Bezeq The Israel Telecommunication Corporation Limited

Condensed Consolidated Interim Financial Statements

As at March 31, 2015

(Unaudited)

bezeq

Contents	Page

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Review Report to the Shareholders of

"Bezeq" -The Israel Telecommunication Corporation Ltd.

Introduction

We have reviewed the accompanying financial information of "Bezeq" -The Israel Telecommunication Corporation Ltd. and its subsidiaries (hereinafter – "the Group") comprising of the condensed consolidated interim statement of financial position as of March 31, 2015 and the related condensed consolidated interim statements of income, comprehensive income, changes in equity and cash flows for the three-month period then ended. The Board of Directors and Management are responsible for the preparation and presentation of this interim financial in accordance with IAS 34 "Interim Financial Reporting", and are also responsible for the preparation of financial information for this interim period in accordance with Section D of the Securities Regulations (Periodic and Immediate Reports), 1970. Our responsibility is to express a conclusion on this interim financial information based on our review.

We did not review the condensed interim financial information of a certain consolidated subsidiary whose assets constitute 0.9% of the total consolidated assets as of March 31 2015, and whose revenues constitute 1.2% of the total consolidated revenues for the three month period then ended. The condensed interim financial information of that company was reviewed by other auditors whose review report thereon was furnished to us, and our conclusion, insofar as it relates to amounts emanating from the financial information of that company, is based solely on the said review report of the other auditors.

Scope of Review

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

Conclusion

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

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

Without qualifying our abovementioned conclusion, we draw attention to lawsuits filed against the Group which cannot yet be assessed or the exposure in respect thereof cannot yet be estimated, as set forth in Note 5.

Somekh Chaikin

Certified Public Accountants (Isr.)

Condensed Consolidated Interim Statements of Financial Position

	March 31, 2015	March 31, 2014	December 31, 2014
	(Unaudited)	(Unaudited)	(Audited)
Assets	NIS million	NIS million	NIS million
Cash and cash equivalents	**1,168**	1,049	660
Investments	**2,541**	1,345	2,223
Trade receivables	**2,290**	2,499	2,227
Other receivables	**271**	293	238
Inventory	**87**	100	96
Assets classified as held for sale	**15**	50	22
Total current assets	**6,372**	5,336	5,466
Trade and other receivables	**541**	618	566
Broadcasting rights, net of rights exercised	**460**	-	-
Property, plant and equipment	**6,956**	6,008	6,079
Goodwill (see Note 4.2)	**2,478**	1,172	1,040
Intangible assets (see Note 4.2)	**2,025**	867	753
Deferred and other expenses	**256**	260	253
Investments in equity-accounted investees (see Note 4.2)	**29**	1,032	1,057
Investments	**103**	81	99
Deferred tax assets	**-**	29	-
Total non-current assets	**12,848**	10,067	9,847
Total assets	**19,220**	15,403	15,313

Condensed Consolidated Interim Statements of Financial Position (Contd.)

	March 31, 2015	March 31, 2014	December 31, 2014
	(Unaudited)	(Unaudited)	(Audited)
Liabilities and equity	NIS million	NIS million	NIS million
Debentures, loans and borrowings	**1,852**	1,113	1,481
Trade payables	**1,074**	624	664
Other payables, including derivatives	**953**	818	710
Liability to Eurocom DBS Ltd, related party (see Note 4.2.2)	**781**	-	-
Current tax liabilities	**670**	529	600
Provisions	**84**	122	62
Employee benefits	**274**	269	259
Dividend payable	**-**	802	-
Total current liabilities	**5,688**	4,277	3,776
Loans and debentures	**10,060**	8,604	8,606
Employee benefits	**238**	235	233
Provisions	**69**	68	69
Deferred tax liabilities	**23**	32	17
Derivatives	**126**	21	94
Deferred income and others	**92**	74	77
Total non-current liabilities	**10,608**	9,034	9,096
Total liabilities	**16,296**	13,311	12,872
Total equity	**2,924**	2,092	2,441
Total liabilities and equity	**19,220**	15,403	15,313

Shaul Elovitch	**Stella Handler**	**David (Dudu) Mizrahi**
Chairman of the Board of Directors	CEO	Deputy CEO and CFO

Date of approval of the financial statements: May 20, 2015

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

Condensed Consolidated Interim Statements of Income

		Three months ended March 31		Year ended December 31
		2015	2014	2014
		(Unaudited)	(Unaudited)	(Audited)
	Note	NIS million	NIS million	NIS million
Revenues	7	**2,174**	2,311	9,055
Costs of activity				
Depreciation and amortization		**317**	314	1,281
Salaries		**439**	448	1,768
General and operating expenses	8	**799**	869	3,366
Other operating income, net	9	**(17)**	(8)	(586)
Total operating expenses		**1,538**	1,623	5,829
Operating profit		**636**	688	3,226
Financing expenses (income)				
Financing expenses		**101**	113	486
Financing income		**(64)**	(71)	(356)
Financing expenses, net		**37**	42	130
Profit after financing expenses, net		**599**	646	3,096
Share in the losses (profits) of equity-accounted investees		**(16)**	19	170
Profit before income tax		**615**	627	2,926
Income tax		**152**	170	815
Profit for the period		**463**	457	2,111
Earnings per share (NIS)				
Basic and diluted earnings per share		**0.17**	0.17	0.77

Condensed Consolidated Interim Statements of Comprehensive Income

	Three months ended March 31		Year ended December 31
	2015	2014	2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Profit for the period	**463**	457	2,111
Items of other comprehensive income (net of tax) (mainly including hedging transactions and actuarial gains)	**17**	13	(36)
Total comprehensive income for the period	**480**	470	2,075

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

Condensed Consolidated Interim Statements of Changes in Equity

	Share capital	Share premium	Capital reserve for employee options	Capital reserve for transactions between a corporation and a controlling shareholder	Other reserves	Deficit	Total
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Three months ended March 31, 2015 (Unaudited)							
Balance as at January 1, 2015	**3,855**	**253**	**131**	**390**	**(105)**	**(2,083)**	**2,441**
Profit for the period	**-**	**-**	**-**	**-**	**-**	**463**	**463**
Other comprehensive income for the period, net of tax	**-**	**-**	**-**	**-**	**17**	**-**	**17**
Total comprehensive income for the period	**-**	**-**	**-**	**-**	**17**	**463**	**480**
Transactions with shareholders recognized directly in equity							
Exercise of options for shares	**3**	**19**	**(19)**	**-**	**-**	**-**	**3**
Balance as at March 31, 2015	**3,858**	**272**	**112**	**390**	**(88)**	**(1,620)**	**2,924**
Three months ended March 31, 2014 (Unaudited)							
Balance as at January 1, 2014	3,842	143	242	390	(67)	(2,127)	2,423
Profit for the period	-	-	-	-	-	457	457
Other comprehensive income for the period, net of tax	-	-	-	-	13	-	13
Total comprehensive income for the period	-	-	-	-	13	457	470
Transactions with shareholders recognized directly in equity							
Dividend to Company shareholders	-	-	-	-	-	(802)	(802)
Share-based payments	-	-	(1)	-	-	-	(1)
Exercise of options for shares	2	18	(18)	-	-	-	2
Balance as at March 31, 2014	3,844	161	223	390	(54)	(2,472)	2,092
Year ended December 31, 2014 (Audited)							
Balance as at January 1, 2014	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	-	-	-	-	-	(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

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

Condensed Consolidated Interim Statements of Cash Flows

	Three months ended March 31		Year ended December 31
	2015	**2014**	**2014**
	(Unaudited)	**(Unaudited)**	**(Audited)**
	NIS million	**NIS million**	**NIS million**
Cash flows from operating activities			
Profit for the period	**463**	457	2,111
Adjustments:			
Depreciation and amortization	**317**	314	1,281
Profit from sale of the shares of Coral Tell Ltd.	**-**	-	(582)
Share in the losses (profits) of equity-accounted investees	**(16)**	19	170
Financing expenses, net	**67**	63	229
Profit from gaining control in an investee (see Note 4.2)	**(12)**	-	-
Capital gains, net	**(11)**	(17)	(175)
Share-based payments	**-**	(1)	(1)
Income tax expenses	**152**	170	815
Miscellaneous	**(1)**	(3)	(3)
Change in inventory	**9**	21	28
Change in trade and other receivables	**84**	163	549
Change in trade and other payables	**(45)**	(62)	(39)
Change in provisions	**3**	(4)	(63)
Change in employee benefits	**4**	13	3
Net income tax paid	**(53)**	(90)	(527)
Net cash from operating activities	**961**	1,043	3,796
Cash flow used for investing activities			
Investment in intangible assets and deferred expenses	**(66)**	(48)	(194)
Proceeds from the sale of property, plant and equipment	**13**	29	230
Acquisition of financial assets held for trading and others	**(440)**	(210)	(2,720)
Proceeds from the sale of financial assets held for trading and others	**121**	-	1,635
Cash in a company consolidated for the first time (see Note 4.2.4)	**299**	-	-
Purchase of property, plant and equipment	**(302)**	(267)	(1,081)
Payments for long-term investments	**(4)**	(3)	(19)
Net consideration for the sale of Coral Tell Ltd. shares	**-**	-	596
Miscellaneous	**1**	2	7
Net cash used for investing activities	**(378)**	(497)	(1,546)
Cash flows used in financing activities			
Repayment of debentures and loans	**(58)**	(82)	1,446
Issue of debentures and receipt of loans	**-**	-	(1,149)
Dividends paid	**-**	-	(2,069)
Interest paid	**(20)**	(27)	(431)
Miscellaneous	**3**	2	3
Net cash used for financing activities	**(75)**	(107)	(2,200)
Increase in cash and cash equivalents, net	**508**	439	50
Cash and cash equivalents at beginning of period	**660**	610	610
Cash and cash equivalents at end of period	**1,168**	1,049	660

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

1. General

1.1. Reporting Entity

Bezeq – The Israel Telecommunication Corporation Limited ("the Company") is a company registered in Israel whose shares are traded on the Tel Aviv Stock Exchange. The consolidated financial statements of the Company include those of the Company and its subsidiaries (together referred to as "the Group"), as well as the Group's interests in associates. The Group is a principal provider of communication services in Israel (see also Note 11 – 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. Accordingly, the statement of financial position as at March 31, 2015 includes the assets and liabilities of DBS. Due to the proximity of the business combination to the date of the financial statements, the effect of the operating results of DBS on the Group's statement of income for the three months ended March 31, 2015 was insignificant and was included under "Share in losses of equity-accounted investees". For further information see Note 4.2 regarding discontinued operations.

2. Basis of Preparation

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

2.2 The condensed consolidated interim financial statements do not contain all the information required in full annual financial statements, and should be reviewed in the context of the annual financial statements of the Company and its subsidiaries as at December 31, 2014 and the year then ended, and their accompanying notes ("the Annual Financial Statements"). The notes to the interim financial statements include only the material changes that have occurred from the date of the most recent Annual Financial Statements until the date of these consolidated interim financial statements.

2.3 The condensed consolidated interim financial statements were approved by the Board of Directors on May 20, 2015.

2.4 Use of estimates and judgment

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

Other than the contents of Note 3.2, the judgments made by management, when applying the Group's accounting policies and the key assumptions used in assessments that involve uncertainty, are consistent with those applied in the Annual Financial Statements.

Below is information about significant estimates and judgments for which changes in the assessments and assumptions could potentially have a material effect on the financial statements, in addition to the information in Note 1.7.1 to the annual financial statements:

Subject	Principal assumptions	Possible effects	Reference
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 market participant assumptions.	Change in profit/loss from gaining control	Note 4.2
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 4.2
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 4.2 and Note 10.1.3

3. Reporting Principles and Accounting Policy

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

3.2 Accounting policy for new transactions or events

In view of consolidation of DBS in these financial statements for the first time, as described in Note 4.2, below is a description of the accounting policy implemented in these condensed consolidated interim financial statements:

3.2.1 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.

3.2.2 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.

3.2.3 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.

3.2.4 In a step acquisition, 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.**

3.2.5 The Group implements the anticipated acquisition method, whereby it undertook to acquire the equity instruments of a subsidiary in return for cash or another financial asset. The commitment to acquire a subsidiary's equity instruments is recognized as a financial liability at the present value. The commitment is recognized at the agreement date, if the preconditions to the agreement are not under the Group's control.

Based on the anticipated acquisition method, non-controlling interests are derecognized at the recognition date of the commitment to acquire the subsidiary's equity instruments. Accordingly, the Group's share in the subsidiary's equity and operating expenses includes the share of the holders of non-controlling interests.

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

4. Group Entities

4.1 A detailed description of the Group entities appears in Note 10 to the Annual Financial Statements. Below is a description of the material changes that occurred in connection with the Group entities since publication of the Annual Financial Statements.

4.2 Business combination with DBS Satellite Services (1998) Ltd. ("DBS") that occurred in the period

4.2.1 As described in Note 10.1.2 to the annual financial statements, 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 will 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 tax synergy 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.

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, which has not yet been completed. At this stage, the agreement with Eurocom DBS has been extended by 90 days. In accordance with the agreement, each party to the agreement has the right to extend the agreement by 90 days.

4.2.2 An increase in the Company's holding in DBS to 58.4% constitutes acquisition of control in DBS, therefore, the Company consolidates 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 as a step acquisition.

The binding agreement between the Company and Eurocom DBS for acquisition of the entire holdings of Eurocom DBS in DBS is contingent on obtaining the approval of the Ministry of Communications, which has not yet been received, therefore, as at March 31, 2015, the transaction for acquisition of 100% of the rights in DBS has not yet been completed, as stated above.

As at the date of the business combination, a liability of NIS 680 million to Eurocom DBS was recognized. This amount includes the fair value of the outstanding shareholder loans of NIS 183 million from Eurocom DBS to DBS. In addition, a liability of NIS 101 million was recognized for contingent consideration as described in Note 10, Financial Instruments. Therefore, the total liability to Eurocom DBS recognized in the statement of financial position amounts to NIS 781 million.

Accordingly, as from the date of the business combination, the Company consolidates the full results of DBS and the statement of changes in equity does not include the share of non-controlling interests in DBS.

4.2.3 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 whose opinion is attached to these financial statements. In accordance with the valuation, the 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 for the three months ended March 13, 2015.

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 is 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 subscribers, 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 a participant in the relevant market that might acquire the Company's holdings in DBS and does not take into account the specific operational and tax synergies between the companies.

4.2.4 **Identifiable assets and liabilities acquired (according to provisional amounts set out below):**

	March 23, 2015
	(Unaudited)
	NIS million
Cash and cash equivalents	**299**
Trade and other receivables	**184**
Broadcasting rights	**449**
Property, plant and equipment	**801**
Intangible assets (including excess cost attributed to customer relations and brand as described below)	**1,284**
Debentures, loans, and borrowings (including excess cost attributed to debentures as described below)	**(1,947)**
Trade payables and other liabilities	**(632)**
Contingent liabilities (including excess cost attributed to contingent liabilities as described below)	**(19)**
Identifiable assets, net	**419**

The Company carried out temporary attribution of the acquisition cost in relation to the fair value of the assets and liabilities that were acquired in the business combination, due to the proximity of the gain of control to the date of the financial statements. Temporary attribution was based on the valuation performed by an independent assessor whose opinion is attached to these financial statements.

As at the approval date of these financial statements, the excess cost amounted to NIS 2,405 million. The Company has not yet completed measurement of the tax asset, to the extent that it concludes that it should be recognized. In addition, goodwill arising on acquisition has not yet been attributed to the Group's operating segments.

The excess cost that was determined provisionally was attributed as follows:

	March 23, 2015
	(Unaudited)
	NIS million
Customer relations (see section A below)	790
Brand (see section B below)	347
Goodwill (see section C below)	1,438
Total excess cost attributed to intangible assets	**2,575**
Debentures (see section D below)	(160)
Contingent liabilities (see section E below)	(10)
Total excess cost	**2,405**

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 value:** 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. **Goodwill:** Following the acquisition of control, goodwill was recognized as follows:

	March 23, 2015
	(Unaudited)
	NIS million
Consideration value	781
Fair value of the investment in DBS prior to the acquisition	1,076
Less the fair value of net identifiable assets	(419)
Goodwill	**1,438**

The amount of goodwill was estimated provisionally and includes the cash consideration and the contingent consideration to Eurocom DBS for the amount expected to be paid to the holders of non-controlling interests.

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 excess cost represents a present obligation arising from a class action filed by DBS customers.

4.2.5 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. When determining the amounts, the management assumed that the fair value adjustments at the date of the business combination, which were determined provisionally, are the same as the adjustments that would have been received had the business combination taken place on January 1, 2015.

4.2.6 Since the beginning of its operations, DBS has accumulated considerable losses. In 2014, DBS recorded a loss of NIS 322 million. As a result of these losses, as at March 31, 2015, DBS had an equity deficit and a working capital deficit of NIS 4,667 million and NIS 525 million, respectively.

4.2.7 As at March 31, 2015, DBS is in compliance with the financial covenants established under the financing and debenture agreements. As at March 31, 2015, DBS is in compliance with the debt/EBITDA ratio covenant established in Deed of Trust B (as at March 31, 2015, the debt/EBITDA ratio was 2.6). Furthermore, DBS is in compliance with the debt/EBITDA ratio covenant set out in Debenture 2012 (as at March 31, 2015, the debt/EBIDTA ratio was 2.5) and the debt/E-C ratio covenant set out in Debenture 2012 (as at March 31, 2015, the debt-E-C ratio was 6.4).

Subsequent to the date of the financial statements, DBS issued additional debentures as described in Note 13 below.

4.2.8 The management of DBS believes that the financing resources available to DBS, which include the working capital deficit, and its debt raising activities, will be sufficient for the operations of DBS for the coming year, based on the forecasted cash flows approved by DBS's board of directors. If additional resources are required to meet its operational requirements for the coming year, DBS will adjust its operations to preclude the need for additional resources beyond those available to it.

5. 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 legal claims, the financial statements include appropriate provisions of NIS 80 million, where provisions are required to cover the exposure arising from such legal claims.

In the opinion of the managements of the Group companies, the additional exposure (beyond these provisions) as at March 31, 2015 for claims filed against Group companies on various matters and which are unlikely to be realized, amounted to NIS 3.1 billion. There is also additional exposure of NIS 2.5 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 5.2 below.

5.1 Below is a description of the contingent liabilities of the Group (including DBS) as at March 31, 2015, classified into groups with similar characteristics:

Claims group	Nature of the claims	Provision	Additional exposure	Exposure for claims that cannot yet be assessed
		NIS million		
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.	**9**	**131**	**-**
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.	**40**	**2,670**	**456**
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**	**122**	**-**
Claims for punitive damages, real estate and infrastructure	Claims for alleged physical damage or damage to property caused by Group companies and in relation to real estate and infrastructure. The additional amount of exposure for punitive damages does not include claims for which the insurance coverage is not disputed.	**2**	**63**	**-**
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**	**46**	**2,000***
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.	**15**	**35**	**-**
Total legal claims against the Company and subsidiaries		**80**	**3,067**	**2,456**

* A claim filed by shareholders against the Company and officers in the Company amounting to NIS 1.1 billion or NIS 2 billion (according to the method of calculating the damage to be determined).

5.2 Subsequent to the reporting date, claims amounting to NIS 52 million were filed against Group companies, and another claim without a monetary estimate. At the approval date of the financial statements, the chances of these claims cannot yet be assessed. In addition, claims with exposure of NIS 36 million came to an end.

6. Capital

6.1 Below are details of the Company's equity:

Registered			Issued and paid up		
March 31, 2015	March 31, 2014	December 31, 2014	March 31, 2015	March 31, 2014	December 31, 2014
(Unaudited)	(Unaudited)	(Audited)	(Unaudited)	(Unaudited)	(Audited)
Number of shares	Number of shares	Number of shares	Number of shares	Number of shares	Number of shares
2,825,000,000	2,825,000,000	2,825,000,000	**2,746,010,675**	2,731,837,758	2,743,283,920

6.2 On May 6, 2015, the general meeting of the Company's shareholders approved the recommendation of the Company's Board of Directors of March 25, 2015 to distribute a cash dividend of NIS 844 million to the Company's shareholders. The dividend will be paid on May 27, 2015.

7. Revenues

	Three months ended March 31		Year ended December 31
	2015	2014	2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Domestic fixed-line communication			
Fixed-line telephony	**395**	417	1,636
Internet - infrastructure	**383**	332	1,394
Transmission and data communication	**207**	207	802
Other services	**58**	57	220
	1,043	1,013	4,052
Cellular telephony			
Cellular services and terminal equipment	**486**	623	2,399
Sale of terminal equipment	**224**	280	966
	710	903	3,365
International communications, internet and NEP services	**371**	332	1,425
Other	**50**	63	213
	2,174	2,311	9,055

8. General and Operating Expenses

	Three months ended March 31		Year ended December 31
	2015	2014	2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Terminal equipment and materials	**226**	262	928
Interconnectivity and payments to domestic and international operators	**212**	206	847
Maintenance of buildings and sites	**150**	156	639
Marketing and general	**119**	139	555
Services and maintenance by sub-contractors	**34**	40	137
Vehicle maintenance	**35**	37	154
Content services	**13**	15	58
Collection fees	**10**	14	48
	799	869	3,366

9. Other Operating Expenses (Income), Net

	Three months ended March 31		Year ended December 31
	2015	2014	2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Profit from gaining control in DBS Satellite Services (1998) Ltd.	**12**	-	-
Profit from the sale of property, plant and equipment (mainly real estate)	**11**	12	167
Profit from copper sales	**-**	5	8
Elimination of provision for contingent liabilities, net	**-**	-	23
Profit from sale of the shares of Coral Tell Ltd.	**-**	-	582
Other operating income	**23**	17	780
Provision for contingent liabilities, net	**6**	-	-
Provision for severance pay in voluntary redundancy	**-**	8	176
Expenses for collective agreement at Pelephone	**-**	-	18
Others	**-**	1	-
Total other operating expenses	**6**	9	194
	(17)	(8)	(586)

10. Financial Instruments

10.1. Fair value

10.2.1 Financial instruments at fair value for disclosure purposes only

The table below shows the differences between the carrying amount and the fair value of financial liabilities. The methods used to estimate the fair values of financial instruments are described in Note 28.7 to the Annual Financial Statements.

	March 31, 2015		March 31, 2014		December 31, 2014	
	Carrying amount (including accrued interest)	Fair value	Carrying amount (including accrued interest)	Fair value	Carrying amount (including accrued interest)	Fair value
	(Unaudited)		(Unaudited)		(Audited)	
	NIS million		NIS million		NIS million	
Bank loans (unlinked)	**2,131**	**2,328**	2,105	2,240	2,112	2,292
Debentures issued to the public (CPI-linked)	**3,793**	**4,072**	3,154	3,420	3,820	4,033
Debentures issued to the public (unlinked)	**1,354**	**1,432**	1,354	1,471	1,335	1,426
Debentures issued to financial institutions (unlinked)	**410**	**480**	410	456	403	467
Debentures issued to financial institutions (CPI-linked)	**1,748**	**1,908**	-	-	-	-
	9,436	**10,220**	7,023	7,587	7,670	8,218

10.2.2 Fair value hierarchy

The table below presents an analysis of the financial instruments measured at fair value, with details of the evaluation method. The methods used to measure the fair value of investments in ETFs, monetary funds, and forward contracts are described in Note 28.7 to the annual financial statements. The methods used to measure the fair value of contingent consideration for a business combination are described in Note 10.1.3 below.

	March 31, 2015	March 31, 2014	December 31, 2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Level 1: investment in exchange-traded funds and financial funds	**1,392**	1,281	1,513
Level 2: forward contracts	**(144)**	(34)	(110)
Level 3: contingent consideration for a business combination (Note 4.2)	**(101)**	-	-
Level 3: investment in non-marketable shares	**9**	11	9
	1,156	1,258	1,412

10.2.3 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 4.2:

	March 31, 2015	
	Maximum additional consideration under the agreement	**Fair value**
	(Unaudited)	**(Unaudited)**
	NIS million	**NIS million**
Additional consideration for tax synergy (first additional consideration)(A)	200	84
Additional consideration for the business results of DBS (second additional consideration) (B)	170	17
	370	101

A. First additional consideration

The fair value of the first additional contingent consideration was calculated by an independent assessor, whose opinion is attached to these financial statements, based on a legal opinion on tax issues related to the possible merger between the Company and DBS. The legal opinion includes the probability of the chances and risks facing the Company regarding utilization of losses.

The estimated fair value of the contingent consideration will increase as the probability attributed to major risks in utilization of losses, as assessed in the legal opinion, decreases.

A 10% change in the probability attributed to major risks will result in a change of NIS 36 million in the first contingent consideration.

B. Second additional consideration

The fair value of the first additional consideration was estimated by the assessor, whose opinion is attached to these financial statements, using the Monte Carlo simulation with risk neutral measure of the underlying asset which is the expected cash flow. The unobservable parameter that was used in the model and would have significantly changed the fair value is the expected cash flows in 2015-2017. To calculate the value of the second contingent consideration, a free cash flow was assumed as presented in the fair value assessment of Bezeq's holdings in DBS prior to gain of control as described in Note 4.2.3.

An increase of 10% in the expected cash flow will result in an increase of NIS 7 million in the estimated contingent consideration.

11. Segment Reporting

11.1. Operating segments

	Three months ended March 31, 2015 (Unaudited)						
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television*	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	1,042	709	368	440	49	(440)	2,168
Inter-segment revenues	71	18	25	-	4	(112)	6
Total revenues	1,113	727	393	440	53	(552)	2,174
Depreciation and amortization	176	104	32	76	3	(74)	317
Segment results – operating profit	547	32	61	59	(2)	(61)	636
Financing expenses	98	3	4	104	-	(108)	101
Financing income	(44)	(17)	(3)	(42)	(4)	46	(64)
Total financing expenses (income), net	54	(14)	1	62	(4)	(62)	37
Segment profit (loss) after financing expenses, net	493	46	60	(3)	2	1	599
Share in profits (losses) of associates	-	-	-	-	-	16	16
Segment profit (loss) before income tax	493	46	60	(3)	2	17	615
Income tax	126	10	16	-	-	-	152
Segment results – net profit (loss)	367	36	44	(3)	2	17	463

	Three months ended March 31, 2014 (Unaudited)						
	Domestic fixed-line communication	Cellular communications	International communications and internet services	Multi-channel television *	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	1,011	902	331	424	62	(424)	2,306
Inter-segment revenues	66	15	24	-	5	(105)	5
Total revenues	1,077	917	355	424	67	(529)	2,311
Depreciation and amortization	168	106	32	70	7	(69)	314
Segment results – operating profit	504	126	58	73	1	(74)	688
Financing expenses	106	6	5	123	2	(129)	113
Financing income	(50)	(24)	(3)	(16)	-	22	(71)
Total financing expenses (income), net	56	(18)	2	107	2	(107)	42
Segment profit (loss) after financing expenses, net	448	144	56	(34)	(1)	33	646
Share in profits (losses) of associates	-	-	1	-	-	(20)	(19)
Segment profit (loss) before income tax	448	144	57	(34)	(1)	13	627
Income tax	116	36	15	-	3	-	170
Segment results – net profit (loss)	332	108	42	(34)	(4)	13	457

	Year ended December 31, 2014 (Audited)						
	Domestic fixed-line communication	**Cellular communications**	**International communications and internet services**	**Multi-channel television ***	**Other**	**Adjustments**	**Consolidated**
	NIS million	**NIS million**	**NIS million**	**NIS million**	**NIS million**	**NIS million**	**NIS million**
Revenues from external sources	4,045	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
Financing expenses	472	21	18	620	2	(647)	486
Financing income	(285)	(77)	(9)	(26)	(11)	52	(356)
Total financing expenses (income), net	187	(56)	9	594	(9)	(595)	130
Segment profit (loss) after financing expenses, net	1,793	505	223	(321)	638	258	3,096
Share in profits (losses) of associates	-	-	1	-	(3)	(168)	(170)
Segment profit (loss) before income tax	1,793	505	224	(321)	635	90	2,926
Income tax	478	132	60	1	147	(3)	815
Segment results – net profit (loss)	1,315	373	164	(322)	488	93	2,111

11.2. Adjustment of profit or loss for reporting segments

	Three months ended March 31		Year ended
	2015	**2014**	**December 31, 2014**
	(Unaudited)	**(Unaudited)**	**(Audited)**
	NIS million	**NIS million**	**NIS million**
Operating profit for reporting segments	**699**	761	2,934
Cancellation of results for a segment classified as an associate *	**(59)**	(73)	(273)
Financing income (expenses), net	**(37)**	(42)	(130)
Share in profits (losses) of associates	**16**	(19)	(170)
Profit (loss) for operations classified in other categories and other adjustments	**(4)**	-	565
Consolidated profit before income tax	**615**	627	2,926

* The Company's investment in DBS was accounted for using the equity method up to March 25, 2015. As from this date, the financial statements of DBS are consolidated with the financial statements of the Group as described in Note 4 above. The Group reports on multi-channel TV as an operating segment without adjustment to ownership rates in each reporting period, as described in Note 26 to the annual financial statements.

12. Condensed Financial Statements of Pelephone, Bezeq International, and DBS

12.1. Pelephone Communications Ltd.

Selected data from the statement of financial position

	March 31, 2015	March 31, 2014	December 31, 2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	**1,695**	1,828	1,658
Non-current assets	**1,866**	1,996	1,883
	3,561	3,824	3,541
Current liabilities	**750**	906	610
Long-term liabilities	**89**	128	86
Total liabilities	**839**	1,034	696
Capital	**2,722**	2,790	2,845
	3,561	3,824	3,541

Selected data from the statement of income

	Three months March 31		Year ended December 31,
	2015	2014	2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Revenues from services	**499**	637	2,453
Revenues from sales of terminal equipment	**228**	280	966
Total revenues from services and sales	**727**	917	3,419
Cost of services and sales	**607**	681	2,537
Gross profit	**120**	236	882
Selling and marketing expenses	**63**	83	309
General and administrative expenses	**25**	27	106
Other operating expenses	**-**	-	18
	88	110	433
Operating profit	**32**	126	449
Financing expenses	**3**	6	21
Financing income	**(17)**	(24)	(77)
Financing income, net	**(14)**	(18)	(56)
Profit before income tax	**46**	144	505
Income tax	**10**	36	132
Profit for the period	**36**	108	373

12.2. Bezeq International Ltd.

Selected data from the statement of financial position

	March 31, 2015	March 31, 2014	December 31, 2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	**544**	515	487
Non-current assets	**750**	751	730
	1,294	1,266	1,217
Current liabilities	**437**	363	313
Long-term liabilities	**71**	122	79
Total liabilities	**508**	485	392
Capital	**786**	781	825
	1,294	1,266	1,217

Selected data from the statement of income

	Three months March 31		Year ended December 31,
	2015	2014	2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Revenues from services	**393**	355	1,504
Operating expenses	**251**	218	951
Gross profit	**142**	137	553
Selling and marketing expenses	**53**	50	209
General and administrative expenses	**28**	29	112
	81	79	321
Operating profit	**61**	58	232
Financing expenses	**4**	5	18
Financing income	**(3)**	(3)	(9)
Financing expenses (income), net	**1**	2	9
Share in profits of equity-accounted associates	**-**	1	1
Profit before income tax	**60**	57	224
Income tax	**16**	15	60
Profit for the period	**44**	42	164

12.3. DBS Satellite Services (1998) Ltd.

Selected data from the statement of financial position

	March 31, 2015	March 31, 2014	December 31, 2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	**481**	290	434
Non-current assets	**1,398**	1,346	1,386
	1,879	1,636	1,820
Current liabilities	**1,006**	939	980
Long-term liabilities	**1,422**	1,413	1,450
Loans from shareholders	**4,118**	3,661	4,054
Total liabilities	**6,546**	6,013	6,484
Capital deficit	**(4,667)**	(4,377)	(4,664)
	1,879	1,636	1,820

Selected data from the statement of income

	Three months March 31		Year ended December 31,
	2015	2014	2014
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Revenues from services	**440**	424	1,724
Operating expenses	**295**	269	1,110
Gross profit	**145**	155	614
Selling and marketing expenses	**36**	40	154
General and administrative expenses	**50**	42	187
	86	82	341
Operating profit	**59**	73	273
Financing expenses	**104**	123	620
Financing income	**(42)**	(16)	(26)
Financing expenses (income), net	**62**	107	594
Loss before income tax	**(3)**	(34)	(321)
Income tax	**-**	-	1
Loss for the period	**(3)**	(34)	(322)

13. Subsequent Events

13.1 In April and May 2015, the Company entered into agreements with banks, whereby the Company received an undertaking from the banks to provide credit to the Company to refinance its future debt in June 2016 in a total amount of NIS 900 million, with a duration of 4.6 years (payable in five equal annual payments commencing on June 1, 2019 through to June 1, 2023), and a fixed NIS unlinked interest rate of 3.7%.

The terms of the undertaking 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 Note 11.2.1 to the annual financial statements, including the following: an undertaking to refrain from creating additional liens 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 period of the undertaking to provide credit.

13.2 In April 2015, DBS issued additional debentures (Series B) by expanding the series, amounting to NIS 198 million. For information about the terms of the debentures, see Note 10.1.5 to the Annual Financial Statements.