November 7, 2012

Quarterly report for period ended September 30, 2012

- Update to Chapter A (Description of Company Operations) of the Periodic Report for 2011
- Board of Directors' Report on the State of the Company's Affairs for the period ending September 30, 2012
- Interim Financial Statements as at September 30, 2012

bezeq

Update to Chapter A (Description of Company Operations) of the Periodic Report for 2011

bezeq

Update to Chapter A (Description of Company Operations) [1] of the Periodic Report for 2011 ("Periodic Report") of "Bezeq" - The Israel Telecommunication Corporation Ltd. ("the Company")

1. Description of the general development of Bezeq Group's business

Section 1.1 - Bezeq Group activities and business development

Section 1.1.1 – General

Beginning April 9, 2012, the Company holds all the shares of Walla!, further to completion of a full tender offer for the shares of Walla! held by the public (regarding this, see update to Section 1.1.2).

Following are details of the current holdings in the Company including fully diluted holdings, assuming exercise of all the options allotted to the Group's employees and managers as at September 30, 2012 and November 6, 2012:

Shareholders	Percentage of holdings		
	As at September 30, 2012	As at November 6, 2012	Fully diluted as at November 6, 2012[2]
B Communications (through B Tikshoret)[3]	30.97%	30.97%	30.19%
The public	69.03%	69.03%	69.81%

Section 1.1.2 - Mergers and acquisitions

Concerning the full tender offer for Walla! shares - pursuant to publication of the full tender offer for the purchase of all the shares in Walla! held by shareholders from the public, on April 5, 2012 the tender offer was accepted by the majority stipulated in the Companies Law (of the number of shares offered for sale, 12,980,972 shares accounting for 28.45% of the share capital of Walla!, notice of acceptance was received for 11,371,893 shares, accounting for 24.92% of the share capital of Walla!), and accordingly all the shares of Walla! that were held by the public were acquired, so that subsequent to the acquisition and beginning April 15, 2012, Walla! was delisted from the Tel Aviv Stock Exchange and became a private company wholly owned by the Company. Regarding this, also see Note 4.1 to the Company's consolidated financial statements for the period ended September 30, 2012.

Section 1.4 - Distribution of dividends

Section 1.4.2 - Distribution of a dividend

On April 24, 2012, the General Meeting of the Company's shareholders (further to a recommendation of the Board of Directors from March 14, 2012), approved the distribution of a cash dividend to the Company's shareholders in the total sum of NIS 1,074 million, which on the determining date for the distribution (May 4, 2012) amounts to NIS 0.3951788 per share and 39.51788% of the Company's issued and paid-up share capital. The dividend was paid on May 21, 2012. Together with this distribution, the third portion of the special distribution, in the amount of NIS 500 million, was paid, which on the determining date for the distribution (May 4, 2012) amounts to NIS 0.1839752 per share

[1] The update is in accordance with Article 39A of the Securities Regulations (Periodic and Immediate Reports), 5730-1970, and includes material changes or innovations that have occurred in the corporation in any matter which must be described in the periodic report. The update relates to the Company's periodic report for the year 2011 and refers to the section numbers in Chapter A (Description of Company Operations) in the said periodic report.

[2] The calculation of full dilution assumes that all the allotted options will be exercised into shares. In view of the mechanism of net exercise of stock appreciation rights in the plan for managers and senior employees of the Group from November 2007 and the employee stock option plan (2010) this assumption is only theoretical, since in practice, the recipients exercising the stock options, will not be allotted all the shares deriving from them, but only shares of an amount that reflects the financial benefit embedded in the stock options.

[3] From the total holdings described above, 3,000,000 shares are held jointly by the Chairman of the Board of Directors, Mr. Shaul Elovitch, and his brother Mr. Josef Elovitch, the Company's controlling shareholders (in concatenation). 72,360 shares are held by Mrs. Iris Elovitch, wife of controlling shareholder Shaul Elovitch, and 11,566 shares are held by Mrs. Irena Elovitch, daughter-in-law of Shaul Elovitch. These holdings amount to a total of 0.11% of all holdings in the Company.

and 18.39752% of the Company's issued and paid-up share capital (regarding this, also see the update to Section 1.4.3).

On September 6, 2012, the General Meeting of the Company's shareholders (further to a recommendation of the Board of Directors from August 1, 2012), approved the distribution of a cash dividend to the Company's shareholders in the total sum of NIS 997 million, which on the determining date for the distribution (September 23, 2012) is NIS 0.3659618 per share and 36.59618% of the Company's issued and paid-up share capital. The dividend was paid on October 10, 2012. Together with this distribution, the fourth portion of the special distribution was paid in the amount of NIS 500 million, which on the determining date for the distribution (September 23, 2012) amounted to NIS 0.1835315 per share and 18.35315% of the Company's issued and paid-up share capital (regarding this, also see the update to Section 1.4.3).

The outstanding, distributable profits at the reporting date amount to NIS 342 million.[4]

Section 1.4.3 - Distribution that is not in compliance with the earnings test

On March 29, 2012 and on April 4, 2012, two objections were filed in the Economic Department of the Tel Aviv District Court to the continuation of payments in respect of the distribution which is not in compliance with the earnings test which was approved by the same court on March 31, 2011. The motions were filed by two holders of Debentures (Series 5) of the Company who had also filed a similar objection in 2011 and an application to be included therein as detailed in the Periodic Report for 2011. The Company submitted its response to the objections, rejecting the arguments detailed in the objections, and requesting the court to dismiss the objections in limine and in substance. On May 14, 2012, the court decided to dismiss the aforementioned objections, and as requested by the Company, on May 22, 2012, the court stated that as per its decision from May 14, 2012, there is no need for the Company to apply to the court before payment of each of the remaining portions of the special dividend, which the court approved on March 31, 2011. The Company therefore intends to continue to pay the distributions as it has in the past, while reviewing its compliance with the repayment ability test prior to the payments, and without this review necessitating any further application by the Company to the court. Regarding this, also see the Company's Immediate Report dated May 15, 2012, and supplementary immediate reports to this report dated May 21, 2012, May 22, 2012, and May 30, 2012, presented here by way of reference.

It should be noted that during August-September 2012, various motions were filed in the Tel Aviv District Court (Economic Department) by the same entities which had filed the above-mentioned objections, expressing a possible objection with regard to the distribution of the fourth portion of the Special Distribution. However, at a court hearing which took place on September 24, 2012, these entities announced that they are no longer insistent on conducting the proceeding, and the fourth portion was distributed on time, as detailed in the update to Section 1.4.2.

[4] Subject to complying with the distribution tests.

Section 1.5 - Financial information concerning Bezeq Group's operations

Section 1.5.4 - Principal results and operational data

A. Bezeq Fixed Line (the Company's operations as a domestic carrier)

	Q3 2012	Q2 2012	Q1 2012	Q4 2011	Q3 2011	Q2 2011	Q1 2011
Revenues (NIS millions)	1,149	1,161	1,199	1,114	1,186	1,170	1,178
Operating profit (NIS millions)	419	437	539	384	546	517	211
Depreciation and amortization (NIS millions)	185	178	178	175	180	171	162
(EBITDA) (NIS millions) (7)	604	615	717	559	726	688	373
Net profit (NIS millions)	246	263	348	301	311	330	123
Cash flow from operating activities (NIS millions)	470	376	651	550	641	496	419
Payments for investments in property, plant & equipment and intangible assets (NIS millions) (6)	249	238	269	259	268	319	319
Proceeds from sale of property, plant & equipment and intangible assets (NIS millions) (6)	96	22	46	40	68	48	72
Free cash flow (NIS millions) (1)(8)	317	160	428	216	441	225	287
Number of active subscriber lines at end of period (in thousands) (2)	2,299	2,335	2,368	2,367	2,363	2,356	2,358
Average monthly revenue per line (NIS) (ARPL)(3)	73	73	74	70	78	77	79
No. of outgoing minutes (millions)	2,125	2,226	2,360	2,339	2,482	2,415	2,521
No. of incoming minutes (millions)	1,590	1,514	1,543	1,526	1,602	1,535	1,577
No. of internet subscribers at end of period (thousands) (2)	1,153	1,136	1,121	1,111	1,100	1,088	1,079
% of subscribers using NGN services out of total Internet subscribers connected to the NGN network (%)(4)	60%	57%	55%	51%	47%	43%	40%
Average monthly revenue per internet subscriber (NIS)	80	80	84	81	81	80	79
Average bandwidth per internet subscriber (Mbps)	9.0	8.3	7.5	6.7	6.0	5.3	4.8
Churn rate (5)	4.2%	3.9%	3.2%	2.8%	2.8%	2.8%	3.3%

(1) Cash from operating activities less purchase of property, plant and equipment, and intangible assets, net.

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

(3) Excluding revenues from transmission services and data communication, Internet services, services to communications operators and contractor and other works. Calculated based on the average lines for the period.

(4) The numbers for 2011 and the first quarter of 2012 were corrected in view of the revised number of Company internet subscribers connected to the NGN network, as a result of data optimization.

(5) The number of telephony subscribers who left Bezeq Fixed Line during the period divided by the average number of registered telephony subscribers in the period. The numbers in the previous quarters are presented after calculation to an accuracy(insignificant) of 0.1% per quarter.

(6) Excluding the purchase and sale (Back to Back) of a real-estate asset in the amount of NIS 115 million during 2011.

(7) EBITDA(NIS millions) is a financial index which is not based on GAAP. The Company presents this index as an additional index for estimating its business results, as it is an accepted index for company activities which disregards aspects arising from variance in the equity structure, various taxation perspectives, and the manner and period of the depreciation of property plant and equipment and intangible assets. This index is not a substitute for indices which are based on GAAP and it is not used as a sole index for estimating the results of the Company's activities or cash flows. Additionally, the index presented in this report may not be calculated in the same manner as parallel indices among other companies.

(8) Free cash flow is a financial index which is not based on GAAP. Free cash flow is defined as cash from operating activities less cash for the purchase/sale of property, plant and equipment, and intangible assets, net. The Company presents free cash flow as an additional index for estimating business performance and cash flows, given that the Company is of the opinion that the free cash flow is an important liquidity index which reflects the Company's cash from its operating activities after the investment of cash in infrastructure, property plant and equipment and in other intangible assets.

B. Pelephone

	Q3 2012	Q2 2012	Q1 2012	Q4 2011	Q3 2011	Q2 2011	Q1 2011
Revenues from services (NIS millions)	816	857	834	849	914	925	949
Revenues from the sale of terminal equipment (NIS millions)	233	291	410	390	507	513	501
Total revenues (NIS millions)	1,049	1,148	1,244	1,239	1,421	1,438	1,450
Operating profit (NIS millions)	199	259	267	262	342	357	399
Depreciation and amortization (NIS millions)	130	137	135	140	139	143	139
(EBITDA)(NIS millions)(1)	329	396	402	401	481	500	539
Net profit (NIS millions)	154	194	216	204	263	279	310
Cash flow from operating activities (NIS millions)	490	556	294	223	168	101	308
Payments for investments in property, plant & equipment and intangible assets, net (NIS millions)	84	109	115	92	71	86	133
Free cash flow (NIS millions) (1)	406	447	179	131	97	15	175
Number of subscribers at end of period (thousands) (2), (6)	2,839	2,859	2,876	2,847	2,842	2,827	2,861
Average number of minutes per subscriber per month (MOU) (3), (6)	425	409	399	384	385	370	359
Average monthly revenue per internet subscriber (NIS) (ARPU) (4), (6)	95	99	97	100	107	109	110
Revenues from value added services (included in revenues from services) (NIS millions)	268	312	307	311	310	297	283
Revenues from value added services as percentage of revenues from cellular services	35.1%	39.0%	39.6%	39.5%	36.3%	34.5%	32.1%
Churn rate (5), (6)	6.7%	6.0%	3.9%	5.3%	6.1%	6.6%	5.0%

(1) Regarding the definition of EBITDA and free cash flow, see comments (7) and (8) in the Bezeq Fixed Line table.

(2) Subscriber data include Pelephone subscribers (excluding subscribers to other operators who are hosted on the Pelephone network), and do not include subscribers connected to Pelephone services for six months or more but who are inactive. Inactive subscribers are those who in the past six months have not received or made at least one call or have not paid for Pelephone services.

(3) Average monthly use per subscriber in minutes. The index is calculated by the average monthly total outgoing minutes and incoming minutes in the period, divided by the average number of subscribers in the same period.

(4) Average monthly revenue per subscriber. The index is calculated by dividing the average total monthly revenues from cellular services, from Pelephone subscribers and other telecom operators, including revenues from cellular operators who use Pelephone's network (from which revenues began in 2012), repair services and warranty in the period, by the average number of active Pelephone subscribers in the same period.

(5) The churn rate is calculated according to the ratio of subscribers who disconnected from Pelephone's services and subscribers who became inactive during the period to the average number of active subscribers during the period.

(6) In the report for 2011, due to greater movement of subscribers to prepaid tracks in the initial months after the reduction of the disconnect fees, Pelephone decided not to include subscribers who had not made calls during the fourth quarter as active subscribers. Consequently, Pelephone deleted 91,000 subscribers. These subscribers were deleted retroactively from each quarter in which they were transferred to prepaid tracks. As a result of the foregoing, data for subscribers, ARPU, MOU and churn rates were amended retroactively in each quarter of 2011.

C. Bezeq International

	Q3 2012	Q2 2012	Q1 2012	Q4 2011	Q3 2011	Q2 2011	Q1 2011
Revenues (NIS millions)	339	330	332	342	351	332	329
Operating profit (NIS millions)	55	53	50	59	61	60	61
Depreciation and amortization (NIS millions)	34	34	34	31	28	26	24
(EBITDA)(NIS millions)(1)	89	87	84	89	89	87	85
Net profit (NIS millions)	40	39	36	44	46	46	46
Cash flow from operating activities (NIS millions)	63	64	58	76	57	68	42
Payments for investments in property, plant & equipment and intangible assets, net (NIS millions)(2)	28	36	71	103	92	47	46
Free cash flow (NIS millions) (1)	35	28	(13)	(27)	(35)	21	(4)
Churn rate (3)	4.6%	4.1%	4.3%	3.7%	3.2%	2.8%	2.9%

(1) Regarding the definition of EBITDA and free cash flow, see comments (7) and (8) in the Bezeq Fixed Line table.

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

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

D. DBS

	Q3 2012	Q2 2012	Q1 2012	Q4 2011	Q3 2011	Q2 2011	Q1 2011
Revenues (NIS millions)	403	409	417	404	405	404	406
Operating profit (NIS millions)	54	74	52	106	63	65	61
Depreciation and amortization (NIS millions)	64	54	66	62	74	71	69
(EBITDA)(NIS millions)(1)	118	128	118	168	137	136	130
Net profit (loss) (NIS millions)	(119)	(107)	(64)	7	76)	(88)	(73)
Cash flow from operating activities (NIS millions)	83	100	116	119	134	119	141
Payments for investments in property, plant & equipment and intangible assets, net (NIS millions)	87	69	56	62	67	64	71
Free cash flow (NIS millions) (1)	(4)	31	60	57	67	55	70
No. of subscribers (at end of period, thousands) (2)	581	582	585	586	585	581	580
Average monthly revenue per subscriber (ARPU) (NIS) (3)	231	234	237	229	232	232	234
Churn rate (4)	4.1%	3.9%	3.6%	2.8%	2.8%	2.9%	3.3%

(1) Regarding the definition of EBITDA and free cash flow, see comments (7) and (8) in the Bezeq Fixed Line table.

(2) Subscriber - a single household or small business customer. In the event of a business customer with multiple reception points or a large number of decoders (such as a hotel, collective community settlement, or gym), the number of subscribers is calculated by dividing the total payment received from the business customer by the average revenue from a small business customer.

(3) Average monthly revenue per subscriber is calculated by dividing DBS's total revenues (revenues from content and equipment, premium channels, advanced products, and other) by the average number of customers.

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

1.6 Group forecast

The Bezeq Group revised its forecast for anticipated performance in 2012 in its financial statements for the second quarter of 2012, as a result of increased competition in the cellular market. The Group's forecast for 2012, as published in those reports, is:

- Revenues: NIS 10.2 - 10.5 billion.
- Net profit for the shareholders: NIS 1.75 - 1.85 billion.
- EBITDA: NIS 4.4 - 4.5 billion.

The Group expects free cash flow to improve significantly compared to 2011, mainly against the backdrop of an improvement in working capital and the completion of major investment projects, and it is expected to amount to more than NIS 2.5 billion.

The Group is ready to meet the challenges facing the industry and it has introduced streamlining measures which are expected to reduce sector effects on the Group. The full impact of these measures is expected to be expressed in the short and medium term.

The Company's forecasts in this section are forward-looking information, as defined in the Securities Law, which are based on the Company's assessment of, among other things, the structure of competition in the communications market and the applicable regulation, the economic situation in the country as a whole, the Company's investments, and that there will be no further employee retirement plans this year, other than those that have been discussed and approved. Actual results may differ significantly from the aforementioned if any of the above assessments do not materialize or insofar as one or more of the risk factors listed in Sections 2.21, 3.24, 4.22 and 5.22 of the chapter - Description of Company Operations in the Periodic Report for 2011 materialize.

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

In recent months, competition in the telecommunications industry, particularly in cellular telephony, has intensified (with the entry of the new operators - Golan Telecom and Hot Mobile), with comprehensive service packages and communications packages being offered for a fixed price with unlimited use. This stronger competition has led to lower prices, increased movement of customers, a decline in the sale of cellular terminal equipment, and higher churn rates (in fixed-line services, also due to cancellation of the charge for the ADSL only service), and this in turn has affected the Group's results. In an effort to limit the impact on performance, as noted, the Group companies are introducing streamlining measures as well as various moves to improve the services they provide and to differentiate themselves from their competitors.

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

Sub-section B - Easing of structural separation – joint service bundles - on July 3, 2012, the Company's license was amended to that it is also permitted to offer business subscribers joint service bundles with the subsidiaries, subject to their approval by the Ministry of Communications, and subject to the unbundling conditions specified in sub-par. B above. The marketing of joint service bundles to the business sector by the subsidiaries, which include the Company's services, is also subject, according to their licenses, to similar restrictions, including unbundling. This excludes a bundle which is marketed by a subsidiary and only consists of the Company's internet services; additionally, pursuant to the Ministry's clarification in the hearing decision document, the Ministry does not view the amendment to the licenses as a change in the previously existing practice, with respect to the ability of ISPs belonging to the Group and others outside the Group to offer business customers the ISP component as well as the Company's infrastructure which is purchased as an input, without this being considered a "joint service bundle".

Sub-sections C and D – for additional limitations on the granting of benefits to the Group companies and cooperation between them and restrictions regarding the control of DBS, see the update to Section 5.17.3.

Section 1.7.3 - Regulatory oversight and changes in the regulatory environment

Sub-section A - Policy for regulating competition - Hayek Commission

On May 2, 2012, the Ministry of Communications published a policy document on the expansion of competition for fixed-line communications - wholesale market, according to which the Minister of Communications ("the Minister") adopted the key recommendations of the "Committee for reviewing and revising Bezeq's rate structure and setting wholesale service tariffs for fixed-line communications", headed by Amir Hayek CPA ("Hayek Committee"), in the manner specified in that document which was included in the Company's Immediate Report dated May 2, 2012, presented here by way of reference.

Following are the main points of the policy document:

1. Owners of nation wide fixed-line access infrastructures who provide retail services, including the Company, will be obligated to sell wholesale services to holders of telecommunications licenses, including Bitstream Access, lease of access segments, dark fibers, tubes and transmission services, on a non-discriminatory basis and with no discounts for size. In this regard, a procedure was established whereby an agreement for these services will be

negotiated and as soon as such agreement is signed, the infrastructure owner will publish a shelf offering for sale of the services based on the agreement and which also includes additional services as the Ministry determines from time to time ("the Shelf Offering"). In certain circumstances, the Minister has the power to stipulate conditions or prices for the services. The infrastructure owners must submit to the relevant license owners the distribution of their existing infrastructures, with exceptions to be defined.

2. Upon publication of the shelf offering, corporations with an interest in the infrastructure owner may also purchase wholesale services from it, without discrimination. The Company will be able to provide wholesale telephony services to its subsidiaries that are not supplied over a broadband network, provided that these services are also available to everyone and without discrimination.

3. Within 9 months of publication of the shelf offering, the Minister will order elimination of the structural separation between the infrastructure provider who published the aforementioned offering and the international call providers and ISPs), replacing it with accounting separation (unless the Minister believes that this will adversely affect competition or the public interest), so that the Company will be able to offer subsidized plans. Furthermore, insofar as the wholesale market develops and the degree of competition based on joint service bundles that combine fixed-line and mobile services in the private sector (according to indices or conditions stipulated by the Minister) allows this, the Minister will consider an easing or cancellation of the structural separation between an infrastructure provider and a cellular operator who has an interest in the said provider.

4. The Minister will review the subject of the unbundling of broadcast services included in the joint service packages, which also include Bezeq services (fixed or mobile) or broadband access services. The structural separation between the infrastructure providers and multi-channel TV area will be eliminated by granting suppliers without nation-wide fixed-line infrastructure a reasonable possibility to provide a basic TV service package over the internet.

5. If no wholesale market develops in the correct manner (based on indices to be defined for this purpose) within 24 months of the publication of the policy document, the Minister will take action to implement structural separation between the infrastructure and the services provided by general domestic carrier license holders.

6. Within six months of publication of the shelf offering, the Minister will take action to change the method of oversight of the Company's prices so that prices will be controlled by the setting of a maximum price.

7. Within 9 months, the Ministry of Communications will formulate regulations aimed at increasing the investment in and upgrading fixed-line communications infrastructure in Israel.

At this stage, the Company is unable to estimate the effect of the policy document on its business performance.

On June 12, 2012, the Ministry of Communications began to convene an engineering forum of the operators regarding wholesale services, which discusses, inter alia, service portfolios (including service portfolios submitted by the Company) for certain service configurations relating to the supply of Bitstream Access and passive infrastructures. This is concurrent with advanced negotiations that the Company is conducting directly with various operators.

Sub-par. B - Increase in the rate of royalties - on August 1, 2012, an amendment was published to the Royalties Regulations which is relevant for the Company, Pelephone, DBS, BIP and Bezeq International, so that the rate of royalties for 2012 will be reduced on average to 1.75% for the Company and DBS, to - 1.3% for Pelephone, (the rate of royalties for Bezeq International and BIP is 1%), and from 2013 it will be 0% for all of them.

Sub-par. D – Limitation of the exit penalty that a license-holder can collect from a subscriber - concerning cancellation of exit fees on mobile telephony networks, see update to Section 3.7.2(D).

Sub-par. E – Consumer legislation – on December 12, 2012, the Consumer Protection (Provision of telephony service) Regulations, will become valid.

Sub-par. F - Enforcement and financial sanctions - concerning government bills to amend the Communications Law, the Protection of Privacy Law and the Antitrust Law which address enforcement and the imposition of financial sanctions - on May 14, 2012, an amendment to the Antitrust Law was published on this subject. On August 5, 2012, the amendment to the Communications Law on this subject was published. The other bills are in the advanced stages of legislation.

GBE connection (Gigabit Ethernet) for ISPs

On June 26, 2012, the Ministry of Communications published a hearing asking for the operators' comments on changes in the existing regulations for connecting ISPs to the Company's network and to the Hot Telecom network, whereby the "high-speed access by means of internet providers" (the Company's XDSL) portfolio, and Hot Telecom's "broadband access for ISPs" portfolio, will be amended so that these services will include all the necessary components for providing those buying the service with surfing speed, including conveying traffic on the core and access networks, and payments imposed on the ISPs for GBE will be eliminated. The infrastructure owners will price the internet access services for the end customers, including the GBE segment, and excluding the P2P transmission segment which connects networks with infrastructure to the ISPs' facilities, which will be priced separately. Likewise, the infrastructure owners will be obligated to provide GBE connections at a speed to be derived from the "load ratio" (the ratio between the volume of GBE connections provided to the supplier and the scope of the aggregate speeds ordered by all the supplier's subscribers) as the Ministry determines from time to time. At this time, the Ministry is of the opinion that the appropriate load ratio is 5%. The Company objects to this change, which is far from the norm in the telecommunications industry, and believes that the hearing and the proposed arrangement contain administrative flaws and are unreasonable. The Company submitted its position to the Ministry on August 8, 2012.

2. Domestic fixed-line communications; "Bezeq" - The Israel Telecommunication Corporation Ltd. ("the Company")

Section 2.1.9 - Structure of competition in this area of activity and the applicable changes

Concerning stronger competition in the telecommunications industry - see update to Section 1.7.

Section 2.2.5 – Other services

In July 2012, the Company launched a Free Wi-Fi service, enabling its customers to share part of their wireless bandwidth in return for browsing outside their home as well.

Section 2.6.4 - Additional factors that could influence competition

On August 19, 2012, the Ministry of Communications published a memorandum to the amendment to the Communications Law, prohibiting all licensees under the Communications Law (including broadcasts) from placing a restriction on or blocking communications equipment which is designed or required for receiving services from the licensee; on the subscriber's ability to use any service or application which is provided over the internet; on integral features or properties of the communications equipment; on the subscriber's ability to use communications equipment on any Bezeq network of a licensee/broadcasting network, insofar as the said equipment is essentially designed to operate on such networks (concerning a similar restriction on the sale of terminal equipment by a cellular network, see Section 3.7.2(D) of the Periodic Report for 2011).

Sub-section B - Regarding the process of choosing an investor for a communications venture with IEC, the scheduled date for the submittal of basic offers (April 23, 2012) was postponed from time to time and as far as the Company is aware, the planned date for submittal of these proposals is scheduled for November 2012.

Sub-section C - Technological developments - On October 16, 2012, the Ministry of Communications published a hearing according to which as a means of improving the possibility of providing the public with fixed-line communications services, it is considering granting permission to the domestic carrier license holder to offer the use of WLAN (Wireless Local Access Network) technology by installing access points everywhere and under any law, and removing the restriction on connecting "enclosed premises". The submittal date for public responses to the hearing is scheduled for November 9, 2012.

Section 2.7.2 – Domestic fixed line Communications infrastructure

Further to the Company's technology review, the Board of Directors resolved on August 29, 2012, to approve extension of the Company's optical fiber deployment so that the fibers will be as close as possible to the customer's premises (FTTH/FTTB), as a basis for future provision of more advanced and broader-band communications services than those currently provided. In this context, a detailed planning of the project, pilots, and the purchase of optical fibers and advanced optical technologies is to be prepared. The project will be modular and the Company will review the scope and outline of the project, as well as the need for adjustments, on a regular basis, in part in view of the advancement of relevant technologies and development of customer needs.

Section 2.7.3 - Computerization (and Section 2.10.3 - Dependence on suppliers, and Section 2.19.4 - Main projects, planned and in progress)

Concerning sub-par. D, Company-wide systems -, on July 2, 2012, the Board of Directors of the Company resolved to terminate the Oracle based CRM system integrated with Matrix, while continuing to use modules that have already been developed and which can still be utilized. The Company is reviewing alternatives to this system. Regarding this, see also Note 13.2 to the Company's consolidated financial statements for the period ended September 30, 2012.

Section 2.7.4 - Real estate (and also Section 2.20 - Forecast for developments in the coming year)

Sub-par. E - concerning negotiations to acquire a plot slated for the construction of offices and communications facilities to replace the existing offices that are currently rented for the Group's companies - on July 2, 2012, the Company's Board of Directors resolved to suspend the negotiations to acquire the aforementioned plot. The Company intends to continue to examine various alternatives, including rental, to house the offices and communications facilities for the Group's companies.

Section 2.9.1 – Organizational structure

On October 18, 2012, the Company's Board of Directors resolved to appoint the VP of Economics, Mr. David Mizrahi, to the position of Deputy CEO and CFO, effective from January 1, 2013, instead of Mr. Alan Gelman who announced his resignation from the Company from that date. The Board of Directors also approved action by the Company's management to amalgamate the Finance Division with the Economic and Budget Division to form a single division under the management of Mr. David Mizrahi.

Section 2.9.3 – Early retirement plan for employees

On November 7, 2011, the Board of Directors of the Company approved a budget supplement of NIS 16 million for the early retirement of 19 employees in 2012. This supplement is in addition to an expense of NIS 12 million which was recognized for the revised provision in 2012.

Section 2.9.6 - Compensation plans for employees

Sub-section A - on March 24, 2012, five years after the end of the allotment period, the stock options plan from 2007 came to an end (as part of this plan, 78,107,470 options were exercised).

Section 2.9.7 - Officers and senior management in the Company

On April 24, 2012, Mr. Yehuda Porat's service as an employee director came to an end and on October 11, 2012 Mr. Yair David was appointed to replace him.

Section 2.10.3 - Dependence on suppliers

concerning CRM, see update to Section 2.7.3 above.

Concerning dependence in the area of supply service systems on Anubex NV, which supplied the Company with an open work environment allowing systems that were converted from the MF systems to work in an open environment - the Company is no longer dependent on this company.

Section 2.11 - Working capital

As at September 30, 2012, the Company has a working capital deficit in the amount of NIS 1,080 million (this figure refers to the Company's separate financial statements. In the Company's consolidated financial statements as at September 30, 2012 there is working capital surplus in the amount of NIS 212 million). On November 7, 2012, the Board of Directors determined that despite its deficit in working capital, the Company does not have a liquidity problem. See par. 1.4 of the Board of Directors' Report.

Section 2.13.2 - Limitations on obtaining credit

Sub-par. A - Limitations included in the Company's loans - as at the date of the financial statements and as at the publication date of this report, the Company is in compliance with all the applicable limitations.

Section 2.13.3 – Credit received during the Reporting Period

On October 29, 2012, the Company completed debt financing in the total amount of NIS 500 million through a loan from an Israeli bank, with an average duration of 4.3 years, bearing fixed shekel interest. In this instance, see also Note 13.5 to the Company's consolidated financial statements for the period ended September 30, 2012.

Section 2.13.6 - Credit rating

On July 4, 2012, the Company received notice from Standard & Poor's Maalot rating the Company AA+/Negative Outlook and its debentures AA+, thus reaffirming the current ratings, leaving them unchanged.[5]

On July 19, 2012, the Company received notice from the rating company Midroog Ltd., which rates the Company's debentures (Series 5, 6, 7, 8), that it had downgraded these debentures (Series 5, 6, 7, 8) from Aa1/Negative Outlook, to Aa2/Stable Outlook.

Section 2.16.2 – The Company's domestic carrier license

Sub-par. C - Tariffs - on May 31, 2012, the Communications Regulations (Telecommunications and Broadcasts) (Calculation and linkage of Bezeq payments) (Amendment), 2012, were published which include a Temporary Provision according to which the payments will not be updated on June 1, 2012, and that the update of tariffs to be made in June 2013, will include an aggregate update for the last two years.

Section 2.16.4 – Royalties

See update to Section 1.7.3(B).

Section 2.16.9 - The Telegraph Ordinance

Concerning the termination of the claim filed by the State authorities regarding radio frequencies in the Administered Territories, see the update to Section 2.18.6.

Section 2.17.1 – Material agreements concerning debentures

Section A - Deed of trust for Debentures (Series 5) - on March 21, 2012, the appointment of Hermetic Trust Services (1975) Ltd. ("Hermetic") was approved as the trustee for Debentures (Series 5) of the Company, replacing Mizrahi-Tefahot Trust Company Ltd., and accordingly from that date Hermetic serves as the trustee for the aforementioned debentures.

Section 2.18 – Legal proceedings

Section 2.18.1(B) - regarding a claim and application for its certification as a class action that was filed by a former employee of the Company concerning the inclusion of wage components, on April 29, 2012 the Tel Aviv Regional Labor Court handed down a ruling striking out the application and the application for certification as a class action, upon the plaintiff's request and further to the court's recommendation.

Section 2.18.3 - regarding two claims and applications for their certification as class actions claiming unlawful collection of money in cases of disconnection due to non-payment - one claim (claim from February 2011 in the amount of NIS 44 million) and an application for its certification as a class action were dismissed in limine on March 28, 2012, at the Company's request. On May 8, 2012, an appeal was filed against the ruling.

Section 2.18.4 - regarding a claim and application for its certification as a class action in the matter of a delay in the disconnecting of calls - on October 17, 2012, the Supreme Court resolved to strike out (without ordering costs) the appeal which had been filed against the Company in respect of a dismissal of the application for certification as a class action.

Section 2.18.5 - regarding a claim filed and an application for its recognition as a class action concerning subscribing to call tracks for a fixed monthly payment - in June 2012 the court approved publication of a compromise settlement reached by the parties at a cost of NIS 6.5 million to the Company, and instructed that the settlement be sent to the relevant parties before it hands down the verdict.

[5] The same notice also included confirmation of the rating for Pelephone and its debentures. Regarding this, see the update to Section 3.15.5.

Section 2.18.6 - regarding a claim filed by the State authorities for payment of frequency fees in the Administered Territories in the amount of NIS 74 million - on April 2, 2012, a compromise settlement between the parties to the procedure was validated as a court ruling, in which the Company will pay the plaintiffs the total amount of NIS 26 million (plus CPI linkage from February 11, 2010).

Section 2.18.7 - concerning claims which were consolidated on the subject of a malfunction of the Company's network on January 25, 2011 - on October 9, 2012, the court approved the applicants' request to abandon their applications for certification as a class action, based on the court's recommendation and in view of the difficulties encountered by the application for certification.

Section 2.18.8 - regarding an application to approve a derivative claim against directors of the Company concerning the taking of loans, which as alleged in the application were not used for the Company's benefit and were designated for the distribution of dividends - on June 14, 2012, the court resolved to dismiss the application in limine after ruling that the applicant in this procedure is not a "shareholder" of the Company and he is therefore not entitled to file a derivative claim in the Company's name. Subsequently, on July 15, 2012, a new application to approve a derivate claim was filed in the Tel Aviv District Court (Economic Department) by the father of the applicant whose application had been dismissed in limine, (against directors of the Company, the CEO, Deputy CEO, and the CFO of the Company) on the same subject.

It should be noted that on July 4, 2012, a new request for exhaustion of the Company's rights was received by way of the filing of an action prior to applying to the District Court to approve a derivative claim the subject of which is similar to this application. Subsequently, on August 27, 2012, the same applicant sent a supplementary letter which also included, inter alia, allegations in relation to the previous controlling shareholders of the Company and in relation to the members of the Board of Directors who had served before control of the Company was transferred with respect to their conduct in connection with the transfer of control of the Company, and a request that the Company must exhaust its rights by way of filing an action against these entities as well. On August 29, 2012 and on October 10, 2012 (respectively), the Company informed the applicant that it had decided to reject his demands in both the aforementioned applications.

Section 2.18.10 - regarding an application to approve a distribution that is not in compliance with the earnings test, see the update to Section 1.4.3.

Section 2.18.15 - regarding a claim by a group of pensioners of the Company from September 2000 which was dismissed by the District Labor Court on December 16, 2008 and an appeal on the case which was dismissed by the National Labor Court on December 21, 2011 - on July 25, 2012, the Company received a petition to the High Court of Justice for the issue of an order nisi against the National Labor Court and the Company, in which the plaintiffs are petitioning to revoke the ruling and decisions of the National Labor Court. According to HCJ's decision, the Company submitted a preliminary response to the petition.

In September 2012, a claim was filed against the Company in the Tel Aviv District Court together with an application for its certification as a class action, alleging that in contravention of the law, the Company does not include a call details record in the phone bills which it sends to its subscribers. The application estimates the amount of the class action at NIS 154 million. It should be noted that in April 2011, another claim was filed against the Company in the Tel Aviv District Court together with an application for its certification as a class action, making the same claim against the Company, and in which the applicant estimates the amount of the claim at NIS 127 million. For a similar claim which was filed against Pelephone on the same subject, see the update to Section 3.21.

3. Mobile radio-telephone (cellular telephony) - Pelephone Communications Ltd. ("Pelephone")

Section 3.1.5 A - Technology changes that can affect the area of operation

According to the Ministry of Communications plan for 2012, which was published in March 2012, the ministry will work to allocate Generation 4 frequencies (LTE).

Section 3.7.2 - Regulatory moves and legislative amendments for increasing competition in the cellular area

In May 2012, Golan Telecom Ltd. and Mirs Communications Ltd., launched their operations under the brand Hot Mobile ("the New Operators"). The entry of the New Operators immediately caused much stronger competition in the cellular market between all the cellular operators. After launching their operations, the New Operators offered customers cellular communications packages which are significantly cheaper than the packages offered by the cellular operators who were in the market prior to the launch. Like the other cellular operators, Pelephone responded to this new competition by launching new packages which reflect a substantial decline in income per subscriber.

As part of the competitive measures, Partner launched a discount brand called 012mobile, and Cellcom launched a communications package offering a combination of cellular communications, fixed-line communications internet and international calls.

As part of the competition, in the second quarter of 2012 "unlimited" communications packages were offered for the first time. In these packages, the subscriber pays fixed usage fees and is entitled to make unlimited use of the services according to the terms of the plan. These packages are the main packages currently being offered on the cellular market, alongside the basic packages which include low usage fees, if any, allowing customers to use the services up to a certain amount, and beyond this limit they are charged according to their excess usage. The more intense competition has led to a trend of buying a "SIM Only" package - i.e. a communications package that does not include buying a handset.

This more intense competition has led to a higher churn rate and significantly lower prices for communications packages for hundreds of thousands of subscribers.

Pelephone expects these trends to continue, leading to a significant erosion of revenues and profitability. Pelephone is introducing streamlining measures in an effort to reduce the impact on profit.

Pelephone's aforementioned estimates are forward-looking information, as defined in the Securities Law. These estimates may not materialize, may materialize in part or may materialize in a manner materially different from that forecast.

Section 3.7.2 D - Increased competition and the removal of barriers to switching among operators

In September 2012, a reform of the importing of cellular handsets was validated. The reform includes two alleviations which are exemption from obtaining a trade license and exemption from the need to obtain type approval for the import of cellular devices that comply with accepted European and American standards. Pelephone believes that implementation of the reform may intensify competition in the terminal equipment market.

On March 21, 2012, the Knesset approved the amendment to the Communications Law according to which:

1. Exit penalties were eliminated as specified in the Periodic Report for 2011.
2. A license holder will not make a subscriber's commitment to receive cellular services dependent on that subscriber's agreement with it or with any other license holder to purchase, rent, borrow or lease terminal equipment, either in one agreement or in separate agreements, including by way of providing a discount or any other benefit in one agreement that is dependent on the other agreement. The Amendment will take effect on January 1, 2013. The Minister of Communications has the power to postpone the applicability date by six months. In the past, the main sales method was to offer discounts on the price of the services that are dependent on the terminal equipment in the customer's possession. From the validation of this amendment, it will no longer be possible to offer such benefits.

Section 3.11 – Human capital

In September 2012, Pelephone received notice from the New Labor Federation (Histadrut) that more than one third of Pelephone's employees had voted to sign up as members of the Histadrut, and that it therefore constitutes a representative workers union of Pelephone employees. Pelephone informed the Histadrut that it does not accept the aforementioned notice of representation, and that its status as official representative must be heard by the courts.

Section 3.13.4 – Credit policy

During 2012, Pelephone began to deduct customers' debts arising from the sale of terminal equipment in installments by credit card. The withholding transactions are carried out on a non-recourse basis. During the period ended September 30, 2012, Pelephone deducted total of NIS 130 million (gross amount not capitalized).

Section 3.15.2 - Restrictions

Sub-section A - Undertakings towards banks - pursuant to legal position 104-15 of the Securities Authority from October 30, 2011, following are further disclosures in connection with compliance with financial covenants of reportable credit:

Financial covenants to which Pelephone is obligated:	As at September 30, 2012	Maximum required ratio
Pelephone's total debts will not exceed 3 times its equity.	0.70	3.00
Total debts are not to exceed NIS 3.8 billion (linked to the CPI known in January 2002. As at September 30, 2012 = NIS 4.91 billion).	1.97	4.91
Undertaking to a particular bank that debts to it will not exceed 40% of Pelephone's total cumulative debts to financial entities including debenture holders.	14.7%	40%

Section 3.15.5 – Credit rating

In July 2012, Standard & Poor's Maalot, which rates Pelephone's debentures, announced that it is reaffirming the local rating of Pelephone's debentures at AA+/Negative Outlook.

Section 3.18.4 – Site construction licensing

In May 2012, Pelephone and the other old operators filed an application to cancel and alternatively to limit the temporary injunction prohibiting the construction of wireless access facilities that are exempt from a building permit. Concurrently, the New Operators also filed applications to extend the validity of the limit on the temporary injunction. In July 2012, HCJ determined, in connection with an application filed by the old operators, that the temporary injunction from September 16, 2010, as it was limited on February 16, 2011, would remain in place with one change according to which the companies are entitled to replace one existing wireless access device with another, even if the device has not malfunctioned and its capacity has not declined, for the purpose of on-going maintenance, provided that it is in precisely the same location as the substituted device, and the other conditions stipulated in the ruling from February 16, 2011 will apply regarding replacement of the access device as well. HCJ further stipulated, in connection with the application filed by the new operators, that the temporary injunction as it had been limited, will continue to apply until January 31, 2013.

Section 3.21 – Legal proceedings

Section 3.21.1(A) – regarding a claim filed by the State of Israel with the Central Region District Court in respect of a request for royalties in the amount of NIS 260 million, and the appeal which Pelephone filed in the Supreme Court on the amount of the charge – in August 2012, the appeal was dismissed.

Section 3.21.1(C) - regarding a claim filed in December 2007, in the Tel Aviv District Court against Pelephone, Cellcom and Partner, together with an application for its certification as a class action in the amount of NIS 1 billion, which relates to radiation damage from cellular antennae which were ostensibly erected unlawfully - in June 2012, the Court approved the plaintiff's abandonment of the action.

Section 3.21.1(D) - regarding a claim and application for its recognition as a class action in the amount of NIS 240 million, which was filed against Pelephone in July 2008, alleging, inter alia, the collection of payment for standing orders, ostensibly in contravention of Pelephone's license - in May 2012, an additional claim was filed in the Tel Aviv District Court and an application for its recognition as a class action in the amount of - NIS 74 million, alleging the same cause of unlawful billing for payment by standing order, but immediately afterwards the plaintiff abandoned the claim in view of the previous proceeding on the same matter.

Section 3.21.1. (H) – regarding a claim and a motion for its certification as a class action from August 2011 concerning a charge for calls made outside Israel by rounding up the call duration to whole minutes - in September 2012 the court dismissed the claim and the motion for certification as a class action. In November 2012, an appeal was filed against the ruling.

Section 3.21.1 (I) - regarding a claim and application for its certification as a class action in the amount of NIS 285 million, which was filed against Pelephone in November 2011 and alleged that Pelephone recorded service conversations by Pelephone customers at the service stations without their knowledge and without terminating the recording when the representative was not with them, thus infringing on their right to privacy - in April 2012, the court decided to approve abandonment of the claim and of the application for its certification as a class action.

In March 2012, a claim was filed against Pelephone in the Tel Aviv District Court together with an application for its certification as a class action. The claim alleges that Pelephone makes false representations to the public, according to which it provides a surfing experience on its network at extremely high speeds. According to the plaintiffs, they conducted dozens of measurements showing that the surfing speed on the respondent's cellular network is lower than specified. According to the claim, this state of affairs caused and causes cumulative personal loss of NIS 560. The amount of the application is estimated in the total amount of NIS 242 million, subject to data to be produced by Pelephone as part of the proceeding.

In June 2012, a claim was filed against Pelephone in the Tel Aviv District Court together with an application for its certification as a class action. The applicants allege that the Company is in violation of Section 30A of the Communications Law, by sending marketing messages (spam), despite the applicants' failure to agree to receive them. The amount of the application is estimated in the total amount of NIS 455 million. In September 2012 the court resolved to approve abandonment of the claim and the motion for its certification as a class action.

In August 2012, a claim was filed against Pelephone in the Tel Aviv District Court together with a motion for its certification as a class action. The plaintiffs contend that Pelephone unlawfully collects a monthly fee from its customers for payment by standing order. The amount of the application is estimated in the total amount of NIS 161 million.

In September 2012, a claim was filed against Pelephone in the Tel Aviv District Court together with a motion for its certification as a class action. The plaintiff contends that Pelephone unlawfully collected money for the cost of a cellular handset, a cancelled phone line, browsing services, various services, as well as for collection expenses and voucher fees. The amount of the application is estimated at NIS 57 million for the causes claimed plus NIS 1,000 for distress for each member of the group. It should be noted that a class action is currently being conducted against Pelephone, in which some of the grounds for the claim are similar to those in this claim (see Section 3.21.1. (D) in Chapter A of the Periodic Report for 2011).

In September 2012, a claim was filed against Pelephone in the Tel Aviv District Court together with an application for its certification as a class action. The applicant alleges that Pelephone does not include call details record in its phone bill, and this is contrary to Ministry of Communications instructions and Pelephone's license. The total amount of the class action is NIS 110 million. For two similar claims which were filed against the Company on the same subject, see the update to Section 2.18.

4. Bezeq International – international communication and internet services

Section 4.17.6 – Key regulatory developments

Sub-section J – Hearing on internet license consumer issues – on October 31, 2010, Bezeq International received the decision of the Ministry of Communications regarding the amendment to the special license it had received for providing internet access services. The provisions of the amendment will validate gradually, from December 2, 2012 until May 1, 2013. Bezeq International has deployed in time and is continuing to prepare for implementation of the provisions of the amendment.

Section 4.20- Legal proceedings

Section 4.20.1 - On September 19, 2012, the Supreme Court issued a ruling dismissing the application for permission to appeal which Bezeq International had filed against the ruling of the District Court to certify the claim as a class action.

Section 4.20.4 - On June 20, 2012, the Tel Aviv District Court approved the plaintiff's abandonment of a claim and the application for its recognition as a class action in the amount of NIS 39 million, which had been filed against Bezeq International, alleging that Bezeq International does not provide its customers with a written document as required under the Consumer Protection Law when entering into an agreement for changing or adding to a continuing transaction[6].

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

Section 5.1.4 - Market developments in the segment of operation

Sub-par. A - in April 2012, the Broadcasting by means of Digital Broadcast Stations Law, 2012, was published in the Official Gazette.

Section 5.1.5 - Technology changes that can materially affect the segment of operation

Sub-par. A - as far as DBS is aware, some of the cellular operators have announced their intention of offering the public video content which will include DTT broadcasts together with additional content to be transmitted through the internet.

According to DBS, insofar as such services are offered, they may partially substitute DBS' service, thus harming its performance, which may worsen insofar as the services are offered without regulatory supervision.

This opinion is forward-looking information, as defined in the Securities Law, based, in part, on the announcements by some of the cellular operators and on the estimated development of competition in the broadcasts market in relation to the launching of such services. This opinion concerning possible harm may not materialize, or may materialize on a different scale, in part, depending on the services and conditions which are actually offered by the cellular operators, on the actual development of competition in the broadcasts market, and on regulatory decisions which may be made pertaining to the operation of these services or affecting them (see also update to Section 5.17).

Section 5.15.2 - Bank financing

In July 2012, DBS repaid all the long-term bank credit at its disposal (by means of a loan provided to it according to the debenture and in consideration of an expansion of DBS's debentures (Series B), as noted in the update to Section 5.15.3), and upon this repayment, the amendment to the financing agreement validated ("Amendment to the Agreement" and "Amended Financing Agreement"). According to the Amended Financing Agreement, the amount of DBS's current credit limits was increased to NIS 170 million, but utilization of this framework was restricted to the total working capital requirements of DBS.[7] Additionally, as part of the Amended Financing Agreement, the obligations and limitations that applied to DBS under the financing agreement were eliminated or reduced (including those pertaining to its compliance with the business plan, to undertaking liabilities from third parties, transactions with interested parties, the purchase of securities in other corporations, to the offering of securities to the public and mandatory repayment of cash flow surpluses or the issuance of debentures). According to the provisions of the Amendment to the Agreement, the collaterals created by the Company and Eurocom in favor of the banks to secure DBS's bank credit and their liabilities towards the banks in connection with the bank credit of DBS were also cancelled, including the Company's guarantee to the banks.

According to the Amended Financing Agreement, the financial covenants which had applied until now were cancelled, and instead DBS must comply every quarter with both the following financial covenants (subject to periods of improvement and improvement conditions defined in the Amendment to the Agreement): (a) compliance with a maximum debt/EBITDA[8] ratio, and (b) compliance with a

[6] Similar claims against the Company, Pelephone, and DBS also ended after the plaintiffs abandoned the claims or they were dismissed as noted in Chapter A, Sections 2.18.6, 3.21.2G and 5.20.2B of the Periodic Report for 2011.

[7] Calculated according to a formula set forth in the Amended Financing Agreement, which is contingent on the customer balances of DBS, the total unutilized broadcasting rights of DBS, the depreciated cost of the decoders and the total supplier balance of DBS. according to its financial statements.

[8] The ratio between the total debt (debts to financial institutions as defined in the Amended Financing Agreement) at the end of the relevant quarter and the EBITDA of DBS. for the 12 months ending at the end of that quarter. The term "EBITDA" means: with respect to any period of calculation - the total operating profit of DBS from ordinary operations (before finance and tax expenses), plus depreciation and amortization, plus expenses classified under investments in the financial statements of DBS as at December 31, 2010 (and were reclassified to expenses due to accounting policy or the instruction of an authority), and plus extraordinary one-time expenses and provisions. The maximum ratio for a review period ending at the end of 2013 is 5, and for a review period ending at the end of 2015 - 4.65.

maximum debt/E-C[9] ratio. Additionally, according to the Amended Financing Agreement, the restrictions on the repayment of shareholders' loans and distribution of a dividend, stipulated in the Debenture mentioned in Section 5.15.3, apply to the lenders according to the Debenture (replacing the restrictions that applied until now in relation to the repayment of shareholders' loans and the prohibition on distributing a dividend).

The Amended Financing Agreement further stipulates that immediate settlement, or the presence of cause for the immediate settlement of amounts that DBS owes the debenture holders, other banks or financial institutions constitutes cause for immediate recall of the bank credit. According to the Amended Financing Agreement, if S&P Maalot downgrades the loan in accordance with the aforesaid Debenture to "ilBBB" (or a corresponding rating by another rating company, whichever is lower), the annual interest payable to the banks will increase by 0.25% for each notch reduction on the rating scale, as long as the downgrade is in force.[10]

Section 5.15.3 - Debentures

In May 2012, DBS and several institutional entities (in this section: "the Lenders") signed a debenture whereby the Lenders will provide DBS with a loan of NIS 392 million (in this section: "the Debenture").DBS received the loan in July 2012, after compliance with conditions precedent defined in the Debenture.

The loan provided according to the Debenture is to be repaid in ten (unequal) annual principal payments in April of the years 2013-2022,[11] and it bears annual interest at a rate of 6.4%, as mentioned, to be paid in semi-annual installments. The principal and interest on the loan are CPI linked. According to the Debenture, if the loan rating is downgraded to ilBBB or a corresponding rating (whichever is lower), the annual interest paid on the loan will increase by 0.5%, and it will increase by a further 0.25% for each additional notch reduction on the rating scale, as long as the downgrade is valid.

Furthermore, the Debenture sets forth various events (similar to those noted in Deed of Trust B), which if they occur (sometimes after a long period) establish an entitlement to immediate recall of the loan, subject to the provisions of the Debenture, including immediate settlement (not at the initiative of DBS) of another series of debentures that was issued and/or will be issued by DBS and/or of DBS's debts towards a financial institution, subject to the conditions set forth in the Debenture.

Pursuant to the provisions of the Debenture, each quarter DBS must comply with two financial covenants which are identical to the financial covenants stipulated in the Amended Financing Agreement (see update to Section 5.15.2).[12] The Debenture also sets forth restrictions in relation to the distribution of a dividend and the repayment of shareholders' loans similar to the restrictions that apply according to Deed of Trust B.[13]

For additional information about the collaterals which were created to guarantee the Debenture and for changes in the conditions of the aforesaid Debenture and collaterals if the Company should provide a guarantee in favor of the lenders under the conditions set forth in the Debenture - see Note 6 to the financial statements of DBS as at September 30, 2012.

The target for the maximum EBITDA/debt ratio covenant as at September 30, 2012 as defined in the amended financing agreement and the Debenture was 5. D.B.S. was in compliance with this covenant (the ratio as at September 30, 2012 was 2.9). The covenant target for maximum E-C/debt ratio as at

[9] The ratio between the total debt, as it is at the end of the relevant quarter, and the E-C of DBS for the 12 months ending at the end of that quarter. The term: "E-C" means: the EBITDA of DBS for the 12 months ending at the end of that quarter, minus the CAPEX (amount of the additions to property, plant and equipment, without the deduction of depreciation and amortization) of DBS for that period, where the maximum ratio is 9.5.

[10] Except if the said downgrade does not provide any lender, according to the Debenture, with additional interest in respect of the loan due to the Company providing a guarantee in its favor - see Note 6 to the financial statements of DBS as at September 30, 2012.

[11] In each of the years 2013-2017, payment of the principal will be 8% of the nominal value of the debentures, and in each year thereafter payment of the principal will be 12% of the nominal value of the debentures.

[12] Where the maximum ratio of debt to EBITDA in respect of the review period commencing in 2016 is 4.3 and the maximum ratio of debt to (E-C) that applies from January 1, 2016 is 7.8

[13] The target of the financial covenant applicable to this is lower (more stringent) than the covenant which applies according to Deed of Trust B.

September 30, 2012 as defined in the amended financing agreement and in the Debenture was 9.5. DBS was in compliance with this covenant (the ratio as at September 30, 2012 was 7.5).

As at September 30, 2012, DBS was in compliance with the debt/EBITDA ratio covenant specified in Deed of Trust B (the ratio of the debt of DBS to its EBITDA as at September 30, 2012 was 3.16).

In July 2012, DBS issued additional debentures (Series B), by way of an expansion of the series, in the amount of NIS 10 million. The proceeds from this issuance, together with the money from the loan which is the subject of the Debenture, were used to repay the full amount of the long-term bank credit (see Section 5.15.2).

In May 2012, S&P Maalot determined a rating of ilA- for the Debenture and the expansion of debentures (Series B) of DBS, in relation to a total raising of up to NIS 450 million, par value. In October 2012, S&P Maalot reaffirmed the ilA- rating of DBS and all the series of debentures of DBS (including the Debenture described above in this section) with a stable outlook rating for DBS.

Section 5.17 - Restrictions and supervision of the corporation

In September 2012, after inviting the public to present its positions on the subject, the Council amended the Communications Rules so as to obligate DBS and HOT to offer, in addition to the basic package of channels that licensees are obligated to offer to all their subscribers by law, a package which, in addition to the compulsory channels, includes at least four channels produced in Israel, including a sports channel and a channel for pre-schoolers and/or a channel for children and teens ("the limited group of channels"). Likewise, the amendment regulates the obligation of DBS and HOT to invest in various categories of local productions on the channels included in the limited group of channels as well as the scope of sports broadcasts which must be broadcast. The Council also stipulated that DBS and HOT must submit for the approval of the Council Chair, the list of channels they will include in the limited group of channels, the various marketing tracks of the limited group of channels and its price lists. According to the decision, DBS and HOT must offer the limited group of channels commencing December 1, 2012 (at the latest) and up to May 31, 2013, and during this period the Council will once again review its decision based on the data it receives from DBS and HOT.

DBS believes that the proposed plan for limited group of channels in the Council's decision will adversely affect its performance.

DBS's opinion is forward-looking information, as defined in the Securities Law, based, in part, on the aforesaid announcements by the Council and DBS's estimate regarding the way in which it is implemented by the license holders. This estimate may not materialize, or it may materialize on a different scale, in part depending on changes in competition that may occur, taking note of the regulatory procedures.

Section 5.17.7 - Requirement to transmit channels

In April 2012, the HCJ issued an order nisi instructing the Knesset, the State and the other respondents to the petition to explain why the court should not declare that the amendment to the law should not be applied to DBS until reasonable compensation is arranged for DBS, and alternatively why the amendment to the law should not be revoked.

Section 5.17.12 – Wiring in subscribers' homes

On October 30, 2012, pursuant to an application by DBS and HOT to amend the administrative directive, the Ministry of Communications announced the cancellation of the directive. DBS is reviewing the implications of this announcement..

Section 5.17.13 – Offering of service packages

In October 2012, the Antitrust Authority informed DBS that in its opinion, cooperation between DBS and the company which markets the joint service bundle, constitutes cooperation between (potential) competitors in this area of competition (this, subsequent to a ruling by the Supreme Court, see Section 2.16.8 C), which might be construed as a restrictive agreement and requires approval under the Antitrust law (even if it complies with the conditions of the broadcasting license), and that the Commissioner does not intend to grant an exemption from the need for approval of the arrangement.

DBS believes that in view of the Antitrust Commissioner's aforementioned position, it might also be limited regarding cooperation with other entities, insofar as they are deemed potential competitors in the broadcasting sector.

Section 5.18.5 – Agreement with the Company and with Bezeq International

In September 2012, agreements were approved to defer some of the payments which DBS owes the Company and Bezeq International by virtue of previous debt arrangements between DBS and these companies (in amounts of NIS 27 million and NIS 6 million respectively). The arrangements were approved as a transaction in which the Company's controlling shareholder has a personal interest - for details see the transaction report and notice of the convening of a special general meeting dated August 2, 2012 (concerning Transactions A and B in the said report), which are presented here by way of referral.

Section 5.20 - Legal proceedings

Section 5.20.1.A - On March 13, 2012, DBS submitted its response to the Attorney General's position, and on March 15, 2012, the applicant submitted his response to the Attorney General's position. At a hearing held on April 4, 2012, the court suggested that the parties retract their request to approve the settlement and that the applicant and his attorney should withdraw the application for certification. The parties were requested to submit their positions by April 19, 2012.On April 22, 2012, following a joint application by the parties, and in view of the difficulties encountered in the application for certification, the court approved the applicant's abandonment of the application, without ordering expenses.

November 7, 2012	
Date	"Bezeq" - The Israel Telecommunication Corp. Ltd.

Names and titles of signatories:

Shaul Elovitch, Chairman of the Board of Directors

Avi Gabbay, Chief Executive Officer

Directors' Report on the State of the Company's Affairs for the nine-month and three-month periods ended September 30, 2012

bezeq

We respectfully present the Directors' Report on the state of affairs of Bezeq – The Israel Telecommunication Corp. Limited ("the Company") and the consolidated Group companies (the Company and the consolidated companies together are hereinafter referred to as “the Group"), for the nine-month period ended September 30, 2012 and for the three-month period then ended ("Quarter").

The Directors' Report contains a condensed review of its subject-matter, and it assumes that the Directors' Report at December 31, 2011 is also available to the reader.

The Group reports on four main segments of operation in its financial statements:

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

It shall be noted, that in addition, the Company has an "Others" segment in its financial statements, which consists mainly of Internet services and the operation of Internet portals (through Walla), and customer center services (through Bezeq On-Line). The “Others” segment is not material at the Group level.

Profit for the period attributed to the owners of the Company amounted to NIS 1,339 million, compared to NIS 1,542 million in the corresponding period last year, a decrease of approximately 13.2%.
The Group's EBITDA (operating profit before depreciation and amortization) decreased from NIS 3,584 million in the corresponding period to NIS 3,338 in the reporting period, a decrease of approximately 6.9%.

Profit for the Quarter attributed to the owners of the Company amounted to NIS 342 million, compared to NIS 550 million in the corresponding quarter, a decrease of 37.8%.
The Group's EBITDA decreased from NIS 1,301 million in the corresponding quarter to NIS 1,026 million in the Quarter, a decrease of approximately 21.1%.

The results of the reporting period and the Quarter compared to the corresponding period and quarter, were impacted mainly by intensification of competition in the communications market, primarily in the Cellular segment, which led to a decline in revenue which was moderated by a decrease in operating and general expenses. In addition, expenses for early retirement recorded in the first quarter of 2011 in the Domestic Fixed-Line Communications segment also affected the results of the reporting period compared with the corresponding period.

1. Remarks of the Board of Directors on the state of the corporation's affairs, the results of its operations, its equity, cash flows and other subjects

1.1 Financial position

1.1.1 Assets

The Group's assets at September 30, 2012 amount to NIS 16.22 billion, compared with NIS 18.49 billion on September 30, 2011, of which NIS 6.12 billion (38%) of fixed assets compared with NIS 5.96 billion (32%) on September 30, 2011.

The decrease in the Group's assets stems primarily from the Domestic Fixed-Line Communications segment, as described below.

In the Domestic Fixed-Line Communications segment, there was a decrease of NIS 2.06 billion in total assets, without dividend payable, loans, and investment in associates, compared to September 30, 2011. The decrease stemmed mainly from a decrease in cash and cash equivalent balances and in investments in current financial assets, which at September 30, 2011 included receipts in respect of an issue of debentures in the corresponding quarter.

In the Cellular segment, assets decreased from NIS 5.4 billion on September 30, 2011 to NIS 5.09 billion at September 30, 2012. The decrease stemmed mainly from a decrease in the long-term customer balance due to a decrease in revenue from sales of terminal equipment and from the deduction of transactions in instalments paid by credit card. Furthermore, a decrease in the balances of property, plant and equipment, intangible assets and inventory was partly offset by an increase in balances of cash and cash equivalents.

In the International Communications, Internet and NEP services segment, total assets increased by NIS 176 million. Most of the increase occurred in property, plant and equipment balances following investment in laying the sea-bed cable and in cash balances and financial assets held for trade.

In the Multi-Channel Television segment, total assets increased by NIS 113 million, which stemmed mainly from a rise in balances of property, plant and equipment deriving mainly from an increase in decoder balances and a rise in balances of broadcasting rights, mainly as a result of an increase in the original productions balance.

1.1.2 Liabilities

The Group's debt to financial institutions and debentures-holders at September 30, 2012 amounted to NIS 8.94 billion, compared to NIS 9.61 billion on September 30, 2011.[1] The decrease in debt stems from repayment of debentures and loans in the Domestic Fixed-Line Communications segment and in the Cellular segment.

[1] The Group's debt to financial institutions and debenture holders, net of cash and cash equivalents and current investments at September 30, 2012, amounts to NIS 7,19 billion, compared to NIS 5.99 billion on September 30, 2011.

1.2 Results of operations

1.2.1 Principal results

Below is condensed data from the consolidated statements of income.

	For the nine-month period ended September 30				For the three-month period ended September 30			
	2012	2011	Increase	Change	2012	2011	Increase	Change
	NIS millions	NIS millions	(Decrease)	%	NIS millions	NIS millions	(Decrease)	%
Revenue	**7,829**	8,723	(894)	(10%)	**2,494**	2,917	(423)	(15%)
Operating expenses	**5,566**	6,179	(613)	(10%)	**1,827**	1,973	(146)	(7%)
Operating profit	**2,263**	2,544	(281)	(11%)	**667**	944	(277)	(29%)
Finance expenses, net	**88**	168	(80)	(48%)	**55**	86	(31)	(36%)
Profit after finance expenses, net	**2,175**	2,376	(201)	(8%)	**612**	858	(246)	(29%)
Share in losses of associates	**233**	203	30	15%	**92**	66	26	39%
Profit before income tax	**1,942**	2,173	(231)	(11%)	**520**	792	(272)	(34%)
Income tax	**597**	633	(36)	(6%)	**178**	243	(65)	(27%)
Profit for the period	**1,345**	1,540	(195)	(13%)	**342**	549	(207)	(38%)
Attributed to:								
Company owners	**1,339**	1,542	(203)	(13%)	**342**	550	(208)	(38%)
Non-controlling interest	**6**	(2)	8	-	**-**	(1)	1	(100%)
Profit for the period	**1,354**	1,540	(195)	(13%)	**342**	549	(207)	(38%)
Earnings per share								
Base and diluted earnings per share (NIS)	**0.49**	0.57	(0.08)	(14%)	**0.13**	0.20	(0.07)	(35%)

The Group's revenue in the period amounted to NIS 7,829 million, compared to NIS 8,723 million in the corresponding period, a decrease of 10.3%.
The Group's income in the Quarter amounted to NIS 2,494 million, compared to NIS 2,917 million in the corresponding quarter, a decrease of 14.5%.
The decrease in the Group's revenue stemmed mainly from the Cellular segment, due to more intense competition which led to a decrease in revenues from sales of terminal equipment and from services, as described below.

The Group's depreciation and amortization expenses in the period amounted to NIS 1,075 million, compared to NIS 1,040 million in the corresponding period, an increase of 3.4%.
Depreciation and amortization expenses in the Quarter amounted to NIS 359 million compared with NIS 357 million in the corresponding quarter, an increase of 0.6%.The increase stems from the Domestic Fixed-Line Communications segment and the International communications, Internet and NEP services segment, as described below.

The salary expense of the Group in the period amounted to NIS 1,527 million, compared with NIS 1,612 million in the corresponding period, a decrease of 5.3%.
The salary expense in the Quarter amounted to NIS 511 million compared with NIS 540 million in the corresponding quarter, a decrease of 5.4%.
The decrease in the salary expense stems mainly from the Domestic Fixed-Line Communications segment and the Cellular segment, as described below.

Operating and general expenses of the Group in the period amounted to NIS 2,976 million, compared with NIS 3,445 million in the corresponding period, a decrease of 13.6%.
Operating and general expenses in the Quarter amounted to NIS 963 million compared with NIS 1,182 million in the corresponding quarter, a decrease of 18.5%.
The decrease in operating and general expenses stemmed from the Cellular segment, mainly due to the decrease in cost of selling terminal equipment.

Other operating income, net, of the Group in the period amounted to NIS 12 million, compared to expenses of NIS 82 million in the corresponding period.
Other operating income, net, in the Quarter amounted to NIS 6 million, compared to NIS 106 million in the corresponding quarter.
The expense in the corresponding period stemmed from recording a provision of NIS 281.5 million in the first quarter of 2011, for severance in early retirement in the Domestic Fixed-Line Communications segment. Additional details are provided below.

The net finance expenses of the Group in the period amounted to NIS 88 million, compared to NIS 168 million in the corresponding period, a decrease of 47.6%.
Most of the decrease stems from the sale of all the holdings of Stage One Venture Capital Fund (Israel), L.P. in shares of Traffix Communication Systems Ltd., which were classified by the Group as an investment available for sale. As a result of the sale, finance income of NIS 74 million was recorded in the consolidated financial statements for the first quarter of 2012 (see Note 4.3 to the financial statements).
Net finance expenses in the Quarter amounted to NIS 55 million compared with NIS 86 million in the corresponding quarter, a decrease of 36.1%.
The decrease in net finance expenses stems mainly from the Domestic Fixed-Line Communications segment, as explained below.

1.2.2 Segments of operation

A. Below are revenue and operating profit for the Group's segments of operation.

	For the nine-month period ended September 30				For the three-month period ended September 30			
	2012		2011		2012		2011	
	NIS millions	% of total income	NIS millions	% of total income	NIS millions	% of total income	NIS millions	% of total income
Revenue by segment of operation								
Domestic Fixed-Line Communications	**3,509**	**44.8%**	3,534	40.5%	**1,149**	**46.1%**	1,186	40.7%
Cellular	**3,441**	**43.9%**	4,309	49.4%	**1,049**	**42.1%**	1,421	48.7%
International Communications, Internet and NEP Services	**1,001**	**12.8%**	1,012	11.6%	**339**	**13.6%**	351	12.0%
Multi-Channel TV	**1,228**	**15.7%**	1,215	13.9%	**403**	**16.1%**	405	13.9%
Others and setoffs*	**(1,350)**	**(17.2%)**	(1,347)	(15.4%)	**(446)**	**(17.9%)**	(446)	(15.3%)
Total Group revenue	**7,829**	**100%**	8,723	100%	**2,494**	**100%**	2,917	100%

	For the nine-month period ended September 30				For the three-month period ended September 30			
	2012		2011		2012		2011	
	NIS millions	% of total income	NIS millions	% of total income	NIS millions	% of total income	NIS millions	% of total income
Operating profit by segment of operation								
Domestic Fixed-Line Communications	**1,395**	**39.8%**	1,274	36.1%	**419**	**36.5%**	546	46.0%
Cellular	**725**	**21.1%**	1,098	25.5%	**199**	**19.0%**	342	24.1%
International communications, Internet and NEP Services	**157**	**15.7%**	182	18.0%	**55**	**16.2%**	61	17.4%
Multi-Channel TV	**180**	**14.7%**	190	15.6%	**54**	**13.4%**	63	15.6%
Others and setoffs*	**(194)**	**-**	(200)	-	**(60)**	**-**	(68)	-
Consolidated operating profit / % of Group's revenue	**2,263**	**28.9%**	2,544	29.2%	**667**	**26.7%**	944	32.4%

* Setoffs are mainly in respect of The Multi-Channel Television segment, which is an associated company.

B. Domestic Fixed-Line Communications segment

Revenue

Segment revenue in the period amounted to NIS 3,509 million compared to NIS 3,534 million in the corresponding period, a decrease of 0.7%.

Segment revenue in the Quarter amounted to NIS 1,149 million compared to NIS 1,186 million in the corresponding quarter, a decrease of 3.1%.

The decrease in the segment's revenue stems primarily from a decrease in revenues from telephony, mainly as a result of erosion of revenue per telephone line, and from a decrease in the number of subscribers. There is also a decrease in revenue from interconnect fees to the cellular networks (with a corresponding decrease in expenses as described below), and in revenue from transmission.

The decrease in revenue was moderated by an increase in high speed Internet use, primarily a result of an increase in the number of Internet subscribers and an increase in revenue per subscriber in the reporting period (figures for the Quarter remained stable), against a backdrop of surfing speed upgrades. There was also a rise in revenue from data communication.

Costs and expenses

Depreciation and amortization expenses in the period amounted to NIS 541 million compared to NIS 513 in the corresponding period, an increase of 5.5%.

Depreciation and amortization expenses in the Quarter amounted to NIS 185 million compared to NIS 180 million in the corresponding quarter, an increase of 2.8%.

The increase in depreciation and amortization expenses, which stems from investments in the NGN project, was moderated by the end of depreciation of other property, plant and equipment.

The salary expense in the period amounted to NIS 808 million compared to NIS 859 million in the corresponding period, a decrease of 5.9%.

The salary expense in the Quarter amounted to NIS 274 million compared to NIS 284 million in the corresponding quarter, a decrease of 3.5%.

The decrease in the salary expense stemmed mainly from a decrease in share-based payments and employee retirement, and was partly offset by wage creep and hiring new employees.

Operating and general expenses in the period amounted to NIS 778 million compared with NIS 806 million in the corresponding period, a decrease of 3.5%.

Operating and general expenses in the Quarter amounted to NIS 278 million compared with NIS 282 million in the corresponding quarter, a decrease of 1.4%.

The decrease in these expenses in the period stemmed mainly from a decrease in a liability to pay frequency fees in the first quarter of 2012 (see Note 13.1 to the financial statements). The decrease was moderated by an increase in terminal equipment and materials expenses.

There was also a decrease in expenses of interconnect fees to the cellular networks in the period and the Quarter, with a corresponding decrease in revenue from interconnect fees.

Other operating income, net, in the period amounted to NIS 13 million compared to expenses of NIS 82 million in the corresponding period.

Other operating income, net, in the Quarter amounted to NIS 7 million compared to NIS 106 million in the corresponding quarter.

The transition from expenses to income in the reporting period stems from recording a provision of NIS 281.5 million in respect of early retirement severance in the first quarter of 2011. In contrast, in the second quarter of 2012 the Company recognized a loss of NIS 54 million resulting from its decision to terminate the CRM project (see Note 13.2 to the financial statements). In addition, in the reporting period and in the Quarter capital gains from the sale of real estate decreased and there was a loss from forward transactions in respect of copper compared to a profit in the corresponding period and quarter.

Profitability

Operating profit in the segment in the reporting period amounted to NIS 1,395 million compared to NIS 1,274 million in the corresponding period, an increase of 9.5%.

Operating profit in the Quarter amounted to NIS 419 million compared to NIS 546 million in the corresponding quarter, a decrease of 23.3%.

The change in operating profit stems from the changes described above in the income and expense items.

Finance expenses, net

Net finance expenses in the period were stable compared to the corresponding period.

The increase in financing expenses in the reporting period, stemmed mainly from a rise in interest expenses in respect of debentures and bank credit at fixed and variable shekel interest received at the end of the first half and beginning of the second half of 2011. The increase in finance income stemmed mainly from finance income from loans provided to associates, recording finance income after a decrease in a liability to pay frequency fees in the first quarter of 2012 (see Note 13.1 to the financial statements), and finance income from shareholder loans to DBS.

Net finance expenses in the Quarter amounted to NIS 63 million compared to NIS 88 million in the corresponding quarter a decrease of 28.4%.

The decrease in net finance expenses in the quarter stemmed primarily from an increase in finance income from shareholder loans to DBS, a decrease in finance expenses in respect of revaluation of a liability to distribute a dividend that does not comply with the profit test, and finance income from loans provided to associates. The decrease was moderated mainly by a decrease in profits from financial assets held for trade.

C. Cellular segment

Revenue

Segment revenue in the period amounted to NIS 3,441 million compared to NIS 4,309 million in the corresponding period, a decrease of 20.1%.

Revenue in the Quarter amounted to NIS 1,049 million compared to NIS 1,421 million in the corresponding quarter, a decrease of 26.2%.

The decrease in revenue stems from a significant intensification in competition in the segment (see section 3.7.2 in the Update to Chapter A of the Periodic Report for 2011).

Segment revenues from services (including value added services) in the period amounted to NIS 2,507 million compared to NIS 2,788 million in the corresponding period, a decrease of 10.1%.

Segment revenues from services in the Quarter amounted to NIS 816 million compared to NIS 914 million in the corresponding quarter, a decrease of 10.7%.

The decrease in revenue from services stemmed from tariff erosion as a result of greater competition, which led to a decrease in revenue per subscriber (ARPU). The decrease on the Quarter was partly offset by revenue received since the beginning of 2012 from cellular operators that use the segment's network

Segment revenues from sales of terminal equipment in the period amounted to NIS 934 million compared to NIS 1,521 million in the corresponding period, a decrease of 38.6%.

The decrease in revenue from sales of terminal equipment was primarily due to a decrease in quantities sold, which was partly offset by a rise in the selling prices of the terminal equipment following a change in the mix of models sold.

Segment revenues from sales of terminal equipment in the Quarter amounted to NIS 233 million compared to NIS 507 million in the corresponding quarter, a decrease of 54%.

The decrease in revenues from the sale of terminal equipment stemmed mainly from a decline in the number of sales.

Costs and expenses

Depreciation and amortization expense in the period amounted to NIS 402 million compared to NIS 421 million in the corresponding period, a decrease of 4.5%.

Depreciation and amortization expense in the Quarter amounted to NIS 130 million compared to NIS 139 million in the corresponding quarter, a decrease of 6.5%.

The decrease in depreciation and amortization expenses stemmed mainly from termination of the capitalization of the costs of subscriber acquisition.

The salary expense in the period amounted to NIS 386 million compared to NIS 452 million in the corresponding period, a decrease of 14.6%.

The salary expense in the Quarter amounted to NIS 124 million compared to NIS 153 million in the corresponding quarter, a decrease of 19%.

The decrease in the salary expense stemmed mainly from a decrease in the number of positions.

Operating and general expenses in the reporting period amounted to NIS 1,928 million compared to NIS 2,338 million in the corresponding period, a decrease of 17.5%.

Operating and general expenses in the Quarter amounted to NIS 596 million compared to NIS 787 million in the corresponding quarter, a decrease of 24.3%.

The decrease stemmed primarily from a decrease in the cost of selling terminal equipment, due mainly to a decrease in the number of handsets sold, which was partly offset by a rise in the prices of the handsets.

Profitability

Operating profit in the period amounted to NIS 725 million compared to NIS 1,098 million in the corresponding period, a decrease of 34%.

Operating profit in the Quarter amounted to NIS 199 million compared to NIS 342 million in the corresponding quarter, a decrease of 41.8%.

The decrease in operating profit stemmed mainly from erosion of revenue from services and from a decline in the volume of sales of terminal equipment, as noted above.

Finance income, net

Net finance income in the period amounted to NIS 32 million compared to net finance expenses of NIS 23 million in the corresponding period, an increase of 39.1%.

The increase in net finance income stemmed primarily from finance income resulting from an increase in the credit embodied in the sale of terminal equipment in installments in the past three years, which was partly offset by higher expenses in respect of loans from the parent company and by exchange rate differences.

Net finance income in the Quarter amounted to NIS 10 million compared to NIS 4 million in the corresponding quarter.

The increase in net finance income stemmed primarily from finance income resulting from an increase in the credit embodied in the sale of terminal equipment in installments, and exchange rate differences following a fall in the dollar exchange rate in the Quarter compared to a rise in the corresponding quarter last year, which was partly offset by higher expenses in respect of loans from the parent company.

D. **International communications, internet and NEP services**

Revenue

Revenue in the segment in the reporting period amounted to NIS 1,001 million compared to NIS 1,012 million in the corresponding period, a decrease of 1.1%.

Revenue in the Quarter amounted to NIS 339 million compared to NIS 351 million in the corresponding quarter, a decrease of 3.4%.

The decrease in revenue from outgoing and incoming calls which stems from a decline in the overall volume of traffic in the market and from a decrease in revenue from call transfer operations communications carriers around the world, was moderated by an increase in Internet revenue as a result of an increase in the number of customers, and by growth in the reporting period in communications solutions for business (ICT).

Costs and expenses

Depreciation and amortization expenses in the reporting period amounted to NIS 103 million, compared to NIS 79 million in the corresponding period, an increase of 30.4%.

Depreciation and amortization expenses in the Quarter amounted to NIS 34 million, compared to NIS 28 million in the corresponding period, an increase of 21.4%.

Most of the increase stems from the first-time depreciation of the sea-bed cable at the beginning of 2012.

The salary expense in the reporting period amounted to NIS 207 million compared to NIS 195 million in the corresponding period, an increase of 6.2%.

The salary expense in the Quarter amounted to NIS 70 million compared to NIS 65 million in the corresponding quarter, an increase of 7.7%.

The increase in the salary expense stems primarily from an increase in the number of employees providing outsourcing services in the ICT operation, and in respect of termination of the capitalization of subscriber acquisition costs.

Operating and general expenses in the reporting period amounted to NIS 532 million, compared to NIS 566 million in the corresponding period, a decrease of 4.3%.

Operating and general expenses in the Quarter amounted to NIS 179 million, compared to NIS 197 million in the corresponding quarter, a decrease of 9.1%.

The decrease in these expenses stems from a corresponding erosion of revenue, primarily costs in respect of incoming and outgoing calls, and a decrease in international cable maintenance expenses resulting from use of the sea-bed cable.

Profitability

Operating profit in the segment in the reporting period amounted to NIS 157 million compared to NIS 182 million in the corresponding period, a decrease of 13.7%.

Operating profit in the segment in the Quarter amounted to NIS 55 million compared to NIS 61 million in the corresponding quarter, a decrease of 9.8%.

The decrease in operating profit stems from the changes described above in the income and expenses items.

E. **Multi-channel television (stated by the equity method)**

Revenue

Revenue in the segment in the reporting period amounted to NIS 1,228 million compared to NIS 1,215 million in the corresponding period, an increase of 1.1%.

Most of the increase stems from a rise in revenue from the use of advanced converters, an increase in revenue from premium channels, and one-time sales of content in the first quarter of 2012.

Income in the segment in the Quarter amounted to NIS 403 million compared to NIS 405 million in the corresponding period, a decrease of 0.5%.

Costs and expenses

Cost of sales in the reporting period amounted to NIS 801 million compared to NIS 809 million in the corresponding period, a decrease of 1%.

Most of the decrease stems from a decrease in depreciation expenses, which was moderated by an increase in content expenses and expenses for consumption of space segments.

Cost of sales in the Quarter amounted to NIS 273 million compared to NIS 268 million in the corresponding period, an increase of 1.9%.

Sales, marketing and administrative and general expenses in the reporting period amounted to NIS 247 million compared to NIS 216 million in the corresponding period, an increase of 14.4%.

Sales, marketing and administrative and general expenses in the Quarter amounted to NIS 76 million compared to NIS 74 million in the corresponding period, an increase of 2.7%.

The increase stemmed from termination of capitalization of subscriber acquisition costs and from a rise in advertising and depreciation expenses.

Profitability

Operating profit in the reporting period amounted to NIS 180 million compared to 190 million in the corresponding period, a decrease of 5.3%.

Operating profit in the Quarter amounted to NIS 54 million compared to 63 million in the corresponding period, a decrease of 14.3%.

The decrease in operating profit stems from the changes described above in the income and expense items.

1.2.3 Income tax

The Group's tax expenses in the reporting period amounted to NIS 597 million, which is 27.5% of the profit after finance expenses net, compared to NIS 633 million and 26.6% of the profit after finance expenses net in the corresponding period.
The Group's tax expenses in the Quarter amounted to NIS 178 million, which is 29.1% of the profit after finance expenses net, compared to NIS 243 million and 28.3% of the profit after finance expenses net in the corresponding quarter.
The rise in the percentage of tax after finance expenses net stems mainly from a rise in the corporate tax rate (from 24% in 2011 to 25% in 2012).

1.3 Equity

Equity attributed to the owners of the Company at September 30, 2012 amounted to NIS 1.95 billion, which is approximately 12% of the total balance sheet, compared to NIS 2.05 billion and 11.1% of the total balance sheet on September 30, 2011.
The increase in equity, which stemmed mainly from the Group's profits, was offset completely by the distribution of a dividend of NIS 2.07 billion during the period, in respect of the profits of the second half of 2011 and the first half of 2012. (See Notes 6.4 and 6.5 to the financial statements).

1.4 Cash flow

Consolidated cash flow from operating activities in the reporting period amounted to NIS 3,012 million, compared to NIS 2,327 million in the corresponding period, an increase of NIS 685 million.
Consolidated cash flow from operating activities in the Quarter amounted to NIS 1,024 million, compared to NIS 882 million in the corresponding quarter, an increase of NIS 142 million.
Most of the increase in the reporting period stems from the Cellular segment, due to a decrease in working capital offset by a decrease in net profit. The decrease in working capital in the Cellular segment stemmed mainly from a decline in the volume of sales of terminal equipment in installments, which led to a decrease in the customer balance, and as a result of the deduction of transactions in installments paid by credit card (see Note 10.2 to the financial statements). The increase was moderated by a decrease in cash flow from operating activities in the Domestic Fixed-Line Communications segment, mainly due to changes in the working capital and income tax payments.

Cash flow from operating activities is one of the sources for financing the Group's investments. In the reporting period these included NIS 1,009 million in the development of communications infrastructure and NIS 200 million in intangible assets and deferred expenses, compared to NIS 1,190 million and NIS 244 million respectively in the

corresponding period. In addition, NIS 126 million net was invested in financial assets held for trade compared to NIS 2,004 million in the corresponding period.
Furthermore, the Group received NIS 96 million in proceeds from realization of investments and non-current loans, which include the sale of assets available for sale (see Note 4.3 to the financial statements).

In the reporting period, the Group repaid debts and paid interest amounting to NIS 1,010 million, of which NIS 452 million of debentures, NIS 241 million of loans and NIS 317 million of interest payments, compared to debt repayment and interest payments of NIS 1,690 million in the corresponding period. Conversely, no debt was raised in the reporting period, while NIS 5.29 billion of debt was raised in the Domestic Fixed-Line Communications segment in the corresponding quarter.
In addition, in respect of an increase in the percentage of its holding in a subsidiary, the Group paid NIS 77 million in the reporting period.
Also in the reporting period, a dividend of NIS 1.57 billion was paid, compared to a dividend of NIS 1.66 million in the corresponding period (see Note 6.4 to the financial statements).

Average of long-term liabilities (including current maturities) to financial institutions and debenture holders in the reporting period amounted to NIS 9,278 million.
Average supplier credit in the reporting period was NIS 864 million, and average short-term customer credit was NIS 3,087 million. The average long-term customer credit was NIS 1,312 million.

The Group's working capital surplus at September 30, 2012 amounted to NIS 212 million, compared with a working capital surplus of NIS 1,336 million on September 30, 2011.

At September 30, 2012, the Company (according to its separate financial statements) has a working capital deficit of NIS 1,080 million, compared with a working capital surplus of NIS 140 million on September 30, 2011. The Company's working capital deficit stems primarily from a decrease in balances of cash and cash equivalents and in current investments in current financial assets, which at September 30, 2012 included proceeds in respect of an issue of debentures in the corresponding quarter. The deficit was moderated by a decrease in the Company's current liabilities.

The Board of Directors of the Company reviewed the existing and expected cash sources and needs in the foreseeable future, as well as the investment needs of the Company. It also examined the sources of finance and the potential amounts available to the Company. Based on its review of all these factors, the Board of Directors concluded that despite the deficit in the Company's working capital (according to the separate financial statements), the Company does not have a liquidity problem. It has the ability to meet existing and foreseeable future cash needs, by generating cash from operations, by receiving dividends from subsidiaries, and by raising debt, should it choose to do so, from banking and non-bank sources.[2]

The above information includes forward looking information based on he Company's assessments as to liquidity. The actual data might differ significantly from those assessments if a change occurs in any of the factors taken into account in making them.

2. Market Risks – Exposure and Management

2.1 Following its adoption and application of a policy for the management of exposure to financial risks on June 26, 2008 (see Part 4 of the Directors' Report for 2011) –

2.1.1 On October 18, 2012 the Board of Directors of the Company made the following revisions to the hedging policy for the CPI risk:

[2] For this reason, there are no warning signs in the Company as provided in Article 10(b)(14) of the Securities Regulations (Periodic and immediate reports) for attaching a project cash flow report.

2.1.1.1 Transactions will be discretionary and will be made according to the limitations of market trading, will be reviewed in relation to the inflationary expectations embodies in the debentures market and the inflation forecast expectations, as well as in relation to the inflation target band of the Bank of Israel.

2.1.1.2 The hedging transactions will be coordinated with the amortization schedule of the CPI-linked financial debt.

2.1.1.3 The Company will ensure that the hedging transactions meet the requisite terns enabling the application of hedging accounting for them.

2.1.1.4 If the CPI exposure exceeds NIS 500 million, the hedge percentage should be no less than 40% and not more than 100% of the exposure in respect of CPI-linked financial debt; if that exposure is less than NIS 500 million, the hedge should be no more than 50% of the exposure stemming from CPI-linked financial debt.

2.1.2 Copper prices – At September 30, 2012, the Company has open trades for forward sales of 4,686 tons. The total fair value at that date was a negative NIS 2.9 million.

2.2 The sensitivity analyses for the fair value and the effect of the change in market prices on the fair value of the balances in and off the balance sheet, for which there is strong engagement at September 30, 2012, do not differ materially from the report at December 31, 2011.

2.3 The linkage base report at September 30, 2012 does not differ materially from the report of December 31, 2011.

3. Aspects of Corporate Governance

3.1 Disclosure on the proceeding for approval of the financial statements

3.1.1 The committee

The Company's Financial Statements Review Committee is a separate committee that does not serve also as the Audit Committee.

3.1.2 The members of the committee

The committee has three members: Itzchak Idelman, Chairman (external director), Mordechai Keret (external director), and Dr. Yehoshua Rosenzweig (independent director). All three have accounting and financial expertise. All the members of the committee provided a statement prior to their appointment. For additional details about the directors who comprise the committee, see Chapter D of the Company's 2011 Periodic Report.

3.1.3 Procedure for approval of the financial statements

A. The Financial Statements Review Committee discussed the financial statements and formulated its recommendations to the Board of Directors at its meetings on October 28, 2012 and November 4, 2012.

B. All the members of the committee participated in the above meetings.

C. Other than the members of the committee, the meetings on October 28, 2012 and November 4, 2012 were attended by the Chairman of the Board – Mr. Shaul Elovitz, the CEO of the Company – Mr. Avi Gabbay, the CFO and Deputy CEO – Mr. Alan Gelman, the VP Economics and Budget – Mr. Dudu Mizrachi, the Company's comptroller – Mr. Danny Oz, the Company Secretary – Ms Linor Yochelman, the internal auditor – Mr. Lior Segal, the General Counsel – Mr.

Amir Nachlieli, Mr. Rami Nomkin – director, the external auditors, and other office-holders in the Company.

D. Among other things, the committee reviewed the assessments and estimates made in connection with the financial statements, internal controls relating to financial reporting, the integrity and propriety of the disclosure in the financial statements, and the accounting policy adopted in the material affairs of the corporation.

E. The recommendations of the committee were forwarded to the Board of Directors of the Company in writing, on November 4, 2012.

F. The Board of Directors discussed the recommendations of the Financial Statements Review Committee and the financial statements themselves, on November 7, 2012.

G. The Board of Directors believes that the recommendations of the Financial Statements Review Committee were submitted a reasonable time (two business days) before the Board of Directors meeting, even taking into account the scope and complexity of the recommendations.

H. The Board of Directors of the Company accepted the recommendations of the Financial Statements Review Committee and resolved to approve the financial statements of the Company for the third quarter of 2012.

3.2 Application of the provisions of the Sarbanes-Oxley Act of 2002 (SOX)

Commencing 2011, the Company ceased to apply the provisions of the Securities (Periodic and immediate reports) (Amendment) Regulations, 2009, in the matter of internal control; instead, it applies the provisions of the Sarbanes-Oxley Act of 2002 (SOX), as a significant subsidiary of a foreign private issuer.

4. Disclosure concerning the Financial Reporting of the Corporation

4.1 Critical accounting estimates

Preparation of the financial statements in accordance with IFRS requires management to make assessments and estimates that affect the reported values of assets, liabilities, income and expenses, as well as disclosure in connection with contingent assets and liabilities. Management bases these assessments and estimates on past experience and on valuations, expert opinions and other factors which it believes are relevant in the circumstances. Actual results might differ from these assessments on different assumptions or in different conditions. The financial statements provide information about primary topics of uncertainty in critical estimates and judgments in the application of the accounting policy. We believe these assessments and estimates to be critical since any change in them and in the assumptions could potentially and materially affect the financial statements.
We believe these assessments and estimates to be critical since any change in them and in the assumptions could potentially and materially affect the financial statements.

4.2 Given the significance of the claims filed against the Group, which cannot yet be assessed or in respect of which the exposure cannot yet be calculated, the auditors drew attention to them in their opinion on the financial statements

4.3 Material events after the date of the financial statements

On October 2012, the Company raised bank debt of NIS 500 million with an average date to maturity of 4,3 years, at fixed shekel interest (see Note 13.5 to the financial statements).

5. Details of Series of Liability Certificates

5.1 Debentures Series 5

5.1.1 On March 21, 2012, Hermetic Trust (1975) Ltd. ("Hermetic") was approved as trustee for the Debentures (Series 5) of the Company, replacing Mizrachi Tefahot Trust Co. Ltd., and accordingly, Hermetic commenced service as trustee for those debentures.

Details of the trustee:
Trust company – Hermetic Trust (1975) Ltd.
Contact person in the trust company – Dan Avnon, CEO
E-mail – avnon@hermetic.co.il
Telephone – 03-5274867
Address – Hermetic House, 113 Hayarkon Street, Tel Aviv

5.1.2 On June 1, 2012, NIS 397,827,833 par value was repaid.

The stock exchange fair value of Debentures Series 5 at September 30, 2012, is NIS 2,178,505,215.

5.2 Other than the foregoing, the details relevant to the series of liability certificates at September 30, 2012 do not differ materially from the report of December 31, 2011.

5.3 On July 4, 2012, the Company received notification from Standard & Poor's Maalot, which rates the Company (AA+/Negative Outlook) and its debentures (AA+), ratifying and leaving unchanged the above ratings.

On July 19, 2012, the Company received notification from Midroog Ltd., which rates the Company's Debentures (Series 5, 6, 7, 8), that the rating of the Company's debentures (series 5, 6, 7, 8) was being lowered from Aa1/Negative Outlook to Aa2/Stable Outlook.

The rating reports are attached to this report.

6. Miscellaneous

For information about the liabilities of the reporting corporation and the consolidated and proportionately consolidated companies in its financial statements at September 30, 2012, see the reporting form uploaded by the Company to Magna on November 7, 2012.

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

Shaul Elovitch	Avraham Gabbay
Chairman of the Board	CEO

Date of signature: November 7, 2012

"Bezeq" The Israel Telecommunication Corporation Ltd.

Condensed Consolidated Interim Financial Statements

September 30, 2012

(Unaudited)

bezeq

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

Contents

Somekh Chaikin
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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 September 30, 2012 and the related condensed consolidated interim statements of income, comprehensive income, changes in equity and cash flows for the nine and three month periods then ended. The Board of Directors and Management are responsible for the preparation and presentation of the financial information for these interim periods in accordance with IAS 34 "*Interim Financial Reporting"*, and are also responsible for the preparation of financial information for these interim periods in accordance with Section D of the Securities Regulations (Periodic and Immediate Reports), 1970. Our responsibility is to express a conclusion on the financial information for these interim periods based on our review.

We did not review the condensed interim financial information of certain consolidated subsidiaries whose assets constitute approximately 2 % of the total consolidated assets as of September 30, 2012, and whose revenues constitute approximately 1.8 % and 2%of the total consolidated revenues for the nine and three month periods then ended, respectively. The condensed interim financial information of those companies was reviewed by other auditors whose review reports thereon were furnished to us, and our conclusion, insofar as it relates to amounts emanating from the financial information of such companies, is based solely on the said review reports 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 reports of other auditors, nothing has come to our attention that causes us to believe that the abovementioned financial information is 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 reports of other auditors, nothing has come to our attention that causes us to believe that the abovementioned 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.)

November 7, 2012

Condensed Consolidated Interim Statements of Financial Position as at

Assets	September 30, 2012 (Unaudited) NIS million	September 30, 2011 (Unaudited) NIS million	December 31, 2011 (Audited) NIS million
Cash and cash equivalents	**676**	1,564	1,352
Investments, including derivatives	**1,071**	2,056	946
Trade receivables	**3,044**	3,008	3,059
Other receivables	**250**	229	286
Inventory	**149**	199	204
Assets classified as held for sale	**44**	12	23
Total current assets	**5,234**	7,068	5,870
Investments, including derivatives	**94**	115	119
Trade and other receivables	**1,193**	1,594	1,499
Property, plant and equipment	**6,116**	5,959	6,022
Intangible assets	**2,175**	2,237	2,257
Deferred and other expenses	**276**	268	282
Investments in equity-accounted investees (mainly loans)	**984**	1,031	1,059
Deferred tax assets	**144**	218	223
Total non-current assets	**10,982**	11,422	11,461
Total assets	**16,216**	18,490	17,331

Condensed Consolidated Interim Statements of Financial Position as at(Contd.)

Liabilities and equity	Note	September 30, 2012 (Unaudited) NIS million	September 30, 2011 (Unaudited) NIS million	December 31, 2011 (Audited) NIS million
Debentures, loans and borrowings		**608**	776	765
Trade payables		**771**	919	890
Other payables, including derivatives		**670**	892	792
Current tax liabilities		**475**	432	397
Deferred income		**60**	52	56
Provisions		**172**	220	186
Employee benefits		**288**	467	389
Dividend payable	6	**1,978**	1,974	971
Total current liabilities		**5,022**	5,732	4,446
Debentures		**4,265**	4,670	4,663
Loans		**4,066**	4,168	4,150
Employee benefits		**228**	271	229
Other liabilities		**86**	44	93
Provisions		**71**	70	69
Deferred tax liabilities		**54**	60	69
Dividend payable	6	**473**	1,386	924
Total non-current liabilities		**9,243**	10,669	10,197
Total liabilities		**14,265**	16,401	14,643
Equity				
Total equity attributable to equity holders of the Company		**1,951**	2,048	2,650
Non-controlling interests		**-**	41	38
Total equity		**1,951**	2,089	2,688
Total liabilities and equity		**16,216**	18,490	17,331

Shaul Elovitch
Chairman of the Board of Directors

Avi Gabbay
CEO

Alan Gelman
Deputy CEO and CFO

Date of approval of the financial statements: November 7, 2012

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

Condensed Consolidated Interim Statements of Income

	For the nine month period ended September 30		For the three months period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues (Note 8)	**7,829**	8,723	**2,494**	2,917	11,373
Operating results					
Depreciation and amortization	**1,075**	1,040	**359**	357	1,395
Salaries	**1,527**	1,612	**511**	540	2,103
General and operating expenses (Note 9)	**2,976**	3,445	**963**	1,182	4,494
Other operating expenses (revenues), net – see also Note 13.2	**(12)**	82	**(6)**	(106)	139
	5,566	6,179	**1,827**	1,973	8,131
Operating profit	**2,263**	2,544	**667**	944	3,242
Financing expenses (income)					
Financing expenses	**506**	445	**181**	186	599
Financing income	**(418)**	(277)	**(126)**	(100)	(389)
Financing expenses, net	**88**	168	**55**	86	210
Profit after financing expenses (income), net	**2,175**	2,376	**612**	858	3,032
Share in losses of equity-accounted investees	**233**	203	**92**	66	216
Profit before income tax	**1,942**	2,173	**520**	792	2,816
Income tax	**597**	633	**178**	243	755
Profit for the period	**1,345**	1,540	**342**	549	2,061
Attributable to:					
Owners of the Company	**1,339**	1,542	**342**	550	2,066
Non-controlling interests	**6**	(2)	**-**	(1)	(5)
Profit for the period	**1,345**	1,540	**342**	549	2,061
Earnings per share (NIS)					
Basic and diluted earnings per share	**0.49**	0.57	**0.13**	0.20	0.76

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

Condensed Consolidated Interim Statements of Comprehensive Income

	For the nine month period ended September 30		For the three months period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Profit for the period	**1,345**	1,540	**342**	549	2,061
Actuarial gains, net of tax	**-**	-	**-**	-	27
Net change in fair value of financial assets classified as available for sale transferred to profit or loss, net of tax	**(6)**	-	**-**	-	-
Effective share of the change in fair value of instruments used for cash flow hedging, net of tax	**2**	-	**4**	-	-
Other items of comprehensive income for the period, net of tax	**(1)**	2	**(1)**	3	8
Total comprehensive income for the period	**1,340**	1,542	**345**	552	2,096
Attributable to:					
Owners of the Company	**1,334**	1,544	**345**	553	2,101
Non-controlling interests	**6**	(2)	**-**	(1)	(5)
Total comprehensive income for the period	**1,340**	1,542	**345**	552	2,096

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

Condensed Consolidated Interim Statements of Changes in Equity

	Share capital NIS million	Share premium NIS million	Capital reserve for employee options NIS million	Capital reserve for a transaction between a corporation and a controlling shareholder NIS million	Other reserves NIS million	Retained deficit NIS million	Total NIS million	Non-controlling interests NIS million	Total equity NIS million
	Attributable to owners of the Company								
For the nine month period ended September 30, 2012									
Balance as at January 1, 2012 (Audited)	3,826	68	220	390	(2)	(1,852)	2,650	38	2,688
Profit for the period (Unaudited)	-	-	-	-	-	1,339	1,339	6	1,345
Other comprehensive loss for the period, net of tax (Unaudited)	-	-	-	-	(5)	-	(5)	-	(5)
Total comprehensive income for the period	-	-	-	-	(5)	1,339	1,334	6	1,340
Transactions with owners recognized directly in equity									
Dividends to Company shareholders (Unaudited) *	-	-	-	-	-	(2,071)	(2,071)	-	(2,071)
Share-based payments (Unaudited)	-	-	60	-	-	-	60	-	60
Exercise of options for shares (Unaudited)	11	31	(35)	-	-	-	7	-	7
Exercise of options for subsidiary shares (Unaudited)	-	-	-	-	2	-	2	6	8
Acquisition of non-controlling interests (Unaudited)	-	-	-	-	(31)	-	(31)	(46)	(77)
Distribution to holders of non-controlling interests less investment in a subsidiary (Unaudited)	-	-	-	-	-	-	-	(4)	(4)
Balance as at September 30, 2012 (Unaudited)	3,837	99	245	390	(36)	(2,584)	1,951	-	1,951

* See Note 6.4 and 6.5 below.

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

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

	Share capital	Share premium	Capital reserve for employee options	Capital reserve for a transaction between a corporation and a controlling shareholder	Other reserves	Retained deficit	Total	Non-controlling interests	Total equity
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
	Attributable to owners of the Company								
For the nine month period ended September 30, 2011									
Balance as at January 1, 2011 (Audited)	6,213	378	146	390	(10)	(1,790)	5,327	43	5,370
Profit for the period (Unaudited)	-	-	-	-	-	1,542	1,542	(2)	1,540
Other comprehensive income for the period, net of tax (Unaudited)	-	-	-		2	-	2	-	2
Total comprehensive income for the period	-	-	-	-	2	1,542	1,544	(2)	1,542
Transactions with owners recognized directly in equity									
Dividends to Company shareholders – distribution not in compliance with the earnings test (Unaudited)	(2,415)	(396)	-	-	-	-	(2,811)	-	(2,811)
Dividends to Company shareholders (Unaudited)	-	-	-		-	(2,155)	(2,155)	-	(2,155)
Share-based payments (Unaudited)	-	-	127	-	-	-	127	-	127
Exercise of options for shares (Unaudited)	23	71	(78)	-	-	-	16	-	16
Balance as at September 30, 2011 (Unaudited)	3,821	53	195	390	(8)	(2,403)	2,048	41	2,089

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

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

	Share capital	Share premium	Capital reserve for employee options	Capital reserve for a transaction between a corporation and a controlling shareholder	Other reserves	Retained deficit	Total	Non-controlling interests	Total equity
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
	Attributable to owners of the Company								
For the three month period ended September 30, 2012									
Balance as at July 1, 2012 (Unaudited)	3,831	82	242	390	(39)	(1,929)	2,577	-	2,577
Profit for the period (Unaudited)	-	-	-	-	-	**342**	**342**	-	**342**
Other comprehensive income for the period, net of tax (Unaudited)	-	-	-	-	**3**	-	**3**	-	**3**
Total comprehensive income for the period	-	-	-	-	**3**	**342**	**345**	-	**345**
Transactions with owners recognized directly in equity									
Dividends to Company shareholders (Unaudited) *	-	-	-	-	-	**(997)**	**(997)**	-	**(997)**
Share-based payments (Unaudited)	-	-	**21**	-	-	-	**21**	-	**21**
Exercise of options for shares (Unaudited)	**6**	**17**	**(18)**	-	-	-	**5**	-	**5**
Balance as at September 30, 2012 (Unaudited)	**3,837**	**99**	**245**	**390**	**(36)**	**(2,584)**	**1,951**	**-**	**1,951**

* See Note 6.5 below.

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

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

	Share capital	Share premium	Capital reserve for employee options	Capital reserve for a transaction between a corporation and a controlling shareholder	Other reserves	Retained deficit	Total	Non-controlling interests	Total equity
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
	Attributable to owners of the Company								
For the three month period ended September 30, 2011									
Balance as at July 1, 2011 (Unaudited)	3,814	35	171	390	(11)	(1,961)	2,438	42	2,480
								-	
Profit for the period (Unaudited)	-	-	-	-	-	550	550	(1)	549
Other comprehensive income for the period, net of tax (Unaudited)	-	-	-	-	3	-	3	-	3
Total comprehensive income for the period	-	-	-	-	3	550	553	(1)	552
Transactions with owners recognized directly in equity									
Dividends to Company shareholders (Unaudited)	-	-	-	-	-	(992)	(992)	-	(992)
Share-based payments(Unaudited)	-	-	43	-	-	-	43	-	43
Exercise of options for shares(Unaudited)	7	18	(19)	-	-	-	6	-	6
Balance as at September 30, 2011 (Unaudited)	3,821	53	195	390	(8)	(2,403)	2,048	41	2,089

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

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

	Attributable to owners of the Company								
	Share capital NIS million	Share premium NIS million	Capital reserve for employee options NIS million	Capital reserve for a transaction between a corporation and a controlling shareholder NIS million	Other reserves NIS million	Retained deficit NIS million	Total NIS million	Non-controlling interests NIS million	Total equity NIS million
For the year ended December 31, 2011									
Balance as at January 1, 2011 (Audited)	6,213	378	146	390	(10)	(1,790)	5,327	43	5,370
Profit for the period (Audited)	-	-	-	-	-	2,066	2,066	(5)	2,061
Other comprehensive income for the year, net of tax (Audited)	-	-	-	-	8	27	35	-	35
Total comprehensive income for the year (Audited)	-	-	-	-	8	2,093	2,101	(5)	2,096
Transactions with owners recognized directly in equity									
Dividends to Company shareholders not in compliance with the earnings test (Audited)	(2,415)	(396)	-	-	-	-	(2,811)	-	(2,811)
Dividends to Company shareholders (Audited)	-	-	-	-	-	(2,155)	(2,155)	-	(2,155)
Share-based payments (Audited)	-	-	167	-	-	-	167	-	167
Exercise of options for shares (Audited)	28	86	(93)	-	-	-	21	-	21
Balance as at December 31, 2011 (Audited)	3,826	68	220	390	(2)	(1,852)	2,650	38	2,688

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

Condensed Consolidated Interim Statements of Cash Flows

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows from operating activities					
Profit for the period	**1,345**	1,540	**342**	549	2,061
Adjustments:					
Depreciation	**838**	802	**282**	275	1,080
Amortization of intangible assets	**218**	217	**72**	74	287
Amortization of deferred and other expenses	**19**	21	**5**	8	28
Share in losses of equity-accounted investees	**233**	203	**92**	66	216
Financing income and expenses	**200**	232	**91**	113	293
Capital loss (gain), net	**(22)**	(167)	**(24)**	(80)	(181)
Share-based payment transactions	**60**	127	**21**	43	167
Income tax expenses	**597**	633	**178**	243	755
Expenses (income) in respect of derivatives, net	**5**	(20)	**11**	(20)	(19)
Change in inventory	**49**	(33)	**56**	71	(33)
Change in trade and other receivables	**320**	(744)	**226**	(237)	(756)
Change in trade and other payables	**(239)**	(137)	**(116)**	(68)	(131)
Change in provisions	**(14)**	(31)	**(2)**	(33)	(64)
Change in employee benefits	**(103)**	164	**(38)**	(18)	82
Change in deferred and other income	**(8)**	-	**6**	-	50
Net income tax paid	**(486)**	(480)	**(178)**	(104)	(649)
Net cash from operating activities	**3,012**	2,327	**1,024**	882	3,186
Cash flow used in investing activities					
Investment in intangible assets and deferred expenses	**(200)**	(244)	**(58)**	(86)	(355)
Refund from the Ministry of Communications for frequencies	**-**	36	**-**	36	36
Proceeds from the sale of property, plant and equipment	**166**	305	**97**	69	230
Acquisition of financial assets held for trading	**(2,315)**	(2,857)	**(460)**	(2,853)	(2,859)
Proceeds from the sale of financial assets held for trading	**2,189**	853	**14**	851	1,967
Purchase of property, plant and equipment	**(1,009)**	(1,190)	**(309)**	(393)	(1,548)
Proceeds from disposal of investments and long-term loans	**96**	7	**3**	1	11
Interest and dividend received	**13**	19	**3**	7	37
Miscellaneous	12	(9)	3	5	(10)
Net cash used in investment activities	**(1,048)**	(3,080)	**(707)**	(2,363)	(2,491)

Condensed Interim Statements of Cash Flows (contd.)

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows used in financing activities					
Issue of debentures	**-**	3,092	**-**	2,692	3,092
Bank loans received	**-**	2,200	**-**	600	2,200
Repayment of debentures	**(452)**	(825)	**(68)**	(68)	(835)
Repayment of loans	**(241)**	(633)	**(137)**	(609)	(648)
Net short-term borrowing	**2**	(3)	**(1)**	-	(5)
Dividends paid	**(1,574)**	(1,663)	**-**	-	(3,155)
Interest paid	**(317)**	(232)	**(41)**	(39)	(377)
Increase in the rate of holding in a subsidiary	**(77)**	-	**-**	-	-
Proceeds from exercise of options	**15**	16	**5**	6	21
Miscellaneous	**4**	-	**(2)**	-	(1)
Net cash from (used in) finance activities	**(2,640)**	1,952	**(244)**	2,582	292
Increase (decrease) in cash and cash equivalents	**(676)**	1,199	**73**	1,101	987
Cash and cash equivalents at the beginning of the period	**1,352**	365	**603**	463	365
Cash and cash equivalents at the end of the period	**676**	1,564	**676**	1,564	1,352

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

Notes to the Financial Statements

1. Reporting Entity

1.1 Bezeq – The Israel Telecommunication Corp. Ltd. ("the Company") is a company registered in Israel whose shares are traded on the Tel Aviv Stock Exchange. The condensed 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 major provider of communication services in Israel (see also Note 11 – Segment Reporting).

1.2 As from April 14, 2010, the ultimate controlling shareholder in the Company is Shaul Elovitch, (together with his brother, Yosef Elovitch), through their holdings in Eurocom Communications Ltd., the controlling shareholder in Internet Gold-Golden Lines Ltd., which controls B Communications Ltd. ("B Communications"). B Communications holds Company shares through companies that it controls, and as at September 30, 2012, holds 30.97% of the Company's shares. Each of these companies is also considered as a controlling shareholder in the Company. In addition to these holdings, the controlling shareholder and his relatives hold, directly or indirectly, another 0.11% of the Company's shares.

2. Basis of Preparation

2.1 The condensed interim consolidated financial statements have been prepared in accordance with IAS 34 – Interim Financial Reporting, and the disclosure provisions in 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, 2011 and the year then ended, and their accompanying notes ("the Annual Financial Statements"). The notes to the interim financial statements include only disclosure of the material changes that have occurred from the date of the most recent Annual Financial Statements until the date of these consolidated interim financial statements.

2.3 The condensed consolidated interim financial statements were approved by the Board of Directors on November 7, 2012.

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 the estimates used.

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.

3. Reporting Principles and Accounting Policy

The significant accounting policies applied in these condensed consolidated interim financial statements are consistent with those applied in the Financial Statements for the year ended December 31, 2011, except as described below.

3.1. Recognition of actuarial gains or losses

The Group did not recognize actuarial gains or losses in the nine and three-month period ended September 30, 2012, since in the interim period, there were no significant changes in the principal actuarial assumptions in a defined benefit plan: discount rate, expected return on plan assets, life expectancy, employee churn rate and the rate of future salary increases.

It is noted that on July 11, 2012, the Commissioner of the Capital Market, Insurance and Savings issued a draft circular regarding a new study about life expectancy. The draft circular indicates the need to revise the mortality tables and other actuarial assumptions that the Company uses to calculate some of its employee benefit liabilities. A study carried out by the Company indicates that a change in actuarial assumptions, based on the draft circular, is not expected to have a material effect on its employee benefit liabilities. The proposed change in the assumptions is not reflected in these financial statements.

3.2. Hedge accounting

Forward contracts to hedge exposure to changes in the CPI for debentures issued by the Company (as described in Note 10 below) were accounted for in the reporting period for the first time as hedge accounting. Accordingly, the Company's hedge transactions in the reporting period were presented in these financial statements, with application of cash flow accounting hedges as follows:

Forward contracts are measured at fair value. Attributable transaction costs are recognized in the statement of income as incurred. Subsequent to initial recognition, changes in the fair value of derivatives designated as a cash flow hedge, in respect of the effective portion of the hedge are recognized in other comprehensive income, directly in a hedging reserve. in respect of the ineffective portion of the hedge, changes in fair value are recognized in profit or loss. The amount recognized in the hedging reserve is reclassified to the statement of income in the same period as the cash flows affect the statement of income and is recognized in the same line item in the statement of income as the hedged item.

On initial designation of the hedge, the Company formally documented the relationship between the hedging instrument and hedged item, including the risk management objectives and strategy in undertaking the hedge transaction, together with the methods that will be used to assess the effectiveness of the hedging relationship.

The Company estimated, both at the inception of the hedge and in subsequent periods, that the hedging instruments are expected to be highly effective in offsetting the changes in the fair value of the respective hedged risk items during the period for which the hedge is designated, and that the actual results of the hedge are within a range of 80-125%.

3.3. New standards not yet adopted

3.3.1. Further to Note 3.20.2 regarding the significant accounting policies in the Annual Financial Statements for a new suite of accounting standards: IFRS 10, Consolidated Financial Statements; IFRS 11, Joint Arrangements; and IFRS 12, Disclosure of Interests in Other Entities ("the New Standards"), the Group examined the effect of adopting the New Standards on the financial statements. The Group estimates that implementation of the new standards is not expected to have a material impact on the financial statements.

3. Reporting Principles and Accounting Policy (Contd.)

3.3 New standards not yet adopted (contd.)

3.3.2. Further to Note 3.20.4, Significant Accounting Policies in the Annual Financial Statements regarding the amendment to IAS 19, Employee Benefits ("the Amendment"), the Group assessed the effect of the Amendment on the financial statements. The Group estimates that implementation of the revised standard is not expected to have a material impact on the financial statements.

4. Group Entities

A detailed description of the Group entities appears in Note 12 to the Group's Annual Financial Statements as at December 31, 2011. Below is a description of the material changes that occurred in connection with the Group entities since publication of the Annual Financial Statements.

4.1. Walla! Communications Ltd. ("Walla")

4.1.1. Further to Note 32.3 to the Annual Financial Statements, regarding the Company's complete tender offer to purchase all the shares of Walla held by the public, on April 5, 2012, the tender offer was accepted by the majority stipulated in the Companies Law (of the number of shares offered for sale, 12,980,972 shares representing 28.45% of the share capital of Walla, notices of acceptance were received for 11,371,893 shares representing 24.92% of the share capital of Walla) and accordingly, all the shares of Walla held by the public were acquired for NIS 77 million (including exercise of employee options), so that subsequent to the acquisition and as of April 15, 2012, Walla was delisted from the TASE and became a private company wholly owned by the Company. Following the purchase of Walla shares from the public, in the nine month period ended September 30, 2012, the Company recognized a decrease of non-controlling interests amounting to NIS 46 million and a decrease in equity attributable to owners of the Company (under capital reserve) amounting to NIS 31 million.

4.1.2. In August 2012, the Company provided a bank guarantee for Teletel Communication Channels Ltd. (a wholly-owned subsidiary of Walla) for a loan of NIS 70 million taken by Teletel. The guarantee is for the unpaid balance of the loan (amounting to NIS 66 million at the date the guarantee was provided) plus interest and other payments related to the loan. The guarantee was provided against cancellation of a similar guarantee provided by Walla and cancellation of Walla's letter of undertaking to comply with financial covenants.

4.2. DBS Satellite Services (1998) Ltd. (an equity-accounted associate)

4.2.1 The Group attaches the condensed interim financial statements of DBS Satellite Services (1998) Ltd. to these condensed consolidated interim financial statements.

4.2.2 Since the beginning of its operations, DBS has accumulated substantial losses. These losses amounted to NIS 230 million in 2011 and NIS 289 million in the nine month period ended September 30, 2012. As a result of these losses, the capital deficit and working capital deficit of DBS as at September 30, 2012 amounted to NIS 3,939 million and NIS 628 million, respectively.

4. Group Entities (Contd.)

4.2 DBS Satellite Services (1998) Ltd. (an equity-accounted associate) (contd.)

4.2.3 As at September 30, 2012, DBS is in compliance with the financial covenants under the financing agreements and the debentures.

The management of DBS believes that the financial resources at its disposal will be sufficient for its operations for the coming year, based on the cash flow forecast approved by DBS's Board of Directors. If additional resources are required to meet its operational requirements for the coming year, DBS will adapt its operations to preclude the need for additional resources beyond those available to it. In recent years, DBS was required to raise external financial resources intended, inter alia, to expand its investments. At the reporting date, a significant increase in the investments of DBS will require an expansion of the financial resources at its disposal.

For further information about the financing sources, see the Notes below.

4.2.4 In May 2012, a debenture was signed by DBS and a number of institutional entities ("the lenders") whereby the lenders would extend to DBS a loan of NIS 392 million ("the debenture"). The proceeds of the funds raised were used for full repayment of the long-term credit granted to the Company by the banks as described in section 4.2.5 below.

The loan granted under the debenture will be used to repay the principal in ten annual unequal installments, where from 2013 - 2017, the payment of the principal will be 8% of the par value of the debenture, and in each subsequent year, the payment of the principal will be 12% of the par value of the debenture.

The debenture bears annual interest at a rate of 6.4% payable in six-monthly installments. The principal and interest of the loan are linked to the CPI. The debenture includes terms for adjusting the interest rate (in accordance with the credit rating), terms for calling for immediate repayment of the debenture, liens, and financial covenants which DBS is required to fulfill. In addition, limitations were set for the debenture in respect of the distribution of the dividends and repayment of owners loans similar to the restrictions applicable under the prior debenture. The applicable ratio of the financial covenant is lower (more stringent) than the financial covenant stipulated in the prior debenture.

4.2.5 Further to Note 12.1.5 to the Annual Financial Statements regarding the financial covenants and stipulations applicable to DBS, in July 2012, DBS repaid the long-term bank credit in full (through a loan granted under the debenture as described in section 4.2.4 above and expansion of debentures (Series B) amounting to NIS 10 million). Upon repayment, the amendment to the financing agreement came into effect, according to which DBS's credit facility was increased to NIS 170 million, terms for its use were defined and the liabilities and restrictions that applied to DBS under the financing agreement were canceled or reduced (including those related to compliance with the business plan, taking liability from third parties, transactions with interested parties, purchase of securities in other corporations, public offerings of securities and mandatory repayment of excess cash flows or issuing of debentures).

In addition, in accordance with the amendment to the agreement, the collateral provided by the Company in favor of the banks to secure DBS's bank credit and its liabilities to the banks for DBS's bank credit, including the Company's guarantee to the banks (described in Note 19.6 to the Annual Financial Statements) were canceled.

The financial covenants that were applicable to date have been canceled and instead, in each quarter, DBS is required to comply with two financial covenants that are the same as the financial covenants set out in the new debenture as described in section 4.2.4 above and terms were defined for calling for immediate payment of credit.

4. Group Entities (Contd.)

4.2 DBS Satellite Services (1998) Ltd. (an equity-accounted associate) (contd.)

4.2.6 The balance of DBS's current debt to the Group companies as at September 30, 2012 amounts NIS 41 million, of which NIS 31 million is to the Company.

It is noted that on September 6, 2012, the general meeting of the Company's shareholders approved an agreement between the Company and DBS regarding a new debt arrangement. In accordance with the agreement, all payments by virtue of prior debt arrangements with a payment date from August 1, 2012 to June 10, 2013 (including additional payments in accordance with prior debt arrangements with an original payment date subsequent to December 31, 2011, other than current payments) will each be postponed for 18 months from the designated repayment date, and in this postponement period, each payment will bear interest at a rate of prime + 4% plus VAT. The deferred payments amount to NIS 26.7 million. Each party may terminate the agreement unilaterally, with notice as set out in the agreement.

The general meeting also approved a similar arrangement for DBS's debt of NIS 5.9 million to Bezeq International.

4.3. Stage One Venture Capital Fund (Israel) L.P. ("the Fund")

Further to Note 12.2.3(F) to the Annual Financial Statements, in February 2012, the Fund signed an agreement to sell all its holdings in Traffix Communications Systems Ltd. Following the agreement, in March 2012, the Group recognized financing income of NIS 74 million from the disposal of an available-for-sale asset.

5. Contingent Liabilities

During the normal course of business, legal claims were filed against Group companies or there are pending claims (“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 152 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 September 30, 2012, due to legal claims filed against Group companies on various matters and which are unlikely to be realized, amounts to NIS 11.4 billion of which NIS 1.3 billion is for claims, which at this stage cannot be assessed, as set out in section 5.2 below. For updates subsequent to the reporting date, see section 5.2 below. 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 motions for certification of class action suits to which the Group has exposure beyond the aforesaid (since the claims do not state an exact amount), see sections 5.2 and 5.4 below.

A detailed description of the Group's contingent liabilities appears in Note 17 to the Annual Financial Statements. Following is a description of the Group's contingent liabilities as at September 30, 2012, classified into groups with similar characteristics.

5. Contingent Liabilities (Contd.)

5.1. Employee claims

The financial statements include provisions of NIS 73 million for employee damages.

As at September 30, 2012, the additional exposure (beyond the provisions included in these financial statements) resulting from employee claims amounts to NIS 227 million and relates mainly to legal claims filed by groups of employees or individual claims, which can possibly have an across-the-board effect on the Company.

5.2. Customer claims

The financial statements include provisions of NIS 25 million for customer claims,

As at September 30, 2012, the additional exposure resulting from customer claims amounts to NIS 5.9 billion (beyond the provisions included in these financial statements). An amount of NIS 369 million is for a legal claim filed against the Company, Pelephone and other communication companies unrelated to the Group, without details of the amount claimed from each defendant.

In addition, there are claims amounting to NIS 1.3 billion, the success of which cannot yet be assessed at this stage.

In addition, there are other claims for which the Group has additional exposure beyond the aforesaid, which cannot be quantified, as the exact amount of the claim is not stated in the claims.

Subsequent to the reporting date, customer claims with exposure of NIS 650 million came to an end.

5.3. Supplier and communication provider claims

The financial statements include provisions of NIS 12 million for supplier and communication provider claims.

As at September 30, 2012, the amount of the additional exposure for supplier and communication supplier claims amounts to NIS 1 billion (beyond the provisions included in these financial statements).

5.4. Claims for punitive damages

The financial statements include provisions of NIS 1 million for punitive damages.

As at September 30, 2012, the additional exposure for punitive damages amounts to NIS 4 billion (beyond the provisions included in these financial statements). This amount does not include claims for which the insurance coverage is not disputed. In addition, there are other claims for which the Group has additional exposure beyond the aforesaid, which cannot be quantified, as the exact amount of the claim is not stated in the claim.

5.5. Claims by enterprises and companies

The financial statements include provisions of NIS 11 million for claims by enterprises and companies.

As at September 30, 2012, the additional exposure for legal claims filed by enterprises and companies amounted to NIS 59 million (beyond the provisions included in these financial statements).

5. Contingent Liabilities (Contd.)

5.6. Claims by the State and authorities

The financial statements include provisions of NIS 30 million for legal claims filed by the State and authorities.

As at September 30, 2012, the additional exposure for legal claims filed by the State and authorities amounted to NIS 184 million (beyond the provisions included in these financial statements).

Further to Note 17.6 to the Annual Financial Statements regarding the legal claim filed in December 2000 by the government to the district court for royalties of NIS 260 million, and the appeal filed by Pelephone at the Supreme Court regarding the amount of the debt, in August 2012, the appeal was dismissed.

5.7. Contingent claims referring to the associate DBS Satellite Services (1998) Ltd. ("DBS")

As at September 30, 2012, the exposure for claims against DBS for various matters amounted to NIS 196 million (before linkage and interest)

6. Equity and Share-based Payments

6.1 Below are details of the Company's equity:

Registered			Issued and paid up		
September 30, 2012	September 30, 2011	December 31, 2011	September 30, 2012	September 30, 2011	December 31, 2011
(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	**2,724,581,334**	2,708,724,551	2,713,627,744

6.2 Following the exercise of options by employees in accordance with the options plans set out in Note 26 to the Annual Financial Statements, in the nine month period ended September 30, 2012, the Company issued 10,953,590 ordinary shares of NIS 1 par value each.

6.3 Further to Note 20.2.2 of the Annual Financial Statements regarding a distribution not in compliance with the earnings test, the balance of the dividend payable as at September 30, 2012 for the special distribution is presented as follows:

	September 30, 2012	
	Dividend payable, undiscounted	Presented in the statement of financial position *
	NIS million	NIS million
Current liabilities	**1,000**	**981**
Non-current liabilities	**500**	**473**
	1,500	**1,454**

* Dividend payable for the special distribution presented in the statement of financial position at present value as at March 31, 2011 (the date of court approval for the distribution), plus financing expenses accumulated up to September 30, 2012

6. Equity and Share-based Payments (Contd.)

Further to Note 20.2.2 to the Annual Financial Statements as at December 31, 2011, regarding applications to the Tel Aviv District Court concerning the objection to the distribution of the dividend which is not in compliance with the earnings test, on March 29, 2012 and April 4, 2012, the same parties filed two new objections at the Tel Aviv District Court (Economic Division).

On May 14, 2012, the Court decided to dismiss these objections and further to the Company's request, on May 22, 2012, the court clarified that in accordance with its decision of May 14, 2012, the Company is not required to apply to the court for each payment of the remaining lots of the special dividend approved by the court on May 31, 2011. Therefore, the Company intends to continue payments of the distribution as in the past, while assessing its compliance with the solvency test prior to payment, without having to apply to the court for the assessment.

It is noted that in August and September 2012, the same parties filed various applications at the Tel Aviv District Court (Economic Division) expressing a possible objection to the fourth lot of the special distribution, however, in a hearing of the case on September 24, 2012, the parties announced that they do not insist on the procedure (while maintaining their claims and rights) and the fourth lot was distributed on the date specified in section 6.5 below.

6.4 On May 21, 2012, a cash dividend of NIS 1,074 million was paid to the Company's shareholders (after approval of the general meeting of the Company's shareholders), representing NIS 0.3951788 per share and 39.51788% of the issued and paid up share capital of the Company. In addition, on May 21, 2012, the third lot of the special distribution of NIS 500 million was paid (described in Note 20.2.2 to the Annual Financial Statements and section 6.3 above) representing NIS 0.1839752 per share and 18.39752% of the issued and paid up capital of the Company.

6.5 On September 6, 2012, the general meeting of the Company's shareholders approved the recommendation of the Company's Board of Directors of August 1, 2012 to distribute a cash dividend to the Company's shareholders in the amount of NIS 997 billion, representing NIS 0.3659618 per share and 36.59618%% of the Company’s issued and paid up capital on the record date (September 23, 2012). The dividend was paid on October 10, 2012. Alongside this distribution, the fourth lot of the special distribution (described in Note 20.2.2 to the Annual Financial Statements and section 6.3 above) of NIS 500 million was paid, representing NIS 0.1835315 per share and 18.35315% of the Company's issued and paid up capital at the record date (September 23, 2012).

7. Transactions with interested and related parties

7.1 Further to Note 29.5.2(A)(3) to the Annual Financial Statements regarding the Board of Directors' approval of the amendment to the agreement between DBS and Eurocom Digital Communications Ltd. and ADB, on March 27, 2012, the general meeting of the Company's shareholders approved the amendment to the agreement.

7.2 Further to Note 29.5.2(A)(4) to the Annual Financial Statements at December 31, 2011, regarding the Board of Directors' approval of the engagement of DBS in a transaction to acquire converters from Eurocom Digital Communications Ltd. and ADB and regarding credit from suppliers, on April 24, 2012, the general meeting of the Company's shareholders approved the amendment to the agreement.

7.3 On May 8, 2012, the Company's Board of Directors resolved (after the approval of the audit committee) that the Company would vote in favor of DBS's transaction to raise capital of up to NIS 450 million at the general meeting of the shareholders of DBS. For further information about the capital raised by DBS, see Note 4.2.4 above.

7.4 On July 25, 2012, the general meeting of the Company's shareholders approved the Company's vote at the general meeting of the shareholders of DBS in favor of the amendment to the agreement between Eurocom Digital Communications Ltd. and ADB, in accordance with the approval of the general meeting on August 4, 2011 ("the Original Agreement") as set out in section 29.5.2.A. (2) of the Annual Financial Statements, which amended the agreement regarding some of the converters (42% of the original approved quantity) so that the maximum additional total cost for the Original Agreement (due to an increase in the price of hard drives as set out in this report) will be up to USD 1.337 million. In addition, the date of supply was extended to September 30, 2013 for 16% of the original approved quantity.

7.5 On July 25, 2012, the general meeting of the Company's shareholders resolved to vote at the general meeting of shareholders of DBS in favor of DBS's purchase of yesMaxTotal converters from Eurocom and ADB in accordance with an existing framework agreement, for a total cost of USD 20.7 million, for the period up to March 31, 2014. The general meeting also resolved that insofar as the state of the global market for hard drives necessitates additional cost, the additional cost for this acquisition will be up to USD 3.245 million, and will serve only as a supplement following the increase in the price of hard drives. The general meeting also approved USD supplier credit from Eurocom Digital Communications for an additional 60 days ("the Additional Credit Period"), over and above the period defined in the framework agreement, for the purchase of converters as set out above. The payment terms set out in the framework agreement are EOM + 35 days and DBS will pay interest at a rate of 1% (6% in nominal annual terms) for the Additional Credit Period. The scope of the credit is estimated at an average of NIS 15 million and payment of the annual interest is estimated at NIS 900 thousand.

7.6 For further information about the approval of the general meeting of the Company's shareholders on September 6, 2012 regarding the new debt arrangement with DBS, see Note 4.2.6 above.

7.7 Subsequent to the reporting date, on October 11, 2012, the general meeting of the Company's shareholders approved an extension, expansion and amendment of Pelephone's agreement with Eurocom Cellular Communications Ltd. ("Eurocom Communications"), which was approved at the general meeting of shareholders on June 10, 2010. The amendment refers to regulation of the purchase and supply of Nokia terminal equipment, spare parts and accessories to Pelephone. In the amendment, the agreement will be expanded to include products manufactured by the Chinese electronics manufacturer ZTE, which is expected to market cellular terminal equipment in Israel through its new official representative, Eurocom Communications. In accordance with the agreement, the volume of annual purchases will not deviate from an aggregate amount of NIS 300 million (before VAT) per year for Nokia and ZTE products together. It is noted that Pelephone has no obligation to purchase from Eurocom Communications. The agreement will be extended by three years until December 31, 2015.

8. Revenues

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Domestic fixed-line communication					
Fixed-line telephony	**1,661**	1,777	**537**	593	2,320
Internet - infrastructure	**872**	810	**291**	276	1,092
Transmission and data communication	**589**	563	**196**	192	749
Other services	**173**	175	**53**	55	215
	3,295	3,325	**1,077**	1,116	4,376
Cellular telephony					
Cellular services and terminal equipment	**1,554**	1,831	**524**	580	2,346
Value added services	**887**	890	**268**	310	1,201
Sale of terminal equipment	**931**	1,521	**231**	507	1,911
	3,372	4,242	**1,023**	1,397	5,458
International communications, internet and NEP services	**963**	967	**325**	338	1,289
Other	**199**	189	**69**	66	250
	7,829	8,723	**2,494**	2,917	11,373

9. Operating and general expenses

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011*	2012	2011*	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Terminal equipment and materials	**957**	1,327	**285**	454	1,693
Interconnectivity and payments to domestic and international operators	**675**	688	**229**	242	910
Maintenance of buildings and sites	**489**	480	**169**	160	641
General and marketing expenses - see also Note 13.1	**430**	491	**156**	177	655
Services and maintenance by sub-contractors	**112**	131	**35**	42	170
Vehicle maintenance expenses	**121**	112	**44**	37	142
Content services expenses	**69**	95	**21**	30	123
Royalties and collection fees	**123**	121	**24**	40	160
	2,976	3,445	**963**	1,182	4,494

* Certain expenses were reclassified to present all expenses according to their nature.

10. Financial instruments

10.1. Hedging transactions

In the second quarter of 2012, the Company entered into four forward contracts amounting to NIS 370 million to reduce exposure to changes in the CPI for CPI-linked debentures issued by the Company. These contracts hedge specific cash flows of some of the CPI-linked debentures and are recognized as cash-flow hedge accounting. The contracts expire on June 2, 2013 and comply with the repayment schedule of the relevant debentures. In the nine month period ended September 30, 2012, the Company recognized a profit of NIS 2 million for these contracts, recognized in other comprehensive income. The fair value of the forward contracts is based on available market information.

It is noted that subsequent to the date of the financial statements, the Company entered into additional forward contracts amounting to NIS 357 million to reduce its exposure to CPI changes for its CPI-linked debentures. The contracts will expire on June 1, 2014.

As at the reporting date, the Company has additional forward contracts amounting to NIS 250 million (to reduce its exposure to CPI changes for CPI-linked debentures) for which the Company does not apply hedge accounting. These contracts are recognized as current assets at their fair value of NIS 2 million. In addition, at the reporting date, the Company has forward contracts to reduce exposure to changes in the copper price for 4,686 tons, for which the Company does not apply hedge accounting and their fair value at the reporting date totaled a negative amount of NIS 2.9 million.

10.2. Debt factoring

Pelephone factors receivables arising from the sale of terminal equipment in payment transactions paid using credit cards. Factoring transactions are made on a non-recourse basis. Trade receivables are derecognized in accordance with the criteria set out in IAS 39, Financial Instruments: Recognition and Measurement In the nine months ended September 30, 2012, Pelephone factored NIS 130 million (par value).

11. Segment Reporting

11.1. Operating segments

	For the nine month period ended September 30, 2012 (Unaudited):						
	Domestic fixed-line communication	Cellular	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	3,289	3,370	962	1,228	190	(1,228)	7,811
Inter-segment revenues	220	71	39	-	30	(342)	18
Total revenues	3,509	3,441	1,001	1,228	220	(1,570)	7,829
Depreciation and amortization	541	402	103	184	18	(173)	1,075
Segment results – operating profit (loss)	1,395	725	157	180	(3)	(191)	2,263
Financing expenses	455	79	14	470	5	(517)	506
Financing income	(267)	(111)	(8)	(2)	-	(30)	(418)
Total financing expenses (income), net	188	(32)	6	468	5	(547)	88
Segment profit (loss) after financing expenses, net	1,207	757	151	(288)	(8)	356	2,175
Share in losses (profits) of equity-accounted investees	-	-	(1)	-	-	234	233
Segment profit (loss) before income tax	1,207	757	152	(288)	(8)	122	1,942
Income tax	350	193	37	1	(1)	17	597
Segment results – net profit (loss)	857	564	115	(289)	(7)	105	1,345
Additional information:							
Segment assets	8,684	5,092	1,344	1,369	380	(2,820)	14,049

11. Segment Reporting (contd.)

11.1 Operating segments (Contd.)

	For the nine month period ended September 30, 2011 (Unaudited):						
	Domestic fixed-line communication	Cellular	International communications and internet services	Multi-channel television	Other	Adjustments	Consolidated
	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from external sources	3,322	4,240	966	1,215	185	(1,215)	8,713
Inter-segment revenues	212	69	46	-	26	(343)	10
Total revenues	3,534	4,309	1,012	1,215	211	(1,558)	8,723
Depreciation and amortization	513	421	79	214	17	(204)	1,040
Segment results – operating profit	1,274	1,098	182	190	4	(204)	2,544
Financing expenses	381	52	8	438	4	(438)	445
Financing income	(194)	(75)	(7)	(11)	-	10	(277)
Total financing expenses (income), net	187	(23)	1	427	4	(428)	168
Segment profit (loss) after financing expenses, net	1,087	1,121	181	(237)	-	224	2,376
Share in losses of equity-accounted investees	-	-	(1)	-	-	204	203
Segment profit (loss) before income tax	1,087	1,121	182	(237)	-	20	2,173
Income tax	323	269	44	1	1	(5)	633
Segment results – net profit (loss)	764	852	138	(238)	(1)	25	1,540

Additional information:

Segment assets	9,855	5,397	1,168	1,256	308	(1,708)	16,276

11. Segment Reporting (contd.)

11.1 Operating segments (Contd.)

	For the three month period ended September 30, 2012 (Unaudited)						
	Domestic fixed-line communication	Cellular	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	1,075	1,023	324	403	63	(403)	2,485
Inter-segment revenues	74	26	15	-	13	(119)	9
Total revenues	1,149	1,049	339	403	76	(522)	2,494
Depreciation and amortization	185	130	34	64	7	(61)	359
Segment results – operating profit (loss)	419	199	55	54	(2)	(58)	667
Financing expenses	161	30	5	173	3	(191)	181
Financing income	(98)	(40)	(2)	(1)	-	15	(126)
Total financing expenses (income), net	63	(10)	3	172	3	(176)	55
Segment profit (loss) after financing expenses, net	356	209	52	(118)	(5)	118	612
Share in losses (profits) of equity-accounted investees	-	-	(1)	-	-	93	92
Segment profit (loss) before income tax	356	209	53	(118)	(5)	25	520
Income tax	110	55	13	1	(1)	-	178
Segment results – net profit (loss)	246	154	40	(119)	(4)	25	342

11. Segment Reporting (contd.)

11.1 Operating segments (Contd.)

	For the three month period ended September 30, 2011 (Unaudited)						
	Domestic fixed-line communication	Cellular	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	1,114	1,396	338	405	66	(405)	2,914
Inter-segment revenues	72	25	13	-	8	(115)	3
Total revenues	1,186	1,421	351	405	74	(520)	2,917
Depreciation and amortization	180	139	28	74	6	(70)	357
Segment results – operating profit (loss)	546	342	61	63	(1)	(67)	944
Financing expenses	166	30	3	139	2	(154)	186
Financing income	(78)	(34)	(2)	(1)	-	15	(100)
Total financing expenses (income), net	88	(4)	1	138	2	(139)	86
Segment profit (loss) after financing expenses, net	458	346	60	(75)	(3)	72	858
Share in losses of equity-accounted investees	-	-	(1)	-	-	67	66
Segment profit (loss) before income tax	458	346	61	(75)	(3)	5	792
Income tax	147	83	15	1	-	(3)	243
Segment results – net profit (loss)	311	263	46	(76)	(3)	8	549

11. Segment Reporting (contd.)

11.1 Operating segments (Contd.)

	For the year ended December 31, 2011 (Audited)						
	Domestic fixed-line communication	Cellular	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	4,371	5,454	1,288	1,619	236	(1,619)	11,349
Inter-segment revenues	277	94	66	-	41	(454)	24
Total revenues	4,648	5,548	1,354	1,619	277	(2,073)	11,373
Depreciation and amortization	688	561	109	276	21	(260)	1,395
Segment results – operating profit	1,658	1,360	241	295	3	(315)	3,242
Financing expenses	531	67	11	547	5	(562)	599
Financing income	(291)	(105)	(9)	(23)	-	39	(389)
Total financing expenses (income), net	240	(38)	2	524	5	(523)	210
Segment profit (loss) after financing expenses, net	1,418	1,398	239	(229)	(2)	208	3,032
Share in earnings (losses) of equity accounted investees	-	-	1	-	-	(217)	(216)
Segment profit (loss) before income tax	1,418	1,398	240	(229)	(2)	(9)	2,816
Income tax	353	342	58	1	4	(3)	755
Segment results – net profit (loss)	1,065	1,056	182	(230)	(6)	(6)	2,061
Additional information:							
Segment assets	9,202	5,404	1,260	1,282	314	(2,373)	15,089

11. Segment Reporting (contd.)

11.2. Adjustments for segment reporting of revenues and profit or loss

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues					
Revenues from reporting segments	**9,179**	10,070	**2,940**	3,363	13,169
Revenues from other segments	**220**	211	**76**	74	277
Cancellation of revenues from inter-segment sales except for revenues from sales to an associate reporting as a segment	**(342)**	(343)	**(119)**	(115)	(454)
Cancellation of revenues for a segment classified as an associate	**(1,228)**	(1,215)	**(403)**	(405)	(1,619)
Consolidated revenues in the period	**7,829**	8,723	**2,494**	2,917	11,373

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Profit or loss					
Operating profit for reporting segments	**2,457**	2,744	**727**	1,012	3,554
Cancellation of expenses for a segment classified as an associate	**(180)**	(190)	**(54)**	(63)	(295)
Other financing income (expenses), net	**(88)**	(168)	**(55)**	(86)	(210)
Share in losses of equity-accounted investees	**(233)**	(203)	**(92)**	(66)	(216)
Profit (loss) for operations classified in other categories	**(3)**	4	**(2)**	(1)	3
Other adjustments	**(11)**	(14)	**(4)**	(4)	(20)
Consolidated profit for the period before income tax	**1,942**	2,173	**520**	792	2,816

12. Condensed Financial Statements of Pelephone Communications Ltd. and Bezeq International Ltd.

12.1. Pelephone Communications Ltd.

Data from the Statement of financial position

	September 30, 2012	September 30, 2011	December 31, 2011
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Current assets	**2,395**	2,244	2,280
Non-current assets	**2,697**	3,153	3,124
Total assets	**5,092**	5,397	5,404
Current liabilities	**1,326**	1,290	1,263
Long-term liabilities	**928**	572	992
Total liabilities	**2,254**	1,862	2,255
Equity	**2,838**	3,535	3,149
Total liabilities and equity	**5,092**	5,397	5,404

Data from the Statement of income

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues from services	**1,620**	1,898	**548**	604	2,436
Revenues from value added services	**887**	890	**268**	310	1,201
Revenues from sales of terminal equipment	**934**	1,521	**233**	507	1,911
Total revenues from services and sales	**3,441**	4,309	**1,049**	1,421	5,548
Cost of services and sales	**2,299**	2,755	**716**	926	3,587
Gross profit	**1,142**	1,554	**333**	495	1,961
Selling and marketing expenses	**332**	367	**105**	125	480
General and administrative expenses	**85**	89	**29**	28	121
	417	456	**134**	153	601
Operating profit	**725**	1,098	**199**	342	1,360
Financing expenses	**79**	52	**30**	30	67
Financing income	**(111)**	(75)	**(40)**	(34)	(105)
Financing income, net	**(32)**	(23)	**(10)**	(4)	(38)
Profit before income tax	**757**	1,121	**209**	346	1,398
Income tax	**193**	269	**55**	83	342
Profit for the period	**564**	852	154	263	1,056

12. Condensed Financial Statements of Pelephone Communications Ltd. and Bezeq International Ltd. (Contd.)

12.2. Bezeq International Ltd.

Data from the Statement of financial position

	September 30, 2012 (Unaudited) NIS million	September 30, 2011 (Unaudited) NIS million	December 31, 2011 (Audited) NIS million
Current assets	**556**	459	500
Non-current assets	**796**	717	768
Total assets	**1,352**	1,176	1,268
Current liabilities	**362**	279	292
Long-term liabilities	**209**	20	147
Total liabilities	**571**	299	439
Equity	**781**	877	829
Total liabilities and equity	**1,352**	1,176	1,268

Data from the Statement of income

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012 (Unaudited) NIS million	2011 (Unaudited) NIS million	2012 (Unaudited) NIS million	2011 (Unaudited) NIS million	2011 (Audited) NIS million
Revenues from services	**1,001**	1,012	**339**	351	1,354
Operating expenses	**596**	595	**199**	209	788
Gross profit	**405**	417	**140**	142	566
Selling, marketing and development expenses	**157**	151	**54**	51	209
General and administrative and other expenses	**91**	84	**31**	30	116
	248	235	**85**	81	325
Operating profit	**157**	182	**55**	61	241
Financing expenses	**14**	8	**5**	3	11
Financing income	**(8)**	(7)	**(2)**	(2)	(9)
Financing expenses (income), net	**6**	1	**3**	1	2
Share in the earnings of equity-accounted associates	**1**	1	**1**	1	1
Profit before income tax	**152**	182	**53**	61	240
Income tax	**37**	44	**13**	15	58
Profit for the period	**115**	138	**40**	46	182

13. Material Events during the Reporting Period and Subsequent Events

13.1. On April 2, 2012, the settlement between the Company and the Ministry of Communications regarding the claim of government authorities to pay frequency fees in Judea, Samaria and Gaza according to which the Company will pay the plaintiffs NIS 26 million (plus linkage to the CPI of February 11, 2010), was given the validity of a ruling. Following the settlement, in the first quarter of 2012, the Company reduced liabilities for frequency fees and decreased operating and general expenses by NIS 37 million and financing expenses by NIS 13 million.

13.2. On July 2, 2012, the Board of Directors of the Company resolved to suspend the customer relations management (CRM) project, while continuing to use suitable models that have already been developed. Therefore, in the second quarter of the reporting period, the Company recognized a loss of NIS 54 million under other operating expenses.

13.3. Further to Note 18.3 to the Annual Financial Statements, on July 24, 2012, an amendment to the Royalties Regulations relevant to the Company, Pelephone and DBS was issued, so that the rate of royalties for 2012 will be reduced to an average of 1.75% for the Company and DBS, 1.3% for Pelephone (the rate of royalties for Bezeq International is 1%), and as from 2013, 0% for all the companies.

13.4. On August 29, 2012, the Board of Directors resolved to approve extension of the optical fiber deployment so that the fibers will be as close as possible to the customer's premises (FTTH/FTTB), as a basis for a future provision of more advanced and broader-band communication than those currently provided. The work involves detailed planning of the project, pilots, and the purchase of optical fibers and advanced optical technologies. The project will be modular. The Company will regularly assess the scope and route of the project and the need for adjustments, inter alia, in view of relevant maturing technologies and development of customer needs.

13.5. In October 2012, the Company completed debt financing amounting to NIS 500 million, with an average duration of 4.3 years, bearing fixed shekel interest. The negative pledge created by the Company in favor of the lending bank applies, which has the same terms as the terms of the negative pledge provided to the banks, and subject to the exceptions set out therein, as described in Note 13.2.1 to the Annual Financial Statements. In addition, the same terms were set for calling for immediate repayment of the credit and for the financial covenants described in Note 13.2.2 (B) and (C) to the Annual Financial Statements.

13.6. On November 7, 2012, the Board of Directors of the Company approved an additional budget of NIS 16 million for the early retirement of 19 employees in 2012. This is in addition to an expense of NIS 12 million, which was recognized for the adjustment of the provision in the reporting period.

DBS Satellite Services (1998) Ltd.
Condensed Interim Financial Statements
September 30, 2012

Contents	Page

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Review Report to the Shareholders of D.B.S. Satellite Services (1998) Ltd.

Introduction

We have reviewed the accompanying financial information of DBS Satellite Services (1998) Ltd (hereinafter- "the Company") comprising the condensed interim statement of financial position as of September 30, 2012 and the condensed interim statements of operations, comprehensive income, changes in equity and cash flows for the nine and three month periods then ended. The Board of Directors and Management are responsible for the preparation and presentation of these interim financial information in accordance with IAS 34 "*Interim Financial Reporting"*, and are also responsible for the preparation of financial information for these interim period in accordance with Section D of the Securities Regulations (Periodic and Immediate Reports), 1970. Our responsibility is to express a conclusion on the financial information for these interim periods based on our review.

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, nothing has come to our attention that causes us to believe that the abovementioned interim financial information is not prepared, in all material respects, in accordance with IAS 34.

In addition to that mentioned in the previous paragraph, based on our review, nothing has come to our attention that causes us to believe that the abovementioned 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 above conclusion, we draw attention to Note 4 regarding the financial condition of the Company.

Somekh Chaikin
Certified Public Accountants (Isr.)

October 30, 2012

Condensed Interim Statements of Financial Position as at

	September 30, 2012	September 30, 2011	December 31, 2011
	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands
Assets			
Cash and cash equivalents	-	-	13,325
Trade receivables	**166,961**	163,548	159,596
Other receivables	**3,416**	11,919	8,020
Total current assets	**170,377**	175,467	180,941
Broadcasting rights, net of rights exercised	**362,793**	317,341	330,572
Property, plant and equipment, net	**736,498**	663,493	675,954
Intangible assets, net	**99,530**	99,610	94,227
Total non-current assets	**1,198,821**	1,080,444	1,100,753
Total assets	**1,369,198**	1,255,911	1,281,694

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

Condensed Interim Statements of Financial Position as at

	September 30, 2012	September 30, 2011	December 31, 2011
	(Unaudited)	(Unaudited)	(Audited)
	NIS thousands	NIS thousands	NIS thousands
Liabilities			
Borrowings from banks	**84,097**	75,918	85,998
Current maturities for debentures	**90,611**	57,605	57,494
Trade payables and service providers	**394,316**	394,430	409,298
Other payables	**193,793**	166,763*	177,201*
Provisions	**35,906**	88,019*	40,647
Total current liabilities	**798,723**	782,735	770,638
Debentures	**1,458,222**	1,122,953	1,120,806
Bank loans	**-**	365,819	337,679
Loans from shareholders	**3,008,207**	2,598,608	2,677,916
Long-term trade payables	**37,324**	37,440	18,766
Employee benefits	**6,182**	6,570	6,171
Total non-current liabilities	**4,509,935**	4,131,390	4,161,338
Total liabilities	**5,308,658**	4,914,125	4,931,976
Capital deficit			
Share capital	**29**	29	29
Share premium	**85,557**	85,557	85,557
Options	**48,219**	48,219	48,219
Capital reserves	**1,537,271**	1,537,271	1,537,271
Capital reserve for share-based payments	**10,280**	10,278	10,280
Accumulated deficit	**(5,620,816)**	(5,339,568)	(5,331,638)
Total capital deficit	**(3,939,460)**	(3,658,214)	(3,650,282)
Total liabilities and equity	**1,369,198**	1,255,911	1,281,694

David Efrati (Authorized to sign as chairman of the board) (See Note 8)	**Ron Eilon** CEO	**Mickey Naiman** CFO

Date of approval of the financial statements: October 30, 2012

* Reclassified

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

Condensed Interim Income Statements

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues	**1,228,156**	1,214,978	**402,720**	405,468	1,618,809
Cost of revenues	**800,632**	808,676	**272,641**	267,780	1,028,168
Gross profit	**427,524**	406,302	**130,079**	137,688	590,641
Selling and marketing expenses	**135,152**	111,968	**40,060**	37,171	152,737
General and administrative expenses	**112,289**	104,287	**36,029**	37,153	143,036
Operating profit	**180,083**	190,047	**53,990**	63,364	294,868
Financing expenses	**139,240**	139,592	**52,988**	42,941	168,991
Financing income	**(1,587)**	(10,927)	**(740)**	(474)	(23,163)
Financing expenses for shareholder loans	**330,291**	298,221	**119,550**	96,242	377,529
Financing expenses, net	**467,944**	426,886	**171,798**	138,709	523,357
Loss before income tax	**(287,861)**	(236,839)	**(117,808)**	(75,345)	(228,489)
Income tax	**1,317**	788	**864**	540	1,128
Loss for the period	**(289,178)**	(237,627)	**(118,672)**	(75,885)	(229,617)
Basic and diluted loss per share (NIS)	**9,673**	7,948	**3,969**	2,538	7,681

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

Condensed Interim Statements of Comprehensive Income

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Loss for the period	**(289,178)**	(237,627)	**(118,672)**	(75,885)	(229,617)
Other items of comprehensive income:					
Actuarial profit (loss) from a defined benefit plan	**-**	-		-	(80)
Other comprehensive profit (loss) for the period	**-**	-		-	(80)
Total comprehensive loss for the period	**(289,178)**	(237,627)	**(118,672)**	(75,885)	(229,697)

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

Condensed Interim Statements of Changes in Equity

	Share capital	Share premium	Option warrants	Capital reserve	Capital reserve for share-based payments	Accrued deficit	Total
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
For the nine month period ended September 30, 2012 (unaudited)							
Balance as at January 1, 2012 (audited)	**29**	**85,557**	**48,219**	**1,537,271**	**10,280**	**(5,331,638)**	**(3,650,282)**
Total comprehensive loss for the period							
Loss for the period	**-**	**-**	**-**	**-**	**-**	**(289,178)**	**(289,178)**
Other comprehensive loss for the period	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Total comprehensive loss for the period (unaudited)	**-**	**-**	**-**	**-**	**-**	**(289,178)**	**(289,178)**
Balance as at September 30, 2012 (unaudited)	**29**	**85,557**	**48,219**	**1,537,271**	**10,280**	**(5,620,816)**	**(3,939,460)**
For the nine month period ended September 30, 2011 (unaudited)							
Balance as at January 1, 2011 (audited)	29	85,557	48,219	1,537,271	9,391	(5,101,941)	(3,421,474)
Total comprehensive loss for the period							
Loss for the period	-	-	-	-	-	(237,627)	(237,627)
Other comprehensive loss for the period	-	-	-	-	-	-	-
Total other comprehensive loss for the period	-	-	-	-	-	(5,339,568)	(3,659,101)
Transactions with owners recognized directly in equity							
Share-based payments	-	-	-	-	887	-	887
Balance as at September 30, 2011 (unaudited)	29	85,557	48,219	1,537,271	9,990	(5,339,568)	(3,658,214)

Condensed Interim Statements of Changes in Equity (Contd.)

	Share capital	Share premium	Option warrants	Capital reserve	Capital reserve for share-based payments	Accrued deficit	Total
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
For the three month period ended September 30, 2012 (unaudited)							
Balance as at July 1, 2012 (audited)	**29**	**85,557**	**48,219**	**1,537,271**	**10,280**	**(5,502,144)**	**(3,820,788)**
Total comprehensive income for the period							
Loss for the period	**-**	**-**	**-**	**-**	**-**	**(118,672)**	**(118,672)**
Other comprehensive loss for the period	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Total comprehensive loss for the period	**-**	**-**	**-**	**-**	**-**	**(118,672)**	**(118,672)**
Balance as at September 30, 2012 (unaudited)	**29**	**85,557**	**48,219**	**1,537,271**	**10,280**	**(5,620,816)**	**(3,939,460)**
For the three month period ended September 30, 2011 (unaudited)							
Balance as at July 1, 2011 (audited)	29	85,557	48,219	1,537,271	9,990	(5,263,683)	(3,582,617)
Total comprehensive loss for the period							
Loss for the period	-	-	-	-	-	(75,885)	(75,885)
Other comprehensive loss for the period	-	-	-	-	-	-	-
Total other comprehensive loss for the period	29	85,557	48,219	1,537,271	9,990	(5,339,568)	(3,658,502)
Transactions with owners recognized directly in equity							
Share-based payments	-	-	-	-	288	-	288
Balance as at September 30, 2011 (unaudited)	29	85,557	48,219	1,537,271	10,278	(5,339,568)	(3,658,214)

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

Condensed Interim Statements of Changes in Equity (Contd.)

	Share capital	Share premium	Option warrants	Capital reserve	Capital reserve for share-based payments	Accrued deficit	Total
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
For the year ended December 31, 2011 (audited)							
Balance as at January 1, 2011 (audited)	29	85,557	48,219	1,537,271	9,931	(5,101,491)	(3,421,474)
Total comprehensive loss for the year							
Loss for the year	-	-	-	-	-	(229,617)	(229,617)
Other comprehensive loss for the year	-	-	-	-	-	(80)	(80)
Total comprehensive loss for the year						(229,697)	(229,697)
Transactions with owners recognized directly in equity							
Share-based payments	-	-	-	-	889	-	889
Balance as at December 31, 2011 (audited)	29	85,557	48,219	1,537,271	10,280	(5,331,638)	(3,650,282)

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

Condensed Interim Statements of Cash Flow

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows from operating activities					
Loss for the period	**(289,178)**	(237,627)	**(118,672)**	(75,885)	(229,617)
Adjustments					
Depreciation and amortization	**184,076**	213,798	**64,432**	74,074	276,393
Financing expenses, net	**455,478**	417,319	**169,275**	138,718	519,716
Profit (loss) from sale of property, plant and equipment	**441**	(156)	**(25)**	(91)	(515)
Share-based payments	**-**	887	**-**	288	889
Income tax expenses	**1,317**	788	**864**	540	1,128
Change in trade receivables	**(7,365)**	5,299	**(4,888)**	(5,257)	9,251
Change in other accounts receivable	**4,604**	(769)	**2,986**	(1,306)	3,130
Change in trade payables and service providers	**(47,715)**	8,002	**(62,752)**	(868)	32,457
Change in other payables and provisions	**30,410**	565	**41,228**	8,298	(71,868)
Increase in broadcasting rights, net of rights exercised	**(32,221)**	(12,851)	**(9,046)**	(3,563)	(26,082)
Change in employee benefits	**11**	(126)	**(29)**	(207)	(605)
	589,036	632,756	**204,052**	210,626	743,894
Income tax paid	**(1,317)**	(788)	**(864)**	(540)	(1,128)
Net cash from operating activities	**298,541**	394,341	**82,509**	134,201	513,149
Cash flows from investment activities					
Proceeds from the sale of property, plant and equipment	**224**	354	**52**	156	747
Acquisition of property, plant and equipment	**(179,241)**	(156,638)	**(75,056)**	(51,634)	(207,741)
Payments for software licenses	**(32,955)**	(22,931)*	**(11,515)**	*(11,941)	(32,181)
Payments for subscriber acquisition	**-**	*(23,278)	**-**	*(3,761)	(24,414)
Net cash used in investment activities	**(211,972)**	(202,493)	**(86,519)**	(67,180)	(263,589)

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

* Reclassified

Condensed Interim Statements of Cash Flow (Contd.)

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows from financing activities					
Repayment of bank loans	**(423,235)**	(84,851)	**(399,856)**	-	(97,277)
Repayment of debenture principal	**(58,211)**	(57,271)	**(58,211)**	(57,271)	(57,271)
Short-term bank credit, net	**83,655**	(79,660)	**84,097**	6,076	(85,294)
Payment for financing lease obligation	**(972)**	(397)	**(322)**	(397)	(768)
Interest paid	**(96,133)**	(88,221)	**(36,748)**	(35,418)	(114,178)
Issue of debentures, net	**395,002**	118,553	**395,002**		118,553
Net cash used for financing activities	**(99,894)**	(191,847)	**(16,038)**	(87,010)	(236,235)
Increase in cash and cash equivalents	**(13,325)**	-	**20,048**	(19,990)	13,325
Cash and cash equivalents at the beginning of the period	**13,325**	-		19,990	-
Cash and cash equivalents at the end of the period	**-**	-	**20,048**	-	13,325

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

NOTE 1 –REPORTING ENTITY

DBS Satellite Services (1998) Ltd. ("the Company") was incorporated in Israel on December 2, 1998. The Company's head offices are located at 6 Hayozma St., Kfar Saba, Israel.
In January 1999, the Company received a license from the Ministry of Communications for satellite television broadcasts ("the License"). The License is valid until January 2017 and may be extended for an additional six years under certain conditions. The Company's operations are subject, inter alia, to the Communications Law (Telecommunications and Broadcasts), 1982 ("the Communications Law") and the regulations and rules promulgated thereunder and to the license terms.

Pursuant to its license, Bezeq The Israel Telecommunication Corporation Limited ("Bezeq"), is required to maintain full structural separation between it and its subsidiaries, and between it and the Company. Additionally, under the licenses of the Company and Bezeq, there are restrictions on the joint marketing of services (service bundles).

In August 2009, the Supreme Court accepted the Antitrust Commissioner's appeal of the ruling of the Antitrust Tribunal approving the merger (as defined in the Antitrust Law, 1988) between the Company and Bezeq by exercising the options held by Bezeq into Company shares, subject to certain conditions, and ruled against the merger.

In October 2012 the Antitrust Authority notified the Company that in its opinion the cooperation between it and Bezeq in the marketing of a joint service bundle constitutes cooperation between (potential) competitors in the competitive arena (as a result of the above-mentioned Supreme Court decision), which can be deemed to be a cartel arrangement (even if it complies with the terms of the broadcasting license) requiring approval pursuant to the Antitrust Law, and that the Commissioner does not intend to grant an exemption from the requirement for approval of such an arrangement.

The Company believes that as a result of the development of competition between the telecommunications groups and the increasing importance of providing comprehensive communications services, if the restrictions on Bezeq's control of the Company and on Bezeq's cooperation with it remain intact, the adverse effect of these restrictions on the Company's results is liable to increase.

NOTE 2 - BASIS OF PREPARATION

A. Statement of compliance with international reporting standards

The condensed interim financial statements have been prepared in accordance with IAS 34, Interim Financial Reporting, and do not contain all of the information required for full annual financial statements. They should be read in conjunction with the financial statements for the year ended December 31, 2011 ("the annual statements"). In addition, these condensed interim financial statements have been prepared in accordance with the provisions of Chapter D of the Securities Regulations (Periodic and Immediate Reports), 1970.

The condensed interim financial statements were approved by the Company's Board of Directors on October 30, 2012.

B. Use of estimates and judgments

The preparation of the condensed financial statements in accordance with IFRS requires management to make judgments, 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 judgment of management when applying the Company's accounting policy and the principal assumptions used in assessments that involve uncertainty are consistent with those applied in the annual financial statements.

NOTE 3 - ACCOUNTING POLICY

A. The main points of the accounting policy will be applied in these condensed interim financial statements in a manner consistent with those applied in the annual financial statements for the year ended December 31, 2011, except as described below:

Recognition of actuarial gains or losses

The Company does not produce an updated actuarial assessment for measuring employee benefits in every interim reporting period unless there are significant changes during the interim period in the principal actuarial assumptions in a defined benefit plan: discount rate, expected return on plan assets, employee leave rate and the rate of future salary increases. As a result, actuarial gains or losses are not recognized in the reporting period.

B. Further to that stated in Note 3 (15) (2) regarding the main points of the accounting policy in the annual financial statements regarding the amendment to IAS 19 "Employee Benefits" ("the amendment"), the Company has reviewed the implications on the financial statements of implementation of the amendment. The Company believes that amendment of the standard will not have a material effect on the financial statements.

NOTE 4 – FINANCIAL POSITION OF THE COMPANY

A. Since the beginning of its operations, the Company has accumulated substantial losses. The Company's losses in 2011 amounted to NIS 230 million and losses in the nine months ended September 30, 2012 amounted to NIS 289 million. As a result of these losses, the Company's capital deficit and working capital deficit as at September 30, 2012 amounted to NIS 3,939 million and NIS 628 million, respectively. See also note 6.

B. 1. As at September 30, 2012, the Company is in compliance with the financial covenants under the financing agreements and the debentures.

2. The Company's management believes that the financial resources at its disposal will be sufficient for the Company's operations for the coming year, based on the cash flow forecast approved by the Company's Board of Directors. If additional resources are required to meet its operational requirements for the coming year, the Company will adapt its operations to preclude the need for additional resources beyond those available to it. In recent years the Company was required to raise external financial resources intended, inter alia, to expand its investments. At the reporting date, a significant increase in its investments will require an expansion of the financial resources at its disposal. In addition, see Note 6 which describes the material events in the balance sheet period.

NOTE 5 – CONTINGENT LIABILITIES

Legal claims

Legal claims have been filed against the Company or various legal proceedings are pending against it (in this section: "legal claims").

In the opinion of the management of the Company, which is based, inter alia, on legal opinions as to the likelihood of success of the legal claims, appropriate provisions have been included in the financial statements where provisions are required to cover the exposure resulting from such legal claims.

NOTE 5 – CONTINGENT LIABILITIES (CONTD.)

As at September 30, 2012, the exposure resulting from the legal claims filed against the Company in respect of various matters amounts to NIS 196,116,000. These amounts and all the amounts of the claims in this note do not include interest and linkage.

Following is a description of the material legal claims against the Company as at September 30, 2012 classified by groups with similar characteristics.

A. Employee claims

During the normal course of business, employees and former employees filed collective and individual claims against the Company. Most of these claims are for alleged non-payment of salary components and delay in salary payment. As at September 30, 2012, these claims amounted to NIS 54,676,000. In the opinion of the management of the Company, which is based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions of NIS 1,530,000, where provisions are required to cover the exposure resulting from such claims.

B. Customer claims

During the normal course of business, the Company's customers filed claims against the Company. These are mainly motions for certification of class actions (and claims by virtue thereof) which are usually allegations of unlawful collection of money and harm to the services provided by the Company. As at September 30 2012, these claims amounted to NIS 141.040,000. In the opinion of the management of the Company, which is based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions of NIS 2,795,000 where provisions are required to cover the exposure resulting from such claims.

C. Supplier and communication provider claims

During the normal course of business, suppliers of goods and/or services to the Company filed various claims against the Company. As at September 30, 2012, these claims amounted to NIS 400,000. In the opinion of the Company's lawyers, financial resources will not be needed to dismiss these claims.

NOTE 6 –EVENTS IN THE BALANCE SHEET PERIOD

A. In May 2012 a debenture was signed by the Company and a number of institutional entities ("the lenders") whereby the lenders would extend to the Company a loan of NIS 392 million ("the debenture"). The proceeds of the funds raised will be used for full repayment of the long-term credit granted to the Company by the banks. The loan was received by the Company in July 2012 after compliance with the conditions precedent set out in the debentures.

The loan granted under the debenture will be used to repay the principal in ten annual unequal installments, where from 2013 – 2017 the payment of the principal will be 8% of the par value of the debentures and in each subsequent year the payment of the principal will be 12% of the par value of the debentures.

The debenture bears annual interest of 6.4% payable in six-monthly installments. The principal and interest of the loan are linked to the CPI. Under the terms of the debenture, if the rating of the loan is downgraded to BBBil or its equivalent (the lower of the two) the annual interest will be increased by 0.5%, and for each additional notch the annual interest will increase by a further 0.25% throughout the period in which the downgraded rating remains in effect.

NOTE 6 –EVENTS IN THE BALANCE SHEET PERIOD (CONTD.)

In addition, the debenture stipulated various events (similar to the events stipulated in Deed of Trust B). The occurrence of these events (sometimes after an extension period) creates a right to demand immediate repayment of the loan, subject to the provisions of the debenture, including a demand for immediate repayment (not initiated by the Company) of another series of debentures issued or which will be issued by the Company and/or of debts owed by the Company to a financial institution subject to the terms set out in the debenture.

Under the provisions of the debenture, the Company must comply with the following two financial covenants every quarter (subject to the cure periods and cure terms determined in the debentures): (A) compliance with the total debt / EBITDA ratio – the ratio between the total debt (debts to the financial institutions listed in the debenture) at the end of the relevant quarter and the EBITDA of the Company in the 12-month period ending at the end of said quarter. The term “EBITDA” is defined – in relation to the period of any calculation – as the Company's total operating profit from ordinary operations (before financing expenses and taxes) plus depreciation and amortization, plus expenses which are included in the investments item of the Company's financial statements as at December 31, 2010 (and whose classification was changed to expenses as a result of accounting policy or directives from an authority) plus provisions and extraordinary non-recurring expenses.

The maximum ratio set out in the debenture for a trial period up to the end of 2013 will be 5, for a review period up to the end of 2015 the ratio will be 4.65, and for a review period up to the end of 2016 the ratio will be 4.3. (B) compliance with the debt / E-C ratio (EBITDA less CAPEX as defined in the agreement) will not exceed the maximum debt / E-C ratio set out in the debenture where until December 31, 2015 the ratio will be 9.5 and from January 1, 2016 the ratio will be 7.8.

The debenture determined certain restrictions regarding the distribution of dividends and repayment of shareholder loans similar to the restrictions applicable to Deed of Trust B. The financial condition ratio is lower (worse) than that applicable to Deed of Trust B.

The debenture is secured by charges similar to those created in favor of the holders of debentures (Series B). The lenders’ collateral will be of first and equal rank (pari passu) to the collateral created by the Company in favor of the banks to secure the bank credit for the collateral of the holders of debentures (Series A), the collateral of the holders of debentures (Series B) and the collateral financing the additional secured entities, if any. According to the debenture the Company may take credit secured by assets which represent collateral for the lenders subject to compliance with the general financial covenant relating to the debt / EBITDA ratio and if a secured series of debentures is issued, subject to submission of a rating report that the loan rating at that time will not be downgraded as a result of the issuance of the additional series.

In the event that Bezeq provides a guarantee in favor of the lenders, and as long as Bezeq's rating does not fall below (ilAA-) or its equivalent in another rating company (the lower of the two), the collateral granted to the lenders will be abolished and a number of provisions relating to the terms governing funding secured by the Company, the financial covenants, certain grounds for immediate repayment and the restrictions on the distribution of dividends and repayment of shareholder loans will be abolished. If such a guarantee is provided (and with certain changes also in the event of a merger between the Company and between Bezeq) the annual interest rate of the loan will be reduced by a further 1% (in other words to 5.4%, but no lower than the yield of Bezeq's debenture 6 after an adjustment for the difference in duration, and in any event no higher than 6.4%). Interest additions for a fall in the loan rating, if any, will also be abolished.

In July 2012 the Company expanded its debenture series (Series B) by issuing additional debentures in the sum of NIS 10 million, the proceeds of which, together with the funds from the debenture loan, were used in full repayment of the long-term bank credit.

NOTE 6 –EVENTS IN THE BALANCE SHEET PERIOD (CONTD.)

In May 2012 S&P Maalot gave the Company's debenture and the expansion of its debenture (Series B) a rating of ilA- in respect of the funds raised in the amount of NIS 450 million par value.
In July 2012 after the conditions precedent determined in the debenture were fulfilled, the Company made full repayment of its long-term bank credit (by means of a loan provided in accordance with the debenture and in consideration of an expansion of the Company's debenture series (Series B)). With this repayment an amendment to the financing agreement ("the agreement amendment" and "the amended financing agreement" was validated. Under the amended financing agreement the amount of the Company's ongoing credit facility was increased to NIS 170 million, but use of this facility was restricted to the Company's total working capital requirements (calculated on the basis of the formula set out in the amended financing agreement which is dependent on the Company's receivables balance, the amount of unexercised broadcasting rights, the depreciated cost of the decoders and the Company's payables balance according to its financial statements). In addition, under the amended financing agreement the undertakings and restrictions imposed on the Company by the financing agreement were either abolished or reduced (including those relating to compliance with the business plan, third-party liabilities, interested-party transactions, purchase of securities in other corporations, public securities offering and mandatory repayment of surplus cash or debenture issues). The provisions of the amendment to the agreement also abolished the collateral created by Bezeq and Eurocom DBS in favor of the banks to secure the Company's bank credit and the undertakings they made to the banks in connection with the Company's bank credit, among them Bezeq's guarantee to the banks.

The new financing agreement abolished the financial covenants which had been valid and which were replaced by the Company's quarterly obligation to comply with two financial covenants which were identical to those set out in the new debenture.

The amended financing agreement also determined that a demand for immediate repayment or the existence of grounds to make a demand for immediate repayment of amounts owed by the Company to debenture holders, other banks or financial institutions constitutes grounds for immediate repayment of the bank credit. According to the amended financing agreement, if the rating of the loan is downgraded by S&P Maalot to ilBBB (or its equivalent by another rating company, the lower of the two) the annual interest paid to the banks for each additional notch will increase by 0.25% on the rating scale throughout the period in which the downgraded rating remains in effect (unless according to the debenture the downgraded rating does not grant any lender additional interest for the loan owing to the Bezeq guarantee in its favor).

For further details of debentures A and B, see Note 14 to the Company's annual financial statements as at December 31, 2011.

B. In September 2012 the agreements to defer some of the payments owed by the Company to Bezeq and Bezeq International were approved by virtue of the previous debt arrangements between the Company and themselves (in amounts of NIS 27 million and NIS 6 million respectively). According to the agreements the payments will be deferred for an 18-month period during which they will bear interest at the rate of prime + 4%.

NOTE 7 – MATERIAL EVENTS SUBSEQUENT TO THE REPORTING DATE

A. In October 2012 S&P Maalot ratified the ilA- rating for the Company and for each of its debenture series (including the debenture described in section 6 above) with a stable outlook for the Company.

B. See Note 1 regarding the announcement from the Antitrust Authority from October 2012.

NOTE 8 – APPOINTMENT OF THE CHAIRMAN OF THE BOARD OF DIRECTORS FOR THE APPROVAL MEETING

At the date of approval of the financial statements, the Company’s Board of Directors does not have an incumbent chairman. Consequently, on October 30, 2012 the Company’s Board of Directors authorized David Efrati, a director in the Company, to serve as chairman of the Board of Directors’ meeting convened to approve the financial statements and to sign the Company’s financial statements as at September 30, 2012.

Bezeq The Israel Telecommunication Corporation Ltd.

Condensed Separate Interim Financial Information as at September 30, 2012 (Unaudited)

bezeq

Contents	Page

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

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

Introduction
We have reviewed the separate interim financial information presented in accordance with Regulation 38D of the Securities Regulations (Periodic and Immediate Reports) -1970 of "Bezeq"- The Israel Telecommunication Corporation Ltd. (hereinafter- "the Company") as of September 30, 2012 and for the nine and three month periods then ended. The separate interim financial information is the responsibility of the Company's Board of Directors and of its Management. Our responsibility is to express a conclusion on the separate interim financial information for these periods based on our review.

We did not review the separate interim financial information from the financial statements of investee companies in which investments amounted to NIS 234 million as of September 30, 2012, and the Company's share in the profit (loss) from these investee companies amounted to NIS 67 million and NIS (1) million for the nine and three month periods then ended, respectively. The financial statements of those companies were reviewed by other auditors, whose review reports thereon were furnished to us, and our conclusion, insofar as it relates to amounts emanating from the financial statements of such companies, is based solely on the said review reports of the other auditors.

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

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

Without qualifying our abovementioned conclusion, we draw attention to lawsuits filed against the Company which cannot yet be assessed or the exposure in respect thereof cannot yet be estimated, as set forth in Note 4

Somekh Chaikin
Certified Public Accountants (Isr.)

November 7, 2012

Condensed Interim Information on Financial Position as at

	September 30, 2012	September 30, 2011	December 31, 2011
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Assets			
Cash and cash equivalents	**205**	1,320	1,096
Investments, including derivatives	**1,013**	2,047*	940
Trade receivables	**777**	758	731
Other receivables	**154**	119	212
Dividend receivable from investees	**484**	-	-
Inventories	**21**	14	13
Loans granted to investees	**328**	465*	546
Assets classified as held for sale	**44**	12	23
Total current assets	**3,026**	4,735	3,561
Investments, including derivatives	**72**	80	77
Trade and other receivables	**145**	215	116
Property, plant and equipment	**4,424**	4,285	4,319
Intangible assets	**346**	329	368
Investments in investees	**5,881**	6,711*	6,303
Loans granted to investees	**1,280**	732*	1,256
Deferred tax assets	**132**	211	216
Total non-current assets	**12,280**	12,563	12,655
Total assets	**15,306**	17,298	16,216

Condensed Interim Information on Financial Position as at (contd)

	September 30, 2012	September 30, 2011	December 31, 2011
	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million
Liabilities			
Debentures, loans and borrowings	**601**	770	757
Trade payables	**119**	154	177
Other payables, including derivatives	**512**	661	592
Current tax liabilities	**458**	383	361
Deferred income	**36**	23	28
Provisions (Note 4)	**148**	200	163
Employee benefits	**254**	430	351
Dividend payable	**1,978**	1,974	971
Total current liabilities	**4,106**	4,595	3,400
Debentures	**4,599**	5,043	5,034
Loans	**3,946**	3,996	3,996
Employee benefits	**184**	224	182
Deferred income and others	**47**	6	30
Dividend payable	**473**	1,386	924
Total non-current liabilities	**9,249**	10,655	10,166
Total liabilities	**13,355**	15,250	13,566
Equity			
Share capital	**3,837**	3,821	3,826
Share premium	**99**	53	68
Reserves	**599**	577	608
Deficit	**(2,584)**	(2,403)	(1,852)
Total equity	**1,951**	2,048	2,650
Total liabilities and equity	**15,306**	17,298	16,216

Shaul Elovitch	**Avi Gabbay**	**Alan Gelman**
Chairman of the Board of Directors	CEO	Deputy CEO and CFO

* Reclassified See Note 1.3.

Date of approval of the financial statements: November 7, 2012.

The accompanying notes to the Separate Interim Financial Information are an integral part of the financial information.

Condensed Interim Information on Income

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Revenues (Note 2)	**3,509**	3,534	**1,149**	1,186	4,648
Operating Costs					
Depreciation and amortization	**541**	513	**185**	180	688
Salaries	**808**	859	**274**	284	1,089
Operating and general expenses (Note 3)	**778**	806	**278**	282	1,074
Other operating expenses (income), net	**(13)**	82	**(7)**	(106)	139
	2,114	2,260	**730**	640	2,990
Operating profit	**1,395**	1,274	**419**	546	1,658
Financing expenses (income)					
Financing expenses	**455**	381	**161**	166	531
Finance revenues	**(267)**	(194)	**(98)**	(78)	(291)
Financing expenses, net	**188**	187	**63**	88	240
Profit after financing expenses, net	**1,207**	1,087	**356**	458	1,418
Company's share in earnings of investees, net	**502**	778	**96**	239	1,001
Profit before income tax	**1,709**	1,865	**452**	697	2,419
Income tax (see Note 5.4)	**370**	323	**110**	147	353
Profit for the period	**1,339**	1,542	**342**	550	2,066

The accompanying notes to the Separate Interim Financial Information are an integral part of the financial information.

Condensed Interim Information on Comprehensive Income

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Profit for the period	**1,339**	1,542	**342**	550	2,066
Items of other comprehensive income					
Actuarial gains, net of tax	**-**	-	**-**	-	28
Other items of comprehensive income (loss) for the period, net of tax	**(1)**	2	**(1)**	3	3
Effective share of the change in fair value of instruments used for cash flow hedging, net of tax	**2**	-	**4**	-	-
Other comprehensive income (loss) for the period, net of tax with regard to investees	**(6)**	-	**-**	-	4
Other comprehensive income (loss), net of tax	**(5)**	2	**3**	3	35
Total comprehensive income for the period	**1,334**	1,544	**345**	553	2,101

The accompanying notes to the Separate Interim Financial Information are an integral part of the financial information.

Condensed Interim Information on Cash Flows

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows from operating activities					
Profit for the period	**1,339**	1,542	**342**	550	2,066
Adjustments:					
Depreciation	**470**	456	**160**	160	613
Amortization of intangible assets	**71**	57	**25**	20	75
Share in the profits of equity-accounted investees, net	**(502)**	(778)	**(96)**	(239)	(1,001)
Financing income and expenses	**250**	189	**77**	95	243
Capital gain, net	**(23)**	(167)	**(25)**	(80)	(181)
Share-based payment transactions	**60**	125	**21**	42	165
Income tax expenses	**370**	323	**110**	147	353
Expenses (income) for derivatives, net	**5**	(20)	**11**	(20)	(21)
Change in inventory	**(8)**	-	**6**	(7)	2
Change in trade and other receivables	**(95)**	48	**(13)**	16	95
Change in trade and other payables	**(119)**	(155)	**(28)**	7	(80)
Change in provisions	**(15)**	(30)	**(2)**	(33)	(67)
Change in employee benefits	**(96)**	161	**(32)**	(15)	79
Change in deferred income	**17**	-	**7**	-	27
Net cash usedin operating activities with respect to transactions with investees	**(21)**	(39)	**(4)**	(10)	(34)
Net income tax paid	**(206)**	(156)	**(89)**	8	(228)
Net cash from operating activities	**1,497**	1,556	**470**	641	2,106
Cash flow used in investing activities					
Investment in intangible assets	**(103)**	(110)	**(33)**	(41)	(167)
Proceeds from the sale of property, plant and equipment	**164**	303	**96**	68	228
Acquisition of financial assets held for trading	**(2,249)**	(2,849)	**(398)**	(2,849)	(2,850)
Proceeds from the sale of financial assets held for trading:	**2,175**	851	**-**	851	1,961
Purchase of property, plant and equipment	**(653)**	(796)	**(216)**	(227)	(998)
Proceeds (payment) for derivatives	**13**	(8)	**3**	3	(5)
Proceeds from disposal of investments and long-term loans	**2**	4	**(1)**	1	7
Interest and dividends received	**7**	18	**2**	8	33
Increase in the rate of holding in a subsidiary	**(77)**	-	**-**	-	-
Net cash from (used in) investing activities with respect to transactions with investees	**705**	435	**253**	(15)	507
Net cash used in investing activities	**(16)**	(2,152)	**(294)**	(2,201)	(1,284)

The accompanying notes to the Separate Interim Financial Information are an integral part of the financial information.

Condensed Interim Information on Cash Flows (contd)

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Cash flows used in financing activities					
Bank loans received	**-**	2,200	**-**	600	2,200
Issue of debentures	**-**	3,092	**-**	2,692	3,092
Repayment of bank loans	**(204)**	(600)	**(127)**	(600)	(600)
Repayment of debentures	**(316)**	(691)	**-**	-	(702)
Dividend paid	**(1,574)**	(1,663)	**-**	-	(3,155)
Interest paid	**(293)**	(203)	**(31)**	(26)	(346)
Net proceeds (payment) in respect of derivatives	**8**	-	**(2)**	-	(1)
Proceeds from exercise of options	**7**	16	**5**	6	21
Net cash used in financing activities with respect to transactions with investees	**-**	(433)	**-**	-	(433)
Net cash from (used in) financing activities	**(2,372)**	1,718	**(155)**	2,672	76
Increase (decrease) in cash and cash equivalents	**(891)**	1,122	**21**	1,112	898
Cash and cash equivalents at the beginning of the period	**1,096**	198	**184**	208	198
Cash and cash equivalents at the end of the period	**205**	1,320	**205**	1,320	1,096

The accompanying notes to the Separate Interim Financial Information are an integral part of the financial information.

Notes to the Condensed Separate Interim Financial Information

1. Manner of preparing financial information

1.1 Definitions

"The Company" - Bezeq The Israel Telecommunication Corporation Limited.

"Associate", "The Group", "Investee", "Interested Party" - as these terms are defined in the Company's consolidated financial statements for 2011.

1.2 Principles used for preparing financial information

The condensed separate interim financial statements are presented in accordance with Article 38(D) of the Securities Regulations (Periodic and Immediate Reports),1970 and do not include all the information required under Regulation 9(C) and the Tenth Addendum of the Securities Regulations (Periodic and Immediate Reports),1970 with respect to the separate financial information of the corporation. They should be read in conjunction with the separate financial information for the year ended December 31, 2011 and in conjunction with the condensed interim consolidated financial statements as at September 30, 2012 ("the Consolidated Financial Statements").

The accounting policies used in these condensed separate financial information are in accordance with the accounting policies set out in the separate financial information as of and for the year ended December 31, 2011.

1.3 Certain amounts in the comparative figures were reclassified to the relevant sections in the financial statements for the current period.

2. Revenue

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Fixed-line telephony	**1,717**	1,836	**557**	612	2,393
Internet - infrastructure	**872**	810	**291**	276	1,092
Transmission and data communication	**735**	700	**243**	239	931
Other services	**185**	188	**58**	59	232
	3,509	3,534	**1,149**	1,186	4,648

3. General and operating expenses

	For the nine month period ended September 30		For the three month period ended September 30		For the year ended December 31
	2012	2011	2012	2011	2011
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS million	NIS million	NIS million	NIS million	NIS million
Interconnectivity and payments to operators	**217**	236*	**70**	79*	314
Sales and marketing expenses	**104****	147*	**54**	58*	194
Terminal equipment and materials	**79**	62	**28**	23	89
Maintenance of buildings and sites	**192**	185	**70**	63	247
Services and maintenance by sub-contractors	**54**	55	**15**	17	76
Vehicle maintenance expenses	**62**	63	**25**	22	78
Royalties and collection fees	**70**	58	**16**	20	76
	778	806	**278**	282	1,074

* Reclassified

** See Note 13.1 of the Condensed Financial Statements with regard to the settlement arrangement between the Company and the Ministry of Communications on the matter of the government authorities' claim for payment of frequency fees in Judea, Samaria and Gaza. As a result of the foregoing settlement agreement, the Company reduced its commitment to pay frequency fees and reduced its operating and general expenses by an amount of NIS 37 million and financing costs by NIS 13 million.

4. Contingent liabilities

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

In the opinion of the Company's management, based, inter alia, on legal opinions as to the likelihood of success of the claims, the financial statements include appropriate provisions of NIS 148 million, where provisions are required to cover the exposure arising from such legal claims.

In the Company's opinion, the amount of additional exposure (exceeding the foregoing provisions), as of September 30, 2012 for legal claims filed against the Company on various matters for are unlikely to be realized, amounts to NIS 2.5 billion. Of this amount, NIS 361 million is for a claim filed against the Company and other telecommunication companies without specifying the portion of the amount claimed from each of the plaintiffs. In addition, there is further exposure in the amount of NIS 273 million for claims, the success of which cannot be assessed at this stage. All the foregoing amounts are linked to the consumer price index and are before the addition of interest.

Furthermore, there are other claims for which the Company has additional exposure beyond the aforesaid, which cannot be quantified, as the exact amount of the claim is not stated in the claim.

Subsequent to the date of the report, claims for which exposure amounted to NIS 650 million were concluded.

For further information concerning contingent claims see Note 5 to the Consolidated Financial Statements, Contingent Claims.

5. Material agreements and transactions with Investees during and subsequent to the reporting period

5.1. Loans to investees

5.1.1 On March 29, 2012 the Company granted a loan in the amount of NIS 440 million to Pelephone Communications Ltd. ("Pelephone"). The loan bears fixed annual interest of 5.7%. The loan will be repaid in ten equal annual installments commencing March 15, 2013.

5.1.2 The loan that the Company granted to Pelephone on May 17, 2011 in the amount of NIS 280 million was repaid on May 17, 2012 in accordance with the terms of the loan.

During August 2012, Pelephone made early repayment of NIS 270 million of the loan granted to it in December 2011 in the total amount of NIS 450 million. Accordingly, the final repayment date was set for December 2015.

5.1.3 On March 29, 2012 the Company granted a loan in the amount of NIS 40 million to Bezeq International Ltd. ("Bezeq International"). The loan bears fixed annual interest of 4.7%. The loan will be repaid in five equal annual installments, commencing March 2013.

On September 16, 2012 the Company granted another loan in the amount of NIS 40 million to Bezeq International. This loan bears fixed annual interest of 4.68%. The loan will be repaid in five equal annual installments, commencing September 2013.

5.1.4 On January 17, 2012 the Company granted a loan in the amount of NIS 3 million to Bezeq Online Ltd. ("Bezeq Online"). This loan bears fixed annual interest of 4.2%. The loan will be repaid in three equal annual installments, commencing January 17, 2013.

On September 2, 2012 the Company granted another loan in the amount of NIS 5.66 million to Bezeq Online. This loan bears fixed annual interest of 4.68%. This loan will be repaid in two installments as follows: NIS 660,000 will be repaid on January 1, 2012 and the balance, in the amount of NIS 5 million will be repaid on December 31, 2013.

5.1.5 On September 1, 2012 Bezeq Online made early repayment, in the amount of NIS 5.7 million, of the loan granted to it in September 2011.

5.2. Financial Guarantees

For information pertaining to bank guarantees granted in August 2012 in favor of a bank with regard to a loan taken by Teletel Communication Channels Ltd. (a wholly owned subsidiary of Walla! Communications Ltd.) see Note 4.1.2 to the Consolidated Financial Statements.

5.3. Dividends

5.3.1 During May 2012, Pelephone paid the Company a NIS 466 million dividend announced that month.

5.3.2 During July 2012, Pelephone announced the distribution of a dividend in the amount of NIS 410 million. The dividend was paid in October 2012.

5.3.3 During May 2012, Bezeq International paid the Company a NIS 90 million dividend announced that month.

5.3.4 During July 2012, Bezeq International announced the distribution of a dividend in the amount of NIS 74 million. The dividend was paid in October 2012.

5. Material agreements and transactions with Investees during and subsequent to the reporting period (contd.)

5.4. In February 2012, Stage One Venture Capital Fund (Israel) L.P. ("the Fund") signed an agreement to sell all its holdings in Traffix Communication Systems Ltd. In March 2012, the Company received its share in the distribution of the Fund's profits in the amount of NIS 80 million. The profits from the sale are included in the profits of equity-accounted investees and are taxed in the Company. Consequently, the Company's tax expenses include tax expenses for these profits.