunication Corporation Ltd. as of December 31, 2015, and our report dated March 16, 2016 expressed an unqualified opinion on the effectiveness of internal control over financial reporting of "Bezeq" the Israeli Telecommunication Corporation Ltd.

Without qualifying our abovementioned opinion, we draw attention to lawsuits filed against the Company and its Subsidiaries which cannot yet be assessed or the exposure in respect thereof cannot yet be calculated, as set forth in Note 16.

Somekh Chaikin

Certified Public Accountants (Isr.)

March 16, 2016

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**Auditor's Attestation Report**

The Board of Directors and Stockholders
**"Bezeq"- The Israel Telecommunication Corporation Ltd.**

We have audited "Bezeq"- The Israel Telecommunication Corporation Ltd.'s (hereinafter "The Company") internal control over financial reporting as of December 31, 2015, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying "Management's Annual Report on Internal Control Over Financial Reporting". Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2015, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

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The Company Acquired DBS Satellite services (1998) Ltd. ("DBS") during 2015. The Company's management excluded from its assessment of the effectiveness of the Company's internal control over financial reporting as of December 31, 2015, DBS's internal control over financial reporting. DBS' revenues represent 13.4% of the revenues in the consolidated financial statements of 2015. Our audit of internal control over financial reporting of the company excluded an evaluation of the internal control over financial reporting of DBS.

We also have audited, in accordance with generally accepted auditing principles in Israel, the consolidated balance sheets of the Company and its subsidiaries as of December 31, 2015, and 2014, and the related consolidated statements of operations, comprehensive income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2015, and our report dated March 16, 2016 expressed an unqualified opinion on those consolidated financial statements with an explanatory paragraph referring to Note 15 regarding the claims made against the Company and its subsidiaries for which at this point the exposure cannot be assessed or calculated.

Somekh Chaikin

Certified Public Accountants

Jerusalem, Israel
March 16, 2016

## Consolidated Statements of Financial Position as at December 31

| | | 2015 | 2014 |
|---|---|---|---|
| **Assets** | **Note** | **NIS million** | **NIS million** |
| | | | |
| Cash and cash equivalents | 2.3, 3 | **555** | 660 |
| Investments, including derivatives | 2.3, 4 | **762** | 2,223 |
| Trade receivables | 2.3, 5 | **2,058** | 2,227 |
| Other receivables | 2.3, 5 | **269** | 260 |
| Inventory | 2.10 | **115** | 96 |
| **Total current assets** | | **3,759** | 5,466 |
| | | | |
| Trade and other receivables | 2.3, 5 | **674** | 566 |
| Broadcasting rights, net of rights exercised | 2.4, 7 | **456** | - |
| Property, plant and equipment | 2.5, 8 | **6,894** | 6,079 |
| Intangible assets | 2.7, 9 | **3,332** | 1,793 |
| Deferred tax assets | 2.16, 6 | **1,178** | - |
| Deferred expenses and non-current investments | 2.9, 10 | **361** | 352 |
| Investments in equity-accounted investees | 11.3 | **25** | 1,057 |
| **Total non-current assets** | | **12,920** | 9,847 |
| | | | |
| **Total assets** | | **16,679** | 15,313 |

## Consolidated Statements of Financial Position as at December 31 (Contd.)

| | Note | 2015<br>NIS million | 2014<br>NIS million |
|---|---|---|---|
| Debentures, loans and borrowings | 2.3, 12 | **1,913** | 1,481 |
| Trade and other payables | 13 | **1,657** | 1,374 |
| Current tax liabilities | | **624** | 600 |
| Employee benefits | 2.12, 15 | **378** | 259 |
| Liability to Eurocom DBS Ltd, related party | 11.2 | **233** | - |
| Provisions | 2.13, 14 | **100** | 62 |
| **Total current liabilities** | | **4,905** | 3,776 |
| | | | |
| Loans and debentures | 2.3, 12 | **8,800** | 8,606 |
| Employee benefits | 2.12, 15 | **240** | 233 |
| Derivatives and other liabilities | | **226** | 171 |
| Deferred tax liabilities | 2.16, 6 | **51** | 17 |
| Provisions | 2.13, 14 | **46** | 69 |
| **Total non-current liabilities** | | **9,363** | 9,096 |
| | | | |
| **Total liabilities** | | **14,268** | 12,872 |
| | | | |
| **Total equity** | 19 | **2,411** | 2,441 |
| | | | |
| **Total liabilities and equity** | | **16,679** | 15,313 |

| Shaul Elovitch<br>Chairman of the Board of | Stella Handler<br>CEO | David (Dudu) Mizrahi<br>Deputy CEO and CFO |
|---|---|---|

Date of approval of the financial statements: March 16, 2016

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

## Consolidated Statements of Income for the Year Ended December 31

| | Note | 2015 | 2014 | 2013 |
|---|---|---|---|---|
| | | NIS million | NIS million | NIS million |
| **Revenues** | 2.14, 20 | **9,985** | 9,055 | 9,563 |
| **Costs of activity** | | | | |
| General and operating expenses | 21 | **3,869** | 3,366 | 3,576 |
| Salaries | 22 | **1,957** | 1,768 | 1,872 |
| Depreciation and amortization | 2.5, 2.7, 8, 9, 10 | **1,684** | 1,281 | 1,311 |
| Other operating income, net | 23 | **(95)** | (586) | (15) |
| | | **7,415** | 5,829 | 6,744 |
| Operating profit | | **2,570** | 3,226 | 2,819 |
| **Finance expenses** | 2.15, 24 | | | |
| Financing expenses | | **376** | 486 | 573 |
| Financing income | | **(113)** | (356) | (428) |
| Financing expenses, net | | **263** | 130 | 145 |
| Profit after financing expenses, net | | **2,307** | 3,096 | 2,674 |
| **Share in earnings (losses) of equity accounted investees** | 11.2 | **12** | (170) | (252) |
| Profit before income tax | | **2,319** | 2,926 | 2,422 |
| **Income tax** | 2.16, 6 | **598** | 815 | 651 |
| Equity for the year attributable to shareholders of the Company | | **1,721** | 2,111 | 1,771 |
| Earnings per share (NIS) | 26 | | | |
| **Basic earnings per share** | | **0.63** | 0.77 | 0.65 |
| Diluted earnings per share | | **0.62** | 0.77 | 0.65 |

## Consolidated Statements of Comprehensive Income for the Year Ended December 31

| | 2015 | 2014 | 2013 |
|---|---|---|---|
| | NIS million | NIS million | NIS million |
| Profit for the year | **1,721** | 2,111 | 1,771 |
| Items of other comprehensive income (loss) (net of tax) | **7** | (36) | 6 |
| **Total comprehensive income for the year attributable to shareholders of the Company** | **1,728** | 2,075 | 1,777 |

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

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## Comprehensive Statements of Changes in Equity for the Year Ended December 31

| | Share capital | Share premium | Capital reserve for employee options | Capital reserve for transactions between a corporation and a controlling shareholder | Other reserves | Deficit | Total |
|---|---|---|---|---|---|---|---|
| | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million |
| | Attributable to shareholders of the Company | | | | | | |
| **Balance as at January 1, 2013** | 3,837 | 100 | 256 | 390 | (38) | (2,090) | 2,455 |
| Income in 2013 | - | - | - | - | - | 1,771 | 1,771 |
| Other comprehensive income (loss) for the year, net of tax | - | - | - | - | (16) | 22 | 6 |
| Total comprehensive income for 2013 | - | - | - | - | (16) | 1,793 | 1,777 |
| **Transactions with shareholders recognized directly in equity** | | | | | | | |
| Dividend to Company shareholders | - | - | - | - | - | (1,830) | (1,830) |
| Share-based payments | - | - | 29 | - | - | - | 29 |
| Exercise of options for shares | 5 | 43 | (43) | - | - | - | 5 |
| Increase in the rate of holding in a subsidiary | - | - | - | - | (13) | - | (13) |
| Balance as at December 31, 2013 | 3,842 | 143 | 242 | 390 | (67) | (2,127) | 2,423 |
| Income in 2014 | - | - | - | - | - | 2,111 | 2,111 |
| Other comprehensive income (loss) for the year, net of tax | - | - | - | - | (38) | 2 | (36) |
| Total comprehensive income for 2014 | - | - | - | - | (38) | 2,113 | 2,075 |
| **Transactions with shareholders recognized directly in equity** | | | | | | | |
| Dividend to Company shareholders (Note 19.2) | - | - | - | - | - | (2,069) | (2,069) |
| Share-based payments | - | - | (1) | - | - | - | (1) |
| Exercise of options for shares | 13 | 110 | (110) | - | - | - | 13 |
| Balance as at December 31, 2014 | 3,855 | 253 | 131 | 390 | (105) | (2,083) | 2,441 |
| Income in 2015 | **-** | **-** | **-** | **-** | **-** | **1,721** | **1,721** |
| Other comprehensive income (loss) for the year, net of tax | **-** | **-** | **-** | **-** | **7** | **-** | **7** |
| **Total comprehensive income for 2015** | **-** | **-** | **-** | **-** | **7** | **1,721** | **1,728** |
| Transactions with shareholders recognized directly in equity | | | | | | | |
| Dividend to Company shareholders (Note 19.2) | **-** | **-** | **-** | **-** | **-** | **(1,777)** | **(1,777)** |
| Exercise of options for shares | **19** | **115** | **(115)** | **-** | **-** | **-** | **19** |
| **Balance as at December 31, 2015** | **3,874** | **368** | **16** | **390** | **(98)** | **(2,139)** | **2,411** |

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

## Consolidated Statements of Cash Flows for the Year Ended December 31

| | Note | 2015<br>NIS million | 2014<br>NIS million | 2013<br>NIS million |
|---|---|---|---|---|
| **Cash flows from operating activities** | | | | |
| **Profit for the year** | | **1,721** | 2,111 | 1,771 |
| **Adjustments:** | | | | |
| Depreciation and amortization | 8,9,10 | **1,684** | 1,281 | 1,311 |
| Profit from sale of the shares of Coral Tell Ltd. | | **-** | (582) | - |
| Share in losses (profits) of equity-accounted investees | 11.2 | **(12)** | 170 | 252 |
| Financing expenses, net | | **307** | 229 | 278 |
| Capital gain, net | 23 | **(234)** | (175) | (159) |
| Profit from gaining control in DBS | 11.2 | **(12)** | - | - |
| Income tax expenses | 6 | **598** | 815 | 651 |
| Miscellaneous | | **(13)** | (8) | 7 |
| | | | | |
| Change in trade and other receivables | 5 | **322** | 549 | 646 |
| Change in inventory | | **(20)** | 28 | 9 |
| Change in trade and other payables | 13 | **(271)** | (39) | 27 |
| Change in provisions | 14 | **18** | (63) | (29) |
| Change in employee benefits | 15 | **110** | 3 | 2 |
| Change in other liabilities | | **4** | 4 | 11 |
| Net income tax paid | | **(462)** | (527) | (625) |
| **Net cash from operating activities** | | **3,740** | 3,796 | 4,152 |
| **Cash flow used for investing activities** | | | | |
| Purchase of property, plant and equipment | 8 | **(1,324)** | (1,081) | (1,042) |
| Investment in intangible assets and deferred expenses | 9,10 | **(311)** | (194) | (186) |
| Acquisition of financial assets held for trading and others | | **(1,785)** | (2,720) | (1,570) |
| Proceeds from the sale of financial assets held for trading and others | | **3,260** | 1,635 | 1,528 |
| Proceeds from the sale of property, plant and equipment | | **151** | 230 | 312 |
| Cash in a company consolidated for the first time | 11.2.3 | **299** | - | - |
| Miscellaneous | | **(7)** | (12) | 41 |
| Net consideration for the sale of Coral Tell Ltd. shares | | **-** | 596 | - |
| Net cash from (used in) investment activities | | **283** | (1,546) | (917) |
| **Cash flows used in financing activities** | | | | |
| **Issue of debentures and receipt of loans** | 12 | **1,010** | 1,446 | 1,364 |
| Repayment of debentures and loans | 12 | **(2,192)** | (1,149) | (1,120) |
| Dividends paid | 19 | **(1,777)** | (2,069) | (2,830) |
| Interest paid | | **(494)** | (431) | (453) |
| Increase in the rate of holding in a subsidiary | | **-** | - | (50) |
| Payment to Eurocom DBS for acquisition of shares and DBS loan | 11.2 | **(680)** | - | - |
| Miscellaneous | | **5** | 3 | (2) |
| Net cash used for financing activities | | **(4,128)** | (2,200) | (3,091) |
| | | | | |
| Increase (decrease) in cash and cash equivalents, net | | **(105)** | 50 | 144 |
| **Cash and cash equivalents as at January 1** | | **660** | 610 | 466 |
| Cash and cash equivalents as at the end of the year | | **555** | 660 | 610 |

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

# 1. Basis of Preparation

## 1.1. Reporting Entity

Bezeq – The Israel Telecommunication Corporation Limited ("the Company") is a company registered in Israel whose shares are traded on the Tel Aviv Stock Exchange. The consolidated financial statements of the Company include those of the Company and its subsidiaries (together referred to as "the Group"), as well as the Group's interests in associates. The Group is a principal provider of communication services in Israel (see also Note 27 – Segment Reporting).

## 1.2. Material events in the reporting period

On March 23, 2015, the Company gained control in DBS Satellite Services (1998) Ltd. ("DBS") and began consolidation as at that date. On June 24, 2015, the Company completed the acquisition of the entire rights in DBS shares. For further information see Note 11.2, Investees. The accounting policy applied for the business combination with DBS is described in Note 2.1.1 below.

## 1.3. Definitions

In these financial statements:

The Company: Bezeq The Israel Telecommunication Corporation Limited

The Group: Bezeq The Israel Telecommunication Corporation Limited and its subsidiaries, as follows:

Subsidiaries: Companies, the financial statements of which are fully consolidated, directly or indirectly, with the financial statements of the Company, as set out in Note 11.1.

Associates: Companies, including a partnership, in which the Group's investment is included, directly or indirectly, in the consolidated financial statements on the equity basis.

Investees: Subsidiaries or associates

Related parties: As defined in IAS 24, Related Party Disclosures

Interested parties: As defined in paragraph (1) of the definition of an "interested party "in section 1 of the Securities Law, 1968

## 1.4. Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS") and in accordance with the Securities Regulations (Annual Financial Statements), 2010

The consolidated financial statements were approved by the Board of Directors on March 16, 2016.

## 1.5. Functional currency and presentation currency

The consolidated financial statements are presented in NIS, which is the Group's functional currency, and have been rounded to the nearest million. The NIS is the currency that represents the principal economic environment in which the Group operates.

## 1.6. Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following items:

* Financial instruments, including financial derivatives, at fair value through profit or loss
* Inventories measured at the lower of cost and net realizable value
* Equity-accounted investments
* Deferred tax assets and liabilities
* Provisions
* Assets and liabilities for employee benefits
* Liability for payment of contingent consideration in a business combination

For further information about the measurement of these assets and liabilities see Note 2, Significant Accounting Policies.

## 1.7. Operating cycle

The Group’s operating cycle is up to one year. As a result, current assets and current liabilities include items the realization of which is intended and anticipated to take place within one year from the date of the financial statements.

## 1.8. Classification of expenses recognized in the statement of income

Costs and expenses in the statement of income are presented and analyzed on the basis of the function of the expenses. The classification is compatible with the understanding of the Group’s businesses, which address a wide range of services using common infrastructure. All of the costs and expenses are used to provide services.

## 1.9. Use of estimates and judgment

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

The preparation of accounting estimates used in the preparation of the Group’s financial statements requires management to make assumptions regarding circumstances and events that involve considerable uncertainty. Management of the Company prepares the estimates on the basis of past experience. In exercising its judgment when making the estimates, management relies on experience, various facts, external circumstances, and reasonable assumptions according to the relevant circumstances of each estimate.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

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

| Subject | Principal assumptions | Possible effects | Reference |
|---|---|---|---|
| Useful life of property, plant and equipment and intangible assets | Assumptions of the useful life of groups of property, plant and equipment and intangible assets | Change in the value of property, plant and equipment and intangible assets and in depreciation and amortization expenses | Note 8 and Note 9 |
| Fair value measurement of the Company's investment in DBS prior to gaining control in DBS | Assumption of expected cash flows from the operations of DBS, discount rate and assumptions about the identity of the relevant market participant. | Change in profit/loss from gaining control | Note 11 |
| Attribution of excess cost arising from acquisition of control in DBS | Assumption of expected cash flows from identifiable assets in the business combination, timing of recognition, and scope of the deferred tax asset for carry-forward losses | Change in the value of identifiable tangible and intangible assets in the business combination and changes in the value of goodwill | Note 11 |
| Fair value measurement of contingent consideration in a business combination | Assumption of expected cash flows and assumption of DBS's losses for tax purposes. | Change in the value of a liability for contingent consideration recognized in a business combination | Note 11 |
| Measurement of recoverable amounts of cash-generating units that include goodwill | Assumption of expected cash flows from cash-generating units | Recognition of impairment loss | Note 9 |
| Deferred taxes | Assumption of anticipated future realization of the tax benefit in the future, including assumptions for the use of carry-forward losses in DBS. | Recognition or reversal of deferred tax asset in profit or loss | Note 6 |
| Uncertain tax positions | The extent of the certainty that the Group's tax positions will be accepted (uncertain tax positions) and the risk of it incurring any additional tax and interest expenses. This is based on an analysis of a number of matters including interpretations of tax laws and the Group's past experience | Recognition or reversal of income tax expenses | Note 6 |
| Provisions and contingent liabilities | Assessment of the likelihood of claims against Group companies and measuring potential liabilities attributable to claims | Reversal or creation of a provision for a claim and recognition of income/expenses respectively | Note 14 and Note 16 |
| Post-employment employee benefits | Actuarial assumptions such as discount rate, future salary increases and churn rate | Increase or decrease in the post-employment defined benefit obligation | Note 15 |

## 1.10 Determining fair value

When preparing the financial statements, the Group is required to determine the fair value of certain assets and liabilities. Further information about the assumptions made in determining fair values is disclosed in Note 29.7 regarding fair value.

# 2. Significant Accounting Policies

The accounting policies set out below have been applied consistently by Group entities for all periods presented in these consolidated financial statements.

## 2.1. Consolidation of the financial statements

### 2.1.1 Business combinations

In view of the consolidation of DBS as from March 23, 2015, as described in Note 1.2 and Note 11.2, below is a description of the accounting policy for the consolidation of DBS in these financial statements:

A. The Group implemented the acquisition method for all business combinations. The acquisition date is the date on which the acquirer obtained control over the acquiree.

B. The Group recognized goodwill at acquisition based on the fair value of the consideration transferred, and the fair value at the acquisition date of any pre-existing equity right of the Group in the acquiree, less the net amount of the identifiable assets acquired and the liabilities assumed.

C. The consideration transferred includes the fair value of the assets transferred to the previous owners of the acquiree and the liabilities incurred by the acquirer to the previous owners of the acquiree, **including the obligation to acquire the acquiree's equity instruments**. In addition, the consideration transferred includes the fair value of any contingent consideration.

D. In the step acquisitions, the difference between the fair value at the acquisition date of the Group’s pre-existing equity rights in the acquiree and the carrying amount at that date is recognized in the statement of income **under other operating income or expenses.**

E. Costs associated with the acquisition that were incurred by the Group in the business combination such as advisory, legal, valuation and other professional or consulting fees were recognized as expenses in the period the services are received.

### 2.1.2 Subsidiaries

Subsidiaries are entities controlled by the Company. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date of loss of control.

Control exists when the Group is exposed or has rights to variable returns from its involvement with the acquiree and it has the ability to affect those returns through its power over the acquiree. Substantive rights held by the Group and others are taking into account when assessing control.

The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

### 2.1.3 Transactions eliminated on consolidation

Intra-group balances and income and expenses arising from intra-group transactions, are eliminated in the consolidated statements.

## 2.2. Foreign currency transactions

Transactions in foreign currency are translated into the functional currency of the Group at the exchange rate on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies on the reporting date are retranslated to the functional currency at the exchange rate at that date.

## 2.3. Financial instruments:

### 2.3.1 Non-derivative financial assets

Non-derivative financial assets comprise mainly investments in exchange traded funds, trade and other receivables, and cash and cash equivalents.

The Group initially recognizes financial assets at the date the Group becomes a party to contractual provisions of the instrument, meaning the date that the Group fulfills its obligations under the contract.

Financial assets are derecognized when the contractual rights of the Group to the cash flows from the asset expire, or the Group transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred.

Regular way sales of financial assets are recognized on the trade date, meaning on the date the Group undertook to sell the asset.

### 2.3.2 Classification of financial assets and the accounting treatment in each group

The Group classifies its financial assets as follows:

Cash and cash equivalents

Cash comprises cash balances available for immediate use and call deposits. Cash equivalents comprise short-term highly liquid investments (with original maturities of three months or less) that are readily convertible into known amounts of cash and are exposed to insignificant risks of change in value.

Financial assets at fair value through profit or loss

A financial asset is classified at fair value through profit or loss (mainly the Group's investment in exchange-traded funds and deposit notes) if it is classified as held for trading or is designated as such upon initial recognition. These financial assets are measured at fair value, and changes therein are recognized in the statement of income.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognized initially at fair value plus attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

### 2.3.3 Non-derivative financial liabilities

Non-derivative financial liabilities include debentures issued by the Group, loans and borrowings from banks and other credit providers, and trade and other payables.

The Group initially recognizes debt instruments as they are incurred. Financial liabilities are initially recognized at fair value plus any attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortized cost using the effective interest method.

Financial liabilities are derecognized when the obligation of the Group, as specified in the agreement, expires or when it is discharged or canceled.

CPI-linked assets and liabilities that are not measured at fair value

The value of CPI-linked financial assets and liabilities, which are not measured at fair value, is revaluated in each period according to the actual increase in the CPI.

### 2.3.4 CPI-linked assets and liabilities that are not measured at fair value

**The value of CPI-linked financial assets and liabilities, which are not measured at fair value, is revaluated in each period according to the actual increase in the CPI.**

2.3.5 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group currently has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

2.3.6 A. Hedge accounting

The Group holds derivative financial instruments to hedge cash flows for risks to future changes in the CPI.

Forward contracts are measured at fair value. Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognized through other comprehensive income, in a hedging reserve under equity, to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognized in profit or loss. The amount recognized in the hedging reserve is removed and included in profit or loss in the same period as the hedged cash flows affect profit or loss under the same line item in the statement of income as the hedged item.

B. Economic hedging

In addition, the Group holds derivative financial instruments to hedge cash flows for foreign currency risks. Hedge accounting is not applied for these instruments. The derivative instruments are recognized at their fair value; fair value changes are recognized immediately in the statement of income.

## 2.4. Broadcasting rights

***Broadcasting rights are stated at cost, net of rights exercised.***
The costs of rights to broadcast acquired content include the amounts paid to the rights provider, plus direct costs for adjusting the rights to the broadcast. Broadcast rights are amortized in accordance with the actual broadcasts of the total number of expected broadcasts based on the management's estimate or broadcasts permitted under the agreement (the part that is unamortized at the end of the agreement term is amortized in full upon its termination), or on a straight line basis in accordance with the term of the rights agreement or the economic life, whichever is shorter. ***The net adjustment of the broadcasting rights is presented as an adjustment of earnings as part of the ongoing operations in the statements of cash flows***.

## 2.5. Property, plant and equipment

2.5.1 Recognition and measurement

***The Group elected to measure items of property, plant and equipment at cost less accumulated depreciation and accumulated impairment losses.***

Cost includes expenditures that are directly attributable to acquisition of the asset. The cost of self-constructed assets includes the cost of materials, direct labor and financing costs as well as any other cost directly attributable to bringing the asset to the condition for its use intended by the management, and the estimated costs of dismantling and removing the items and restoring the site on which they are located when the Group has an obligation to vacate and restore the site. The cost of purchased software that is integral to the functionality of the related equipment is recognized as part of the cost of the equipment.

Spare parts, servicing equipment and stand-by equipment are classified as property, plant and equipment when they meet the definition of property, plant and equipment in IAS 16, and are otherwise to be classified as inventory.

When major parts of the property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of the property, plant and equipment.

Gain or loss from the disposal of an item of property, plant and equipment is determined by comparing the proceeds from disposal of the asset with its carrying amount. ***Gain or***

***loss from the sale of property, plant and equipment is recognized under "other income" in the statement of income.***

2.5.2 Subsequent expenditure

The cost of replacing part of an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefit embodied in the replaced item will flow to the Group and its cost can be measured reliably. The costs of day-to-day servicing are recognized in the statement of income as incurred.

2.5.3 Depreciation

Depreciation is recognized in the statement of income on a straight-line basis over the estimated useful life of each part of an item of property, plant and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Leased assets under finance lease agreements are depreciated over the shorter of the lease term and their useful lives. An asset is depreciated when it is ready for use, meaning when it reaches the location and condition necessary for it to be capable of operating in the manner intended by management.

Leasehold improvements are depreciated over the shorter of the lease term, including the extension option held by the Group and intended to be exercised and the expected life of the improvement.

The estimated useful lives for the current and comparative periods are as follows:

| | Year | Average depreciation for the reported period (%) |
|---|---|---|
| Fixed line and international network equipment (switches, transmission, power) | 4-12 | 12 |
| Network | 12-33 | 6 |
| Equipment and infrastructure for multichannel television | 3-15 | 14 |
| Subscriber equipment and installations | 4-6 | 20 |
| Vehicles | 6-7 | 15 |
| Office and general equipment | 5-14 | 15 |
| Electronic equipment, computers and internal communication systems | 3-7 | 24 |
| Cellular network | 4-15 | 13 |
| Buildings | 25 | 4 |
| Seabed cable | 4-25 | 4 |

Depreciation methods, useful lives and residual values are reviewed at least in each reporting year and adjusted as required.

## 2.6. Non-current assets held for sale

Non-current assets which will most probably be realized by way of a sale rather than ongoing use are classified as assets held for sale. These assets are presented at the lower of the carrying amount and fair value, less selling costs.

## 2.7. Intangible assets

2.7.1 Goodwill

Goodwill that arises upon the acquisition of subsidiaries is included in intangible assets. Subsequent to initial recognition, goodwill is measured at cost less accumulated impairment losses. Goodwill is measured at least once a year to assess impairment.

2.7.2 Software development costs

Software development costs are recognized as an intangible asset only if the development costs can be measured reliably; the software is technically and commercially applicable; and the Group has sufficient resources to complete the development and intends to use the software. The costs recognized as an intangible asset include the cost of the materials, direct labor and overhead expenses directly attributable to preparation of the asset for its intended use. Other development costs are recognized in the statement of income as incurred.

Capitalized development costs are measured at cost less amortization and accumulated impairment losses.

2.7.3 Software

Software that is an integral part of the hardware, which cannot function without the programs installed on it, is classified as property, plant and equipment. However, licenses for stand-alone software which add functionality to the hardware are classified as intangible assets.

2.7.4 Rights to frequencies

Rights to frequencies refer to frequencies assigned to Pelephone for cellular activities, after it won the dedicated tenders of the Ministry of Communications. Depreciation of the asset is recognized in the statement of income on the straight line method over the term of the allocation of frequencies, which started from the use of the frequencies. The 4G frequencies (LTE) are amortized over a period of 10 years. The 3.5G frequencies (UMTS / HSPA) are amortized over a period of 13 years and seven months.

2.7.5 Other intangible assets

**Other intangible assets acquired by the Group, which have a definite useful life, are measured at cost less amortization and accumulated impairment losses.**

2.7.6 Subsequent expenditure

Subsequent expenditure is recognized as an intangible asset only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure relating to generated goodwill and brands, is recognized in the statement of income as incurred.

2.7.7 Amortization

Amortization of intangible assets is recognized in the statement of income on a straight-line basis over the estimated useful life of the intangible assets, from the date on which the assets are available for use. Goodwill is not systematically amortized but is tested for impairment at least once a year.

Estimated useful lives for the current and comparative periods are as follows:

| Type of asset | Amortization period |
|---|---|
| Frequency usage right | Over the term of the license for 10 to 14 years starting from the use of the frequencies |
| Computer programs and software licenses | 3-10 years depending on the term of the license period or the estimated time of use of the software |
| Customer relationships acquired in a business combination | 5-7 years based on the estimated customer churn rate |
| Brand acquired in a business combination | 12 |
| Other rights | 2-6 years, depending on the useful life |

Amortization methods and useful lives are reviewed at least at each reporting year and adjusted if appropriate.

## 2.8. Leased assets

Leases, including leases of land from the Israel Land Administration, where the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. ***Subsequent to initial recognition, the assets are measured at cost less accumulated amortization and impairment losses***.

Other leases are classified as operating leases and the leased assets are not recognized in the Group's statement of financial position. Payments made under operating leases are recognized in profit or loss on a straight-line basis over the term of the lease.

At inception or upon reassessment of an arrangement, the Group determines whether such an arrangement is or contains a lease. An arrangement is a lease or contains a lease if the following two criteria are met:

A. The fulfillment of the arrangement is dependent on the use of a specific asset or assets; and

B. The arrangement contains rights to use the asset

If, in accordance with these terms, the Group determines that the agreement does not contain a lease, the agreement is accounted for as a service agreement and payments for the service are recognized in profit or loss on a straight line basis, over the service period.

## 2.9. Right of use of capacities

Transactions for acquiring an indefeasible right of use (IRU) of seabed cable capacities are accounted for as service transactions. The prepaid expense is amortized on a straight-line basis as stated in the agreement and no more than the expected estimated useful life of those capacities.

Identifiable capacities which serve the Group exclusively fulfill the definition of a finance lease and were recognized in property, plant and equipment. The asset is depreciated on a straight-line basis as stated in the agreement and no more than the expected estimated useful life of those capacities.

## 2.10. Inventory

Inventories are measured at the lower of cost and net realizable value. ***The Group elected to base the cost of inventories on the moving average principle.***

The inventories include terminal equipment and accessories intended for sale and service, as well as spare parts used for repairs in the repair service provided to its customers.

Slow-moving inventory of terminal equipment, accessories and spare parts are stated net of the provision for impairment.

## 2.11. Impairment

### 2.11.1 Non-derivative financial assets

The Group tests a financial asset for impairment when objective evidence indicates that one or more loss events have had a negative effect on the estimated future cash flows of that asset.

Significant financial assets are tested for impairment on an individual basis. Other financial assets are assessed for impairment collectively in groups that share similar credit risk characteristics, taking into account past experience. The financial statements include specific provisions and Group provisions for doubtful debts, which properly reflect, in the estimation of the management, the loss inherent in debts for which collection is in doubt.

### 2.11.2 Non-financial assets

Timing of impairment testing

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the recoverable amount of the asset is estimated.

The Group assesses the recoverable amount of goodwill once a year, or more frequently if there are indications of impairment.

Measurement of recoverable amount

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset (for which future cash flows were not adjusted).

Determining cash-generating units

For the purpose of impairment testing, the assets are grouped together into the smallest group of assets that generates cash from continuing use that are largely independent of other assets or groups of assets ("cash-generating unit").

Allocation of goodwill to cash-generating units

For purposes of goodwill impairment testing, cash-generating units to which goodwill has been allocated are aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes, but in any event is not larger than an operating segment. Goodwill acquired in a business combination is allocated for the purpose of impairment testing to cash-generating units that are expected to generate benefits from the synergies of the combination.

## 2.12. Employee benefits

2.12.1 Post-employment benefits

The Group has a number of post-employment benefit plans. The plans are usually financed by deposits with insurance companies and they are classified as defined contribution plans and defined benefit plans.

A. Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which the Group pays fixed contributions into a separate entity and has no legal or constructive obligation to pay further amounts.

The Group's obligations for contributions to defined contribution pension plans are recognized as an employee benefit expense in the statement of income in the periods during which services are rendered by employees.

B. Defined benefit plans

The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is presented at its present value, and the fair value of any plan assets is deducted. The calculation is performed annually by a qualified actuary. The discount rate is the yield at the reporting date on high-quality linked corporate debentures denominated in NIS, with maturity dates approximating the terms of the Group's obligations.

Net interest costs on a defined benefit plan are calculated by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability.

***The Group elected to recognize the interest costs that were recognized in profit or loss under financing expenses.***

Re-measurement of the net defined benefit liability comprises actuarial gains and losses and the return on plan assets (excluding interest). Re-measurements are recognized immediately directly in retained earnings through other comprehensive income.

When the benefits of a plan are improved or curtailed, the portion of the increased benefit relating to past service by employees or the gain or loss on curtailment are recognized immediately in profit or loss when the plan improvement or curtailment occurs.

2.12.2 Other long-term employee benefits

The Group's net obligation in respect of long-term employee benefits other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The amount of these benefits is stated at its present value. The discount rate is the yield at the reporting date on high-quality linked corporate debentures denominated in NIS, with maturity dates approximating the terms of the Group's obligations. Any actuarial gains or losses are recognized in the statement of income in the period in which they arise.

2.12.3 Termination benefits

Termination benefits are recognized as an expense when the Group is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan to terminate employment before the normal retirement date. Termination benefits for voluntary redundancies are recognized as an expense if the Group has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

2.12.4 Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

The employee benefits are classified, for measurement purposes, as short-term benefits or as other long-term benefits depending on the date when the benefits are expected to be to be wholly settled,

In the statement of financial position the employee benefits are classified as current benefits or as non-current benefits according to the time the liability is due to be settled.

## 2.13. Provisions

A provision is recognized if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

2.13.1 Legal claims

Contingent liabilities are accounted for according to IAS 37 and its related provisions. Accordingly, the claims are classified by likelihood of realization of the exposure to risk, as follows:

A. More likely than not – more than 50% probability

B. Likely – probability higher than unlikely and less than 50%

C. Unlikely – probability of 10% or less

For claims which the Group has a legal or constructive obligation as a result of a past event, which are more likely than not to be realized, the financial statements include provisions which, in the opinion of the Group, based, inter alia, on the opinions of its legal advisers retained in respect of those claims, are appropriate to the circumstances of each case, despite the claims being denied by the Group companies. There are also a small number of legal proceedings, most of which were received recently, for which the risks cannot be assessed at this stage, therefore no provisions have been made.

Note 16 describes the amount of additional exposure due to contingent liabilities that are likely to be realized.

2.13.2 Site dismantling and clearing costs

The provision in respect of an obligation to dismantle and clear sites is recognized for those rental agreements where Pelephone has an undertaking to restore the rental property to its original state at the end of the rental period, after dismantling and transferring the site, and restoring the site when required. The provision is measured by discounting the future cash flows by risk-free discounted interest reflecting the time until the expected termination of the contract for dismantling of the site by Pelephone. The carrying amount of the provision is adjusted in each period to reflect the time that has passed and is recognized as a financing expense.

## 2.14. Revenues

Revenues are measured at the fair value of the consideration received or receivable, net of returns, trade discounts and volume rebates.

2.14.1 Sale of equipment

Revenues from sales of terminal equipment are recognized in the statement of income when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs can be estimated reliably and the Group companies have no continuing involvement with the goods.

Revenues from the sale of terminal equipment to subscribers in long-term credit arrangements are recognized upon delivery to the customer at the present value of the future cash flow expected from them, ***at the relevant interest rate for transactions of this kind*** (see Note 5). Financing income in respect of these transactions is recognized in the statement of income over the period of the installments by the effective interest method.

2.14.2 Revenues from services

Revenues from services rendered are recognized in the statement of income proportionately over the term of the agreement or upon providing the service if the flow of the economic benefits associated with providing the service is likely.

2.14.3 Reporting gross or net revenues

When the Group acts as an agent or intermediary without bearing the risks and rewards deriving from the transaction, its revenues are recognized on a net basis (as profit or commission). The Group operates as an agent mainly for certain content services provided by other suppliers and payment is collected by the Group. However, when the Group acts as a main supplier and bears the risks and rewards associated with the transaction, its revenues are recognized on a gross basis (such as interconnect fees).

## 2.15. Financing income and expenses

Financing income includes mainly interest income from deposits, income interest and linkage from loans provided to an associate, income interest accrued using the effective interest method in respect of the sale of terminal equipment in installments, gains on the disposal of available-for-sale financial assets, and changes in the fair value of financial assets at fair value through profit or loss.

Financing expenses include interest and linkage expense on borrowings, debentures issued, loss from hedge transactions, impairment losses recognized on financial assets (except for a provision for doubtful debts, which is recognized under operating and general expenses), and financing expenses for provisions arising from legal claims.

In the statements of cash flows, ***interest received and dividends received are presented as part of cash flows from investing activities. The Group elected to present interest and***

***linkage differences paid for loans and debentures under cash flows used for financing activities.***

## 2.16. Income tax expenses

Income tax expenses include current and deferred taxes and are recognized in the statement of income, or in other comprehensive income to the extent that the expenses relate to items recognized in other comprehensive income.

<u>Current taxes</u>

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date. Current taxes also include taxes in respect of prior years.

<u>Uncertain tax positions</u>

A provision for uncertain tax positions, including additional tax and interest expenses, is recognized when it is more likely than not that the Group will have to use its economic resources to pay the obligation

<u>Deferred taxes</u>

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The Group does not recognize deferred taxes for the following temporary differences:

1. Initial recognition of goodwill
2. Differences arising from investment in subsidiaries and associates, if it is probable that they will not reverse in the foreseeable future and if the Group controls the date of reversal.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognized for carry-forward losses, tax benefits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

<u>Offsetting deferred tax assets and liabilities</u>

The Group sets off deferred tax assets and liabilities if there is a legally enforceable right to offset deferred tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, and they intend to settle deferred tax liabilities and assets on a net basis or their deferred tax assets and liabilities will be realized simultaneously.

## 2.17. Dividends

An obligation relating to a dividend proposed or declared subsequent to the reporting date is recognized only in the period in which the declaration was made (approval of the general meeting). In the statements of cash flows, ***a dividend that has been paid is recognized under financing activities.***

## 2.18. New standards and interpretations not yet adopted

| Standard | Subject | Implementation and transition provisions | Expected effects |
|---|---|---|---|
| IFRS 9 (2014), Financial Instruments | IFRS 9 (2014) replaces the requirements included in IAS 39 regarding classification and measurement of financial assets and financial liabilities, hedge accounting, and impairment of financial instruments. | IFRS 9 (2014) will be effective for annual periods starting from January 1, 2018. Early application is permitted. IFRS 9 (2014) will be applied retrospectively, except for a number of exemptions. | The Group is examining the effects of adopting IFRS 9 (2014) on the financial statements. |
| IFRS 15, Revenues from Contracts with Customers | IFRS 15 replaces current guidelines for revenue recognition and presents a new model for recognition of revenues from contracts with customers. The model includes five steps for analyzing transactions to determine the timing and amount of revenue recognition. IFRS 15 also establishes new and more extensive disclosure requirements. | IFRS 9 (2014) will be effective for annual periods starting from January 1, 2018. Early application is permitted. IFRS 15 includes various alternatives for the transition guidelines, so that companies may choose one alternative upon initial application. | The Group is examining the effects of adopting IFRS 9 (2014) on the financial statements. |
| IFRS 16, Fair Value Measurement: Leases | The standard replaces the previous instructions under IAS. For lessees, IFRS 16 eliminates the current classification of leases as either operating leases or finance leases and introduces a single lessee accounting model for all leases on a balance sheet (other than a number of exceptions), which are substantially similar to the accounting treatment for finance leases today. By contrast, the accounting treatment in the lessors' financial statements is expected to remain the same as the accounting treatment today.<br>In addition, the standard establishes new and expanded disclosure requirements, both by lessors and by the lessees. | The standard will be effective for annual periods starting from January 1, 2019. Early application is possible, provided that the Company also applies IFRS 15, Revenue from Contracts with Customers. | The Group will examine the effects of adopting the standard on the financial statements. |

# 3. Cash and Cash Equivalents

As at December 31, 2015, cash and cash equivalents include mainly bank deposits for an average period of 90 days.

# 4. Investments, Including Derivatives

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Bank deposits | **556** | 710 |
| Exchange traded funds | **139** | 1,508 |
| Monetary and other reserves | **67** | 5 |
| | **762** | 2,223 |

Investments in ETFs and financial funds are investments held for trading and are presented at fair value as at the date of the financial statements. ETFs were exercised in January 2016, the deposits are repayable until April 2016, and the other investments are exercisable in 2016.

# 5. Trade and Other Receivables

**5.1** Composition of trade and other receivables

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Trade receivables* | | |
| Open accounts and checks receivable | **841** | 986 |
| Credit cards | **434** | 343 |
| Revenues receivable | **240** | 250 |
| Current maturities of long-term receivables | **534** | 632 |
| Related and interested parties | **9** | 16 |
| | **2,058** | 2,227 |
| **Other receivables and current tax assets** | | |
| Prepaid expenses | **135** | 103 |
| Other receivables (mainly from real estate sales) | **118** | 131 |
| Current tax assets | **16** | 26 |
| | **269** | 260 |
| **Long-term trade and other receivables** | | |
| Trade receivables – open debts | **509** | 531 |
| Other receivables (for the sale of real estate) | **165** | 35 |
| | **674** | 566 |
| | | |
| | **3,001** | 3,053 |

* The amount of trade receivables is stated net of the provision for doubtful debts

**5.2** Discounted interest rates for long-term trade payables are based the estimated credit risk of trade payables. The discounted interest rates used by the Group in 2015 are 3.4% - 3.6% (in 2014: 4.3% - 3.6%).

**5.3** Expected payment dates for long-term trade and other receivables:

| Expected payment dates | December 31, 2015 |
|---|---|
| | NIS million |
| 2017 | **385** |
| 2018 | **281** |
| 2019 | **8** |
| | **674** |

**5.4** Aging of trade receivables at the reporting date:

| | December 31, 2015 | | December 31, 2014 | |
|---|---|---|---|---|
| | Trade receivables, gross | Provision for doubtful debts | Trade receivables, gross | Provision for doubtful debts |
| | NIS million | NIS million | NIS million | NIS million |
| Not past due | **2,377** | **(11)** | 2,607 | (12) |
| Past due up to one year | **201** | **(47)** | 174 | (61) |
| Past due one to two years | **74** | **(50)** | 78 | (52) |
| Past due more than two years | **88** | **(65)** | 73 | (49) |
| | **2,740** | **(173)** | 2,932 | (174) |

**5.5** Change in provision for doubtful debts during the year:

| | 2015 | 2014 |
|---|---|---|
| | NIS million | NIS million |
| Balance as at January 1 | **174** | 202 |
| Impairment loss recognized | **34** | 30 |
| Bad debts | **(35)** | (58) |
| Balance as at December 31 | **173** | 174 |

# 6. Income Tax

## 6.1. Corporate tax rate

The tax rate relevant to the Company is 26.5% in 2015 and 2014 and 25% in 2013.

As at December 31, 2015, the deferred tax balances were calculated according to the enacted tax rate expected to apply on the utilization date (26.5%). For information about the decrease in tax rates as from 2016, see Note 6.7 below.

## 6.2. Components of income tax expenses

| | Year ended December 31 | | |
|---|---|---|---|
| | 2015 | 2014 | 2013 |
| | NIS million | NIS million | NIS million |
| Current tax expenses | **567** | 781 | 579 |
| Deferred taxes | **31** | 34 | 72 |
| Income tax expenses | **598** | 815 | 651 |

### 6.3. Reconciliation between the theoretical tax on the pre-tax profit and the tax expense

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| Profit before income tax | **2,319** | 2,926 | 2,422 |
| Statutory tax rate | **26.5%** | 26.5% | 25% |
| **Income tax at the statutory tax rate** | **614** | 775 | 606 |
| Adjusted tax calculated for the Company's share in the losses of equity-accounted investees | **(3)** | 45 | 63 |
| Expenses (benefits) not recognized for tax purposes, net | **(13)** | (5) | 23 |
| Differences in the tax rate and other adjustments | **-** | - | (41) |
| **Income tax expenses** | **598** | 815 | 651 |

### 6.4. Unrecognized deferred tax assets and liabilities

The calculation of deferred taxes does not take into account the taxes that would be applicable in the case of disposal of investments in subsidiaries and associates, since the Group intends to retain the investment. Deferred taxes in respect of a distribution of profit in subsidiaries and associates were also not taken into account since the dividends are not taxable.

## 6.5. Recognized tax assets and deferred tax liabilities and their changes

| | Balance as at January 1, 2014 | Changes recognized in the statement of income | Changes recognized in equity | Balance as at December 31, 2014 | Changes recognized in the statement of income | Changes recognized in equity | Business combination (see Note 11.2) | Balance as at December 31, 2015 |
|---|---|---|---|---|---|---|---|---|
| **NIS million** | | | | | | | | |
| Carry-forward losses for DBS | - | - | - | - | (7) | - | **1,426** | 1,419 |
| Property, plant and equipment | (315) | (35) | - | (350) | (3) | - | **-** | (353) |
| Intangible assets | - | - | - | - | 37 | - | **(301)** | (264) |
| Employee benefit plans | 230 | (23) | - | 207 | 1 | - | **-** | 208 |
| Other | 90 | 24 | 12 | 126 | (59) | 5 | **45** | 117 |
| | 5 | (34) | 12 | (17) | (31) | 5 | **1,170** | 1,127 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Presented in the statement of financial position** | | | | | | | | |
| Deferred tax assets | 60 | | | - | | | | 1,178 |
| Deferred tax liabilities | (55) | | | (17) | | | | (51) |
| | 5 | | | (17) | | | | 1,127 |

### 6.6. Final tax assessments

6.6.1 The Company has final tax assessments up to and including 2005.

6.6.2 In 2013, the Company signed an agreement with the tax assessor for 2006-2008, which includes undisputed income. In addition, a decision was received according to the best judgment of the tax assessor, whereby financing expenses accumulated on the shareholders' loans that the Company provided DBS should be added to the Company's undisputed income. The Company filed a reservation on this decision. The reservation was dismissed and on February 24, 2015, the Company received orders which it appealed at the Court. For 2009-2010, a decision was reached according to the tax assessor's best judgment regarding the aforesaid, and regarding other matters, mainly non-recognition of financing expenses for various reasons. The Company filed a reservation on the assessment. Subsequent to the date of the financial statements, the Company reached an agreement in principle with the assessor regarding payment of taxes in the amount of NIS 460 million on financing income that accrued up to December 31, 2015 on shareholders loans provided to DBS. In addition, it was agreed that the losses of DBS as at December 31, 2014, which will be recognized in a merger or offset from the income of DBS, will amount to NIS 5.4 billion and the balance of the shareholder loan will be considered as equity in the financial statements of DBS. The agreement in principle has not yet resulted in a signed agreement.

The provision in the financial statements was reduced and amounted to the agreed amount and included an adequate provision for tax for the other disputed income. A deferred tax asset was also recognized for the carry-forward losses of DBS, based on the Company's estimates and taking into account the above.

6.6.3 Pelephone has received final tax assessments up to and including 2012.

6.6.4 Bezeq International has received final tax assessments up to and including 2012.

6.6.5 DBS has received final tax assessments up to and including 2009.

### 6.7. Change in the rate of corporate tax subsequent to the date of the financial statements

On January 4, 2016, the Knesset plenum approved a bill to amend the Income Tax Ordinance, including a reduction in corporate tax by 1.5% from 26.5% to 25%, as from January 1, 2016. Consequently, in 2016, the Group expects to reduce the tax assets and liabilities for deferred taxes and recognize an expense of NIS 64 million for deferred taxes.

## 7. Broadcasting Rights, Net of Rights Exercised

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Cost | **621** | - |
| Less rights exercised | **(165)** | - |
| | **456** | - |

As at December 31, 2015, DBS has agreements for the acquisition of broadcasting rights. In 2015, acquisition of these broadcasting rights amounted to NIS 189 million.

# 8. Property, Plant and Equipment

| | Land and buildings | Fixed line and international network equipment (switches, transmission, power) | Cables and fixed line and international network infrastructure | Cellular network | Equipment and infrastructure for multichannel television | Subscriber equipment | Office equipment, computers and vehicles | Total |
|---|---|---|---|---|---|---|---|---|
| | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million |
| **Cost** | | | | | | | | |
| Balance as at January 1, 2014 | 1,594 | 2,311 | 11,420 | 2,528 | - | 591 | 928 | 19,372 |
| Additions | 43 | 241 | 285 | 255 | - | 203 | 82 | 1,109 |
| Disposals | 86 | (129) | (131) | (254) | - | (82) | (158) | (668) |
| Balance as at December 31, 2014 | 1,723 | 2,423 | 11,574 | 2,529 | - | 712 | 852 | 19,813 |
| Additions | **41** | **273** | **254** | **254** | **164** | **225** | **71** | **1,282** |
| Consolidation | **16** | **-** | **-** | **-** | **749** | **-** | **36** | **801** |
| Disposals | **(132)** | **(99)** | **(160)** | **(86)** | **(46)** | **(59)** | **(117)** | **(699)** |
| Balance as at December 31, 2015 | **1,648** | **2,597** | **11,668** | **2,697** | **867** | **878** | **842** | **21,197** |
| **Depreciation and impairment losses** | | | | | | | | |
| Balance as at January 1, 2014 | 1,122 | 1,058 | 8,834 | 1,482 | - | 299 | 604 | 13,399 |
| Depreciation for the year | 40 | 227 | 187 | 304 | - | 132 | 106 | 996 |
| Disposals | 73 | (128) | (131) | (254) | - | (79) | (142) | (661) |
| Balance as at December 31, 2014 | 1,235 | 1,157 | 8,890 | 1,532 | - | 352 | 568 | 13,734 |
| Depreciation for the year | **46** | **237** | **195** | **314** | **189** | **159** | **105** | **1,245** |
| Disposals | **(118)** | **(99)** | **(160)** | **(85)** | **(46)** | **(59)** | **(109)** | **(676)** |
| Balance as at December 31, 2015 | **1,163** | **1,295** | **8,925** | **1,761** | **143** | **452** | **564** | **14,303** |
| **Carrying amount** | | | | | | | | |
| January 1, 2014 | 472 | 1,253 | 2,586 | 1,046 | - | 292 | 324 | 5,973 |
| December 31, 2014 | 488 | 1,266 | 2,684 | 997 | - | 360 | 284 | 6,079 |
| December 31, 2015 | **485** | **1,302** | **2,743** | **936** | **724** | **426** | **278** | **6,894** |

**8.1** The residual value of the Group's copper cables is assessed at the end of each quarter. The residual value is NIS 140 million as at December 31, 2015 and NIS 190 million as at December 31, 2014. The change in the residual value is mainly due to the decrease in the price of copper.

**8.2** Property, plant and equipment in the Group is derecognized at the end of each year upon reaching full depreciation, except for land, buildings, vehicles, copper cables and specific components for Pelephone's UMTS network, which are derecognized upon their sale. In 2015, the Group derecognized fully depreciated property at a cost of NIS 557 million (in 2014, NIS 707 million).

**8.3** The Group companies reviewed the useful life of the property, plant and equipment through the depreciation committee, in order to determine the estimated useful life of their equipment. The change is not expected to have a material impact on the depreciation expenses of the Group. Following the findings of the committees, minor changes were made in the estimated useful life of certain assets.

**8.4** Most of the real estate assets used by the Company are leased under a capitalized finance lease from the Israel Lands Administration as from 1993 for 49 years, with an option for an extension of another 49 years. Lease rights are amortized over the term of the lease period.

**8.5** In 2013, the Company started to install a fiber optic network that will reach the subscriber's home. As at December 31, 2015, the unexercised investment in assets amounts to NIS 294 million.

**8.6** At the reporting date, there are agreements to purchase property, plant and equipment amounting to NIS 75 million (in 2014, NIS 88 million).

**8.7** In accordance with the Telecommunications Order (Telecommunications and Broadcasts) (Determination of Essential Service Provided by Bezeq The Israel Telecommunication Corp. Ltd.), 1997, approval from the Prime Minister and Minister of Communications is required to confer rights in some of the Company's assets (including switches, cable network, transmission network, and information and databases).

**8.8** In accordance with its cellular license, Pelephone is not permitted to sell, lease or pledge any of its assets used for the implementation of the license, without the consent of the Minister of Communications, except for:

A. A pledge on one of the license assets in favor of a bank operating lawfully in Israel, to receive bank credit, provided that it submitted notice to the Ministry of Communications regarding the pledge it intends to register, noting that the pledge agreement includes a clause ensuring that in any event, exercise of the rights by the bank will not impair, in any way, the services provided under the license.

B. Sale of items of equipment when implementing an upgrade, including sale of equipment by the trade-in method.

**8.9** For information about pledges for loans and borrowings, see Note 12.

# 9. Intangible Assets

| | Goodwill | Software and licenses | Cellular communication usage rights | Customer relations and brand - multichannel television | Other | Total |
|---|---|---|---|---|---|---|
| | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million |
| Cost | | | | | | |
| Balance as at January 1, 2014 | 1,225 | 1,243 | 384 | - | 291 | 3,143 |
| Acquisitions or additions from in-house development | - | 162 | - | - | 15 | 177 |
| Disposals | - | (68) | - | - | (9) | (77) |
| Deconsolidation | (179) | - | - | - | (86) | (265) |
| Balance as at December 31, 2014 | 1,046 | 1,337 | 384 | - | 211 | 2,978 |
| Acquisitions or additions from in-house development | **-** | **188** | **96** | **-** | **28** | **312** |
| Consolidation | **385** | **148** | **-** | **1,137** | **-** | **1,670** |
| Disposals | **-** | **(60)** | **-** | **-** | **(51)** | **(111)** |
| Balance as at December 31, 2015 | **1,431** | **1,613** | **480** | **1,137** | **188** | **4,849** |
| **Amortization and impairment losses** | | | | | | |
| Balance as at January 1, 2014 | 53 | 712 | 146 | - | 172 | 1,083 |
| Amortization for the year | - | 205 | 28 | - | 28 | 261 |
| Disposals | - | (68) | - | - | (9) | (77) |
| Deconsolidation | (47) | - | - | - | (35) | (82) |
| Balance as at December 31, 2014 | 6 | 849 | 174 | - | 156 | 1,185 |
| Amortization for the year | **-** | **242** | **31** | **141** | **20** | **434** |
| Disposals | **-** | **(60)** | **-** | **-** | **(42)** | **(102)** |
| Balance as at December 31, 2015 | **6** | **1,031** | **205** | **141** | **134** | **1,517** |
| **Carrying amount** | | | | | | |
| January 1, 2014 | 1,172 | 531 | 238 | - | 119 | 2,060 |
| December 31, 2014 | 1,040 | 488 | 210 | - | 55 | 1,793 |
| December 31, 2015 | **1,425** | **582** | **275** | **996** | **54** | **3,332** |

## 9.1. Assessment of impairment of cash-generating units that include goodwill

To assess impairment, goodwill was attributed to the Group's operating segments as follows:

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Cellular communications (Pelephone) | **1,027** | 1,027 |
| Domestic fixed-line communication (Bezeq) * | **265** | - |
| Multichannel television (DBS) * | **120** | - |
| Other | **13** | 13 |
| | **1,425** | 1,040 |

* Goodwill acquired in the business combination with DBS, as described in Note 11.2 below.

## 9.2. Assessment of cellular communications goodwill (Pelephone)

The value in use for Bezeq Group of a cellular cash-generating unit (Pelephone), was calculated using the future discounted cash flow (DCF) method, based on the expected cash flow for the next five years. The expected cash flow is based on Pelephone's results in recent years, such that future growth and market shares are affected by directions in the cellular market, such as price competition, regulation and the operation scope of the new cellular operators. The revenue forecast is based on assumptions regarding the number of users, average revenue per user, and sales of terminal equipment. The main assumption underlying the forecast is the recovery in Pelephone's business activity as from 2017, due to the expected stabilization of the market and the start of competitive balance. In addition, the valuation included synergies on the Group revenue level based on the high certainty of the structural separation in the long term.

The operating, sales, marketing and investment expenses were adjusted for Pelephone's volume of operations. The cost of nominal capital used is 10% (after tax). In addition, it was assumed that the permanent growth will be 2.5%. The valuation was made by an independent appraiser. Based on this valuation, the Group was not required to record amortization for impairment of a cellular communication cash-generating unit.

## 9.3. Assessment of goodwill impairment in domestic fixed-line communications (Bezeq)

The value in use for Bezeq Group of a domestic fixed line cash-generating unit was calculated using the future discounted cash flow (DCF) method, based on the expected cash flow for the next five years. The expected cash flow is based on results of the domestic fixed-line communications segment in recent years, taking into account the effect of opening up the wholesale market in 2015. The revenue forecast is based on assumptions about the number of users and average revenue per user of internet infrastructure, the number of users and average revenue per user of telephony services, and revenue from transmission, data communication and other revenue. The main assumption underlying the forecast is that the wholesale market will function properly and will provide effective competition to the infrastructure owners. In addition, the effect of the elimination of the structural separation on the domestic fixed-line communication segment was not taken into account.

The operating, sales, marketing and investment expenses were adjusted for domestic-fixed line communication operations. The price of nominal capital used is 7.5% (after tax). In addition, it was assumed that the permanent growth will be 1%. The valuation was made by an independent appraiser. Based on this valuation, the Group was not required to record amortization for impairment of a fixed line domestic communications cash-generating unit.

## 9.4. Assessment of goodwill impairment for multichannel television (DBS)

The value in use for Bezeq Group of a multichannel television cash-generating unit was calculated using the discounted cash flow (DCF) method, based on the expected cash flow for the next five years. The expected cash flow is based on the results of DBS in recent years, such that future growth and market shares are affected by directions in the multichannel television market, such as competition, regulation, and the entry of new players. The revenue forecast is based on assumptions regarding the number of users and average revenue per user. The main assumption underlying the forecast is erosion in market share and a decrease in average revenue per user due to the expected increase in competition in the coming years.

The operating, sales, marketing and investment expenses were adjusted for the volume of operations of DBS. The price of nominal capital used is 8.5% (after tax). In addition, it was assumed that the permanent growth will be 1%. The valuation was made by an independent appraiser. Based on this valuation, the Group was not required to record amortization for impairment of a multichannel television cash-generating unit.

# 10. Deferred Expenses and Non-Current Investments

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Deferred expenses (see Note 10.1 below) | **256** | 253 |
| Non-current investments (see Note 10.2 below) | **105** | 99 |
| | **361** | 352 |

**10.1** Deferred expenses include prepaid expense amounts for acquisition of an indefeasible right of use (IRU) of seabed cable capacities. The prepaid expense is amortized on a straight-line basis up to 2022 and 2027 according to the period set out in the agreements.

**10.2** Non-current investments include a bank deposit for loans to the Company's employees with a redemption date that has yet to be determined and a deposit for hedge transactions.

# 11. Investees

## 11.1. Subsidiaries:

The place of incorporation of the companies held directly by the Company is Israel. Information about companies held directly by the Company and the Company's rights in capital:

| | Company's equity rights as at 31 December | |
|---|---|---|
| | 2015 | 2014 |
| Pelephone Communications Ltd. | **100%** | 100% |
| Bezeq International Ltd. | **100%** | 100% |
| Bezeq Online Ltd. | **100%** | 100% |
| Bezeq Zahav (Holdings) Ltd. | **100%** | 100% |
| Walla! Communications Ltd. | **100%** | 100% |
| DBS Satellite Services (1998) Ltd., see Note 11.2 for information about the business combination in 2015. | **100%** | 49.78% |
| Stage One Venture Capital Fund | **-** | 71.8% |

The Company's subsidiaries have investments in other subsidiaries that are not material.

## 11.2. Business combination in 2015

11.2.1 Acquisition transaction

As of December 31, 2014, the Company holds 49.78% of the share capital of DBS and it holds options that confer the right to 8.6% in DBS shares, which the Company is unable to exercise. Accordingly, the Company accounted for its investment in DBS in accordance with the equity method.

On March 26, 2014, the Company received the decision of the Antitrust Authority, according to which, under the terms set out in the decision, the merger between the Company and DBS ("the Merger") will be permitted.

Further to the aforesaid, on February 10, 2015, the Board of Directors' subcommittee that was established for this matter, the audit committee and the Board of Directors of the Company approved the Company's engagement in a transaction with Eurocom DBS. In the transaction, the Company will acquire the entire holdings of Eurocom DBS in DBS ("the Acquisition Transaction"), which at this date represent 50.22% of the issued share capital of DBS (41.62% fully diluted) and all the shareholder loans provided by Eurocom to DBS. It was further decided that prior to the Acquisition Transaction, the Company and DBS will accept the merger terms and the Company will exercise the option granted, at no cost, for the allotment of DBS shares at a rate of 8.6% of the issued capital of DBS.

Under the terms of the acquisition transaction, the Company was required to pay Eurocom DBS NIS 680 million in cash on the closing date, against acquisition of the shares and shareholder loans. Eurocom DBS will also be entitled to two additional contingent considerations, as follows: the first additional consideration of up to NIS 200 million will be paid in accordance with the amount of the carry-forward losses of DBS used for tax purposes and the second additional consideration of up to NIS 170 million will be paid in accordance with the business results of DBS in the next three years.

On March 23, 2015, the general meeting of the Company's shareholders approved the acceptance of the merger terms and exercise of the option, and the Company's engagement in the Acquisition Transaction, as described above. Subsequently, the Company and DBS announced the acceptance of the merger terms, and on March 25, 2015, the Company exercised the option and it was allotted DBS shares at a rate of 8.6% of the issued capital of DBS, so that as from this date, the Company holds 58.4% of DBS. Accordingly, the Company consolidated the financial statements of DBS as from March 23, 2015 (the date that the general meeting approved exercise of the option to DBS shares by the Company). In view of the Company's holding of 49.78% of DBS shares prior to gaining control, the acquisition transaction was accounted for in the financial statements as a step acquisition.

The Company's engagement in the transaction with Eurocom DBS for acquisition of the entire holdings of Eurocom DBS in DBS is subject to the approval of the Ministry of Communications for transfer of control in DBS such that the Company will control DBS and will hold the entire issued and paid up share capital of DBS. This approval was received unconditionally on June 23, 2015, and on June 24, 2015, the transaction was completed. On the completion date, the Company transferred the cash consideration of NIS 680 million to Eurocom DBS and Eurocom DBS transferred its rights and the rights to DBS shares to the Company and assigned to the Company its entire rights in the shareholders loans of DBS. On completion of the transaction, DBS became a wholly owned subsidiary (100%) of the Company.

As at December 31, 2015, the Company has a liability to Eurocom DBS for the first additional consideration of NIS 204 million (including accrued interest) and NIS 29 million for the second additional consideration.

11.2.2 <u>Valuation at the acquisition date</u>

At the date of the business acquisition, the Company presented its investment in shares, share options and loans to DBS prior to acquisition of control, according to the equity method based on a valuation by an independent assessor. In accordance with the valuation, the fair value of the Company's investments prior to acquisition of control is estimated at NIS 1.076 billion. Accordingly, the Company recognized a profit of NIS 12 million from the gain of control under other operating income in the statement of income.

The valuation was based on the income approach, whereby the discounted cash flow method (DCF) was applied on the basis of the forecasted cash flow for 2015 through to 2019. The cash flow forecast was based on the results of DBS for 2011-2014 and the three months ended March 31, 2015. In the valuation, it was assumed that the market share of DBS is expected to remain stable and will be 42%-43% throughout the years of the forecast. It was also assumed that gradual erosion in the ARPU of DBS is expected between 2015 and 2018, while in 2019 and thereafter, it is expected that a fixed nominal ARPU will be maintained. The revenue forecast was based on the forecast of the number of users, average income and competition in the market.

Assumed cost of capital: 8.5% (net of tax). In addition, it was assumed that the permanent growth will be 1%.

The valuation was based on assumptions regarding the identity of the relevant market participant that might acquire the Company's holdings in DBS and does not take into account the specific operational and tax synergies between the companies.

11.2.3 Identifiable assets and liabilities acquired in a business combination:

| | March 23, 2015 |
|---|---|
| | NIS million |
| Cash and cash equivalents | 299 |
| Trade and other receivables | 182 |
| Broadcasting rights | 449 |
| Property, plant and equipment | 801 |
| Intangible assets (including excess cost attributed to customer relations and brand as described below) | 1,284 |
| Deferred tax asset, net of deferred tax liabilities (see Note 11.2.4 C below) | 1,170 |
| Debentures, loans, and borrowings (including excess cost attributed to debentures as described below) | (1,946) |
| Trade payables and other liabilities | (632) |
| Contingent liabilities (including excess cost attributed to contingent liabilities as described below) | (19) |
| **Identifiable assets, net** | **1,588** |

11.2.4 Attribution of identifiable excess cost in the business combination

The Company attributed the acquisition cost in relation to the fair value of the assets and liabilities that were acquired in the business combination. The attribution was based on the valuation prepared by an external assessor. During the year, the attribution was adjusted as follows:

| | March 23, 2015 |
|---|---|
| | NIS million |
| Customer relations (see section A below) | 790 |
| Brand (see section B below) | 347 |
| Deferred tax asset, net of deferred tax liabilities (see section C below) | 1,170 |
| Debentures (see section D below) | (160) |
| Contingent liabilities (see section E below) | (10) |
| Goodwill (see section F below) | 385 |
| Total excess cost | 2,522 |

A. **Customer relations**: The valuation was based on the income approach, using the multi-period excess earning method. Under this approach, the value of the asset is derived from the present value of the cash flows that are expected to arise from it over the remaining economic life of the asset. Amortization will be based on the customer churn rate.

B. **Brand**: The valuation was prepared in accordance with the relief from royalty method. In accordance with this method, the value of the asset is estimated as the present value of the appropriate royalty that the entity would have to pay a third party for the use of the asset, if the company did not own it. The useful life of the brand assumed in the model is 12 years.

C. **Deferred tax asset**: Following completion of the acquisition transaction on June 24, 2015, and in accordance with the agreement in principle that was made with the Tax Authority regarding use of the carry-forward losses of DBS, the Company believes that will be able to take advantage of the tax asset for the accrued losses from future profits of DBS and due to the possible merger between the companies.

The Company accounted for completion of the acquisition transaction and the agreement in principle that was made with the Tax Authority as described in Note 6.6 after acquiring control, as new information obtained in the measurement period regarding the facts and circumstances that existed at the acquisition date and, therefore, as at December 31, 2015, the Company recognized a deferred tax asset at the date control was acquired and updated the liability for the first contingent consideration accordingly (retrospectively).

Composition of the tax asset:

| | March 23, 2015 |
|---|---|
| | NIS million |
| Tax asset for cumulative losses of DBS | 1,426 |
| Tax reserve for attributed excess cost | (256) |
| Deferred tax asset, net | 1,170 |

D. **Debentures:** The excess cost reflects the fair value of the debentures at the acquisition date based on a capitalization rate of 1.9%-2.3%.

E. **Contingent liabilities**: The amounts represent a present obligation arising from a class action filed by DBS customers.

F. **Goodwill:** Following the business combination with DBS, goodwill was recognized as follows:

| | March 23, 2015 |
|---|---|
| | NIS million |
| Consideration value | 897 |
| Fair value of the investment in DBS prior to the acquisition | 1,076 |
| Less the fair value of net identifiable assets | (1,588) |
| Goodwill | 385 |

To assess impairment, goodwill of NIS 265 million was allocated to the domestic-fixed line communications segment, and goodwill of NIS 120 million was allocated to the multichannel television segment. Goodwill is allocated on the basis of the valuation of an external assessor and the Company's estimates regarding the cash-generating units that are expected to benefit from the synergy of the business combination.

11.2.5 Effect of the business combination on the statement of income

The contribution of DBS to Group revenue in 2015 amounted to NIS 1,333 million and its contribution to profit as from the date of the business combination amounted to NIS 49 million (this amount includes amortization of surplus cost amounting to NIS 43 million).

The management estimates that had the business combination taken place on January 1, 2015, the revenue in the consolidated statement of income would have increased by NIS 434 million and there would have been no significant change in consolidated profit in 2015. When determining the amounts, the management assumed that the fair value adjustments at the date of the business combination are the same as the adjustments that would have been received had the business combination taken place on January 1, 2015.

11.2.6 Shareholder loans

The Company provided a shareholder loan to DBS between 1999 and 2005. In addition, at the acquisition date of the rights of Eurocom in DBS in June 2015, as described in section 11.2.1 above, the Company acquired the shareholders loan provided by Eurocom to DBS. The total amount of the shareholder loans in accordance with the contractual terms and fair value as at December 31, 2015 (including interest and linkage differences) is NIS 5.1 billion and NIS 1.4 billion, respectively.

For the purpose of rating the Debentures (Series A) issued by DBS, with a balance of NIS 368 million as at December 31, 2015 (as described in Note 12.4 below), in 2007, DBS undertook to S&P Maalot (and to S&P Maalot alone) that it would not make any repayment on account of the shareholder loans proved to it up to the date that the undertaking is provided, until the end of the life of the debentures in July 2017.

It is noted that in December 2015, the Company provided another shareholder loan to DBS, amounting to NIS 323 million, as described in Note 12.4.3 below.

11.2.7 Financial position of DBS

Since the beginning of its operations, DBS has accumulated considerable losses. The losses of DBS in 2015 and 2014 amounted to NIS 354 million and NIS 322 million, respectively. As a result of these losses, as at December 31, 2015, DBS had an equity deficit and a working capital deficit of NIS 5,018 million and NIS 584 million, respectively.

The management of DBS believes that the financial resources at its disposal, which include the deficit in working capital and receipt of loans from the Company, will be sufficient for its operations for the coming year, based on the cash flow forecast approved by DBS's board of directors.

### 11.3. Equity-accounted associates

The Group's investment in associates as at December 31, 2015 includes the Company's investments in immaterial associates amounting to NIS 25 million.

The Group's investment in associates as at December 31, 2014 included the Company's investment in DBS amounting to NIS 1,026 million and from investments in other immaterial associates amounting to NIS 31 million. In 2015, the Company acquired control in DBS and started to consolidate its financial statements as described in Note 11.2 above.

## 12. Debentures, Loans and Borrowings

### 12.1. Composition:

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Current liabilities | | |
| Current maturities of debentures | **1,202** | 862 |
| Current maturities of bank loans | **711** | 619 |
| | **1,913** | 1,481 |
| Non-current liabilities | | |
| Debentures | **6,291** | 5,451 |
| Bank loans | **2,509** | 3,155 |
| | **8,800** | 8,606 |
| | | |
| | **10,713** | 10,087 |

## 12.2. Debentures and loan terms

| | | December 31, 2015 | | December 31, 2014 | | |
|---|---|---|---|---|---|---|
| | Note | Carrying amount | Nominal value | Carrying amount | Nominal value | Interest rate range |
| | | NIS million | NIS million | NIS million | NIS million | |
| **Loans** | | | | | | |
| Total unlinked loans at variable interest | 12.3 | **1,331** | **1,331** | 1,656 | 1,656 | Prime -0.33% to +0.2% |
| Total unlinked loans at fixed interest | 12.3 | **1,589** | **1,589** | 1,796 | 1,796 | 6.85% - 5% |
| Total unlinked loans at fixed interest | 12.3 | **300** | **300** | 300 | 300 | 2.4% |
| CPI-linked loans at fixed interest | | **-** | **-** | 22 | 18 | 4.45%-4.6% |
| **Total loans** | | **3,220** | **3,220** | 3,774 | 3,770 | |
| **Debentures issued to the public** | | | | | | |
| CPI-linked debentures at fixed interest - Series 5 | 12.3.1 | **310** | **251** | 613 | 503 | 5.3% |
| CPI-linked debentures at fixed interest - Series 6 | 12.3 | **3,087** | **2,874** | 3,165 | 2,874 | 3.7% |
| Unlinked debentures at variable interest - Series 7 | 12.3 | **734** | **734** | 734 | 734 | One year Makam +1.4% |
| Unlinked debentures at fixed interest - Series 8 | 12.3 | **886** | **886** | 1,329 | 1,329 | 5.7% |
| Unlinked debentures at fixed interest - Series 9 | 12.3 | **388** | **388** | - | - | 3.65% |
| CPI-linked debentures at fixed interest - Series 10 | 12.3 | **400** | **400** | - | - | 2.2% |
| **Total debentures issued to the public** | | **5,805** | **5,533** | 5,841 | 5,440 | |
| **Non-marketable debentures issued to financial institutions:** | | | | | | |
| Unlinked debentures at fixed interest | 12.3 | **400** | **400** | 400 | 400 | 6.65% |
| CPI-linked debentures at fixed interest | 12.4 | **1,288** | **1,097** | - | - | 5.35%-8.4% |
| CPI-linked debentures at fixed interest | | **-** | **-** | 72 | 58 | 4.4%-4.6% |
| **Total debentures issued to financial institutions** | | **1,688** | **1,497** | 472 | 458 | |
| **Total debentures** | | **7,493** | **7,030** | 6,313 | 5,898 | |
| **Total interest-bearing liabilities** | | **10,713** | **10,250** | 10,087 | 9,668 | |

## 12.3. Loans and debentures issued by the Company

Below are details of the terms that the Company undertook for the loans that were received and the debentures that were issued:

12.3.1 For Debentures (Series 5), standard grounds were established for immediate repayment, including breach events, insolvency, dissolution procedures or receivership.

12.3.2 For Debentures (Series 6 to 10) and bank loans and for debentures issued to financial institutions in the amount of NIS 400 million, the Company has undertaken not to create additional pledges on its assets unless pledges are created at the same time in favor of the debenture holders and the lending banks (negative lien). The lien includes exceptions, including regarding a lien on assets that will be purchased or expanded by the Company, if the undertakings underlying the lien are created for the purchase or expansion of those assets and for the matter of a token lien.

12.3.3 For Debentures (Series 6 to 8) and bank loans and for debentures issued to financial institutions in the amount of NIS 400 million, standard grounds were included for immediate repayment of the debentures and loans, including breach events, insolvency, dissolution procedures or receivership. In addition, a right was determined to call for immediate repayment if a third party lender calls for immediate repayment of the Company's debts in an amount exceeding the amount determined.

12.3.4 For Debentures (Series 6 to 10) and banks loans in the amount of NIS 2.03 billion as at December 31, 2015 (out of the total bank loans in the amount of NIS 3.2 billion), and for debentures issued to financial institutions in the amount of NIS 400 million, the Company has undertaken that if it the Company makes an undertaking towards any entity in respect of compliance with financial covenants, the Company will also provide the same undertaking to these debenture holders and banks (subject to certain exceptions).

12.3.5 For Debentures (Series 6 to 10), the Company has undertaken to the debenture holders to take steps so that, to the extent under its control, the debentures will be rated by at least one rating agency, so long as there are debentures of the relevant series in circulation.

12.3.6 In addition, for Debentures (Series 9 and 10), standard grounds were included for immediate repayment of the debentures, including events of default, insolvency, liquidation proceedings, or receivership, as well as the right to call for immediate repayment if a third party lender calls for immediate repayment of the Company's debts (in an amount exceeding NIS 150 million, if another series of marketable debentures is called for immediate repayment - an unlimited amount), in the event of the sale of more than 50% of the Group's assets (consolidated) such that communications will cease being the Group's main activity, in the event of a change of control following which the current controlling shareholders in the Company will cease being controlling shareholders (other than transfer of control to a transferee that received approval to control the Company in accordance with the provisions of the Communications Law or change in control under other circumstances that were established), in the event that a going concern qualification is recorded in the Company's financial statements for two consecutive quarters, in the event of a material deterioration in the Company's business compared with the situation at the time of the issue, and there is real concern that the Company will not be able to repay the debentures on time (as set out in section 35I(1)(a)(1) in the Securities Law), all under the terms set out in the deed of trust of the debentures.

As at December 31, 2015 and the approval date of the financial statements, the Company was in compliance with all its liabilities, there were no grounds to call for immediate repayment, and financial covenants were not set out as described above.

## 12.4. Non-marketable debentures issued by DBS

12.4.1 DBS has two series of debentures with a balance of NIS 1,288 million as at December 31, 2015. The debentures were issued for institutional investors and were listed on the TACT-Institutional system of the TASE. Below are details of the terms that DBS undertook in respect of the debentures:

A. Standard events were established (such as insolvency proceedings, default and exercise of pledges on most of the Company's assets), which, should they occur, after the warning periods that were established, will allow the right to call for immediate repayment of the debentures subject to the provisions in the deeds of trust, and the right to call for immediate payment if another debenture series issued by DBS is called for immediate repayment, if the balance for settlement exceeds the amount set out in the deed of trust ( a right that was cancelled for Debentures (Series B), following a letter of guarantee provided by the Company as described in section 12.4.2 below).

B. In accordance with the deed of trust for Debentures (Series A) (with a par value of NIS 305 million as at December 31, 2015), DBS created an unlimited floating first lien in favor of Trustee A on all of its assets (other than exemptions arising from the provisions of the Communications Law), including a stipulation that limits additional pledges (subject to the exceptions set out in Deed of Trust A and the mortgage deed), and (subject to exceptions in accordance with the Communications Law) unlimited fixed first pledges on the rights and assets of DBS, including its rights under material agreements to which it is a party, its unissued registered capital, goodwill, certain intellectual property rights and insurance rights under its insurance policies.

Under Deed of Trust A, DBS may register first pledges in favor of additional holders of debentures that it might issue and/or add them to pledges in favor of Trustee A, without the consent of Trustee A.

12.4.2 In September 2015, the Company signed a letter of guarantee for the undertakings of DBS to pay the entire balance of its debts of NIS 1.05 billion to holders of Debentures (Series B), (amounting to NIS 792 million as at December 31, 2015) against a reduction of 0.5% in the annual interest rate for the debenture and cancellation of securities (which were similar to those registered in favor of Trustee A) and certain provisions of the deed of trust and the debenture (including the DBS's undertaking to comply with the financial covenants and restrictions on distribution of a dividend by DBS), all in accordance with the terms of the deed of trust of the debenture and the debenture. In accordance with the terms of the debenture, a reduction in the interest rate and cancellation of the collateral and certain provisions in the debentures are contingent on the rating of the Company not falling below a rating of AA- by Maalot or a corresponding rating ("the Minimum Rating"), a condition that was fulfilled as at the date of the guarantee. If, in the future, the rating of the Company falls below the Minimum Rating, then the reduction in the interest rate will be cancelled, the collateral that was cancelled will be provided again, the provisions that were cancelled will be applicable again, and the guarantee will expire.

12.4.3 Up to December 2015, DBS was a party to another debenture series opposite several institutions ("the 2012 Debentures"). On December 20, 2015, DBS paid the full unpaid balance of Debenture 2012 ahead of its repayment date plus a premature repayment fee of NIS 323 million through a loan provided by the Company at that date.

## 12.5. Reportable credit

Below is information about the Group's reportable credit, in accordance with Legal Bulletin No. 104-15: Reportable Credit Events, issued by the Israel Securities Authority on October 30, 2011. All loans and debentures were taken by the Group without a specific purpose. The loan principal is repayable in equal payments with the interest payable on the outstanding loan principal, as set out in the table below.

| Lender | Date of loan | Date of final repayment | Type of loan | Amount of the original loan or par value (NIS million) | Estimated reserve (plus interest payable) December 31, 2015 (NIS million) | Number of principal payments in the year | Principal payments as from | Number of interest payments in the year | Interest rate December 31, 2015 | Fair value of the liability December 31, 2015 (NIS million) | Imputed effective interest at fair value as at December 31, 2015 | Imputed effective interest at fair value as at December 31, 2014 | Special conditions | Right to early repayment |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Bank A* | May 12, 2011 | November 12, 2020 | Unlinked fixed interest NIS | 500 | 505 | 2 | 2017 | 2 | 6.85% | 576 | 2.1% | 2.55% | Notes 12.3.2 to 12.3.4 | Yes |
| Bank B** | May 12, 2011 | November 12, 2020 | Unlinked variable interest NIS | 500 | 501 | 2 | 2017 | 2 | Prime + 0.2% | 501 | 1.8% | 1.95% | Notes 12.3.2 to 12.3.4 | Yes |
| Debentures (Series 5) | June 1, 2004 | June 1, 2016 | CPI-linked fixed interest | 1,507 | 318 | 1 | 2011 | 1 | 5.30% | 322 | 2.1% | 0.97% | Note 12.3.1. | No |
| Debentures (Series 6) | July 3, 2011 | December 1, 2022 | CPI-linked fixed interest | 2,874 | 2,962 | 1 | 2018 | 2 | 3.70% | 3,278 | 1.43% | 1.45% | Notes 12.3.2 to 12.3.5 | No |
| Debentures (Series 7) | July 3, 2011 | December 1, 2022 | Unlinked variable interest NIS | 734 | 735 | 1 | 2018 | 4 | Makam + 1.4% | 751 | 1.08% | 0.93% | Notes 12.3.2 to 12.3.5 | No |
| Debentures (Series 8) | July 3, 2011 | June 1, 2017 | Unlinked fixed interest NIS | 1,329 | 890 | 1 | 2015 | 2 | 5.70% | 933 | 0.46% | 0.85% | Notes 12.3.2 to 12.3.5 | No |
| Debentures (Series 9) | October 15, 2015 | December 1, 2025 | Unlinked fixed interest NIS | 388 | 390 | 1 | 2022 | 2 | 3.65% | 407 | 3.08% | - | Note 12.3 | No |
| Debentures (Series 10) | October 15, 2015 | December 1, 2025 | CPI-linked fixed interest | 400 | 401 | 1 | 2022 | 2 | 2.2% | 406 | 2.04% | - | Note 12.3 | No |
| DBS Debentures (Series A) | July 5, 2007 | July 5, 2017 | CPI-linked fixed interest | 808 | 376 | 1 | 2010 | 2 | 8.4% | 400 | 1.79% | 2.44% | Note 12.4 | No |
| DBS Debentures (Series B) | November 8, 2010 | November 8, 2019 | CPI-linked fixed interest | 1,244 | 841 | 1 | 2013 | 2 | 5.35% | 914 | 1.61% | 2.62% | Note 12.4 | No |

* The Group's loans from Bank A amount to NIS 964 billion

* The Group's loans from Bank B amount to NIS 1.764 billion

For information about the Company's agreements for undertakings to provide credit for 2016-2017, see Note 12.6 below.

### 12.6. Undertakings to provide credit for 2016-2017

In 2015, the Company entered into agreements with banks and financial institutions, whereby the Company received an undertaking from these institutions to provide credit to the Company in a total amount of NIS 1.4 billion to refinance its future debt in 2016 (with an average duration of between 4.6 to 4.9 years and a fixed NIS interest rate of 3.7% to 4.3 %), and an undertaking to provide credit of NIS 600 million in 2017 (with an average duration of 4.5 years and an average fixed NIS interest rate of 4.3%).

The terms of all the undertakings and the loans to be provided thereunder include terms that are similar to the terms provided for other loans taken by the Company, as described in section 12.3 above, including the following: an undertaking to refrain from creating additional pledges on the Company's assets (with certain restrictions); an undertaking that if the Company assumes an undertaking towards a party in respect of compliance with financial covenants, the Company will also assume the same undertaking for this credit (subject to certain exceptions); and standard terms for immediate repayment (such as default events, insolvency, liquidation or receivership), and cross default (with certain restrictions), which will also apply, with the required changes, to the periods of the undertaking to provide credit.

In addition, some of the undertakings to provide credit in 2017 also include terms that are similar to the terms that were established for Debentures (Series 9 and 10) as set out in Note 12.3.6 above.

Subsequent to the date of the financial statements, the Company signed another agreement to provide a loan of NIS 300 million in 2017.

## 13. Trade and Other Payables

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| **Trade payables (open accounts)*** | **913** | 664 |
| **Other payables, including derivatives** | | |
| Liabilities to employees and other liabilities for salaries | **369** | 324 |
| Institutions | **79** | 127 |
| Expenses due | **90** | 110 |
| Accrued interest | **72** | 64 |
| Deferred income | **85** | 50 |
| Derivative instruments | **22** | 16 |
| Other | **27** | 19 |
| **Total other payables** | **744** | 710 |
| **Total trade and other payables** | **1,657** | 1,374 |

* Of which, the carrying amount of trade payables that are related parties and interested parties as at December 31, 2015 amounts to NIS 17 million (as at December 31, 2014, NIS 3 million).

## 14. Provisions

| | Customer claims | Additional legal claims | Dismantling and clearing of cellular and other sites | Total |
|---|---|---|---|---|
| | NIS million | NIS million | NIS million | NIS million |
| **Balance as at January 1, 2015** | 24 | 35 | 72 | 131 |
| Provisions created | **18** | **13** | **1** | **32** |
| Provisions used | **(4)** | **(4)** | **(4)** | **(12)** |
| Provisions canceled | **(3)** | **(2)** | **(20)** | **(25)** |
| Consolidation of DBS | **17** | **3** | **-** | **20** |
| **Balance as at December 31, 2015** | **52** | **45** | **49** | **146** |
| Presented in the statement of financial position as: | | | | |
| Current provisions | **52** | **45** | 3 | 100 |
| Non-current provisions | **-** | **-** | 46 | 46 |
| | **52** | **45** | 49 | 146 |

For further information about legal claims, see Note 16.

## 15. Employee Benefits

Employee benefits include post-employment benefits, other long-term benefits, termination benefits, short-term benefits and share-based payments. For further information about share-based payments, see Note 25 below.

### 15.1. Liabilities for employee benefits

| | | 2015 | 2014 |
|---|---|---|---|
| | Note | NIS million | NIS million |
| **Current liabilities for:** | | | |
| Holiday | | **104** | 86 |
| Sick pay | 15.4 | **117** | 111 |
| Voluntary redundancy | 15.5 | **150** | 55 |
| Current maturities of pensioner benefits | 15.3.4 | **7** | 7 |
| Total current liability for employee benefits | | **378** | 259 |
| Non-current liabilities for: | | | |
| * Liability for pensioner benefits | 15.3.4 | **114** | 121 |
| Severance compensation (net) (see composition below) | 15.3.1 | **55** | 48 |
| Early notice | 15.3.3 | **16** | 20 |
| Pension | 15.3.2 | **55** | 44 |
| Total non-current liabilities for employee benefits | | **240** | 233 |
| Total liabilities for employee benefits | | **618** | 492 |
| **Composition of liabilities for severance pay:** | | | |
| Liabilities for severance pay | | **221** | 215 |
| Fair value of plan assets | | **(166)** | (167) |
| | | **55** | 48 |

## 15.2. Defined contribution plans

15.2.1 Liabilities for employee benefits at retirement age in respect of the period of their service in the Company and its subsidiaries, and for employees to which Section 14 of the Severance Pay Law – 1963 applies, are covered in full by regular payments to pension funds and insurance companies

| | 2015 | 2014 | 2013 |
|---|---|---|---|
| | NIS million | NIS million | NIS million |
| Amount recognized as an expense for a defined contribution plan | **199** | 191 | 182 |

15.2.2 The pension rights of Company employees for the period of their employment in the civil service through January 31, 1985, are covered by a pension fund ("the Makefet Fund"), which assumed the State's obligation following an agreement between the Government of Israel, the Company, the Histadrut and the Makefet Fund.

15.2.3 The severance obligation to employees who leave their employment on terms entitling them to compensation is covered, for the period from February 1, 1985, by regular contributions to such pension funds and insurance companies (in accordance with Section 14 of the Severance Pay Law).

Severance pay for the period of employment in the civil service through January 31, 1985, is paid by the Company, and the monies accumulated in the Makefet Fund for that period are kept in a fund that will be used for the employees' rights.

15.2.4 For certain employees, the Group has an obligation to pay severance in excess of the amount accumulated in the compensation fund which is in the employees' names. See section 15.3.1 below.

## 15.3. Defined benefit plans

Obligations for defined benefit plans in the Group include the following:

15.3.1 The severance obligation for the balance of the obligation not covered by contributions and/or insurance policies in accordance with the existing labor agreements, the Severance Pay Law, and the salary components which the managements of the companies believe entitle the employees to receive compensation. For this part of the obligation, there are deposits in the name of Group companies in pension funds and insurance companies. The deposits in pension funds and insurance companies include accrued linkage differences and interest. Withdrawal of the reserve monies is contingent upon fulfillment of the provisions in the Severance Pay Law.

15.3.2 An obligation in accordance with the collective agreement of 2006 for employees who transferred from civil service to the Company, and who are entitled, following retirement, to a supplement in pension payments for the difference between the Civil Service Law and the standard policy of Makefet. The Company also has an obligation to a number of senior employees who are entitled to voluntary redundancy terms (pension and retirement grants) which are not dependent on the existing retirement agreements for all employees

15.3.3 An obligation in accordance with the employment agreements of some of the senior employees in the Group for payment of a benefit for notice upon severance.

15.3.4 Company retirees receive, in addition to pension payments, benefits which consist mainly of a holiday gift (linked to the dollar exchange rate), financing for the upkeep of retiree clubs and social activities The Company's liability for these costs accumulates during the employment period. The Company’s financial statements include the liabilities for expected costs in the severance period.

## 15.4. Provision for illness (other long-term benefit)

The financial statements include a provision in respect of redemption and use of sick leave. The right to accumulate sick leave was taken into account for all employees in the Group. Only employees eligible under the terms of the employment agreement may redeem sick leave. The provision was computed on the basis of an actuarial calculation, including the assumption of positive accumulation of days by most of the employees and use of days by the last in first out (LIFO) method.

## 15.5. Termination benefits

15.5.1 According to the collective agreement of December 2006, between the Company and the employees union and the New Histadrut, and according to the amendment to the agreement of August 2015, the Company may, at its discretion, terminate the employment of 163 permanent employees in each of the years 2015-2021 (the Company's right is accumulated over the years).

The Company recognizes expenses for voluntary redundancy when the Company is committed demonstrably, without realistic possibility of withdrawal, to a defined plan to terminate employment before the defined date, according to a defined plan. The collective agreement allows the Company to dismiss employees, but does not create a demonstrable commitment without realistic possibility of withdrawal. Accordingly, the expenses for voluntary redundancy are recognized in the Company's financial statements at the approval date of the plan.

In 2015, voluntary redundancy expenses amounted to NIS 117 million.

## 15.6. Actuarial assumptions

The main actuarial assumptions for defined benefit plans at the reporting date are as follows:

15.6.1 Mortality rates are based on the rates published in Insurance Circular 2013-3-1 of the Ministry of Finance.

15.6.2 Churn rates were determined on the basis of the past experience of the Company and the subsidiaries, distinguishing between different employee populations and taking into account the number of years of employment. The churn rates include a distinction between severance with entitlement to full severance compensation and severance without entitlement to this right.

15.6.3 The discount rate (nominal) is based on the yield on linked high-quality corporate debentures with maturity dates approximating those of the gross obligation.

15.6.4 The main discount rates are as follows:

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | Average discount rate | Average discount rate |
| Severance compensation | **4.1%** | 3.7% |
| Retirement benefits | **4.74%** | 4.7% |

15.6.5 Assumptions regarding salary increments for calculation of the liabilities were made on the basis of the management's assessments, distinguishing between the groups of employees. The main assumptions (in nominal terms) regarding salary increases of the main employee groups are as follows:

| | Salary increase assumptions |
|---|---|
| Permanent employees in the Company | Average adjustment of 7% for young employees, decreasing gradually to 2.7% at the age of 66. |
| Permanent employees in the Company | Average adjustment of 3.2% for young employees, decreasing gradually to 1.4% at the age of 66. |
| Company's employees that are not permanent | 6.5% for young employees decreasing gradually to 0%, 3.5% for senior employees |
| Pelephone employees | An increase of 3.1% as from 2015, as set out in the collective agreement at Pelephone |

Regarding the Company's employees, as well as the assumption of the age-dependent wage increase, an expected individual wage growth was assumed for 2016-2026, arising from the collective agreement that was signed in August 2015.

15.6.6 Sensitivity analysis for actuarial assumptions

Changes in the actuarial assumptions which are reasonably possible as at the reporting date, are not expected to have a material effect on the liabilities for employee benefits.

15.6.7 Average weighted useful life of liabilities for the main severance benefits:

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | **Years** | **Years** |
| Severance compensation | **10.2** | 10.9 |
| Retirement benefits | **14.4** | 15.7 |

## 16. Contingent Liabilities

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

In the opinion of the managements of the Group companies, based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include adequate provisions (as described in Note 14), where provisions are required to cover the exposure resulting from such claims.

In the opinion of the managements of the Group companies, the additional exposure (beyond these provisions) as at December 31, 2015 for claims filed against Group companies on various matters and which are unlikely to be realized, amounted to NIS 5.5 billion. There is also additional exposure of NIS 4 billion for claims, the chances of which cannot yet be assessed.

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

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

For updates subsequent to the reporting date, see section 16.2 below.

**16.1** Following is a detailed description of the Group's contingent liabilities as at December 31, 2015, classified into groups with similar characteristics:

| | | Provision | Additional exposure | Exposure for claims that cannot yet be assessed |
|---|---|---|---|---|
| **Claims group** | **Nature of the claims** | **NIS million** | | |
| Claims of employees and former employees of Group companies | Mainly collective and individual claims filed by employees and former employees of the Company in respect of recognition of various salary components as components for calculation of payments to Company employees, some of which have wide ramifications in the Company. | **10** | **115** | **-** |
| Customer claims | Mainly motions for certification of class actions concerning contentions of unlawful collection of payment and impairment of the service provided by the Group companies. | **52** | **3,112** | **4,083** |
| Supplier and communication provider claims | Legal claims for compensation for alleged damage as a result of the supply of the service and/or the product. | **3** | **222** | **6** |
| Claims for punitive damages, real estate and infrastructure | Claims for alleged physical damage or damage to property caused by Group companies and in relation to real estate and infrastructure.<br>The additional amount of exposure for punitive damages does not include claims for which the insurance coverage is not disputed. | **2** | **35** | **-** |
| Claims by enterprises and companies | Claims alleging liability of the Group companies in respect of their activities and/or the investments made in various projects. | **11** | **2,047*** | **-** |
| Claims by the State and authorities | Various claims by the State of Israel, government institutions and authorities (“the Authorities”). These are mainly procedures related to regulations relevant to the Group companies and financial disputes concerning monies paid by the Group companies to the authorities (including property taxes) or by the authorities to the Group companies. | **19** | **15** | **-** |
| **Total legal claims against the Company and subsidiaries** | | **97** | **5,546** | **4,089** |

* This sum includes a total exposure of NIS 2 billion for a claim filed by a shareholder against the Company and officers in the Company, which the plaintiff estimates at NIS 1.1 billion or NIS 2 billion (according to the method of calculating the damage to be determined).

**16.2** Subsequent to the reporting date, claims amounting to NIS 93 million were filed against Group companies. At the approval date of the financial statements, the chances of these claims cannot yet be assessed. In addition, claims with exposure of NIS 549 million came to an end.

## 17. Agreements

**17.1** Group companies have operating lease agreements for land, property and vehicles used by Group companies. The minimum future contractual rental payments during the next five years, calculated according to the rental fees in effect as at December 31, 2015, are as follows:

| | Real estate | Vehicles | Total |
|---|---|---|---|
| Year ended December 31 | NIS million | NIS million | NIS million |
| 2016 | **238** | **132** | **370** |
| 2017 | **227** | **104** | **331** |
| 2018 | **174** | **62** | **236** |
| 2019 | **139** | **-** | **139** |
| 2020 | **99** | **-** | **99** |
| 2021 onwards | **104** | **-** | **104** |
| | **981** | **298** | **1,279** |

**17.2** In May 2013, Pelephone signed an agreement with Apple International ("Apple") for continued acquisition and distribution of iPhones in Israel. According to the agreement, under certain circumstances, Pelephone is required to purchase a minimum number of iPhones every year for three years at the prices in effect at the manufacturer on the actual purchase date. Pelephone believes that, similar to previous years, these quantities will constitute a substantial part of the quantities of iPhones that it expects to sell in the agreement period.

**17.3** Pelephone has open orders for the acquisition of terminal equipment amounting to NIS 74 million (as at December 31, 2014, NIS 95 million).

**17.4** DBS has agreements for the acquisition of channels. In 2015, expenses for consumption of channels acquired by DBS amounted to NIS 287 million.

**17.5** For information about agreements for the acquisition of broadcasting rights by DBS, see Note 7. For information about agreements for the purchase of property, plant and equipment, see Note 8.6 above.

**17.6** On October 26, 2015, the District Planning and Building Committee approved the validation of the outline plan for an area of 70 dunam (net) for warehouses and offices in Saqiya (near the Messubim junction). As at this date, the Company is entitled to receive this area in a capitalized lease contract for 49 years that commenced on March 22, 1993 with an option to extend for another 49 years, for no consideration. This right was granted to the Company under the settlement agreement of May 15, 2003 between the Company and the government of Israel and the Israel Lands Administration, which was given the force of a court ruling on March 10, 2004. Exercise of the right is subject to approval from the planning institutions for planning the complex, which was received on October 26, 2015.

As at the reporting date, the fair value of the Company's rights to the land is estimated at NIS 450 million.

**17.7** For information about agreements for undertakings to provide credit for 2016-2017, see Note 12.6 above.

**17.8** For information about agreements with related parties, including the agreement between DBS and Space Communications Ltd. for the lease of space segments, see Note 28.3.2.

## 18. Securities, Pledges and Guarantees

The Group's policy is to provide tender, performance and legal guarantees. In addition, the Company provides bank guarantees, where necessary, for banking obligations of subsidiaries.

**18.1** The Group companies have guarantees of NIS 190 million in favor of the Ministry of Communications to secure the terms of their licenses (mostly linked to the USD exchange rate).

**18.2** The Group companies have bank guarantees totaling NIS 92 million in favor of third parties.

**18.3** For information about the conditions for loans and borrowings, see Note 12.

**18.4** For information about the guarantee provided by the Company in respect of DBS's liability for Debentures (Series B), see Note 12.4.2.

# 19. Capital

## 19.1. Share capital

| | Registered share capital | | Issued and paid up share capital | |
|---|---|---|---|---|
| | Number of shares | | Number of shares | |
| | December 31, 2015 | December 31, 2014 | December 31, 2015 | December 31, 2014 |
| Ordinary shares of NIS 1 par value | **2,825,000,000** | 2,825,000,000 | **2,762,148,573** | 2,743,283,920 |

## 19.2. Dividends

19.2.1 Dividend distribution policy

On August 4, 2009, the Board of Directors resolved to distribute a dividend to the shareholders amounting to 100% of the semi-annual profit (after tax) (profit for the period attributable to the shareholders of the Company), in accordance with the consolidated financial statements of the Company. Application of the policy to distribute a dividend is subject to the provisions of the law, including the distribution criteria prescribed in the Companies Law, and the estimation of the Board of Directors of the Company regarding the Company’s ability to meet its existing and anticipated liabilities, taking into consideration the projected cash flow, the Company's operations and liabilities, the cash balance, its plans and position as will be from time to time and subject to the approval of the general meeting of the Company's shareholders regarding any specific distribution, as set out in the articles of association of the Company. As at the publication date, the policy is in effect.

It is noted that following the Board of Director's resolution of February 10, 2015 regarding the Company's engagement with Eurocom DBS for acquisition of the full holdings of Eurocom DBS in DBS, the Board of Directors determined that the revaluation gains, which are expected to arise for the Company in accordance with accounting principles, if the transaction is completed, will be excluded from the dividend policy and will not be distributed as a dividend. These gains amounted to NIS 12 million.

19.2.2 Distributions made by the Company in 2014-2015:

| Distribution date | Distributed amount per share (NIS) | 2015 NIS million | 2014 NIS million |
|---|---|---|---|
| April 4, 2014 | 0.294 | **-** | 802 |
| October 2, 2014 | 0.463 | **-** | 1,267 |
| May 27, 2015 | 0.307 | **844** | - |
| October 26, 2015 | 0.339 | **933*** | - |
| | | **1,777** | 2,069 |

* The dividend is distributed for profits of the first half of 2015 amounting to NIS 945 million less revaluation gains of NIS 12 million for the gain of control in DBS, which were excluded from the Company's dividend policy as explained in Note 19.2.1 above.

19.2.3 On March 16, 2016, the Board of Directors of the Company resolved to recommend to the general meeting of the Company's shareholders the distribution of a cash dividend to the shareholders in the amount of NIS 776 million. As at the approval date of the financial statements, the dividend has not yet been approved by the general meeting.

19.2.4 The Company also issued share options to employees, managers and senior employees in the Group (see Note 25).

## 20. Revenues

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| **Domestic fixed-line communication** | | | |
| Fixed-line telephony | **1,543** | 1,636 | 1,908 |
| Internet - infrastructure | **1,530** | 1,394 | 1,283 |
| Transmission and data communication | **840** | 802 | 794 |
| Other services | **212** | 220 | 220 |
| | **4,125** | 4,052 | 4,205 |
| **Cellular communications** | | | |
| Cellular services and terminal equipment | **1,948** | 2,399 | 2,744 |
| Sale of terminal equipment | **884** | 966 | 1,000 |
| | **2,832** | 3,365 | 3,744 |
| **International communications, internet and NEP services** | **1,487** | 1,425 | 1,367 |
| **Multichannel television** | **1,333** | - | - |
| **Other** | **208** | 213 | 247 |
| | **9,985** | 9,055 | 9,563 |

## 21. General and Operating Expenses

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| Terminal equipment and materials | **880** | 928 | 1,071 |
| Interconnectivity and payments to domestic and international operators | **909** | 847 | 905 |
| Maintenance of buildings and sites | **616** | 639 | 607 |
| Marketing and general | **640** | 603 | 614 |
| Content costs | **458** | 58 | 65 |
| Services and maintenance by sub-contractors | **199** | 137 | 162 |
| Vehicle maintenance | **167** | 154 | 152 |
| | **3,869** | 3,366 | 3,576 |

Operating and general expenses are presented net of expenses of NIS 63 million recognized in 2015 for investments in property, plant and equipment and intangible assets (in 2014, NIS 63 million and in 2013, NIS 64 million),

## 22. Salaries

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| Salaries and incidentals - operating | **1,871** | 1,691 | 1,741 |
| General and administrative | **585** | 560 | 589 |
| Share-based payments | **-** | 1 | 34 |
| Total salaries and incidentals | **2,456** | 2,252 | 2,364 |
| Less salaries recognized in investments in property, plant and equipment and intangible assets | **499** | 484 | 492 |
| | **1,957** | 1,768 | 1,872 |

## 23. Other Operating Expenses (Income), Net

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| Profit from the sale of property, plant and equipment (mainly real estate) | **(234)** | (175) | (167) |
| Profit from sale of the shares of Coral Tell | **-** | (582) | - |
| Provision for severance pay in voluntary redundancy (see Note 15.5) | **117** | 176 | 90 |
| Others | **22** | (5) | 62 |
| Other operating income, net | **(95)** | (586) | (15) |

## 24. Financing Expenses (Income), Net

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| Interest expenses for financial liabilities | **339** | 386 | 428 |
| Linkage and exchange rate differences | **51** | 44 | 58 |
| Financing expenses for employee benefits | **16** | 21 | 15 |
| Reduction of the provision for assessor interest expenses (see Note 6.6.2) | **(76)** | - | - |
| Other financing expenses | **46** | 35 | 72 |
| Total financing expenses | **376** | 486 | 573 |
| Income for credit in sales | **52** | 84 | 122 |
| Interest and linkage differences from loans to an associate | **21** | 213 | 226 |
| Other financing income, net | **40** | 59 | 80 |
| Total financing income | **113** | 356 | 428 |
| | | | |
| Financing expenses, net | **263** | 130 | 145 |

## 25. Share-Based Payments

As of December 31, 2015, the Company has one option plan settled in shares through the net exercise mechanism. All the options that were granted are non-marketable, the exercise price is adjusted for changes in capital and distribution of a dividend. Additional information:

| **Name of plan** | **Number of options granted (before forfeiture and exercise) (thousands)** | **Number of options in circulation as at December 31, 2015 (in thousands)** | **Exercise price as at December 31, 2015 (NIS)** | **Weighted average of remaining contractual life** |
|---|---|---|---|---|
| Employee option plan of 2010 | 69,495 | 4,347 | 2.72 | One month |

In 2015, 27 million options were exercised, for which the Company issued 19 million ordinary shares of NIS 1 par value each.

## 26. Earnings per Share

### Basic and diluted earnings per share

The calculation of basic earnings per share was based on the profit attributable to holders of ordinary shares, and on a weighted average number of ordinary shares outstanding, calculated as follows:

| | 2015 | 2014 | 2013 |
|---|---|---|---|
| | NIS million | NIS million | NIS million |
| Profit attributable to holders of ordinary shares | **1,721** | 2,111 | 1,771 |
| Weighted average number of ordinary shares (basic) | **2,750** | 2,736 | 2,726 |
| Effect of share options exercised | **13** | 19 | 15 |
| Weighted average number of ordinary shares (diluted) | **2,763** | 2,755 | 2,741 |

The average market value of the Company's shares for purposes of calculating the dilutive effect of share options was based on quoted share prices for the period in which the options were outstanding.

## 27. Segment Reporting

**27.1** The Group operates in various segments in the communications sector, so that every company in the Group operates in one separate business segment. The primary reporting format, by business segments, is based on the Group's management and internal reporting structure.

Each company provides services in the segment in which it operates, using the property, plant and equipment and the infrastructure it owns (see also Note 20). The infrastructure of each company is used only for providing its services. Each of the companies in the Group is exposed to different risks and yield expectations, mainly in the matter of the technology and competition in the segment in which it operates. Accordingly, the separable component in the Group is each company in the Group.

Based on the above, the business segments of the Group are as follows:

1. Bezeq The Israel Telecommunication Corp. Ltd.: fixed line domestic communications
2. Pelephone Communications Ltd.: cellular communications
3. Bezeq International Ltd.: international communications, internet services and network end point
4. DBS Satellite Services (1998) Ltd.: multichannel television

The other companies in the Group are presented under the "Other" item. Other operations include call center services (Bezeq Online) and online shopping and classified ads, (through Walla). These operations are not reported as reporting segments as they do not fulfill the quantitative thresholds.

Inter-segment pricing is set at the price determined in a transaction between unrelated parties.

The results, assets and liabilities of a segment include items directly attributable to that segment, as well as those that can be allocated on a reasonable basis.

Segment capital expenditure is the total cost incurred during the period for acquisition of property, plant and equipment and intangible assets.

It is noted that the Company's investment in DBS was accounted for using the equity method up to March 23, 2015. As from this date, the financial statements of DBS are consolidated with the financial statements of the Group as described in Note 11.2 above. The Group reports on multichannel television as an operating segment without adjustment to ownership rates and excess cost in all reporting periods.

**27.2** After DBS became a wholly-owned subsidiary of the Company on June 24, 2015, the Company updated the internal management reporting structure for financing income for the shareholders loans that were provided to DBS. Accordingly, the Company restated financing income under the separate interim financial information. As from 2015, the Company no longer recognizes financing income for the shareholders loans under the financing income of the fixed-line domestic communications segment. Financing expenses in the multichannel television segment include financing expenses for the loans without any change. The comparative figures were restated to reflect the change in the reporting structure: financing income in the amount of NIS 213 million was eliminated in the fixed-line domestic communications segment for the year ended December 31, 2014, and NIS 226 million in the year ended December 31, 2013.

## 27.3 Operating segments

| | Year ended December 31, 2015 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Domestic fixed-line communication | Cellular communications | International communications and internet services | Multichannel television | Other | Adjustments | Consolidated |
| | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million |
| Revenues from external sources | 4,122 | 2,831 | 1,485 | 1,774 | 197 | (440) | 9,969 |
| Inter-segment revenues | 285 | 59 | 93 | - | 24 | (445) | 16 |
| Total revenues | 4,407 | 2,890 | 1,578 | 1,774 | 221 | (885) | 9,985 |
| Depreciation and amortization | 725 | 419 | 132 | 322 | 13 | 73 | 1,684 |
| Segment results – operating profit (loss) | 2,148 | 157 | 240 | 250 | (15) | (210) | 2,570 |
| Finance expenses | 362 | 4 | 15 | 635 | 2 | (642) | 376 |
| Financing income | (30) | (53) | (7) | (32) | (17) | 26 | (113) |
| Total financing expenses (income), net | 332 | (49) | 8 | 603 | (15) | (616) | 263 |
| Segment profit (loss) after financing expenses, net | 1,816 | 206 | 232 | (353) | - | 406 | 2,307 |
| Share in profits (losses) of associates | - | - | - | - | (2) | 14 | 12 |
| Segment profit (loss) before income tax | 1,816 | 206 | 232 | (353) | (2) | 420 | 2,319 |
| Income tax | 492 | 55 | 60 | 1 | - | (10) | 598 |
| Segment results – net profit (loss) | 1,324 | 151 | 172 | (354) | (2) | 430 | 1,721 |
| Segment assets | 7,311 | 3,269 | 1,160 | 1,667 | 659 | 1,163 | 15,229 |
| Investment in associates | - | - | 4 | - | 7 | 14 | 25 |
| Goodwill | - | - | 6 | - | 10 | 1,409 | 1,425 |
| Segment liabilities | 12,117 | 513 | 343 | 6,685 | 104 | (5,494) | 14,268 |
| Investments in property, plant and equipment and intangible assets | 837 | 419 | 127 | 281 | 33 | (80) | 1,617 |

| | Year ended December 31, 2014 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Domestic fixed-line communication | Cellular communications | International communications and internet services | Multichannel television | Other | Adjustments | Consolidated |
| | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million | NIS million |
| Revenues from external sources | 4,045 | 3,361 | 1,419 | 1,724 | 209 | (1,724) | 9,034 |
| Inter-segment revenues | 272 | 58 | 85 | - | 17 | (411) | 21 |
| Total revenues | 4,317 | 3,419 | 1,504 | 1,724 | 226 | (2,135) | 9,055 |
| | | | | | | | |
| Depreciation and amortization | 688 | 430 | 130 | 297 | 23 | (287) | 1,281 |
| | | | | | | | |
| Segment results – operating profit | 1,980 | 449 | 232 | 273 | 629 | (337) | 3,226 |
| Finance expenses | 472 | 21 | 18 | 620 | 2 | (647) | 486 |
| Financing income | (72)* | (77) | (9) | (26) | (11) | (161)* | (356) |
| Total financing expenses (income), net | 400* | (56) | 9 | 594 | (9) | (808)* | 130 |
| | | | | | | | |
| Segment profit (loss) after financing expenses, net | 1,580* | 505 | 223 | (321) | 638 | 471* | 3,096 |
| Share in profits (losses) of associates | - | - | 1 | - | (3) | (168) | (170) |
| Segment profit (loss) before income tax | 1,580* | 505 | 224 | (321) | 635 | 303* | 2,926 |
| Income tax | 478 | 132 | 60 | 1 | 147 | (3) | 815 |
| Segment results – net profit (loss) | 1,102* | 373 | 164 | (322) | 488 | 306* | 2,111 |
| | | | | | | | |
| Segment assets | 8,483 | 3,541 | 1,207 | 1,820 | 682 | (2,517) | 13,216 |
| Investment in associates | - | - | 4 | - | 11 | 1,042 | 1,057 |
| Goodwill | - | - | 6 | - | 10 | 1,024 | 1,040 |
| Segment liabilities | 12,369 | 696 | 392 | 6,484 | 107 | (7,176) | 12,872 |
| Investments in property, plant and equipment and intangible assets | 835 | 339 | 110 | 332 | 17 | (332) | 1,301 |

| | Year ended December 31, 2013 | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Domestic fixed-line communication** | **Cellular communications** | **International communications and internet services** | **Multichannel television** | **Other** | **Adjustments** | **Consolidated** |
| | **NIS million** | **NIS million** | **NIS million** | **NIS million** | **NIS million** | **NIS million** | **NIS million** |
| Revenues from external sources | 4,198 | 3,741 | 1,365 | 1,633 | 241 | (1,633) | 9,545 |
| Inter-segment revenues | 280 | 68 | 68 | 2 | 21 | (421) | 18 |
| Total revenues | 4,478 | 3,809 | 1,433 | 1,635 | 262 | (2,054) | 9,563 |
| Depreciation and amortization | 683 | 458 | 130 | 263 | 31 | (254) | 1,311 |
| Segment results – operating profit | 1,998 | 608 | 227 | 268 | (4) | (278) | 2,819 |
| Finance expenses | 534 | 46 | 23 | 654 | 6 | (690) | 573 |
| Financing income | (91)* | (137) | (9) | (7) | - | (184)* | (428) |
| Total financing expenses (income), net | 443* | (91) | 14 | 647 | 6 | (874)* | 145 |
| Segment profit (loss) after financing expenses, net | 1,555* | 699 | 213 | (379) | (10) | 596* | 2,674 |
| Share in profits (losses) of associates | - | - | 1 | - | - | (253) | (252) |
| Segment profit (loss) before income tax | 1,555* | 699 | 214 | (379) | (10) | 343* | 2,422 |
| Income tax | 410 | 178 | 56 | 2 | 5 | - | 651 |
| Segment results – net profit (loss) | 1,145* | 521 | 158 | (381) | (15) | 343* | 1,771 |

* Restated See section 27.2 above

## 27.2. Adjustments for segment reporting of revenue, profit or loss, assets and liabilities

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| **Revenues** | | | |
| Revenues from reporting segments | **10,649** | 10,964 | 11,355 |
| Revenues from other segments | **221** | 226 | 262 |
| Cancellation of revenues from inter-segment sales except for revenues from sales to an associate reporting as a segment | **(445)** | (411) | (421) |
| Cancellation of revenues for a segment classified as an associate (up to the date of acquisition of control) | **(440)** | (1,724) | (1,633) |
| Consolidated revenues | **9,985** | 9,055 | 9,563 |
| | | | |
| **Profit or loss** | | | |
| Operating profit for reporting segments | **2,795** | 2,934 | 3,101 |
| Cancellation of expenses for a segment classified as an associate (up to the date of acquisition of control) | **(59)** | (273) | (268) |
| Financing income (expenses), net | **(263)** | (130) | (145) |
| Share in profits (losses) of associates | **12** | (170) | (252) |
| Profit (loss) for operations classified in other categories and other adjustments | **(16)** | 574 | (5) |
| Amortization of excess cost | **(150)** | (9) | (9) |
| Consolidated profit before income tax | **2,319** | 2,926 | 2,422 |

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | **NIS million** | **NIS million** |
| **Assets** | | |
| Assets from reporting segments | **13,417** | 15,061 |
| Assets attributable to operations in other categories | **676** | 703 |
| Goodwill not attributable to an operating segment | **1,409** | 1,024 |
| Surplus cost not attributable to an operating segment | **2,173** | - |
| Investment in an associate (mainly loans) reported as a segment | **-** | 1,026 |
| Cancellation of assets for a segment classified as an associate | **-** | (1,820) |
| Less inter-segment assets and other adjustments | **(996)** | (681) |
| Consolidated assets | **16,679** | 15,313 |
| | | |
| **Liabilities** | | |
| Liabilities from reporting segments | **19,658** | 19,941 |
| Liabilities attributable to operations in other categories | **104** | 107 |
| Cancellation of liabilities for a segment classified as an associate | **-** | (6,484) |
| Less inter-segment liabilities | **(5,494)** | (692) |
| Consolidated liabilities | **14,268** | 12,872 |

# 28. Transactions with Interested and Related Parties

## 28.1. Identity of interested and related parties

The Company's interested and related parties as defined in the Securities Law and in IAS 24 – Related Party Disclosures include mainly B Communications Ltd. ("B Communications), related parties of B Communications, associates, directors and key management personnel in the Company or the parent company and a person who is close to a family member of any of these individuals.

## 28.2. Balances with interested and related parties

| | December 31 | |
|---|---|---|
| | **2015** | **2014** |
| | **NIS million** | **NIS million** |
| Trade receivables - associates | **9** | 15 |
| Loan to an associate * | **-** | 2,181 |
| Liabilities to related parties, net * | **(17)** | (41) |
| Liability to Eurocom DBS Ltd. for contingent consideration (see Note 11.2.1) | **(233)** | - |

* The Company provided a shareholder loan to DBS between 1999 and 2005. As from the date of acquisition of control in DBS as described in Note 11.2 above and consolidation of the financial statements of DBS in the Group's consolidated financial statements, these loans are not shown in the statement of financial position.

## 28.3. Transactions with interested and related parties

| | Year ended December 31 | | |
|---|---|---|---|
| | **2015** | **2014** | **2013** |
| | **NIS million** | **NIS million** | **NIS million** |
| **Revenues** | | | |
| From associates (including financing income for shareholders' loans) * | **30** | 229 | 246 |
| From related parties | **10** | 9 | 8 |
| **Expenses** | | | |
| To related parties | **127** | 119 | 126 |
| To associates | **3** | 1 | 7 |
| **Property, plant and equipment** | | | |
| Related parties | **76** | 76 | 66 |
| **Acquisition of holdings from Eurocom DBS in DBS (see Note 11.2.1)** | **913** | - | - |

* Income from associates is mainly from financing income for the shareholder loans to DBS described in Note 11.2.6 and Note 28.2 above.

## Transactions with interested and related parties

28.3.1 Negligible transactions

On March 7, 2011, the Company's Board of Directors resolved to adopt guidelines and regulations to classify a transaction of the Company or its subsidiary with an interested party as a negligible transaction, which is not an extraordinary transaction, as set out in Article 41(A)(6) of the Securities Regulations (Annual Financial Statements), 2010 ("the Annual Financial Statements Regulations"). These guidelines and regulations are also used to assess the scope of disclosure in the periodic report and prospectus (including shelf offering reports) regarding a transaction of the Company, a company under its control and a subsidiary or associate with a controlling shareholder or in which the controlling shareholder has a personal interest as set out in Article 22 of the Securities Law (Periodic and Immediate Reports), 1970 ("the Periodic Reports Regulations") and Article 54 of the Securities Regulations (Prospectus Details and Draft Prospectus – Structure and Form), 1969, and to assess the need to submit an immediate report for the transaction of the Company, as set out in Article 37(A)(6) of the periodic reports regulations (types of transactions determined in the financial statements regulations) and the prospectus details regulations referred to above ("the Interested Party Transactions").

From time to time, the Company and its subsidiaries carry out negligible transactions, which are not extraordinary transactions, with an interested party in the Company or with related parties, of the types and nature detailed below:

1. Sales of communications services and products by Group companies, including: basic communication services (telephony, transmission and PRI) and hosting at server farms; cellular services, value added services and sales and upgrading of cellular end equipment; web browsing services, international telephony services, hosting services and data communication services; multichannel television services

2. Purchase of devices from Eurocom Group companies (companies owned by the controlling shareholder of the Company or companies controlled by the controlling shareholder at the approval date of the agreement), including acquisition of electronic equipment, terminal equipment, communication equipment, and pit covers

3. Acquisition of maintenance and development services from companies in the Eurocom Group, including maintenance, development and upgrading services for systems used in the Group companies, maintenance and spare parts for exchanges, content development services and communication applications.

4. Sales of maintenance, upgrading and development services by Group companies, including: maintenance of equipment, content development services and communication applications

5. Sale of user rights in communication infrastructure, call transfer, including sale of user rights in international communication infrastructure and supply of a local segment in Israel, hosting services at server farms, and reciprocal call transfer and completion agreements with Eurocom Group companies.

6. Placement and outsourcing services

7. Rental, management and real estate acquisition agreements, including rental of areas used for communication facilities and warehouses; and rental of areas to Eurocom Group companies in properties owned by the Company

8. Acquisition of advertising and content services, including agreements to acquire media slots from media companies in the Eurocom Group; agreement for to use content on Pelephone's cellular portal; acquisition of portals from Eurocom Group companies; media content management services by Eurocom Group companies.

9. Transactions relating to joint marketing, advertising, discounts and sponsorship with Eurocom Group companies or related to products of Eurocom Group companies, including distribution agreements (dealer) for marketing Company services, joint marketing campaigns, consignment agreements for the sale of Eurocom Digital Communications equipment, and technological sponsorship at exhibitions organized by the Company.

10. Contribution to the community together with Eurocom Group companies and contribution to organizations/projects in which the controlling shareholder of the Company or his relative volunteers as an officer. These contributions are part of the Company's contribution policy.

In the absence of special qualitative considerations all the circumstances, a transaction that is in the Company’s regular course of business, is carried out in market conditions and has no material effect on the Company, shall be deemed negligible if all the following parameters exist:

A. The amount of the transaction does not exceed NIS 10 million.

B. The Company is not required to issue an immediate report for the transaction under Article 36 of the periodic reports regulations or any other law.

C. The transaction does not include the terms of the office and employment (as defined in the Companies Law, 1999, ("the Companies Law") of an interested party or his relative, and does not constitute a transaction as set out in section 270(4) of the Companies Law (transaction of a public company with a holder of control therein, directly or indirectly, including through a company he controls, in respect of receiving services from it by the Company and if such person is also an officer - as to the conditions of his office and employment, and if he is an employee of the Company but not an officer, as to his employment by the Company).

According to the provisions of the Companies Law, as amended from time to time, once a year, before publication of the annual financial statements, the audit committee will review the parameters set out above, and whether they require updating. In general, each transaction will be tested separately for negligibility. Notwithstanding the aforesaid, separate transactions that are part of the same continuing transaction or very similar transactions that are carried out routinely and repeatedly, will be tested as one transaction on an annual basis for negligibility, provided the scope of the transaction does not exceed NIS 10 million, as set out above.

The Board of Directors may, from time to time and at its discretion, amend the parameters for a negligible transaction. This amendment will be duly reported.

28.3.2 Below are transactions listed in section 270(4) of the Companies Law, which are not considered as negligible transactions

| Approval date of the general meeting (after approval of the Company's audit committee and Board of Directors), unless otherwise stated. | Nature of the transaction | Amount of the transaction | Nature of the personal interest |
|---|---|---|---|
| April 25, 2013<br>Approved by the Company's Board of Directors in accordance with the Companies Regulations (Relief in Transactions with Interested Parties), 2000 ("the Relief Regulations for Transactions with Interested Parties") | Extension of the arrangements approved at the Company's general meeting on October 14, 2010, between the Company and DBS and between Bezeq International and DBS for reciprocal marketing of products and services until December 31, 2015 | The fees to be paid by the parties to each other will be in accordance with the criteria approved by the general meeting as part of the original approval for the agreement | Section B below |
| May 8, 2013 | Approval of the Company's vote at the general meeting of DBS in favor of DBS's agreement with Space Communications Ltd. ("Space Communications") for leasing space segments, in which the original agreement will be amended and extended. The agreement is valid until the end of 2028. | Total amount of up to USD 227 million (net including discounts for satellite segments leased in the existing agreement) | Section D below. |
| June 13, 2013 | The amendment to the Company's three-year agreement with Eurocom Communications Ltd. ("Eurocom Communications") for ongoing management and consultation services valid until May 31, 2016, unless one of the parties announces its intention to terminate the agreement with three months' notice. For further information see section E below. | NIS 5.5 million per year | Section E below |
| November 6, 2013<br>Approved by the Company's Board of Directors in accordance with the relief regulations for transactions with interested parties | Amendment and extension of the agreement between DBS and Eurocom Digital Communications Ltd. ("Eurocom") and Advanced Digital Broadcast SA ("ADB") for the purchase of YesMaxTotal3 converters, for a period up to December 31, 2016. | The total cost will be USD 10 million per year | Sections A and B below |
| January 27, 2014 | Approval of the Company's vote at the general meeting of DBS in favor of DBS's agreement with Eurocom and ADB for the acquisition of an additional quantity of yesMaxTotal converters and power supplies for yesMax HD converters, until June 30, 2015. | For converters: Total cost of USD 14 million In addition, there is an additional 2.42% of the price for the cost of the hard drive only, if there are changes due to an increase in hard drive prices<br>For power supplies: a total cost of USD 197 thousand | Sections A and B below |
| November 27, 2014<br>Approved by the Company's Board of Directors in accordance with the relief regulations for transactions with interested parties | Extension of supplier credit terms in accordance with the agreement between DBS and Space Communications for lease of space segments, up to December 31, 2014. | NIS 874 thousand | Section D below. |

| Approval date of the general meeting (after approval of the Company's audit committee and Board of Directors), unless otherwise stated. | Nature of the transaction | Amount of the transaction | Nature of the personal interest |
|---|---|---|---|
| January 14, 2015 | Approval of the Company's vote at the general meeting of DBS in favor of DBS's agreement with Eurocom and ADB for the order of an additional quantity of yesMaxTotal converters, until December 31, 2015. | A total cost of USD 12 million and an additional price of up to 1.9% for the cost of the hard drive only, if there are changes due to an increase in hard drive prices | Sections A and B below |
| March 23, 2015 | Approval of the Company's acquisition agreement with Eurocom DBS Ltd. ("Eurocom DBS") whereby the Company will acquire the entire holdings of Eurocom DBS in DBS shares DBS and all the shareholder loans provided by Eurocom DBS to DBS (including acceptance of the terms established by the Antitrust Commissioner's in his approval of the merger on March 26, 2014, both by the Company and by DBS, and announcement of the exercise of the Company's option for the allotment of 6,221 DBS shares, at no cost, representing 8.6% of the share capital of DBS). | The total cost is comprised of:<br>A. Total cash of NIS 680 million<br>B. Total cash of up to NIS 200 million (subject to certain conditions)<br>C. Total cash of up to NIS 170 million (subject to certain conditions) For information about the conditions relating to B and C, see Note 11.2 above. | Section F below. |
| October 19, 2015 | Approval of the Company's vote at the general meeting of shareholders of DBS in favor of DBS's agreement with Eurocom and ADB for the order of yesMaxTotal3 converters, under the existing agreement, until December 31, 2017 | Total cost of USD 14 million | Section A and B below |
| December 8, 2015 | Amendment to the framework agreement between Pelephone and Eurocom Cellular Communications Ltd., so that it will be extended to other products and brands, including related services for all products and its extension until December 31, 2018 (or three years after the acquisition date of any additional products or brands, whichever is earlier). | Annual scope of up to NIS 50 million (for all the products) | Section C below |

A transaction with a controlling shareholder that is not an irregular transaction that was in effect in the reporting period:

| **Approval date of the general meeting (after approval of the Company's audit committee and Board of Directors)** | **Nature of the transaction** | **Amount of the transaction** | **Nature of the personal interest** |
|---|---|---|---|
| November 27, 2014<br>Approved by the Company's Board of Directors as a transaction with a controlling shareholder that is not an irregular transaction | The Company's agreement to bring forward payments with Eurocom, according to which DBS may advance, at the supplier's request, payments that are due, or will be due, to Eurocom for orders of converters. | Up to a total cost of USD 6 million | Sections A and B below |

The financial values of the transactions described in section 28.3.2 above, which were carried out in 2015, are as follows.

| | Amounts included in the consolidated statement |
|---|---|
| | NIS million |
| Expenses | 105 |
| Property, plant and equipment | 46 |
| Acquisition of Eurocom DBS holdings in DBS (see Note 11.2.1) | 913 |

A. B Communications Ltd., the controlling shareholder of the Company, has a personal interest, since Eurocom is a related company to B Communications. Eurocom is controlled by Eurocom Communications, which is the controlling shareholder (tiered) of B Communications.

In addition, the director Shaul Elovitch has a personal interest as the controlling shareholder (tiered) in Eurocom Communications; directors Or Elovitch and Orna Elovitch-Peled have a personal interest being a relative of the controlling shareholder; the director Amikam Shorer has a personal interest being an employee and/or officer in Eurocom Group companies.

B. B Communications has a personal interest in the transaction, since as at the date of this transaction, 50.2% of the shares of DBS were held by Eurocom DBS Ltd, which is controlled by Eurocom Communications, the controlling shareholder (tiered) of B Communications.

In addition, the directors Shaul Elovitch, Or Elovitch, Orna Elovitch-Peled, and Amikam Shorer have a personal interest as described in section A above.

C. B Communications has a personal interest in the transaction, since Eurocom Cellular Communications Ltd. (a party to the transaction) is a related company to B Communications. Eurocom Cellular Communications Ltd. is controlled by Eurocom Communications, which is the controlling shareholder (linked) of B Communications.

In addition, the directors Shaul Elovitch, Or Elovitch, Orna Elovitch-Peled, and Amikam Shorer have a personal interest as described in section A above.

D. See section B above; in addition, Or Elovitch, Shaul Elovitch, and Amikam Shorer serve as directors in Space Communications (Or Elovitch serves as chairman of the board of directors of Space Communications).

E. Eurocom Communications will provide the services of Shaul Elovitch, who will serve as executive chairman of the Board of Directors of the Company and its subsidiaries. Executive chairman services will be provided in a scope of 70% and will include: service as active chairman of the Board of Directors of the Company and all its subsidiaries; management of work interfaces with the managements of the Company and its subsidiaries; active supervision authority for the effective management and performance of the Board of Directors of the Company and its subsidiaries; management of formation of the Group's strategy (subject to approval by the Company's Board of Directors); and more

Eurocom will provide directors on its behalf, to serve on the boards of directors of the Company and the subsidiary companies, in addition to the chairman of the board of directors.

Eurocom will also provide ongoing consultation services in diverse areas, in a monthly scope of at least 45 hours of monthly consulting services, provided by Or Elovitch, Amikam Shorer, and any other party set out in the agreement.

For services provided by the Eurocom Communications as described above, the Company will pay the following consideration to Eurocom Communications: (a) NIS 1.7 million per year for the participation of directors serving on behalf of the Company's controlling shareholders, as part of their membership and position as directors in the Company and/or its subsidiaries and the various committees, subject to adjustments in accordance with their number and presence in meetings; (b) NIS 3.5 million per year for the service and activities of Shaul Elovitch as active chairman of the boards of directors of the Company and its subsidiaries; (c) NIS 324 thousand per year for ongoing consultation services.

F. B Communications has a personal interest in the approval of the transaction, since as at the date of the transaction, B Communications is a company controlled (indirectly) by Eurocom Communications, which is controlled by Shaul and Yosef Elovitch (linked and indirectly), who are also the controlling shareholders in Eurocom DBS (through other companies and indirectly), which, as at the transaction date, held DBS shares.

The controlling shareholders have another personal interest arising from the fact that upon acceptance of the merger conditions by DBS as set out above, Eurocom DBS was released from its obligation to sell its shares in DBS, which was imposed on it by the Antitrust Commissioner as described in Note 11.1.1. above. To the best of the Company's knowledge, Eurocom Communications is a private company controlled by Eurocom Holdings (1979) Ltd., a private company controlled by Shaul Elovitch and his brother Yosef Elovitch.

The controlling shareholders have an additional personal interest arising from the purchase of liability insurance for directors for their service on the board of directors of DBS in the period up to the completion date of the acquisition transaction, as set out in the table.

G. For further information about the transactions included in section 270(4) of the Companies Law, regarding D&O insurance and indemnity, see Note 28.6 below.

## 28.4. Benefits for key officers

Benefits for employment of key managers, including:

| | Year ended December 31 | | |
|---|---|---|---|
| | 2015 | 2014 | 2013 |
| | NIS thousands | NIS thousands | NIS thousands |
| Number of managerial key officers | **5** | 4 | 4 |
| Salary (28.4.1) | **8,519** | 7,468 | 8,078 |
| Bonus: | **7,375** | 5,940 | 5,302 |
| Share-based payments | **(130)** | (651) | 2,578 |
| | **15,764** | 12,757 | 15,958 |

28.4.1 Key officers in the Group include the chairman of the Board of Directors (who is not entitled to remuneration for his position, beyond the consideration paid as part of the management services agreement with Eurocom Communications Ltd.), the CEO of the Company and the CEOs of Bezeq International, DBS (as from March 23, 2015, the date of initial consolidation of DBS in the financial statements of the Group), Pelephone (as from November 8, 2015), and the former CEO of Pelephone (up to November 7, 2015). As set out in Note 28.3.2 above, in 2015, the Company paid Eurocom Communications NIS 3.5 million for the service and activity of Shaul Elovitch as active chairman of the Board of Directors of the Company and its subsidiaries. This amount is not included in the benefits described above.

28.4.2 In 2015, changes in other provisions (which are included in total salary) include a reduction in the provision, mainly due to payment of early notice to the former CEO of Pelephone amounting to NIS 0.4 million. In 2014, the changes in other provisions include a reduction in provisions, mainly due to the payment for the early notice and leave for the former CEO of Bezeq International, amounting to NIS 0.7 million and creation of a provision for early notice and leave of the incumbent CEO of Bezeq International, amounting to NIS 0.8 million. In 2013, the changes in other provisions include a reduction in provisions due to the payment of the early notice and leave for the former CEO of the Company amounting to NIS 1.2 million and creation of a provision for early notice and leave of the incumbent CEO amounting to NIS 1.1 million.

## 28.5. Benefits for directors

| | Year ended December 31 | | |
|---|---|---|---|
| | 2015 | 2014 | 2013 |
| | NIS thousands | NIS thousands | NIS thousands |
| Remuneration for directors who are not employed by the Company, see section 28.5.1 | **2,912** | 2,818 | 2,168 |
| Number of directors receiving remuneration | **6** | 6 | 5 |
| Salary of employee-directors, see 28.5.2 | **587** | 1,608 | 1,358 |
| Number of directors receiving a salary, see 28.5.2 | **1** | 2 | 2 |
| Management fees to the controlling shareholder (see section 28.3.2) | **5,524** | 5,524 | 5,062 |

28.5.1 The directors serving on the Company's Board of Directors, except for the outside directors and the independent directors, do not receive remuneration from the Company.

28.5.2 The salary is paid to an employee-director for his work in the Company and he does not receive any additional pay for his service as a director in the Company. In 2015 and as at the approval date of the financial statements, one director who is an employee serves in the Company.

## 28.6. Additional benefits for directors and officers

| Approval date of the general meeting (after approval of the Company's Board of Directors), unless otherwise stated. | Nature of the transaction | Amount of the transaction |
|---|---|---|
| March 8, 2010 | Conversion of the D&O liability insurance policy to a run-off policy | - |
| May 20, 2015<br>Approved by the Company's Board of Directors in accordance with the relief regulations for transactions with interested parties<br>(following approval by the Company's Board of Directors on April 8, 2014 for the period up to April 13, 2015 and approval of the Company's Board of Directors of April 13, 2015 for the period up to June 14, 2015). | Renewal of the Company's insurance policy for directors and officers liability in the Company and its subsidiaries, in accordance with the Company's compensation policy, for the period up to June 13, 2016 (inclusive), and for a further period of one year up to June 13, 2017 (subject to exercise of the option by the insurer), including the approval of the compensation committee and the Board of Directors that the terms of the agreement for the CEO and for the officers who are controlling shareholders or their relatives are the same as those of the other officers. | The liability limit is up to USD 150 million per claim and in total for all claims in the insurance year (plus reasonable legal expenses). The annual premium is USD 320 thousand. Total annual premium up to April 13, 2015: USD 234.5 thousand; total premium for the extension period until June 14, 2015: USD 55,430 (reflecting an annual cost of USD 332.5 thousand) |
| January 17, 2007 | Undertaking to indemnify officers in the Company, in accordance with the letters of indemnity, as amended on October 26, 2011. | Up to 25% of the Company's equity at the time the indemnity is granted |
| November 5, 2014 | Extension of the validity of the letters of undertaking for indemnification of directors who are controlling shareholders or their relatives for the period up to October 25, 2017. | - |

In addition, subsequent to the reporting date, on March 16, 2016, the Company's Board of Directors, recommended that the general meeting of the Company's shareholders, which convened on May 3, 2016, approve the amendment to the letters of undertaking for indemnification and exemption and to grant them to officers and directors (including those who are controlling shareholders in the Company and/or their representative).

**28.7.** For guarantees provided to DBS, see Note 12.4.

# 29. Financial Instruments

## 29.1. General

The Group is exposed to the following risks, arising from the use of financial instruments:

A. Credit risk

B. Liquidity risk

C. Market risk (which includes currency, interest, CPI risks and other price risks)

This Note provides qualitative and quantitative information about the Group's exposure to each of the above risks, an explanation as to how the risks are managed, and the measurement processes.

## 29.2. Framework for financial risk management

The Board of Directors has overall responsibility for the Group's financial risk management. The purpose of financial risk management in the Group is to define and monitor those risks constantly, and to minimize their possible effects arising from the exposure on the basis of assessments and expectations for parameters that affect the risks.

The Group's policy is to partially hedge, in accordance with the rules determined by the Board of Directors, the exposure arising from fluctuations in foreign exchange rates and the CPI.

## 29.3. Credit risk

Management monitors the Group's exposure to credit risks on a regular basis. Cash and investments in deposits and securities are deposited in highly-rated banks.

Trade and other receivables

The Group's management regularly monitors customer debts, and the financial statements include provisions for doubtful debts which properly reflect, in the management's estimation, the loss inherent in doubtful debts. In addition, the balances of the trade receivables are widely spread.

Investments in financial assets

Any investments in securities are made in liquid, marketable and low-risk securities. Transactions involving derivatives are made with entities that have a high credit rating.

As at the reporting date, there is no material concentration of credit risks.

## 29.4. Liquidity risk

The Group estimates that its liquidity risk is low.

For information about the terms of the debentures issued by Group companies and the loans received, and an agreement to receive future loans, see Note 12 above.

The following are the contractual maturities of financial liabilities received in practice up to December 31, 2015, including estimated interest payments (based on known CPI and interest rates on December 31, 2015):

| | December 31, 2015 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Carrying amount | Contractual cash flow | First half of 2016 | Second half of 2016 | 2017 | 2018 to 2020 | 2021 and thereafter |
| | | | | NIS million | | | |
| **Non-derivative financial liabilities** | | | | | | | |
| Trade and other payables | **1,550** | **1,550** | **1,548** | **2** | **-** | **-** | **-** |
| Loans | **3,219** | **3,528** | **85** | **723** | **924** | **1,564** | **231** |
| Debentures | **7,493** | **8,311** | **862** | **517** | **1,155** | **3,358** | **2,415** |
| Liability to Eurocom DBS | **233** | **233** | **233** | **-** | **-** | **-** | **-** |
| | **12,495** | **13,622** | **2,728** | **1,242** | **2,079** | **4,922** | **2,646** |
| **Financial liabilities for derivative instruments** | **168** | **168** | **22** | **-** | **-** | **114** | **32** |

It is not expected that the cash flows included in the analysis of the repayment dates will be materially earlier, or in amounts that are materially different. For further information about the financial covenants, see Note 12.

## 29.5. Market risks

The purpose of market risk management is to manage and oversee the exposure to market risks within accepted parameters to prevent significant exposures to market risks that will influence the Group's results, liabilities and cash flow.

During the normal course of its business, the Group takes full or partial hedging action and takes into account the effects of the exposure in its considerations for determining the type of loans it takes and in managing its investment portfolio.

29.5.1 Exposure to CPI and foreign currency risks

CPI risk

Changes in the rate of inflation affect the Group's profitability and its future cash flows, mainly due to its CPI-linked liabilities. In applying a policy of minimizing the exposure to the CPI, the Group makes forward contracts against the CPI. Hedging transactions are performed against the hedged debt repayment schedules. The Company applies hedge accounting for these forward contracts.

A considerable part of these cash balances is invested in shekel deposits and ETFs-deposit, which are exposed to changes in their real value as a result of a change in the rate of the CPI.

Foreign currency risk

The Group is exposed to foreign currency risks mainly due to payments for purchases of terminal equipment and property, plant and equipment, some of which are denominated in or linked to the USD or EUR. In addition, the Group provides services for customers and receives services from suppliers worldwide for which it is paid and it pays in foreign currency, mainly the dollar.

Statement of financial position in accordance with linkage basis as at December 31, 2015:

| | December 31, 2015 | | | | |
|---|---|---|---|---|---|
| | Unlinked | CPI-linked | In or linked to foreign currency (mainly USD) | Non-monetary balances | Total balances |
| | NIS million | NIS million | NIS million | NIS million | NIS million |
| **Current assets** | | | | | |
| Cash and cash equivalents | 538 | - | 17 | - | 555 |
| Investments, including derivatives | 751 | - | 11 | - | 762 |
| Trade receivables | 2,019 | 21 | 18 | - | 2,058 |
| Other receivables | 19 | 107 | - | 143 | 269 |
| Inventory | - | - | - | 115 | 115 |
| **Non-current assets** | | | | | |
| Trade and other receivables | 482 | 192 | - | - | 674 |
| Broadcasting rights, net of rights exercised | - | - | - | 456 | 456 |
| Property, plant and equipment | | | | 6,894 | 6,894 |
| Intangible assets | | | | 3,332 | 3,332 |
| Deferred tax assets | | | | 1,178 | 1,178 |
| Deferred expenses and non-current investments | 55 | - | 50 | 256 | 361 |
| Equity-accounted investments | - | - | - | 25 | 25 |
| Total assets | 3,864 | 320 | 96 | 12,399 | 16,679 |
| **Current liabilities** | | | | | |
| Debentures, loans and borrowings | 1,220 | 693 | - | - | 1,913 |
| Trade and other payables | 1,313 | 62 | 205 | 77 | 1,657 |
| Current tax liabilities | - | 624 | - | - | 624 |
| Employee benefits | 378 | - | - | - | 378 |
| Liability to Eurocom DBS Ltd. | 233 | - | - | - | 233 |
| Provisions | 38 | 62 | - | - | 100 |
| **Non-current liabilities** | | | | | |
| Loans and debentures | 4,619 | 4,181 | - | - | 8,800 |
| Employee benefits | 192 | - | 48 | - | 240 |
| Derivatives and other liabilities | - | 147 | 5 | 74 | 226 |
| Deferred tax liabilities | - | - | - | 51 | 51 |
| Provisions | 46 | - | - | - | 46 |
| Total liabilities | 8,039 | 5,769 | 258 | 202 | 14,268 |
| | | | | | |
| Total exposure in the statement of financial position | (4,175) | (5,449) | (162) | 12,197 | 2,411 |
| | | | | | |
| **Details of forward contracts** | | | | | |
| Forward contracts | (2,437) | 2,021 | 416 | - | - |

Statement of financial position in accordance with linkage basis as at December 31, 2014:

| | December 31, 2014 | | | | |
|---|---|---|---|---|---|
| | Unlinked | CPI-linked | In or linked to foreign currency (mainly USD) | Non-monetary balances | Total balances |
| | NIS million | NIS million | NIS million | NIS million | NIS million |
| **Current assets** | | | | | |
| Cash and cash equivalents | 653 | - | 7 | - | 660 |
| Investments, including derivatives | 2,223 | - | - | - | 2,223 |
| Trade receivables | 2,187 | 16 | 24 | - | 2,227 |
| Other receivables | 3 | 107 | - | 150 | 260 |
| Inventory | - | - | - | 96 | 96 |
| **Non-current assets** | | | | | |
| Trade and other receivables | 509 | 57 | - | - | 566 |
| Property, plant and equipment | - | - | - | 6,079 | 6,079 |
| Intangible assets | - | - | - | 1,793 | 1,793 |
| Deferred expenses and non-current investments | 90 | - | 9 | 253 | 352 |
| Equity-accounted investments | - | 2,181 | - | (1,124) | 1,057 |
| Total assets | 5,665 | 2,361 | 40 | 7,247 | 15,313 |
| **Current liabilities** | | | | | |
| Debentures, loans and borrowings | 1,074 | 407 | - | - | 1,481 |
| Trade and other payables | 1,148 | 46 | 132 | 48 | 1374 |
| Current tax liabilities | - | 600 | - | - | 600 |
| Employee benefits | 259 | - | - | - | 259 |
| Provisions | 15 | 46 | - | 1 | 62 |
| **Non-current liabilities** | | | | | |
| Loans and debentures | 5,313 | 3,293 | - | - | 8606 |
| Employee benefits | 183 | - | 50 | - | 233 |
| Derivatives and other liabilities | - | 94 | - | 77 | 171 |
| Deferred tax liabilities | - | - | - | 17 | 17 |
| Provisions | 69 | - | - | - | 69 |
| Total liabilities | 8,061 | 4,486 | 182 | 143 | 12,872 |
| | | | | | |
| Total exposure in the statement of financial position | (2,396) | (2,125) | (142) | 7,104 | 2,441 |
| | | | | | |
| **Details of forward contracts** | | | | | |
| Forward contracts on CPI | (2,361) | 2,361 | - | - | - |

29.5.2 CPI

In 2015, the known CPI decreased by 0.9% (in 2014, a decrease of 0.1%; in 2013, an increase of 1.91%)

29.5.3 Sensitivity analysis for the change in the CPI for the change in the USD exchange rate

An increase/decrease of 1% in the CPI at the reporting date would not have a material effect on profit and on capital. In addition, an increase/decrease of 10% in the USD exchange rate at the reporting date would not have a material effect on profit and on capital.

29.5.4 Interest rate risk

Group is exposed to interest rate risk due to its liabilities for debt instruments bearing variable interest.

A. Type of interest

The interest rate for the Group's interest-bearing financial instruments at the reporting date is as follows:

| | Carrying amount | |
|---|---|---|
| | **2015** | **2014** |
| | **NIS million** | **NIS million** |
| Fixed-interest instruments | | |
| Financial assets (mainly deposits and trade receivables) | **2,154** | 2,577 |
| Financial liabilities (loans and debentures) | **(8,648)** | (7,697) |
| | **(6,494)** | (5,120) |
| Variable-interest instruments | | |
| Financial liabilities (loans and debentures) | **(2,065)** | (2,390) |

B. Fair value sensitivity analysis for fixed rate instruments

The Group's assets and liabilities at fixed interest are not measured at fair value through profit or loss. Accordingly, a change in interest rates at the reporting date will not affect profit or loss.

C. Sensitivity analysis of cash flow for instruments at variable interest

An increase/decrease of 1% in the interest rates at the reporting date will not have a material effect on profit and on capital.

## 29.6. Cash flow hedge accounting

29.6.1 The Company entered into several forward contracts, as described in the table below, to reduce exposure to changes in the CPI for CPI-linked Series 5 and Series 6 debentures. These transactions hedge specific cash flows of some of the debentures and are recognized as cash flow hedge accounting. The expiry date of these transactions complies with the repayment schedule of the relevant debentures. The fair value of the forward contracts is based on available market information (tier 2 in the fair value hierarchy)

| | | Number of | Nominal value | Fair value | Capital reserve |
|---|---|---|---|---|---|
| **Hedged item** | **Repayment dates** | **Transactions** | **NIS million** | **NIS million** | **NIS million** |
| December 31, 2015 | | | | | |
| Series 5 debentures | 6.2016 | **2** | **322** | **(22)** | **3** |
| Series 6 debentures | 12.2018 to 12.2022 | **8** | **1,699** | **(146)** | **67** |
| | | **10** | **2,021** | **(168)** | **70** |
| December 31, 2014 | | | | | |
| Series 5 debentures | 6.2015 to 6.2016 | **4** | **662** | **(35)** | **16** |
| Series 6 debentures | 12.2018 to 12.2022 | **8** | **1,699** | **(75)** | **47** |
| | | **12** | **2,361** | **(110)** | **63** |

Subsequent to the date of the financial statements, the Company entered into a new transaction to hedge Debentures (Series 6). The scope of the transaction is NIS 295 million. The maturity date of this transaction is December 2018.

29.6.2 DBS has forward transaction to reduce exposure to changes in the USD exchange rate. As at March 31, 2015, the net fair value of these transactions is NIS 11 million.

## 29.7. Financial instruments measured at fair value

The table below presents an analysis of the financial instruments measured at fair value.

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Level 1: investment in exchange-traded funds and financial funds (see Note 29.7.2) | **193** | 1,513 |
| Level 2 - future credit from banks | **2** | - |
| Level 2: forward contracts (see Note 29.7.3) | **(157)** | (110) |
| Level 3: contingent consideration for a business combination for the business results of DBS (see Note 29.7.4) | **(233)** | - |
| Level 3: investment in non-marketable shares | **2** | 9 |

29.7.1 The fair value of investments in financial funds and ETFs is determined by reference to their average quoted selling price at the reporting date (level 1).

29.7.2 The fair value of forward contracts on the CPI or foreign currency is based on discounting the difference between the price in the forward contact and the price of the present forward contact for the balance of the contract term until redemption, at an appropriate interest rate (level 2). The estimate is made under the assumption that a market participant takes into account the credit risks of the parties when pricing such contracts.

29.7.3 Information about fair value measurement of contingent consideration in a business combination (Level 3)

Below is the fair value of the contingent consideration liability for a business combination, as described in Note 11.2.1:

| | December 31, 2015 | |
|---|---|---|
| | Maximum additional consideration under the agreement | Fair value |
| | NIS million | NIS million |
| Additional consideration for tax synergy (first additional consideration)(A) | **200** | **204** |
| Additional consideration for the business results of DBS (second additional consideration) (B) | **170** | **29** |
| | **370** | **233** |

A. First additional consideration

The fair value of the additional first contingent consideration was calculated on the basis of the agreement in principle with the tax assessor for the scope of the carryforward losses of DBS as described in Note 6.6 above and it includes accrued interest.

B. Second additional consideration

The fair value of the first additional consideration was estimated by the assessor, using the Monte Carlo simulation with risk neutral measure of the underlying asset which is the expected cash flow of DBS for 2016-2017.

## 29.8. Financial instruments at fair value for disclosure purposes only

The table below shows the differences between the carrying amount and the fair value of financial liabilities.

The fair value of debentures issued to the public is based on their quoted closing price at the reporting date (Level 1).

The fair value of the loans and non-marketable debentures is based on the present value of future principal and interest cash flows, discounted at the rate of market interest for similar liabilities, plus the required adjustments for a risk premium or non-marketability, as at the reporting date (Level 2).

| | December 31, 2015 | | | December 31, 2014 | | |
|---|---|---|---|---|---|---|
| | Carrying amount (including accrued interest) | Fair value | Discount rate (weighted average) | Carrying amount | Fair value | Discount rate (weighted average) |
| | NIS million | | % | NIS million | | % |
| Bank loans (unlinked) | **1,904** | **2,044** | **2.05%** | 2,112 | 2,292 | 2.27% |
| Debentures issued to the public (CPI-linked) | **3,816** | **4,006** | **1.55%** | 3,820 | 4,033 | 1.37% |
| Debentures issued to the public (unlinked) | **1,279** | **1,340** | **1.25%** | 1,335 | 1,426 | 0.85% |
| Debentures issued to financial institutions (CPI-linked) | **1,310** | **1,314** | **1.66%** | - | - | - |
| Debentures issued to financial institutions (unlinked) | **403** | **458** | **2.11%** | 403 | 467 | 2.55% |
| | **8,712** | **9,162** | | 7,670 | 8,218 | |

## 29.9. Offset of financial assets and liabilities

The Group has agreements with various communication companies to supply and receive communication services. In accordance with the agreements, each party has the right to offset the amounts due by each party. The table below presents the carrying amount of the offset balances as stated in the statement of financial position:

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Trade and other receivables, gross | **147** | 151 |
| Offset amounts | **(115)** | (114) |
| Trade and other receivables presented in the statement of financial position | **32** | 37 |
| Trade payables, gross | **157** | 165 |
| Offset amounts | **(115)** | (114) |
| Trade and other payables presented in the statement of financial position | **42** | 51 |

# 30. Selected Condensed Data from the Financial Statements of Pelephone Communications Ltd., Bezeq International Ltd., and DBS Satellite Services (1998) Ltd.

## 30.1. Pelephone Communications Ltd.

Data from the statement of financial position

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Current assets | **1,420** | 1,658 |
| Non-current assets | **1,854** | 1,883 |
| | **3,274** | 3,541 |
| Current liabilities | **448** | 610 |
| Non-current liabilities | **70** | 86 |
| Total liabilities | **518** | 696 |
| Equity | **2,756** | 2,845 |
| | **3,274** | 3,541 |

Selected data from the statement of income

| | Year ended December 31 | | |
|---|---|---|---|
| | 2015 | 2014 | 2013 |
| | NIS million | NIS million | NIS million |
| Revenues from services | **1,999** | 2,453 | 2,808 |
| Revenues from sales of terminal equipment | **891** | 966 | 1,001 |
| Total revenues from services and sales | **2,890** | 3,419 | 3,809 |
| Cost of services and sales | **2,383** | 2,537 | 2,711 |
| Gross profit | **507** | 882 | 1,098 |
| Selling and marketing expenses | **247** | 309 | 320 |
| General and administrative expenses | **98** | 106 | 109 |
| Other operating expenses | **5** | 18 | 61 |
| | **350** | 433 | 490 |
| Operating profit | **157** | 449 | 608 |
| Financing expenses (income) | | | |
| Financing expenses | **4** | 21 | 46 |
| Financing income | **(53)** | (77) | (137) |
| Financing income, net | **(49)** | (56) | (91) |
| Income before income tax | **206** | 505 | 699 |
| Income tax | **55** | 132 | 178 |
| Profit for the year | **151** | 373 | 521 |

## 30.2. Bezeq International Ltd.

Data from the statement of financial position

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Current assets | **456** | 487 |
| Non-current assets | **714** | 730 |
| | **1,170** | 1,217 |
| Current liabilities | **314** | 313 |
| Non-current liabilities | **29** | 79 |
| Total liabilities | **343** | 392 |
| Equity | **827** | 825 |
| | **1,170** | 1,217 |

Selected data from the statement of income

| | Year ended December 31 | | |
|---|---|---|---|
| | 2015 | 2014 | 2013 |
| | NIS million | NIS million | NIS million |
| Revenues | **1,578** | 1,504 | 1,433 |
| Operating expenses | **1,015** | 951 | 879 |
| Gross profit | **563** | 553 | 554 |
| Selling and marketing expenses | **209** | 209 | 205 |
| General and administrative expenses | **116** | 112 | 119 |
| Other revenues, net | **(2)** | - | 3 |
| Operating profit | **240** | 232 | 227 |
| Financing expenses (income) | | | |
| Financing expenses | **15** | 18 | 23 |
| Financing income | **(7)** | (9) | (9) |
| Financing expenses (income), net | **8** | 9 | 14 |
| Share in the profits of equity-accounted investees | **-** | 1 | 1 |
| Income before income tax | **232** | 224 | 214 |
| Income tax expenses | **60** | 60 | 56 |
| Profit for the year | **172** | 164 | 158 |

## 30.3. DBS Satellite Services (1998) Ltd.

Data from the statement of financial position

| | December 31, 2015 | December 31, 2014 |
|---|---|---|
| | NIS million | NIS million |
| Current assets | **319** | 405 |
| Non-current assets | **1,348** | 1,387 |
| | **1,667** | 1,792 |
| Current liabilities | **903** | 952 |
| Non-current liabilities | **892** | 4,054 |
| Loans from shareholders | **4,890** | 1,450 |
| Total liabilities | **6,685** | 6,456 |
| Capital deficit | **(5,018)** | (4,664) |
| | **1,667** | 1,792 |

Selected data from the statement of income

| | Year ended December 31 | | |
|---|---|---|---|
| | 2015 | 2014 | 2013 |
| | NIS million | NIS million | NIS million |
| Revenues from services | **1,774** | 1,724 | 1,635 |
| Operating expenses | **1,289** | 1,203 | 1,130 |
| Gross profit | **485** | 521 | 505 |
| Selling and marketing expenses | **140** | 154 | 154 |
| General and administrative expenses | **95** | 94 | 84 |
| | **235** | 248 | 238 |
| Operating profit | **250** | 273 | 267 |
| Financing expenses (income) | | | |
| Financing expenses | **122** | 137 | 168 |
| Financing expenses for shareholder loans, net | **513** | 483 | 486 |
| Financing income | **(32)** | (26) | (7) |
| Financing expenses, net | **603** | 594 | 647 |
| Loss before income tax | **(353)** | (321) | (380) |
| Income tax | **1** | 1 | 1 |
| Loss for the year | **(354)** | (322) | (381) |