



Delek Group

ANNUAL REPORT 2011



IMPORTANT

This document is an unofficial translation for convenience only of the Hebrew original of December 31, 2011 financial report of Delek Group Ltd. that was submitted to the Tel-Aviv Stock Exchange and the Israeli Securities Authority on March 30, 2012.

The Hebrew version submitted to the TASE and the Israeli Securities Authority shall be the sole binding legal version.



Table of Contents

Chapter A | **Corporate Description**

Chapter B | **Board of Directors Report**
on the State of the Company's Affairs

Chapter C | **Financial Statements**
for December 31, 2011

Chapter D | **Additional Information**
on the Corporation

Chapter E | **Annual report for 2011**
on the Effectiveness of Internal
Controls for Financial Reporting
and Disclosure



Delek Group



Chapter A



Corporate Description



Delek Group



Description of the Corporation's Business

Table of Contents

Part One – Description of the Corporation's Business	1
1.1 Company operations and business developments	2
1.2 Operating Segments	6
1.3 Equity investments in the Company and transactions in its shares.....	7
1.4 Distribution of dividends	8
Part Two – Other Information	10
1.5 Financial information concerning the Group's operating segments.....	10
1.6 General environment and impact of external factors	13
Part Three – Description of the Corporation's Business by Operating Segment.....	18
1.7 Refining and Fuels in the USA	18
1.8 Fuel Product Segment in Israel.....	53
1.9 Fuel products in Europe	103
1.10 Motorway Service Areas in the UK	133
1.11 Energy	157
1.12 Insurance and Finance in Israel.....	328
1.13 The Insurance segment in the U.S.	377
1.14 Automotive segment	399
1.15 Additional Information	428
Part Four – Matters Pertaining to the Group as a Whole.....	446
1.16 Property, plant and equipment.....	446
1.17 Human resources.....	446
1.18 Financing.....	447
1.19 Taxation.....	449
1.20 Company liens, loans and guarantees.....	449
1.21 Restrictions and Supervision of the Corporation's Operations	451
1.22 Material Agreements	452
1.23 Legal proceedings and insurance	452
1.24 Business strategy and objectives.....	452
1.25 Financial information concerning geographic regions.....	454
1.26 Discussion of Risk Factors	454

Part One – Description of the Corporation's Business

Key:

In this report the following abbreviations have the following meanings:

Company or Delek Group	- Delek Group Ltd.
IDE	- IDE Technologies Ltd
Excellence	- Excellence Investments Ltd.
Barak Capital	- Barak Capital Ltd.
Gadot	- Gadot Biochemical Industries Ltd.
Delek Ashkelon	- I.P.P. Delek Ashkelon Ltd.
Delek Europe	- Delek Europe Holdings Ltd.
Delek Energy	- Delek Energy Systems Ltd.
Delek Benelux	- Delek Benelux B.V.
Delek Investments	- Delek Investments and Properties Ltd.
Delek Refining	- Delek Refining Inc.
Delek Israel	- Delek The Israel Fuel Corporation Ltd.
Delek Real Estate	- Delek Real Estate Ltd.
Delek Petroleum	- Delek Petroleum Ltd.
Delek Infrastructure	- Delek Infrastructure Ltd.
Delek Automotive	- Delek Automotive Systems Ltd.
Delek Capital	- Delek Capital Ltd.
Delek USA	- Delek US Holdings Inc.
HOT	- HOT Cable Media Systems Ltd.
The Phoenix	- The Phoenix Holdings Ltd.
Cohen Development	- Cohen Development and Industrial Buildings Ltd.
Roadchef	- Roadchef Ltd.
Republic	- Republic Companies Group Inc.
Avner Partnership	- Avner Oil and Gas Exploration – Limited Partnership
Delek Drilling Partnership	- Delek Drilling – Limited Partnership
The Partnerships	- Avner Partnership and Delek Drilling Partnership

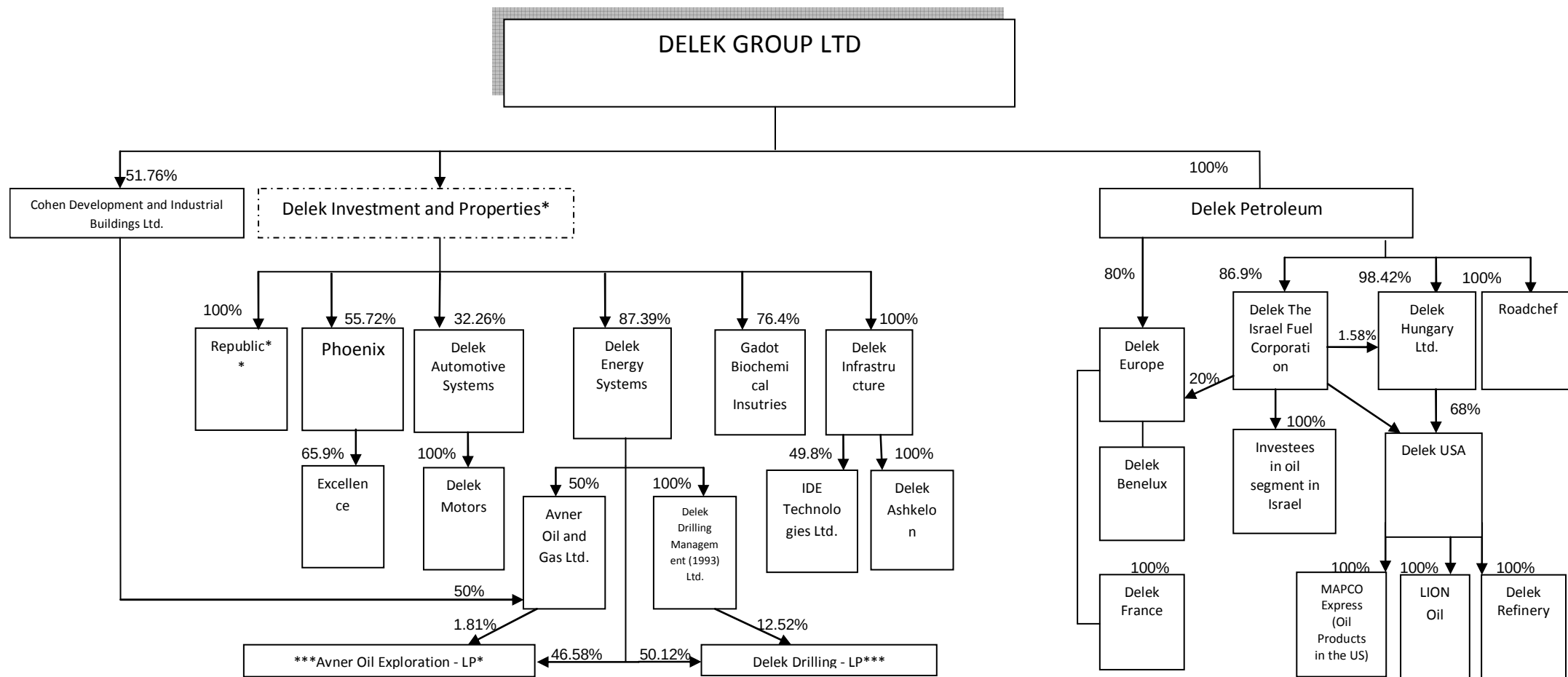
1.1 Company operations and business developments

1.1.1 Delek Group Ltd. ("the Company") is a holdings management company controlling subsidiaries operating in various segments (the Company and the companies under its control are hereinafter referred to, for the sake of convenience as - "the Group" or "Delek Group").

1.1.2 The Company was incorporated on October 26, 1999 as a public company.¹

1.1.3 The following chart illustrates the Group's major holdings as of March 29, 2012:

¹ The Company was incorporated as part of the Group's restructuring in 1999, in which Group operations were separated and divided into three main subsidiaries, with the Company established as a parent company. Prior to restructuring, Group operations were included under Delek, The Israel Fuel Corporation Ltd., which was incorporated on December 12, 1951, and is currently, following the restructuring, responsible for the fuel products in Israel segment.



* Delek Investments and Properties is being merged with the Company, so that all assets, liabilities, and charges in Delek Investments (target company) will be transferred and granted the Company (receiving company). Upon completion of this merger, Delek Investments will be dissolved without liquidation. The merger is expected to be completed by June 2012 according to the timeline set forth in Section 323 of the Companies Law.

** Indirect holding, through Delek France.

*** The Delek Group has direct holdings of 6.53% in Delek Drilling - LP.

**** The Delek Group has direct holdings of 9.11% in Avner Oil Exploration - LP.

- 1.1.4 The Delek Group is holdings management company, with a variety of investments in Israel and abroad, with operations including, inter alia, oil and gas, refining, gas stations, motorway service areas, finance and insurance, desalination, power generation, automotive, and biochemicals. In recent years, inter alia due to natural gas discoveries off the coasts of Israel and in the Mediterranean, in which the Group is involved, the Group's operations have become more energy-focused - exploration, production and sale of natural gas (Upstream Energy) and refining and gas station operations (Downstream Energy).**

Milestones in the Group's operations in the past decade:

1999 – 2000	Discovery of significant quantities of natural gas by the partners in the Yam Tethys project - in the Mari and Noa reservoirs off the coast of Ashkelon.
2000	The Group's shares are listed for trading on the Tel Aviv Stock Exchange. Acquisition of 50% of the shares in the desalination company IDE.
2001	Establishment of Delek USA and acquisition of 198 gas stations and convenience stores in the US.
2004	Start of gas production and sale by the Yam Tethys project.
2005	Delek USA acquires a refinery in Tyler, Texas. Acquisition of control in The Phoenix Holdings, in a two-step process completed in 2006. Initial public offering of shares in the Gadot subsidiary (biochemical operations).
2006	Initial public offering of shares in Delek USA on the New York Stock Exchange.
2007	Initial public offering of shares in Delek Israel. Delek Israel acquires the Pi Giliot storage facility. Establishment of Delek Europe and acquisition of gas stations and convenience stores in Benelux.
2009	Distribution of most of the shares in Delek Real Estate as a dividend in kind. Tamar discovery in the Mediterranean Sea.
2010	Delek Europe acquires gas stations and convenience stores in France. The Group sells 22% of its shares in Delek Automotive. Leviathan discovery in the Mediterranean Sea.
2011	Acquisition of motorway service area operations in the UK (Roadchef) from Delek Real Estate, and increasing the Group's holdings in Roadchef from 25% to 100%. Acquisition of control in Lion Oil. Dolphin discovery in the Mediterranean Sea. Acquisition of control in Cohen Development. Aphrodite discovery in Cyprus's exclusive economic zone.

Material developments in the Group's business in 2010 - 2011 as of near the date of this report:

2010

Energy: In 2010, the Partnerships signed an interim financing agreement for financing the Tamar Project's development costs. Seismic surveys were carried out in the Tamar and Dalit drilling sites, and planning was carried out and equipment purchased for developing the Tamar reservoir. For more information, see Section 1.11.4 of the report.

In October 2010, work began in the Leviathan-1 drill site, whose budget was estimated at approximately USD 150 million (not including production testing costs). At the end of December 2010, the Partnerships announced the discovery of natural gas (in March 2011, the project budget was updated and may reach USD 190 million). The operator announced that very high quality reservoir sands were discovered in the target layers, which contain natural gas, with a total (net) thickness of at least 67 meters in a number of different layers. This information confirmed the operator's previous estimates as to the estimated natural gas resource range, whereby the gross mean natural gas resources in the Leviathan field total approximately 16 TCF (approx. 453 BCM).

In light of the significant gas reserves discovered in Tamar and Leviathan, and the potential of additional exploration areas, the Partnerships began considering various possibilities for commercializing the gas reserves, including export and sale on the international market.

Fuel products in Europe: In October 2010, a transaction was completed for the acquisition of BP France SA's ("BP") fuel marketing operations in France, comprised of 410 BP-branded gas stations, 300 convenience stores with a nation-wide presence, and holdings in 3 fuel supply and storage terminals, and an exclusive usage license to the BP brand in the gas station chain in France. Consideration for the transaction totaled EUR 209 million. For more information, see Section 1.9.1(b) of the report.

Sale of Delek Automotive shares: In October 2010, the Group completed the sale of 22% of Delek Automotive's shares to Mr. Gil Agmon, CEO of Delek Automotive, in consideration for NIS 1 billion. Post-sale, the Delek Group's holdings in Delek Automotive decreased to 32.8% of the shares in Delek Automotive, and the Group ceased being the controlling shareholder in Delek Automotive. For more information, see Section 1.14.1 of the report.

2011

Energy: In December 2011, the Company acquired control of Cohen Development, a public company holding 50% of the share capital in the general partner in the Avner Partnership, and rightsholder to overriding royalties from the Avner Partnership. Consideration for this acquisition totaled NIS 274 million. For more information, see Section 1.11.1 below. In August 2011, the Company issued a complete exchange purchase offer for Delek Energy shares in exchange for participation units in the limited partnerships - Delek Drilling and Avner. For more information, see Section 1.11.2 below. In June 2011, Delek Energy's board of directors approved the budget for the development plan in the Tamar project, to a total amount of USD 3.06 billion. For more information, see Section 1.11.5 of the report. In late March 2011, the Israel Knesset passed the Oil Profits Taxation Law, 2011, which provides a formal statutory anchor for the recommendations submitted by the Sheshinski Committee (the Law"). Enactment of the Oil Profits Taxation Law significantly increased tax liability, and adversely affected the Group's operations in general, and its energy segment in particular. For more information, see Section 1.11.25 of the report.

Roadside service stations in the UK: In January 2011, the Group and Delek Real Estate completed a transaction for the acquisition of a 75% interest in Roadchef, which operates 29 motorway service areas in 19 locations in England, Scotland and Wales. These operations include sales of retail products, and food and refueling services. Consideration for the transaction totaled GBP 86.25 million (approx. NIS 497 million as of the transaction completion date). The consideration was paid by offsetting part of Delek Real Estate's debt to the Group, and also included the purchasing of Delek Real Estate's debt to a bank. Following the transaction, the Group (through Delek Petroleum), holds 100% of Roadchef. For more information about Roadchef's operations, see Section 1.10 of the report; for more information about exposure to Delek Real Estate through remaining loans and guarantees after the transaction, see Section 1.15.5 of the report.

Refining and fuel products in the US: On March 17, 2011, Delek USA signed an agreement with Ergon Inc. ("the Sellers") for acquiring an additional 53.7% interest in Lion Oil's shares, in which Delek USA held a 34.6% interest. Consideration for this transaction consisted of a cash payment of

USD 50 million, allocation of shares (valued at USD 45 million), and settlement of Lion Oil's debt to the Sellers. Subsequent to this acquisition, Delek USA held 88.3% of Lion Oil's shares. In October 2011, Delek USA acquired the remaining non-controlling interest in Lion Oil's shares in consideration for USD 13 million, so that following this acquisition, Delek USA holds 100% of Lion Oil's share capital. For more information, see Section 1.7.1(a) to the report.

2012 (as of the reporting date)

Energy: In January 2012, the partners in the Tamar project signed an agreement for supplying natural gas to Dalia Power Energies Ltd., at a rate of 1.38 BCM a year, for 17 years. For more information, see Section 1.11.12 to the report. In February, 2012, the Partnerships announced a natural gas discovery in the Tanin 1 drill site, located in the 364/Alon-A license. For more information, see Section 1.11.7(b) to the report. On March 14, 2012, the partners in the Tamar project signed an agreement with the Delek Drilling and Avner limited partnerships, for the supply of a total of 42.5 BCM of natural gas to IEC. For more information, see Section 1.11.12(d) to the report.

During the period 2010-2011, the Group raised considerable capital and debt on the capital market. In 2012 (as of the reporting date), the Group did not raise any debt or capital. The Group's major capital-raising activities are described in the chapters on the operating segments, and include the following:

2010

- In January 2010, Delek Energy raised NIS 400 million in a public offering of debentures.
- In April 2010, the Company raised NIS 255 million in a public offering of debentures convertible to shares in the Company.
- In April 2010, Gadot raised NIS 38.5 million in a share issue effected as a rights offering.
- In June 2010, the Company raised NIS 844 million in a public offering of debentures (effected through the expansion of existing series).
- In July 2010, Delek Energy raised NIS 414 million in a public offering of debentures (by expansion of existing series).
- In September 2010, Gadot raised NIS 63 million in a public offering of debentures (by expansion of existing series).
- In September 2010, The Phoenix Insurance issued NIS 375.5 million par value in a public offering of debentures, and in October 2010, The Phoenix Insurance issued NIS 24.5 million par value in a private placement of debentures of the same class.
- In November 2010, the Company raised NIS 559 million in a public offering of debentures.

2011

- In May 2011, Delek Israel raised NIS 327 million in a public offering of debentures.
- In May 2011, Gadot raised NIS 17 million in a share issue effected by way of rights.
- In July 2011, the Company raised NIS 471 million in a public offering of debentures and warrants to debentures.
- In November 2011, the Company raised NIS 258 million in a private placement of debentures to classified investors.

1.2 Operating Segments

1.2.1 The Group operates in the following eight segments:

- A. Refining and Fuel Products in the US – This segment includes holdings in an oil refinery and crude oil pipeline, as well as the marketing of fuel products and operation of gas stations and convenience stores in the US.
- B. Fuel Products in Israel - This segment includes sales of fuels and lubricants, the operation of gas stations with on-site convenience stores, and the provision of fuel storage and distribution services in Israel.

- C. Fuel Products in Europe - This segment includes sales of fuels and lubricants and the operation of gas stations with on-site convenience stores in Benelux and France.
- D. Motorway Service Areas in the UK - This segment includes the provision of motorway services, including sales of retail products, restaurants and hotels, and fuel sales, in motorway service areas throughout the UK.
- E. Energy - This segment includes production and sale of natural gas and oil and natural gas and oil exploration activities.
- F. Insurance and Finance in Israel - This segment includes various insurance operations and long-term savings operations in the finance industry in Israel. Operations are carried out through The Phoenix Insurance and Excellence.
- G. Insurance in the US - This segment includes general insurance operations in the US, carried out through the Republic insurance company.
- H. Automotive - This segment includes a 32.13% interest in Delek Automotive, which imports, markets and sells private and commercial "Mazda" and "Ford" vehicles in Israel.

1.2.2 In addition, the Delek Group engages in various operations that are not covered by the above segments. These include, primarily, Gadot's biochemical operations, in which the Group holds a 76% interest; a 49.8% holding in IDE's desalination operations; other investments in infrastructure projects; a 47.85% holding in Barak Capital's finance operations in Israel; a portfolio of financial investments; and investments in foreign securities (see Section 1.15 below).

1.3 Equity investments in the Company and transactions in its shares

1.3.1 To the best of the Company's knowledge, in 2010-2011 until shortly prior to the report date, the following investments were made in the Company's equity:

Date	Type of transaction	% of issued capital	Equity investment in NIS millions*
Q1/2010	Warrants exercised for shares	0.3	16.4
Q3/2011	Purchase of Company shares (by Delek Investments and Properties Ltd.)	0.16%	10

To the best of the Company's knowledge, in 2010-2011 until shortly prior to the reporting date, the following material transactions were made by the Company's principal shareholders, both on and off the stock exchange:

Date	Principal shareholder	Type of transaction	% of issued capital	Share price in NIS	Consideration in NIS millions	Company value derived from transaction (NIS millions)
Nov. 22, 2010	Yitzhak Sharon (Tshuva)*	Transfer for no consideration	0.17	-	-	-
Sept. 12, 2011	Yitzhak Sharon (Tshuva)*	Purchase on the TASE	0.03	509.122	NIS 1.5 million	5,969
Aug. 10, 2011	Gabriel Last	Purchase on the TASE	0	606.1	NIS 182,000	7,106

* Yitzhak Sharon (Tshuva) through companies under his full ownership and control.

1.4 Distribution of dividends

1.4.1 Distribution of dividends in the past two years and balance of distributable profits

Dividends declared by the Company in 2010-2011 until shortly prior to the reporting date:

Declaration date	Payout date	Dividend per share (NIS)	Total dividend (NIS millions)
Mar. 24, 2010	Apr. 28, 2010	8.7895	100
May 31, 2010	Jun. 30, 2010	13.1842	150
Jul. 26, 2010	Aug. 23, 2010	10.5474	120
Sept. 21, 2010	Oct. 19, 2010	7.9106	90
Nov. 30, 2010	Dec. 24, 2010	43.947	500
Mar. 31, 2011	Apr. 28, 2011	17.5789	200
May 30, 2011	Jun. 30, 2011	9.2289	105
Aug. 31, 2011	Sept. 27, 2011	8.7895	100
Nov. 29, 2011	Dec. 30, 2011	8.7895	100
Mar. 29, 2012	May 3, 2012	10.5474	120

For 2010 and 2011, the Company distributed a total of NIS 1,060 million and NIS 425 million, respectively.

As of the reporting date, the Company's distributable profits, under Section 302 of the Companies Law, 1999, total NIS 3,592 million.

On March 29, 2012, the Company announced the distribution of NIS 120 million in dividends. Following this distribution, the Company's total distributable profits under Section 302 of the Companies Law, 1999, will total NIS 3,472 million.

1.4.2 Dividend distribution policy

On March 30, 2005 the Company's Board of Directors decided on a dividend distribution policy. Accordingly, the Company will strive to distribute approximately 50% of its net annual profit (post-tax) each year. This decision is subject to the following conditions:

- A. The Company's Board of Directors will decide from time to time on the distribution of a dividend, and its decision will be made pursuant to the provisions and limitations of the law.
- B. The Board's decision on the amount of the distribution will depend on the Company's financing requirements, its liabilities, its liquidity, and its investment plan, as may be in effect from time to time.
- C. The Board's decision on the amount of the distribution will be made so that the dividend distribution will not harm the Company's third-party obligations, including its bondholders and the banks.

1.4.3 Limitations on the distribution of dividends

Under the terms of a borrowing agreement signed with a bank, in which the Group's debt balance as of December 31, 2011, was NIS 600 million (including a guarantee of NIS 150 million that was cancelled as of the publication date), the Delek Group is required to obtain prior approval when distributing a dividend that exceeds 60% of its annual net profit. Under the agreement, this limitation applies commencing from the end of 2009. For further information relating to the limitations on distribution of dividend applicable to the Group's companies, see the description of the various areas of operation below.

The Company is studying the applicability of Section 309 to the Companies Law as regards the purchase of shares by Excellence's exchange-traded notes companies. These companies purchase and sell Company shares as part of their prospectus obligations to monitor the share indices in which the Company is included. Similarly, The Phoenix's profit-sharing policies occasionally buy and sell Company shares. Section 309 to the Companies Law dictates that a subsidiary or another corporation controlled by the parent company are entitled to purchase shares in the parent company or securities which are convertible or exercisable for shares in the parent

company, to the same extent that the parent company is entitled to carry out a distribution, provided that the subsidiary's board of directors or the management of the purchasing corporation has determined that had the purchase of the shares or the securities convertible or exercisable for shares been carried out by the parent company, such action would have constituted permissible distribution. However, in light of the fact that these purchases are made using funds managed on behalf of others, and their limitation (to the extent that such limitation is practical) may adversely affect the ETN companies' obligations towards their investors, it seems that both materially and practically, such share purchases should not be equated with the distribution of dividends, nor should they be subject to the distribution tests. In practice, the subsidiaries do not make decisions on whether such purchases constitute permissible distribution by the Company. From an accounting perspective, in preparation of its quarterly or annual financial statements, the Company reviews the net volume of these purchases (i.e. - purchases less of sales in the reporting period) and accounts for them in accordance with Israeli GAAP. Therefore, shares are presented at cost offset from the Company's equity, and gains or losses on sales, purchases, issues or cancellation of treasury shares are recognized directly to equity. Net purchases are detracted from the Company's distributable profits, and as of December 31, 2010 and 2011, the respective amounts of NIS 19 million and NIS 17 million have been detracted from the Company's distributable profits.

Part Two – Other Information

1.5 Financial information concerning the Group's operating segments²

The following table details financial information related to the Group's segments of operation:

2011 (NIS millions)

2011 (NIS millions)		Refining and fuel products in the US	Delek Israel	Delek Europe	Energy	Automotive	Insurance and finance in Israel	Insurance in the US	Other	Consolidation adjustments	Consolidated
Revenues	Revenues from externals	25,755	6,259	16,285	722		6,825	1,409	1,853	51	59,159
	Revenues from other segments	-	-	-	-		-	-	-	-	-
	Total	25,755	6,259	16,285	722		6,825	1,409	1,853	51	59,159
Total attributable costs	Costs constituting revenues for another segment	-	-	-	-		-	-	-	-	-
	Other costs	24,707	6,118	16,101	121		6,354	1,860	1,979	306*	57,546
	Total	24,707	6,118	16,101	121		6,354	1,860	1,979	306	57,546
	Fixed costs attributable to segment	1,387	630	1,070	-						
	Variable costs attributable to segment	23,320	5,488	15,031	121**						
Operating profit attributable to owners of the parent		716	122	179	546		266	(451)	(48)	(1)	1,329
Share in operating profit attributable to minority interests		332	19	5	55		205	-	(78)	(254)	284
Total assets attributable to segment		8,539	4,781	5,992	12,982		64,693	5,449	4,449	1,015	107,900
Total liabilities attributable to segment		3,749	953	2,347	608		58,473	4,088	165	26,427	96,810

* Including adjustments for costs not attributed to operating segments, and the Group's share in the operating profits of investees as included in the segment's results.

** Costs are mostly variable and change according to oil and gas production capacity.

² For information concerning motorway service area operations in the UK, acquired by the Company in January 2011, see Section 1.10.2 below.

2010 (NIS millions)

2010 (NIS millions)		Refining and fuel products in the US	Delek Israel	Delek Europe	Energy	Automotive	Insurance and finance in Israel	Insurance in the US	Other	Consolidation adjustments	Consolidated
Revenues	Revenues from externals	14,019	5,136	13,130	556	3,363	9,717	1,364	693	(3,411) ³	44,567
	Revenues from other segments	-	-	-	-	-	-	-	-	-	-
	Total	14,019	5,136	13,130	556	3,363	9,717	1,364	693	(3,411)	44,567
Total attributable costs	Costs constituting revenues for another segment	-	-	-	-	-	-	-	-	-	-
	Other costs	13,957	4,947	12,940	288	2,883	9,070	1,299	578	(2,620) ⁴	43,342
	Total	13,957	4,947	12,940	288	2,883	9,070	1,299	578	(2,620)	43,342
	Fixed costs attributable to segment	1,090	608	566	-	-					
	Variable costs attributable to segment	12,867	4,339	12,374	288 ⁵	2,883 ⁶					
Operating profit attributable to owners of the parent		44	146	181	213	277	359	63	125	(588)	819
Share in operating profit attributable to minority interests		18	43	9	55	203	288	2	(10)	(203)	406
Total assets attributable to segment		4,052	4,618	5,529	3,134	1,316	62,385	5,334	1,684	3,844	91,896
Total liabilities attributable to segment		1,087	832	2,202	363	-	56,272	3,726	142	22,395	87,019

³ Mainly adjustments for the automotive segment's revenues in 2010 (until cessation of Delek Automotive's consolidation).

⁴ Including adjustments for Delek Automotive's costs (until cessation of Delek Automotive's consolidation, its costs were included in their entirety), costs not attributable to operating segments, and the Group's share in the operating profit of associates as included in the segments' results.

⁵ Mostly variable costs connected with gas and oil production output.

⁶ The vast majority of these costs are variable costs stemming mainly from the purchase of vehicles and spare parts. Therefore, fixed costs have not been stated separately.

2009 (NIS millions)

2009 (NIS millions)		Refining and fuel products in the US	Delek Israel	Delek Europe	Energy	Automotive	Insurance and finance in Israel	Insurance in the US	Other	Consolidation adjustments	Consolidated
Revenues	Revenues from externals	10,413	4,286	10,681	449	4,743	10,699	1,668	575	(4,811) ⁷	38,703
	Revenues from other segments	-	-	-	-	-	-	-	-	-	-
	Total	10,413	4,286	10,681	449	4,743	10,699	1,668	575	(4,811)	38,703
Total attributable costs	Costs constituting revenues for another segment	-	-	-	-	-	-	-	-	-	-
	Other costs	10,224	4,056	10,584	184	4,283	10,251	1,591	289	(3,909) ⁸	37,553
	Total	10,224	4,056	10,584	184	4,283	10,251	1,591	289	(3,909)	37,553
	Fixed costs attributable to segment	1,172	496	585	-	-					
	Variable costs attributable to segment	9,052	3,560	9,999	184 ⁹	4,283 ¹⁰					
Operating profit attributable to owners of the parent		140	179	93	265	266	249	77	271	(647)	893
Share in operating profit attributable to minority interests		49	51	4	-	194	199	-	15	(255)	257
Total assets attributable to segment		4,591	4,407	4,156	2,441	2,356	55,175	5,819	2,113	3,298	84,356
Total liabilities attributable to segment		1,029	833	1,451	171	1,275	49,823	4,004	311	20,871	79,768

For details about the main developments in the financial data, see the Board of Directors' explanations regarding the Corporation's affairs.

⁷ Mostly adjustments for Delek Automotive's revenues, which were classified as discontinued operations after the sale of 22% of Delek Automotive in 2010.

⁸ Including adjustments for Delek Automotive's costs, which were not attributable to operating segments, and the Group's share in the operating profits of associates as included in the segment revenues.

⁹ Mostly variable costs connected with gas and oil production output.

¹⁰ The vast majority of these costs are variable costs stemming mainly from the purchase of vehicles and spare parts. Therefore, fixed costs have not been stated separately.

1.6 General environment and impact of external factors

1.6.1 General

The Company is a holdings and management company controlling a large number of corporations with diverse investments in Israel and abroad, in energy, gas stations and convenience stores, infrastructure and desalination, finance and insurance, automotive, biochemicals and more. Most of these corporations are controlled by the Company, with holdings of more than 50%.

The Company's financial data and its operating results are affected by the financial data and operating results of its investee companies, and by its sale or acquisition of holdings. The Company's cash flow is affected, inter alia, by dividends and management fees distributed by its investee companies, by proceeds earned from the sale of the Company's holdings in such companies, by the Company's ability to raise foreign financing that depends, inter alia, on the value of its holdings, and by investments made by the Group and by dividends it distributes to its shareholders.

1.6.2 Market developments and volatility

Market developments and fluctuations may have a material effect on the results of the Company and its investee companies, on their liquidity, the valuation of their assets, their ability to realize such assets, the state of their business, their financial criteria, their credit rating, their ability to distribute dividends, and their ability to raise funds to finance their ongoing operations and their long-term operations, as well as the terms of such financing. Inter alia, the Group's results are materially affected by developments and volatility in the following relevant markets:

1. The natural gas market in Israel - the oil and gas sector in Israel is materially affected by demands and pricing of natural gas in Israel, where, currently, the largest customer is the Israel Electric Corporation. The market is also affected by the supply of natural gas in Israel, and in particular by competition with EMG, which imports gas from Egypt. Recent political developments in Egypt may, in the future, affect market structure and competition. The gas and oil sector is also materially affected by regulation - including taxation policies which have a materially negative impact on the Group's operations in light of the adoption of the Sheshinski Committee's recommendations and the final approval of the Oil Profits Taxation Law by the Israeli Knesset in March 2011, as well as regulation related to development of the Tamar and Leviathan reservoirs. For more information, see Section 1.11.27 below.
2. Fuel and convenience store products in Israel, Europe, and the US - Fluctuations in demand and in the prices of fuel products in the Group's areas of operation may materially affect the results of the Group's operations. Such fluctuations may be caused by economic conditions in the areas of operation, and by applicable regulation. For more information, see Sections 1.7.1(b), 1.8, and 1.9 below.
3. The US refining market - Refining operations in the US are materially affected by the Tyler refinery's refining margin, the US Gulf Coast 5-3-2 spread, which is affected by the supply and demand of refining products. For more information, see Section 1.7.1(c) below.
4. The Israeli capital market - In addition to the Israeli capital market's effect on those Group companies traded on the Tel Aviv Stock Exchange, including on their ability to raise funding, fluctuations in the Israeli capital market materially affect the results of the Group's insurance and finance operations in Israel. These operations are affected, inter alia, by management fees charged on insurance policies, provident funds and pension funds, and these are tied to yields on investments made in the capital market. The possible negative impact of capital market fluctuations is reflected in The Phoenix's results for 2008, when The Phoenix posted a total loss of approximately NIS 561 million, in light of the global and local capital market crises, while the positive results posted in 2009 and 2010, when The Phoenix recorded a total gain of approximately NIS 435 million and NIS 432 million, respectively, were, inter alia, due to the Israeli capital market emerging from this crisis. For more information, see Section 1.12 below.
5. NASDAQ - The Company holds a portfolio of investments in securities traded on the US NASDAQ. In light of the above, fluctuations in the US capital markets, and mainly in the NASDAQ, may affect the value of these holdings.
6. The Israeli automotive market - In recent years, the automotive segment has materially contributed to the Group's profitability. Even after the sale of part of the Group's holdings in Delek Automotive in 2010, the segment remains material at the group level. Vehicle import

operations depend, inter alia, on demand for vehicles in Israel, on the competition among vehicle importers, and on applicable regulation. For more information, see Section 1.14 below.

1.6.3 Exchange rates

The Company's functional currency and the presentation currency of the Company's financial statements is the NIS. However, the functional currency for some of the Group companies is the USD (Delek USA, Delek Drilling, Republic, and IDE). Delek Europe's functional currency is the EUR, and Roadchef's functional currency is the GBP. Therefore, the Group's results and equity are materially affected by fluctuations in the NIS exchange rates for the aforesaid currencies (as well as additional currencies such as the JPY and the CNY). In 2011, the effects of these exchange rate fluctuations were expressed as a NIS 400 million increase in the Company's equity under a capital reserve classified as "Adjustments from translation of overseas operations".

1.6.4 Regulation

The Company and several of its investee companies are subject to restrictions on their operations imposed by law or by order of various regulatory bodies, such as anti-trust provisions, provisions relating to the obligation to tender, provisions relating to insurance companies, provident funds and retirement funds,¹¹ and provisions relating to the supervision of product and service prices. Furthermore, the Group's ability to raise funds is affected, inter alia, by relevant regulation, such as the Proper Conduct of Banking Business provisions (see below) and regulation of off-bank credit, such as the regulation adopted by the Capital Market Commissioner following the Hodek Committee's recommendations. The Company is affected by developments in anti-trust laws or the application thereof, mainly in those segments where operations are of a significant scope. The Company may further be affected by the adoption of proposals made in the past year to impose restrictions on holding companies in Israel. For more information, see Section 1.26.8 below.

The Company and several of its investee companies are affected by the Proper Conduct of Banking Business Regulations issued by the Supervisor of Banks in Israel. These regulations include, among other things, restrictions on the scope of the loans that Israeli banks can grant to "single borrowers", and the six largest borrowers and the largest "borrower group" in the banking corporation (as these terms are defined in the aforesaid regulations). Accordingly, the scope of the loans issued to the Group's companies and the controlling shareholder in the Company may, under certain circumstances, affect the ability of the Group's companies to borrow additional amounts from banks in Israel.

The Company and its investee companies are also affected by the Government of Israel's policies in various matters (e.g. – monetary policies), and by the requirements of authorities monitoring environmental quality. Furthermore, significant increases in the minimum wage in Israel, other material changes to the labor laws applicable in Israel or strikes or industrial unrest can affect the financial results of the Company and its investee companies.

In October 2010, the Prime Minister of Israel appointed the Committee for Increasing Competitiveness in the Economy ("the Committee"), which was charged with examining the effects of the present structure of the Israeli economy. Following this examination, the Committee was charged with recommending policy measures, including legislative amendments and various actions.¹² In October 2011, the Committee published its draft recommendations ("the Draft Recommendations"). After public feedback and hearing the response of public representatives and various leading figures from the industry and academia, in February 2012 the Committee published its final recommendations. These recommendations focus on three topics: The conditions for

¹¹ On December 30, 2010, the Ministry of Finance Commissioner of the Capital Market, Insurance and Savings ("the Commissioner") granted Mr. Yitzhak Sharon (Tshuva), the controlling shareholder in the Company, a permit for controlling and holding the means of control in an insurer - The Phoenix Holdings Ltd. and its subsidiaries. This permit includes provisions for maintaining certain holdings in The Phoenix Holdings, as well as limitations on the sale or transfer of control blocks and the issue of means of control, as defined in the Supervision of Insurance Law, in the Company, The Phoenix Holdings, and The Phoenix Holdings subsidiaries. The permit also includes various provisions for reporting to the Commissioner, which pertain to changes in holdings in The Phoenix Holdings and its subsidiaries, provisions concerning the holding in trust of control blocks in The Phoenix Holdings, keeping the control blocks in The Phoenix Holdings and its subsidiaries free of all encumbrance, except for those cases detailed in the permit, and Delek Investments' obligation to supplement the equity of the insurance, pension and provident fund companies controlled by The Phoenix Holdings.

¹² From the letter of appointment for the Committee for Increasing Competitiveness in the Economy, attached to the draft recommendations submitted by the Committee for Increasing Competitiveness in the Economy, Ministry of Finance website - <http://www.mof.gov.il/Lists/List26/Attachments/291/2011-1111.pdf>.

allocating public assets; real and financial holdings; and control through a pyramid holdings structure. For information on the Committee's recommendations' effects on the Group's operations in general and on insurance operations in particular, see Section 1.21 and Section 1.12.2(d) below, respectively.

1.6.5 Developments in the Israeli economy

As a material part of the Group's business takes place in Israel, economic developments in Israel materially affect the results of the Group's operations. These developments stem, inter alia, from economic, political and security conditions in Israel. Below is a brief description of trends, events and developments in the Company's macroeconomic environment that have, or are expected to have, an impact on the Group.¹³

General - The Israeli economy, which showed great fortitude in the face of the economic crisis of 2008 as compare to such developed nations as the US and the Eurozone, continued growing in 2010, albeit at a more moderate pace. In 2011, the economic growth rate continued to level out. The Israel market recorded notable growth in GDP, an increase in private consumption, recovery from the economic crisis in most industries, a decrease in unemployment, and lower than expected government deficit.

Israel Central Bureau of Statistics estimates indicate a 4.5% growth in product in 2010, and 4.8% growth in 2011. Among the factors driving the sharp increase in the economic growth rate in 2010 was the increased spending in both private and public sectors. Private consumption saw a marked increase in consumption of durable goods, with investments in fixed assets showing an increase in investments in roads, public buildings and infrastructures. Growth in 2011 was driven by investment in fixed assets, while spending on private consumption grew at a moderate pace and exports, excluding diamonds and start-up companies, showed only minor growth. The downturn in Israeli export activities results from the Eurozone crisis and the global economic slowdown. Imports were also down significantly, mainly of consumer products and raw materials. In 2011, public consumption expenditure went up 4.5%, following a 2.5% increase in 2010, while private consumption expenditure went up 4%, as compared to an increase of 5.3% in 2010.

The Bank of Israel's inflation reports for the second half of 2011, indicate that in contrast to other leading economies around the world, the Israeli economy responded quickly to the expansionary policies implemented by economic policymakers. By the end of the second quarter of 2010, economy and wages were already nearing their pre-crisis levels from 2008. In the second half of 2011, the Israel Consumer Price Index remained static, and after accounting for seasonal influences - increased by a modest 0.4%. This slight increase in the Consumer Price Index was mostly driven by housing and apartment costs. The main factors contributing to slowing down the rate of increase in the Consumer Price Index were food, education and culture, and transportation and communications. In 2011, the inflation rate stood at 2.2% - close to the middle of the target inflation range (as compared to upper-range figures in 2010). The Consumer Price Index, excluding housing costs, increased by only 1%. In the second half of 2011, the Eurozone debt crisis worsened significantly, which adversely affected real economic activities and led to a sharp increase in risk on the global financial markets. The economic slowdown in Europe spread to other developed nations, and to emerging markets as well, and these markets reacted by implementing expansionary monetary policies, primarily by reducing interest rates. On the other hand, economic data in the US improved, but the US economic growth rate remained relatively low compared to pre-crisis levels in 2008.

In 2011, the government's current balance yielded a deficit of NIS 20.2 billion, as compared to a deficit of NIS 17.7 billion in 2010. This increase in the current government deficit in 2011 reflects a 6.4% increase in current revenues, following a 9.2% increase in 2010. Revenue growth in 2011 reflects an increase in tax revenues (mainly through taxes on income). Total tax revenues grew by 6.7% in 2011, following a 9.6% increase in 2010.

Employment and unemployment - The relatively rapid economic growth recorded in Israel from the second half of 2009 has also resulted in expanded employment in the commercial sector, and reduced unemployment rates. This trend continued throughout 2010, with employment rates in most industries rising back to pre-crisis levels or higher. In 2011, the main indices in the labor market stabilized, the average salary rose, and the gap in production became smaller. These data

¹³ The data in this section is based primarily on official publications, including the following: preliminary estimates of the national accounts for 2011, Central Bureau of Statistics, December 29, 2011; Q2 2011 Inflation Report, Bank of Israel; Recent Economic Developments, January-September 2011, Bank of Israel.

are in contrast to the US and Eurozone economies, where unemployment rates remained close to 9% and 10%, respectively.

Exchange rate - After a 5% revaluation in the effective exchange rate in the first half of the year, the trend reversed in the latter half, with a 4.7% devaluation. In general, the surplus that has existed in the current budget in Israel since 20 strengthens the New Israel Shekel. At the same time, payment balance data for capital imports to Israel in 2010 showed an increase in foreign investment in short term loans and deposits in local banks. These caused an increase in the effective exchange rate for the NIS. Due to the need to increase the Bank of Israel's interest rate, which broadened the interest rate differences and made the shekel more attractive, the Bank of Israel made large-scale purchases of foreign currencies, aimed at weakening the shekel. These purchases pushed the country's foreign currency balances to record highs. As of December 2010, Israel's foreign currency deposits amounted to USD 70.9 billion, as compared to USD 59 billion in December 2009. In 2010, the USD-NIS exchange rate fluctuated greatly, with the NIS gaining strength versus the USD by 5.7% and by 13.3% versus the EUR, in annual terms. The main factors for the NIS' devaluation in 2011 are the deficit in the country's current payments balance, the closing gap in the risk-adjusted interest rate in Israel and abroad, and continued implementation of regulatory initiatives.

Interest rate - Starting September 2009, the Bank of Israel began slowly and intermittently raising the interest rate in the market from its record low of 0.5%. At the end of 2010, the interest rate rose to 2%, and in February-March 2011 it was again raised by another 0.5% to 2.5%. This interest rate still represents a negative real interest rate, which creates distortions in the allocation of resources in the market in the short-medium term. In the third quarter of 2011, the Bank of Israel halted its interest rate increases, implemented from mid-2009, and in the final quarter of 2011 began reducing interest rates. The Bank of Israel reduced its interest rate by 0.25 of a percentage point each month from October through December, with the Bank of Israel interest rate standing at 2.75% at year's end. The Bank of Israel continued reducing interest rates after the reporting period, and lowered its interest rate by another 0.25 of a percentage point in February 2012.

1.6.6 Global economic developments¹⁴

2010 was marked by continued global recovery, with developed and developing nations still showing marked differences in their growth rates. In the second half of 2011, the Eurozone debt crisis deteriorated significantly. Economic growth data showed more moderate growth in key economies, while economic growth in the US stabilized at a very moderate rate. The slowdown in economic activity followed an extended period of recovery from the 2008 financial crisis. Towards the end of 2011, the slowdown in economic growth rates reached the emerging markets, although growth rates in these economies remained high when compared to developed nations. The relative weakness in the US and Europe, and the escalation of the European debt crisis, postponed monetary restrictions, which early assessments expected in 2010. This means that these countries continued implementation of expansionary monetary policies, while other countries which weathered the crisis in a more favorable manner (such as Israel, China, India, Australia, etc.), began implementing contractionary monetary policies. The crisis in Europe in the second half of 2011 caused a downturn in real economic activity, and a sharp rise in risk on the global financial markets. The economic slowdown in Europe spread to other developed nations, and to emerging markets as well, and these reacted by implementing expansionary monetary policies, primarily by reducing interest rates. In contrast to economic developments in Europe, the US posted surprising good data showing real economic growth. However, growth in the US remained low when compared to pre-crisis levels from 2007-2009. Developed markets have not yet shown signs of significant recovery in the labor markets, and unemployment rates in these economies remain high. In the US, unemployment went down from its start of year level of 9% to 8.5% at year's end. Concurrently, a gradual increase is expected in real salaries. Data from the US show a recovery in real economic activity, and actual data exceeded forecasts. Despite these favorable signs, growth was mainly driven by public-sector demand and by the Federal Reserve's monetary policies, primarily aimed at easing conditions in the credit market - lowering credit costs by buying medium- and long-term bonds, and increasing supply by introducing liquidity to the financial markets. In contrast, the Eurozone saw a significant slowdown in real economic activity in the second half of 2011. The main risk for growth forecasts in the Eurozone is due to the possible development of a

¹⁴ Data in this section is based primarily on official publications, including the following: H2 2011 Monetary Policy Report, Bank of Israel; Economic Developments in the Market, Appendix to the State Budget for 2011-2012, Ministry of Finance, Economics and Research Division.

severe financial crisis, which would deepen the recession and cause another downturn in global economic growth rates.

In contrast to most developed nations, developing nations posted solid growth throughout most of 2011, led by China where growth reached 10%. However, the global economic slowdown reached these markets towards the end of the year.

In the fourth quarter of 2010 the US Federal Reserve launched another expansionary initiative to purchase USD 600 billion in government bonds (QE2), which continued into 2011. This initiative was accompanied by an expansionary fiscal program based on tax cuts.

Eurozone countries which experienced difficulties in repaying their public-sector debts were supported by other Eurozone countries, as well as additional countries outside the Eurozone, whose efforts allowed the recycling of these default-risk countries' debts. Some of these default-risk countries also introduced local reforms focusing on budget cuts aimed at resolving structural flaws which have existed in these countries for years. However, these measures did not reduce risk levels in the markets, and as of the date of this report, the debt crisis still hampers Europe's economic recovery.

In light of the global economic slowdown and concerns for a financial crisis, most central banks lowered interest rates in the second half of the year, following increases recorded in the first six months. In addition to interest rates, banks used other monetary measures to increase liquidity and reduce long-term yields, so as to reduce credit costs and support financial and real stability as aforesaid.

In an attempt to resolve the crisis in Europe, several countries have implemented extreme contractionary fiscal policies. The US, however, implemented expansionary fiscal policies, aimed at encouraging real economic activity. In Europe, as a prerequisite for economic support, countries were required to implement austerity measures which are liable to aggravate the economic slowdown and undermine political stability. Out of concern for an economic collapse, governments in Europe announced that they will initiate sanctions against non-compliant countries.

The US, however, continued implementing expansionary fiscal policies, aimed at encouraging real economic activity.

In 2011, riots broke out in Egypt, which led to a series of civil uprisings in other Arab countries such as Libya and Yemen. These riots caused a rise in oil prices, which later stabilized for a certain period, and then rose again following assessments that riots in Libya were not a passing incident, and may damage oil supply to the West or even endanger the global economic recovery. Furthermore, the announcement of an economic embargo of Iran also affects the global economy in general, and oil prices in particular.

For more information concerning the general economic environment and external factors that specifically affected the Delek Group's operating segments, see the description for each operating segment below.

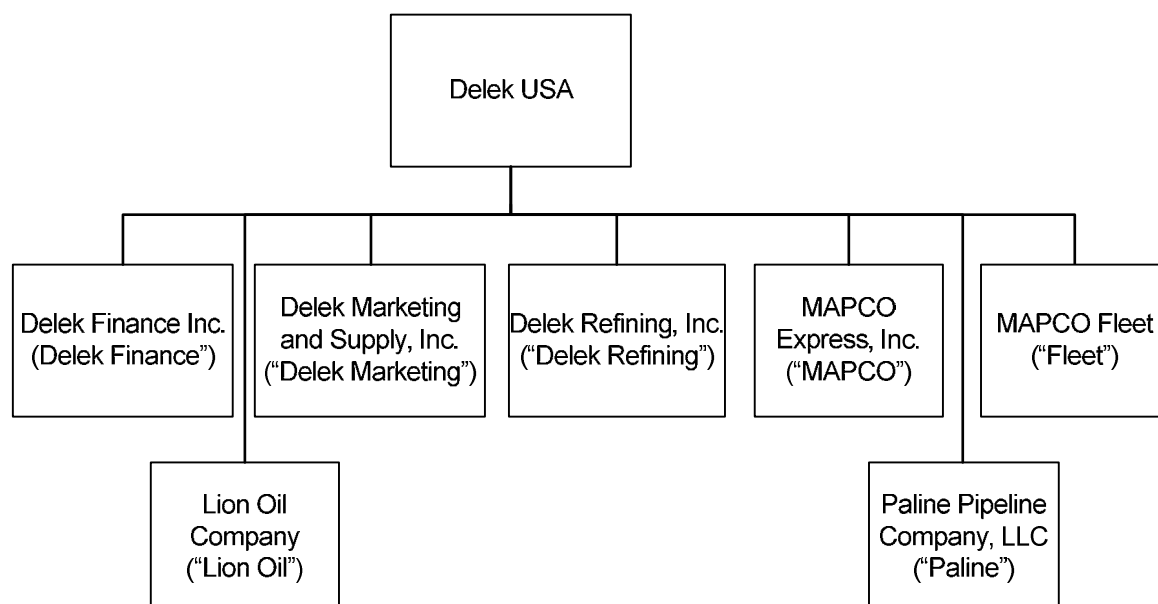
Part Three – Description of the Corporation's Business by Operating Segment

Below is a separate description of the Group's business in each of its operating segments:

1.7 Refining and Fuels in the USA

Refining and fuel operations in the USA are handled by the subsidiary Delek US Holdings, Inc. ("Delek USA"). Delek USA incorporated in Delaware in 2001, and has been registered for trade on the New York Stock Exchange since the issue of its shares in 2006. As of the date of this report, the Group holds (indirectly) approximately 68% of the shares in Delek USA. The business consists of three segments: Refining activity is conducted under Delek Refining, Inc. ("Delek Refining") and Lion Oil Company ("Lion Oil"); marketing activity is conducted under Delek Marketing & Supply, Inc. ("Delek Marketing"); and gas station and convenience store activity is conducted under MAPCO Express, Inc. ("MAPCO"). All said companies are wholly owned by Delek USA.

The following is a diagram of the structure of the principal holdings in the Group's US operation:



The following is information on high and low closing price (in USD) of Delek USA shares on the NYSE in 2010 and 2011 and until shortly prior to the reporting date:

Period	High		Low	
	Date	Price (in USD)	Date	Price (in USD)
2010	March 10, 2010	8.44	May 21, 2010	6.06
2011	July 22, 2011	17.20	January 13, 2011	6.83

The closing price (in USD) of Delek USA shares on March 22, 2012 was USD 13.86. Delek USA is not restricted in the payment of dividends other than by what is set out in the applicable law.

On March 23, 2012, the Delek USA Board of Directors approved payment of a dividend of USD 5.3 million (USD 0.09 per share), to be paid on April 19, 2012.

1.7.1 General Information on Area of Activity

A. Structure of activity

Refining segment

As of the date of the report, Delek USA holds, via Delek Refining and Lion Oil, two refineries with an aggregate production capacity of approximately 140,000 barrels a day, which produce a variety of petroleum products for use in the transportation and industry sectors. The refinery in Tyler, Texas has a maximum production capacity of approximately 60,000 barrels per day ("Tyler Refinery"). The Tyler Refinery purchases most of its raw materials from suppliers in East and West Texas, and sells the fuel products it produces to a variety of local customers, primarily Lion Oil, whose shares were acquired by Delek USA in batches beginning in 2007. A private company, Lion Oil operates an oil refinery in El Dorado, Arkansas with maximum production capacity of close to 80,000 barrels.¹⁵ Lion Oil also owns three crude oil pipelines, two fuel pipelines, a 600-mile network of pipes to collect petroleum and three refined petroleum marketing terminals in Nashville and Memphis, Tennessee, and El Dorado, Arkansas, through which it supplies petroleum to third parties, including Delek USA, which operates 180 gas stations and convenience stores in these areas.

On December 19, 2011, Delek USA acquired all of Paline's share capital from Ergon Terminaling Inc. ("Ergon") for payment of USD 50 million, of which USD 25 million was in cash and the balance a three-year loan. Paline owns and operates a 10-inch, 185-mile pipeline system that runs between Nederland, Texas and Longview, Texas, with a transport capacity of 36,000 barrels of crude oil a day and which was used under the previous ownership to transport crude oil originating on the Gulf Coast to East Texas. Delek USA is currently working to reverse the flow of the pipeline from East Texas to the Gulf Coast in light of the agreement Paline signed with one of the large energy companies in the US to lease the pipeline to the energy company through the end of 2014.

What is refining?

Oil refining is a process whereby the various components of crude oil are separated and then converted into products such as gasoline, diesel oil, and the like. The refining process includes a number of main phases, including separation processes in which the crude oil is separated into groups of products; fractionalization processes which change the chemical composition of the separated materials to obtain products with a higher added value; refining processes whose purpose is to purify and cleanse the products created during the separation process; and finishing processes whose purpose is to make the products compatible with the standards and specifications demanded by law or pursuant to agreements with specific customers (for example: adding fuel additives). It should be noted that the crude oil market and the refined fuel products market are commodities markets, that is to say, markets where there is standardization of commodities and their trading.

Marketing segment

Complementary to the refining activity, Delek USA is engaged in marketing, in other words, the purchase of fuel products (gasoline and diesel) and marketing them to end users through a petroleum pipeline and petroleum refining terminals. To this end, Delek Marketing markets the fuel products in the following ways: (1) transportation of fuel products through seven pipelines and from the petroleum refining terminals to trucks; (2) direct sales of fuel products to third parties through three sales terminals to trucks owned by Delek USA: in San Angelo, Abilene, and Tyler, Texas and through third-party terminals in Aledo, Odessa, Frost and Big Springs, Texas and through other terminals located along the Magellan pipeline (see below); (3) supply of fuel products in swap transactions at terminals in Abilene, San Angelo and Aledo, Texas; (4) marketing services to Delek USA's petroleum refinery in Tyler for wholesale sales and sales under sale agreements; (6) an arrangement with Delek USA's refinery in Tyler, whereby

¹⁵ Through 2011, Delek USA held 34.6% of the shares in Lion Oil Company ("Lion Oil"), which were acquired in 2007. On March 17, 2011, Delek USA entered into an agreement with Ergon Inc. ("the Sellers") for the purchase of an additional 53.7% of the shares in Lion Oil, for cash payment of USD 50 million, allocation of shares and Delek USA will extinguish all debt currently owed by Lion Oil to the Sellers, such that after the purchase Delek USA will hold 88.3% of Lion Oil's shares. The transaction was closed on April 29, 2011. For additional information regarding the purchase agreement, see the Immediate Report dated March 21, 2011 (Reference No. 2011-01-085755) and the Immediate Report dated May 1, 2011 (Reference No. 2011-01-132471), the details of which are included by way of reference. In October 2011, Delek USA acquired the remaining minority interests in Lion (11.7%), which had been held by a consortium of private investors for USD 13 million, which was paid in cash.

Delek Marketing receives 50% of the wholesale margin over a level agreed by the parties. (6) an arrangement with Delek USA's Tyler Refinery, whereby Delek Marketing receives payment for transportation and storage of crude oil in pipelines and storage tanks under its ownership and that are located near the Tyler Refinery. Delek Marketing also owns containers for the storage of a total of approximately one million barrels of fuel products. For information about Delek Marketing's assets, see Section 1.7.9B below.

All the fuel products are supplied to Delek Marketing in accordance with two main supply agreements: the first with Noble Petro, for the supply of up to 20,350 barrels a day, and the second with Magellan for the supply of up to 7,000 barrels a day. For details of these petroleum purchase agreements, see also Section 1.7.12B below.

Fuel Products and Convenience Stores in the USA - MAPCO

This activity is performed by MAPCO and covers the marketing and distribution of fuel and oil products, as well as the operation of gas stations and convenience stores (generally both are operated on the same site). As of December 31, 2011, MAPCO operated 377 gas stations and convenience stores in seven states in the southeastern US (Tennessee, Alabama, Georgia, Arkansas, Virginia, Kentucky and Mississippi) and another 67 gas stations are operated by third parties. For additional information, see Section 1.7.9(C)(1) below.

The gas stations and convenience stores are operated under the brands of MAPCO Express®, MAPCO Mart®, Discount Food Mart™, Fast Food and Fuel™, Delta Express®, East Coast® and Favorite Markets®, with the branded stations selling fuel products of BP, ExxonMobil, Conoco, Shell Marathon.

Over the past three years, MAPCO has reopened, upgraded and improved about 48% of the stores in the different states, so that they conform to the MAPCO Mart® brand, including introducing premium products, convenience products and opening fast food restaurants. It plans to continue to do so for additional stores in 2012. In 2011, Delek USA invested USD 23.4 million in upgrading 53 stores.

B. Economic Environment and Influence of External Factors

Delek USA is exposed to trends, events and developments in the fuel market in the areas of its US operation that impact or could impact its activities and the activities of its competitors, including:

fluctuations in the global prices of crude oil, gasoline, natural gas and energy prices in general and specifically in Delek USA's area of operations. The crude oil that Delek USA purchases as part of its refining activity is the main cost component of the fuel products produced by the refinery. The price of crude oil is dictated by oil prices on the international markets. An increase in the price of crude oil can lead to an increase in the prices of fuel products, resulting in decreased demand for oil and fuel products. Delek USA cannot necessarily incorporate a rise in crude oil prices in the price of fuel products it manufactures, and this could have an adverse effect on its refining margin and Delek USA's results. This is especially true for products such as asphalt, which is produced at the refinery in El Dorado, as its price does not change in correlation with the fluctuations in the prices of crude oil.

In 2010 and 2011, approximately 25.8% and 17.4%, respectively, of the crude oil purchased for the Tyler Refinery was supplied by local suppliers in East Texas. Most of the crude oil for the Tyler Refinery from East Texas is transported in a pipeline owned by Delek USA. The rest is purchased from suppliers in West Texas. In 2011, approximately 68.7% of the crude oil purchased by the refinery in El Dorado was from sources on the Gulf Coast or imported to the US, and 33.2% from local sources and West Texas, including through the local collection system in the area of Arkansas and in neighboring areas.

1. Fluctuations in global fuel prices - Prices of the fuels produced, purchased and sold by Delek USA are influenced by various factors, including changes in the global and local economic conditions, demand for Delek fuel products in the USA, the worldwide political conditions, particularly in significant oil-producing regions (the Middle East, the former Soviet Union, West Africa and South America), production levels of crude oil and petroleum distillates in the USA and worldwide, development and marketing of fuel substitutes, interruptions in supply lines, local factors including market and weather conditions, output at competing refineries and US regulations. A rise in global fuel prices causes a rise in the prices of products sold by MAPCO, may reduce demand for these products, as well as hurt MAPCO's profit on every product sold. In 2011, a substantial increase was recorded in revenues from fuels compared to 2010. In 2010 as well, an

increase in revenues from fuels relative to 2009 was recorded. The marked rise in 2011 was attributable, among other things, to the fluctuation in fuel prices, growth in the output of the Tyler Refinery and the addition of the activity of the refinery in El Dorado to the refining activity results. The average price of a barrel of crude oil from West Texas in 2011 was USD 95.07; in 2010, it was USD 79.50 as opposed to USD 71.22 in 2009.

2. The economic situation and downturn - Most Delek Refining products are for the transportation industry (vehicles and airplanes). An economic downturn in the USA could reduce demand for flights as well as traffic on the roads, thus both reducing demand for the Refinery's petroleum products and the refining margin (as defined in Section 1.7.1C below). An economic slowdown may also have a negative impact on MAPCO operations, and in fact, the economic crisis in the United States led to a general decline in demand for fuel products and retail products in the convenience stores.
3. Legislative restrictions, regulatory developments - Delek USA and particularly Delek Refining are subject to the provisions of laws, regulations and standards stipulated by the competent authorities in its segment of operation, at the federal, state and local levels, primarily in terms of environmental protection and standardization. Also, see details in Section **Error! Reference source not found.** below.
4. Refining capacity - The strict environmental protection regulations applicable to fuel products such as gasoline and diesel for transportation, could limit the maximum potential and expansion of the existing facilities and harm the refining capacity of Delek Refining. Such standards could compel Delek Refining to upgrade its existing facilities and to add new facilities in order to adapt its product basket to demand. It should be noted that in recent years there has been significant growth in the demand for oil distillates. The growth in demand was met by increasing exploitation of global refining capacity and adapting it to the level of demand and to the increasingly strict standards governing the production of fuel products. Historically, increases in demand have led to cycles of increased profitability, which in turn have led to investments that have made it possible to increase supply. This then led to periods of surplus production capacity and a decline in the industry's profitability.

C. Changes in volume and profitability of activity

Refining segment

Oil products such as those produced by Delek USA are traded on international markets, making the prices of its products prone to extreme daily fluctuations. Delek USA therefore enters into agreements with its customers on the basis of a price formula that reflects the changes in market prices.

Results in the refining industry are influenced and measured by the difference between the prices of petroleum distillates and the prices of crude oil, which is known as the refining margin. The refining margin is the difference between the cost of the crude oil (including costs of transportation, insurance, unloading, storage, and transporting to the Refinery), and the consideration from the sale of the refined product mix.

The relevant refining margin for the Tyler Refinery is known as the US Gulf Coast 5-3-2 Spread ("**5-3-2 Spread**"), which measures the difference between the price for a three fifths of a barrel of US Gulf Coast Pipeline 87 Octane Conventional Gasoline - CBOB and two fifths of a barrel of US Gulf Coast Pipeline No. 2 Heating Oil, and the price of five fifths of a barrel of light crude oil, WTI, as quoted on the New York Mercantile Exchange for supply in the following month.

The fluctuations in the energy markets continued in 2011. The 5-3-2 Spread on the US Gulf Coast in 2010 averaged USD 7.93 a barrel, and in 2011 averaged USD 22.98 a barrel. In 2011, the actual refining spread of the Tyler Refinery, plus the marketing fee between the companies, was USD 7.55 a barrel in 2010, and in 2011 was USD 18.47 a barrel.

At this point, given the complexity of the operation and the range of types of oil and products at the El Dorado Refinery, it is not possible to determine the refining spread relevant to its operation. In fact, in 2011, the actual refining spread of the El Dorado refinery, as of the date of acquisition by Delek USA on April 29, 2011, was USD 9.02 a barrel. In the first quarter of 2012, through March 22, 2012, the average 5-3-2 spread was USD 23.1 a barrel, and the average price of crude oil was USD 102.5 a barrel.

The refining margin is influenced by a number of variables:

1. Crude oil prices.
2. Changes in local and international economic conditions.
3. Volume of local and international demand for fuel products.
4. Global refining capacity.
5. The ability of the members of the Organization of Petroleum Exporting Countries to maintain oil prices and production controls.
6. Speculative supply and demand that impact on prices on the commodities market.
7. Changes in the global geopolitical situation, particularly in the oil-producing regions such as the Middle East, West Africa, the CIS (the former Soviet Union) and South America.
8. Local and foreign production levels of crude oil and fuel products and the level of crude oil, other raw materials and fuel products imported into the United States.
9. Utilization levels of refineries in the US and around the world.
10. Development and marketing of alternative fuel products such as ethanol and biodiesel.
11. Stoppages or disruptions in supply to the refineries and distribution channels.
12. Local factors, such as market conditions, climate changes, and activity level of refineries and pipelines in the market.
13. Margin between oil originating in West Texas and oil from the Gulf Coast.
14. Flexibility and ability to open and change the direction of flow of oil and fuel pipelines.
15. Government legislation.

The Refinery's product basket is influenced by the types of crude oil it purchases and by the Refinery's facilities which influence the refining technology. The Tyler Refinery produces mainly "white" products": in 2010 and 2011 some 96% and 95.7%, respectively, of the Tyler Refinery's products were white products (i.e. products that are not fuel oil, such as gasoline, diesel or jet fuel), and the remainder are heavy products and others. Since only the last factor can be influenced by the Refinery, and it is not central to determining the refining margin, profitability in refining activity is more dependent on changes in the global market than on the actions of Delek Refining. In 2011, the El Dorado Refinery produced 78% "white"¹⁶ products such as low-sulfur gasoline and diesel, and the remainder are heavy and other products, including asphalt.

The basket of oil products is refined from crude oil, and the refinery has a marginal ability to influence this basket through the quality of the processed raw material and the manufacturing processes. Lacking the ability to have a significant influence on the product basket, taking into account the level of demand and product prices, there is no significance from the refinery's point of view in relating to the gross profit of a single product, and refineries are judged by the refining margin obtained from sales of the product basket.

It should also be noted on this matter that the ability of a refinery to reduce the amount of refined heavy products by increasing the number of "white" products is measured by the Nelson Complexity Index ("Nelson Index"). The higher the Index, the greater the refinery's ability to produce more "white" products. In addition, the compatibility of the refinery's production should be examined against demand in its area of activity. The Tyler Refinery's current rank on the Nelson Index is 9.4 compared to 9.0 for the El Dorado Refinery. According to data published in the Oil & Gas Journal, the Nelson Index range for refineries in the Gulf of Mexico region is between 1 and 16.9. The acquisition of the El Dorado Refinery in April 2011 more than doubled the refining capacity, but also increased Delek USA's exposure to said fluctuation.

The El Dorado Refinery is equipped with a crude oil processing unit that has production capacity of 100,000 barrels a day. The average annual output for crude oil production varies depending on the economy and market demand as well as other physical limitations that impact on daily output or the refinery's actual use. On the date of Delek USA's acquisition, production capacity of the El Dorado Refinery (as opposed to the crude oil processing unit) was approximately 80,000 barrels a day. The El Dorado Refinery produces a wide array of

¹⁶ The foregoing refers to the 247 days Delek USA operated the El Dorado refinery.

various grades of gasoline, ultra-low sulfur diesel, LPG, propylene and a variety of asphalt products.

For changes in revenues and profitability of Delek USA activities, see Section 1.7.3 below.

D. Competitive structure

For changes in revenues and profitability of Delek USA activities, see Section 1.7.6 below.

E. Critical success factors

Delek USA estimates that the following are the key success factors:

Delek Refining and Marketing -

1. Level of refining margin.
2. Selection of the optimal mix of types of crude oil and identification of supply sources.
3. Availability of capital and operational availability of the refining facilities.
4. Fuel terminal and refinery location – The Tyler Refinery is the only one in a 100-mile radius that offers a range of petroleum distillates. The El Dorado Refinery has access to the Enterprise Products Pipeline System, which is a main transport system that runs from the Gulf Coast to the Midwest. This is a key factor in marketing the products of the El Dorado Refinery and enables access to the fueling terminals owned by Lion Oil in Memphis and by third parties in the Midwest.
5. Optimization of supply chain and production.
6. Ability to comply with product standards and changing regulatory requirements and to adapt the Refinery to these standards.
7. Possibility of using the existing pipeline infrastructure in the areas of operation for transporting fuel products, and the ability to expand the use of this pipeline infrastructure.
8. Synergy between Delek Refining and Delek Marketing.

Gas stations -

1. Widespread deployment of gas stations and convenience stores in MAPCO's area of operations.
2. Financial strength enabling the purchase of new gas stations and convenience stores, investments in setting up new stations and refurbishing and expanding existing stations.
3. Integrating convenience stores and retail centers into gas station spaces.
4. Title to the property on which the gas stations are built.
5. Efficient information systems that provide information in real time for management, inventory, pricing, sales and security.
6. Volume of mixing ethanol with the fuels marketed by MAPCO, which increases the retail fuel margin.

F. Changes in supplier and raw material chain

Delek USA purchases crude oil from a large number of suppliers in East Texas, West Texas, the Gulf Coast and through imports, and it is not dependent on any single supplier. Delek Marketing purchases fuel products from two main suppliers - the Noble Group (which was assigned the rights of Northville, which was a supplier in the past) and Magellan. MAPCO has several suppliers, the largest of which in 2011 was Valero, from which it purchased 17% of its fuel products compared with 20.4% from Motiva in 2010. For more information, see Section 1.7.12 below.

G. Alternatives and technological changes influence the activity of Delek USA

In light of the changes in crude oil prices in recent years and due to issues regarding environmental protection and the range of energy sources, governments world over are examining long-term plans for a partial transition to alternative energy and various companies throughout the world are trying to develop energy alternatives to oil and fuels. As of the date of this report and until such time as efficient and inexpensive energy solutions are found, Delek USA does not anticipate a significant drop in demand in the areas in which it operates due to said alternatives, in the foreseeable future.

The information in this section regarding Delek USA's assessment is forward-looking information. This information is based on general information about the hitherto relatively slow rate of development in the transition to alternative energy, as well as on the continuing demand for oil. The information may not materialize if, *inter alia*, there are significant developments in the development of alternative energy solutions, if greater resources are invested in finding such solutions, or governments decide to enforce or promote incentives for the transition to energy alternatives.

H. Entry and exit barriers

Key barriers to entry are the following:

1. The capital required and the high costs associated with the acquisition, construction and operation of fuel facilities (refineries, oil pipelines, gas stations) at the required standards.
2. The need for significant credit sources to finance the purchase of petroleum products and convenience stores.
3. Competition with other gas companies and retail chains in all the areas of their operation, and against small competitors with lower costs of operation.
4. Existing regulatory restrictions in the sector, including legislation and regulations in planning, construction and environmental protection.
5. The limited capacity of the existing pipeline infrastructures, which in many cases are at full output and make it difficult for new competitors from entering the area of activity.

The following are the key entry barriers:

1. The value and purpose of the various facilities.
2. Environmental implications for the property on which the facilities are located, which may limit other possible uses.
3. Existence of long-term lease/operation contracts with land owners.

1.7.2 Products and services

A. The products marketed by Delek Refining include the following fuel products:

Delek USA's refineries in Tyler, Texas process light sweet crude oil, while medium sour crude oil can be processed in El Dorado. Both of the refineries produce a variety of products that primarily include fuel products for transportation, including gasoline and diesel, while in Tyler diesel and gasoline for jets is also produced. A smaller segment of the products includes residual products, including in El Dorado: Asphalt for paving roads and roofing flux, and additional products used in industry. The volume of refining at the El Dorado Refinery is greater than the volume of refining at the Tyler Refinery.

The breakdown of production in 2011 was as follows:

The Tyler Refinery:

- Gasoline – In 2010 and 2011, gasoline accounted for approximately 56.3% and 54.3%, respectively, of all the products produced by the Tyler Refinery. The Tyler Refinery produces three different types of gasoline, including premium, regular, aircraft fuel and E-10 products, which contain 90% regular gasoline and 10% ethanol.
- Diesel and jet fuel – In 2010 and 2011, diesel and jet fuel accounted for approximately 36.9% and 37.7%, respectively, of all products produced by the Refinery. Delek Refining produces diesel and jet fuel in accordance with the military standard (JP-8), fuel for civilian jet planes, low sulfur diesel and ultra low sulfur diesel.
- Petrochemical products – The Tyler Refinery produces small quantities of propane, propylene and butane.
- Other products – The Refinery produces small quantities of other products, among them coke, slurry oil, sulfur and other mixtures.

It should be noted that the profitability of white products and diesel is relatively higher.

The El Dorado Refinery:¹⁷

- Gasoline – In 2011 gasoline accounted for 41.8% of all El Dorado Refinery products. The El Dorado Refinery produces different types of gasoline, including premium, regular, and E-10 products, which contain 90% regular gasoline and 10% ethanol.
- Diesel – In 2011 diesel accounted for 33.6% of all El Dorado Refinery products.
Petrochemical products, LPG (Liquid Propane Gas) and NGLs (Natural Gas Liquids) - The El Dorado Refinery produces small quantities of petrochemical products, constituting 5.9% of total production.
- Asphalt products - Asphalt and asphalt products made up 18.7% of all El Dorado Refinery products. The El Dorado Refinery produces asphalt for paving roads and roofing flux.
Delek USA does not believe that over the coming year there will be material changes in the product mix of the refineries.

B. The products marketed by Delek Marketing include the following oil products:

- Gasoline – In 2010 and 2011 the various types of gasoline accounted for some 44.7% and 43.9%, respectively, of all the products marketed by Delek Marketing. Delek Marketing markets two different types of gasoline with the addition of ethanol (E-10) (premium - 93 octane and 87 octane).
- Diesel – In 2010 and 2011 the various types of diesel accounted for some 55% and 55.7%, respectively, of all the products marketed by Delek Marketing. Delek Marketing markets ultra low sulfur diesel.

C. Fuel products marketed by MAPCO:

- Various types of gasoline – Used as fuel in vehicles with gasoline engines and sold mainly at gas stations.
- Diesel - used mainly in diesel-powered vehicles as well as for heating and industry.
- Gasoline blended with ethanol - E10 products (gasoline blended with ethanol).

D. Retail products marketed by MAPCO:

Various retail products are sold at the convenience stores. The main products are tobacco products (mostly cigarettes), beer, soft drinks, food (including ready-to-eat products), candy, snacks and many other products, including MAPCO's own private label products. Some of the stores sell lottery tickets and money orders, and operate ATMs. Alcohol and tobacco account for approximately 55% of MAPCO sales.

1.7.3 Breakdown of revenues by products and services

- A. The table below shows the amount and percentage of Delek USA's revenues from the sale of material products or services in each of its areas of operations:

Refining segment¹⁸

	The product	Total sales in USD millions	% of Delek USA revenues	% of Group revenues
2011	Gasoline	2337.9	32.48%	14.14%
	Diesel	1,662.5	23.10%	10.06%
	Other	621.5	8.63%	3.76%
2010	Gasoline	979.3	26.1%	8.54%
	Diesel	651.6	17.4%	5.68%
	Other	52.4	1.4%	0.46%

¹⁷ The data are in respect of the 247 days in 2011 that Delek USA operated the El Dorado Refinery

¹⁸ The information regarding the refinery relates to the 247 days that Delek USA operated the refinery.

Delek Marketing

	The product	Total sales in USD millions	% of Delek USA revenues	% of Group revenues
2011	Gasoline	297.8	4.14%	1.80%
	Diesel	404.9	5.63%	2.45%
	Other	13.6	0.19%	0.08%
2010	Gasoline	211.3	5.6%	1.84%
	Diesel	272.5	7.3%	2.38%
	Other	20.6	0.5%	0.18%

MAPCO

	The product	Total sales in USD millions	% of Delek USA revenues	% of Group revenues
2011	MAPCO fuels	1,484.8	20.63%	8.98%
	Products Retail and other	375.2	5.21%	2.27%
	Total	1,860.0	25.84%	11.25%
2010	MAPCO fuels	1,208.2	32.2%	10.54%
	Products Retail	384.1	10.2%	3.35%
	Total	1592.3	42.4%	13.89%

- B. The following table provides the amount and percentage of gross profit from the sales of material products or services by Delek USA in each of its areas of operation in 2010 - 2011:

	2011			2010		
	% of Group revenues	% of Delek USA revenues	USD million s	% of Group revenues	% of Delek USA revenues	USD million s
Refining	24.52	73	564.7	7.73	40	136.4
Marketing	1.37	4	31.5	1.57	8	27.7
MAPCO fuels	2.97	9	68.4	3.96	20	69.9
Retail products	4.85	15	111.6	6.64	34	117.2
Other	-(0.34)	(1)	(7.9)	-(0.48)	(2)	(8.5)
Total	33.37	100%	768.3	19.42	100	342

1.7.4 Trade receivables

A. Delek USA

As a rule, no single customer accounts for over 10% of Delek USA sales, and Delek USA is not dependent on any single customer.

B. Delek Refining

Acquisition of the complete holdings in Lion Oil expanded the customer base in East and West Texas to local customers located to the northeast of El Dorado as well.

The Tyler Refinery

The Tyler Refinery markets its fuel products to about 100 customers, including large fuel companies, independent refineries, fuel distributors, gas station operators, utility and

transportation companies, independent retailers and the US government.¹⁹ Agreements with the large fuel companies are usually made on the basis of an annual purchasing agreement, where the sale price of the fuel products is a function of the prices of fuel products traded on the Gulf Coast. Sales to other customers are usually on an occasional basis and at a fuel product price set by Delek Refining ex-works. In 2010 and 2011, sales to the Tyler Refinery's largest customer (a leading energy company) accounted for 11.9% and 12.6% of Delek Refining's net sales, respectively. The ten largest customers of the Tyler Refinery accounted for 63.8% and 61.1% of the Tyler Refinery's sales in 2010 and 2011, respectively.

The El Dorado Refinery

The El Dorado Refinery markets most of its products through direct terminals to marketers in the areas of Arkansas, Memphis and north towards Chicago. The connection of the El Dorado Refinery to the Enterprise Products Pipeline System, which is, as aforementioned a main transportation system that runs from the Gulf Coast to the US Midwest, is a key factor in the marketing of El Dorado Refinery's products and facilitates access to the refueling terminals owned by Lion Oil and by third parties in the Midwest, close to the system. Most El Dorado Refinery's sales are done on a cash basis at a large number of terminals along a third-party fuel pipeline, at the price of the fuel products determined by Delek USA each day. Sales to El Dorado Refinery's largest customer accounted for 6.9% of the refinery's net sales in 2011. The ten largest customers of the El Dorado Refinery accounted for 28.3% El Dorado Refinery's net sales in 2011.

C. Delek Marketing

Delek Marketing sells its products to 100 customers, primarily in West Texas, among them large oil companies such as Exxon Mobil, independent refineries such as Murphy Oil, petroleum agents, companies in the service and transportation sectors and others. In 2010 and 2011, sales to Delek Marketing's largest customer (Susser) accounted for 15.6% and 21.3% of Delek Marketing's net sales, respectively. The ten largest customers accounted for 57.6% and 61.3% of Delek Marketing's sales in 2010 and 2011, respectively.

D. MAPCO

MAPCO's principal customer group (approximately 95%) is a group of private consumers who purchase fuel products or retail products at the gas stations and convenience stores. In addition, MAPCO markets fuel products to 67 stores operated by third parties.

1.7.5 Marketing and distribution

A. Delek Refining

Delek Refining products are marketed on a wholesale basis mainly to third parties located in the East Texas area and northeast of El Dorado, including the core markets in Texas, Arkansas and Tennessee.

The Tyler Refinery - Most of the Tyler Refinery's sales are done directly from the Refinery, through the Refinery's supply terminal which has nine lanes, enabling the addition of a wide variety of petroleum additives, including special additives which are sold to the main oil companies that purchase fuels from the Refinery and E-10 products. The Refinery sells coke primarily through railway cars or tankers. The Refinery is connected to a pipeline for the sale of propane.

The El Dorado Refinery - The marketing ability of the El Dorado Refinery is mainly based on the aforementioned connection to the Enterprise Products Pipeline System that runs from the Gulf Coast to the Midwest and provides it access to third parties near said transportation system.

B. Delek Marketing

Delek Marketing sells fuel products through three terminals it owns in West Texas (Abilene, Tyler and San Angelo). The Abilene and San Angelo terminals are connected to each other as well as to a nearby air force base and to a system of pipelines owned by Magellan through seven different pipelines owned by Delek Marketing. In addition, Delek Marketing sells products through four terminals owned by a third party.

¹⁹ The expiration date of the agreement with the US government for the supply of jet fuel is March 31, 2012, and there is no certainty that Delek USA will be awarded the contract for the supply of jet fuel, as aforementioned, for the following year. Total sales under said agreement accounted for 2.9% of the Tyler Refinery's net sales.

Delek Marketing is dependent on the flow infrastructure of Magellan in Texas, since all its products are marketed directly and indirectly (by swap transactions in volumes that are not material) via this pipeline system.

Delek Marketing also holds a 65-mile long storage and transport system for oil in East Texas, which is responsible for moving crude oil to the Tyler Refinery, and its pumping stations and terminals are operated by Delek Marketing.

C. MAPCO

Marketing in gas stations - MAPCO promotes its products and services in a number of ways: regional campaigns and special offers at specific gas stations, and the use of sales promotions. MAPCO also advertises in the media.

Agreements for the purchase of branded fuels - In about 45% of MAPCO-operated gas stations, MAPCO is bound by exclusive agreements with the fuel companies – Marathon, Exxon Mobil, Conoco, Shell and BP for the purchase of fuel products and the use of their brand names. These agreements are for periods of one to 15 years and are at various stages of their lives. On the basis of these agreements, MAPCO can benefit from the marketing efforts and brand strength of the above companies. The agreements to purchase branded fuels were signed as part of the agreements for the purchase of the gas stations. Since the stations can be converted to operate under the MAPCO name, termination of the agreements is not expected to materially influence its operations. MAPCO does not believe it is dependent on any particular supplier.

Brands of convenience store products - MAPCO operates the gas stations and convenience stores under various brands, as described in Section 1.7.10. Between 2008-2011, MAPCO reopened, upgraded and improved approximately 48% of the stores in the various states, to adapt them to operate under the MAPCO Mart® brand. As of December 31, 2011, MAPCO operated 81 fast food restaurants, including 49 under branded chains, including Quiznos®, Subway®, Krispy Krunch Chicken®, and Blimpie®.

1.7.6 Competition

A. Refining and marketing activity

The fuel refining and marketing segment is highly competitive and includes national and international fuel companies operating in various oil-related businesses, including oil exploration, production, refining and marketing of fuel products and operation of convenience stores. The main competitors in refining activity are local refineries in the Midwest and on the Gulf Coast, operators of terminals for the supply of fuels in those areas.

Delek Marketing's competitors are mainly owners of other independent terminals and other fuel companies operating in its segment of operation in West Texas. The competition is expressed mainly in location, price and the range of products and services sold. The costs of transporting the products from the fuel terminals to the end customer limit the geographic size of the market of fuel customers for whom it is economical to purchase from Delek Marketing's fuel terminals. The two main markets of the fuel marketing operation are in West Texas, in the Abilene and San Angelo areas. In the Abilene area, there is direct competition from another refinery that markets fuel products through another fuel terminal. In the San Angelo area there is no competition with the fuel terminal of Delek Refining, with the nearest competitor being located 90 miles from the terminal.

The competition in the refining and marketing operations is affected by the price paid for raw materials, production margins, refinery efficiency, the mix of products produced by the refinery, as well as transportation and distribution costs. Some of the competitors with the refining operation operate larger and more complex refineries than Delek USA, in various geographic regions, and their production costs per barrel may be lower or the price at which they purchase oil may be lower. Furthermore, some of the competitors with the refining and marketing operations are large, international corporations, and some are also engaged in oil exploration and production, allowing them to refine crude oil they own and leverage the advantages inherent in economies of scale. The refining and marketing operations also compete with other energy industries (wind, solar and hydropower) that provide alternative energies to fuel. Delek USA's refining and marketing operations have a negligible share in the sale of fuels in Texas. In its refining operation, Delek USA copes with competition in its segment of operation through location (geographical proximity to some of the fuel purchasers that facilitates a reduction in the cost of shipping and competitive prices or proximity to the Enterprise Products Pipeline System), selection of product mix in response to demand, and

streamlining at the refineries. In additions, the Tyler Refinery has access to suppliers in West Texas, on the Gulf Coast and foreign crude oil at relatively competitive prices.

In addition to foreign crude oil and oil originating on the Gulf Coast, the El Dorado Refinery has limited access to oil from West Texas and access via a system of pipelines for collection of locally sourced sour crude, generally at a discounted price compared to the crude oil purchased by the refinery from other sources.

Delek Marketing copes with competition in its segment of operation through location (geographical proximity to some of the fuel purchasers), cost-cutting and selection of product mix to suit demand.

As stated above, the crude oil and refined fuel product markets are commodity markets, i.e. markets where there is standardization and constant trading. Consequently, the main factors influencing the competitiveness of the Refinery and the fuel terminals include:

1. The location of the Refinery (relative distance from refineries or other terminals) and its accessibility to customers give it an advantage with customers located in its area of operation.
2. The location and accessibility of fuel terminals for local customers.
3. The output of the refineries.
4. Constant monitoring and improvement of product quality so that they comply with the standards, norms and specifications required by law and by customer demand.
5. Selection of the optimal mix of types of crude oil and identifying sources of supply, particularly in light of the fact that since the beginning of 2011, crude oil originating in West Texas is much less expensive than similar crude oil from foreign sources or the Gulf Coast.

B. MAPCO activity

To the best of MAPCO's knowledge, it is one of the five companies with the largest number of gas stations in the areas of its operation in Nashville, Chattanooga and Memphis (Tennessee) and in northern Alabama. The two other large companies in Nashville are Daily's, Exxon and Kroger. The two other large companies in Memphis are Couche Tard and Exxon Tigermarkets. The other two large companies in northern Alabama are Murphy Oil and Pantry. The other large company in eastern Tennessee and northern Georgia is Pantry.

MAPCO has many competitors, primarily the large fuel companies, independent convenience store chains, drugstores, fast-food chains and large supermarket chains such as Wal-Mart whose market share is large compared to MAPCO, and which also market fuel products and oils. MAPCO's convenience stores operate under several brands, and MAPCO plans to continue branding some of its stores under the MAPCO Mart brand in the coming years. MAPCO markets its products to customers who happen to visit the gas stations. MAPCO also operates a fuel credit card service through a subsidiary, but this is insignificant in scope. MAPCO does not have accurate data regarding its market share and that of its competitors.

Competition in gas stations and convenience stores is mainly local, from rival gas stations, convenience stores and businesses in the region. This competition is expressed mainly by competition for location, ease of access, price, range of products and services offered, customer service, branded fuels, store appearance, cleanliness, safety and regular supply.

The following is a description of the main ways MAPCO copes with the competition and factors affecting its competitive status:

1. Expanding its deployment of gas stations and convenience stores in its areas of operation, as well as in adjacent areas. The high concentration of MAPCO gas stations in its areas of operation allows it to be an influential player in the local market and to operate with a relatively small and efficient staff.
2. Expanding its range of products and product quality, in accordance with identified market trends. MAPCO also offers ready-to-eat food products at its convenience stores under brands such as Krispy Krunchy Chicken®, Blimpie®, Subway®, Quizno®, GrilleMarx® (its signature brand), and at present 81 stores offer this service.
3. Investing in improving its information technology, including investments in computerization and management software. The use of information systems to manage the supply, inventory and security systems is designed to achieve efficient management,

including proper pricing of products on a daily basis, taking into account the data of each station, identifying demand and keeping appropriate levels of inventory.

4. Most of MAPCO's gas stations are located in relatively central locations in its areas of operation, which increases ease of access to them.

1.7.7 Seasonality

The demand for gasoline products is generally higher in the summer than in the winter months, due to seasonal increases in vehicle traffic in the summer, although the demand for all types of diesel products is higher in the winter. In addition, historically, the refining margin in the first and fourth quarters of the year is usually lower than in the second and third quarters. Consequently, the operating results of Delek USA are usually lower in the first and fourth quarters. Below is a table showing the average 5:3:2 Spread in the Gulf of Mexico region, in USD, by quarter:²⁰

	Q1	Q2	Q3	Q4
2011	17.54	23.14	30.8	20.34
2010	6.62	9.54	7.45	8.09

1.7.8 Production capacity

- A. The Tyler Refinery's maximum production capacity when operating is approximately 60,000 barrels per day, depending on the raw material processed and its sulfur content. In 2011, the Tyler Refinery refined about 22 million barrels of oil and other raw materials, averaging approximately 60,520 barrels a day over 365 days. In 2010, the Tyler Refinery refined about 19.8 million barrels of oil and other raw materials, averaging approximately 54,286 barrels a day over 365 days. Below is a table listing the products produced by the Tyler Refinery in 2010-2011 (in millions of barrels) and the average daily output of barrels in each year:*

	2010		2011	
	Quantity*	Daily Output**	Quantity*	Daily output
Gasoline	11	30,019	11.8	32,407
Types of diesel	7.2	19,669	8.2	22,521
Other	1.3	3,635	1.74	4,769
Total	19.5	53,323	21.8	59,697

- B. Maximum production capacity of the El Dorado Refinery is 80,000 barrels a day. In the 247 days Delek USA operated the El Dorado Refinery, the refinery refined an average of 80,054 barrels of oil and other raw materials a day. Below is a table listing the products produced by the El Dorado Refinery in the 247 days that Delek USA operated the refinery in 2011 (in millions of barrels) and the average daily output of barrels in each year:*

	2011	
	Quantity*	Daily output
Gasoline	8.3	33,231
Types of diesel	6.6	26,726
Asphalt	3.6	14,820
Other	1.1	4,666
Total	19.6	79,443

* Based on the 247 days that Delek USA operated the El Dorado Refinery.

- C. In 2010 and 2011, Delek Marketing sold some 5.2 million and 5.65 million barrels of oil distillates, respectively, which is an average of 14,354 barrels a day and 15,493 barrels a day, respectively, according to the following breakdown:

²⁰ The 5:3:2 refining margin influences the operations of both of Delek USA's refineries.

	2010		2011	
	Quantity	Daily output	Quantity	Daily output
Gasoline	~2.3	6,419	~2.5	6,815
Types of diesel	~2.9	7,888	~3.15	8,632
Others	-	47	-	46
Total	~5.2	14,354	~5.65	15,493

It should be clarified that for the most part Delek Marketing does not sell fuels produced by Delek Refining.

Investments

Investments in the refining segment can be divided into three main types: discretionary projects, maintenance and turnaround work, as outlined in Section 1.7.9 below, and regulatory investments (mainly for environmental protection), as set out in Section 1.7.17 below. The investments in MAPCO activity are divided into investments in maintenance and various improvements (rebranding, expansion, etc.). Below is a breakdown of investments for 2010 - 2011 and forecast for 2012 (in USD millions):

Capital expenditures	2010	2011	Forecast for 2012
Refining segment	42.3	36	74.7
Marketing segment	0	0.6	0.5
MAPCO	14.4	36.6	29.5
Other	0.1	5.8	8.0
Total	56.8	79	112.7

For details of anticipated environmental investments, see Section 1.7.17F below.

The investments in convenience store activity reached USD 36.6 million in 2011 and are planned to reach USD 29.5 million in 2012. Of the planned investments, USD 7.8 million is for rebranding of about 20 existing stores, USD 12 million for construction of 12 stores in new locations and USD 2.1 million in respect of increasing and/or improving profitability of existing stores. This information regarding the costs of the expected investment is forward-looking information, based on Delek USA's plans for the coming year, and it may change should there be changes in the investment plan, regulatory delays in receipt of the required permits and approvals and the like.

1.7.9 Property, plant and equipment, and facilities

A. Delek Refining assets

The refining facilities in Tyler, Texas are located on land owned by Delek Refining on a contiguous area of 2.428 sq km, of which 405 sq km are built up. Delek Refining's facilities include refinery units, fractionalization processors, additional production units (coker), a sulfur treatment plant, infrastructure facilities (buildings, storage tanks, pipes, etc.) and service facilities (including tanker trucks). Additionally, Delek Refining also owns four terminals for crude oil intake and pumping stations.

The refining facilities in El Dorado include refinery units, fractionalization processors, hydrogen production units, a sulfur treatment plant, infrastructure facilities (buildings, storage tanks, pipes, etc.) and service facilities (including tanker trucks). Additionally, Lion Oil owns an 80-mile Magnolia to El Dorado crude oil transportation system that runs between Shreveport, Louisiana and the Magnolia Terminal, west of the El Dorado refinery; a 28-mile crude oil transportation system that runs from the Magnolia Terminal to the El Dorado Refinery; two associated product pipelines; a crude oil gathering system with a 600-miles of pipeline; three "white" product distribution terminals located in Memphis and Nashville, Tennessee and in El Dorado, Arkansas; and an asphalt distribution terminal located in El Dorado, Arkansas.

As part of its refining activity, Delek USA performs regular maintenance work on the refineries on an average of once every three or five years and in two stages. The division into two stages was designed to enable the refinery to operate on a partial basis and avoid shutting

down for over a month. In 2009, Delek Refining completed multi-year maintenance work, turnaround, at a total cost of USD 52.5 million. The cost of maintenance, including turnaround, in 2010 was USD 6 million and USD 13.7 million in 2011. Delek USA estimates that the next round of scheduled multiyear turnaround work at the Tyler and El Dorado Refineries will be in 2013 or 2014. The work is generally performed in two stages. Each stage requires about 14-21 days, during which the refinery works at reduced capacity. Below is a breakdown of the Refinery's investments in ongoing maintenance (including work in accordance with a multi-annual turnaround plan, which includes a regular investment in the refinery's facilities and equipment) in 2009, 2010, 2011 and a forecast for 2012 (in USD millions):

2009	2010	2011	2012 (forecast)
52.5	6	13.7	20.5

On November 20, 2008, an explosion rocked the Tyler Refinery, resulting in a fire. Two employees were killed and others injured. The causes of the incident are being investigated concurrently by several organizations, including an internal investigation by Delek USA, the Occupational Safety and Health Administration (OSHA), and the Chemical Safety Board (CSB) and the US Environmental Protection Agency (EPA). In May 2009, OSHA completed its investigation and issued an announcement recommending that Delek USA be fined USD 0.2 million. Delek USA is appealing this and does not believe that the result will have a material impact on its business. Although Delek USA cannot with certainty predict the final result of legal actions, investigations and other claims against it, including possible fines or other enforcement actions, it does not expect the current proceedings to have a negative impact on its business standing. Said estimate is forward-looking information, based *inter alia* on Delek USA's estimates and assumptions regarding the enforcement of the relevant agencies, amount of damage caused to employees and third parties, and the labor laws that mandate compensation to employees by the state. Said information may not materialize, if the enforcement agencies, employees or third parties that incurred damage act differently and initiate new legal action, or the results of the existing legal proceedings are different than said assessment. Operations at the refinery resumed in May 2009, as normal. As of December 31, 2010, Delek USA had recognized revenues from insurance payments of USD 141.4 million over the three years prior to this year, and the receipt of additional payments in respect of the 2008 insurance claim is not expected.

B. Delek Marketing assets

As of December 31, 2011, Delek Marketing owns two refined petroleum product terminals in Abilene and San Angelo; seven pipelines of approximately 114 miles in length, for transporting fuel products between the refining terminals in Abilene and San Angelo, Texas, which include a line connecting Delek USA's facilities to Dyess Air Force Base. Storage tanks with a total shell capacity of more than one million barrels; approximately 65 miles of crude oil lines that transport crude oil to the refineries; the entire pipeline system is deployed on leased property. Alternatively, Delek USA has priority right to use these lands.

In the past several months, Delek USA has completed three strategic acquisitions of logistical assets in its areas of operation. As aforementioned, in December 2011, Delek acquired a 300 km pipeline for the transport of crude oil that runs from East Texas to the Gulf Coast "Paline," for consideration of USD 50 million. Additionally, in January 2012, Delek Marketing acquired a 55 km pipeline for the transport of crude oil that runs from the Tyler Refinery to Delek's storage sources in the Nettleton, Texas area, for consideration of USD 12 million. In addition, in February 2012, Delek Marketing acquired a 32 km pipeline for the transport of fuels and a terminal for the marketing of produces in the area of the Tyler Refinery for USD 11 million.

C. MAPCO assets

1. As of December 31, 2011, MAPCO owned 222 gas stations and convenience stores, and it leased/rented another 167 assets, most through long-term contracts of up to 25 years with an extension option. MAPCO operates 377 gas stations and convenience stores itself, and it leases approximately 12 gas stations and convenience stores to third parties.

The following table shows the ownership rights of MAPCO in the gas stations as of December 31, 2011:

State	Number of MAPCO operated stations	No. of stations owned by third parties and not owned or rented by MAPCO	Number of stations owned	Number of leased or rented stations	Number of stations with leases with less than 3 years to run**	Number of stations with leases with more than 3 years to run**
Tennessee	205	17	117	92	31	61
Alabama	85	33	57	33	7	26
Virginia	8	--	--	8	--	8
Arkansas	12	--	8	4	3	1
Kentucky	3	--	1	2	1	1
Mississippi	2	--	2	--	--	--
Georgia	62	5	37	28	16	12
Total	377	55	222	167	58	109

** Including options to extend the lease/rental term, as of December 31, 2011.

Most of the lease agreements stipulate that MAPCO will pay property taxes, insurance and station operating costs. For those lease/rental agreements that will end within three years, MAPCO estimates that it can negotiate to extend the agreements for their operation under acceptable terms, if requested to do so. There are two types of lease agreements, and in most of them MAPCO is responsible for construction of the station and installation of the filling equipment, which it owns. Under these agreements, MAPCO rents the land and is liable for environmental claims connected with its activities. In some of this type of rental agreements, MAPCO is responsible for removing underground filling equipment at the end of the rental term. In other cases, MAPCO rents the land as well as the filling equipment and existing structures. In these agreements, MAPCO also bears liability for environmental claims connected with its activities. From an operational standpoint, in the case of an external operator of a station in which MAPCO has the proprietary right (ownership or leasing/rental), either the external operator pays rent or they share the margin created from the fuel sales. In the case of an external operator of a MAPCO station in which it has no proprietary right, MAPCO supplies these operators with fuel products only. Revenues from the stations operated by third parties amounted to 5% of MAPCO sales.

MAPCO owns a fleet of trucks and tankers that deliver approximately half of the fuel sold at its stations.

In 2007 MAPCO began rebranding some of its convenience stores under the MAPCO Mart brand and continued this in 2009-2011, when it refurbished 22, 13 and 51 stores, respectively. Over the past three years, a total of 85 stores have been refurbished and 20 more are expected to be refurbished in 2012. MAPCO believes that this step, alongside the refurbishment and redesign of its stores, will lead to an expansion of its customer base. For additional information regarding the expected costs of investment in 2012, see Section 1.7.8C above.

1.7.10 Intangible assets

Delek USA has registered or submitted applications to the US Patent and Trademark Office to register various trademarks, trade names and service marks for use in retail fuel and convenience stores. Delek USA owns the following trademarks registered with the US Patent and Trademark Office: MAPCO®, MAPCO MART®, MAPCO EXPRESS & Design®, EAST COAST®, GRILLE MARX®, CAFÉ EXPRESS FINEST COFFEE IN TOWN MAPCO & Design®, GUARANTEED RIGHT! MAPCO EXPRESS & Design®, FAVORITE MARKET®, FLEET ADVANTAGE®, DELTA EXPRESS®.

Although MAPCO has not registered or applied to register the mark DISCOUNT FOOD MART™ and FAST FOOD AND FUEL™ with the US Patent and Trademark Office, MAPCO believes that the use of this mark enjoys the specific legal protection afforded to marks which are not registered. The rights to use the brand name MAPCO are restricted to the fuel products and convenience store activity. Delek USA believes that the use of the MAPCO brand is an important component in the success of its MAPCO activity, and it intends to expand the use of the aforementioned brand.

1.7.11 Human capital

- A. In 2011, the number of people employed in the refining segment and at Delek USA headquarters grew as a result of the acquisition of the shares and addition of Lion Oil activity. At the same time, the number of people employed by MAPCO declined, in view of the lower number of stores it operated. The following table outlines the employee headcount of Delek USA in 2010 and 2011:

Delek USA	Dec. 31, 2010	Dec. 31, 2011
Delek USA - HQ	61	83
Refining segment:		
Tyler	254	272
Lion Oil		580
Total refining segment	254	852
Marketing Segment		
Pipeline - Tyler (under marketing segment)	8	10
Fuel marketing	14	14
Total marketing segment	22	24
MAPCO		
Company headquarters	124	125
Regional headquarters	78	60
Fuel distribution	45	45
Stores and gas stations	2,811	2,612
Total MAPCO	3,058	2,842
Total Delek USA	3,395	3,801

- Investments in training – Delek Refining and Delek Marketing conduct safety training for all employees. Employees participate in seminars and professional training. Delek Refining and Marketing invest resources in the professional training of operation and maintenance personnel in their areas of occupation, while safety training is provided to all employees pursuant to relevant laws.
 - With the exception of several executives, refining and marketing employees do not have personal employment contracts. As of December 31, 2011, approximately 370 refining employees are members of unions and are governed by a collective bargaining agreement.
 - Most MAPCO employees are offered the opportunity to participate in a number of plans that include social benefits, medical insurance and life assurance, which includes insurance for work disability.
- B. Executive Officers
- About ten executive officers are employed under personal agreements and in addition to salary are entitled to various benefits such as grants, reimbursement of expenses, options in accordance with the compensation plan set out below, etc.
 - In accordance with the long-term incentive policy of 2006 ("Compensation Plan"), as amended, Delek USA may grant its employees, consultants, officers and others various types of options, including restricted stock units or share-based rights of up to 5,053,092 options (jointly, "the Options"). In 2009, employees and officers were offered the option to replace the Options with new options for the purchase of fewer shares at a lower exercise price. Following the replacement, most of the options vest over a period of 4 years. The condition for exercise of the Options is the continuous provision of services to Delek USA through exercise. As aforementioned, Options were allotted under the Compensation Plan for Delek Refining employees (except for temporary workers and unionized employees), MAPCO managers (up to the regional manager level), officers and directors of Delek USA.

Payroll expenses related to the stock options plan (as included in the financial statements of Delek USA) in 2010 and 2011 amounted to USD 3.1 million and USD 2.7 million. In the year ended December 31, 2010, no Options were exercised, and in the year ended December 31, 2011, 312,912 Options were exercised.

3. On February 21, 2010, Mr. Uzi Yemin, President and CEO of Delek USA, exercised the last 1,319,493 Options held by Delek USA, granted to him in the employment agreement dated May 1, 2004. As a result, Mr. Yemin was issued 638,909 shares, and 680,584 were canceled. As of December 31, 2011 Mr. Yemin held 6,444,009 shares of Delek USA and stock appreciation rights with respect to 1,850,040 shares of Delek USA. As of December 31, 2011, the shares and Options (included those that had not yet vested) constituted 4.2% of Delek USA shares. In September 2009, Delek USA entered into a new employment contract with Mr. Yemin for a period through October 31, 2014. For information about the terms of Mr. Yemin's employment, see details in accordance with Standard 21 in Part 4 of the periodic report.

1.7.12 Raw materials and suppliers

A. Delek Refining

The main raw material used in the refining segment of operation is crude oil. The market for crude oil and products is a commodities market, which is sophisticated and has a high level of negotiability in both the physical arena and in futures trading, executed on stock exchanges or with large international entities. Delek USA purchases its crude oil from various suppliers in the US.

The Tyler Refinery

Below is a chart showing the breakdown of crude oil purchased by Tyler Refinery in 2010 and 2011:

Source	2010	2011
Crude oil from East Texas	25.8%	17.4%
Crude oil from West Texas	71.7%	82.6%
Other	2.5%	—
Total	100%	100%

In 2011, all the crude oil that was processed by the Tyler Refinery originated in Texas, with one fifth from East Texas in close proximity to the refinery, and the rest from West Texas. The refinery usually enters into agreements with 10 to 15 suppliers, although there is nothing to prevent it from entering into agreements with additional suppliers. In 2010 and 2011, the largest supplier supplied the refinery with some 13,000 and 11,000 barrels a day, respectively (accounting for about 25% and 19% of its crude oil purchases in 2010 and 2011, respectively), and its agreements with that supplier are on a monthly basis or agreements that are automatically renewed each month. The balance of its crude oil purchases from suppliers is performed a spot basis, and not on the basis of long-term transactions. The refinery is not dependent on one specific supplier since it has access to the crude oil markets in West Texas and on the Gulf Coast. The refinery purchases oil in East and West Texas based on the economic profitability of processing the different kinds of oil.

The El Dorado Refinery

The El Dorado Refinery is adapted to mainly process a combination of medium sour crude. Below is a chart showing the breakdown of crude oil purchased by the El Dorado Refinery in 2011:*

Source	2011
Crude oil from the Gulf Coast	56.1%
Local crude oil / and crude oil from Texas	33.2%
Foreign crude oil	10.7%
Total	100%

* Based on the 247 days during which Delek USA operated the El Dorado Refinery.

In 2011, 56.1% of the crude oil processed at the El Dorado Refinery originated in the Gulf Coast, 33.2% from West and East Texas and sources nearby the refinery, which are transferred to the refinery through the collection system in the Arkansas area. The El Dorado Refinery purchased approximately 69% of the crude oil from BP. As local producers rely on the pipeline that belongs to Lion Oil to transport the oil, it is more advantageous for the El Dorado Refinery to purchase local crude oil than crude from West Texas.

B. Delek Marketing

In 2011, Delek Marketing purchased 96.8% of all fuel products purchased from two suppliers under two, different long-term agreements. The first agreement was with Noble Petro, and pursuant to which Delek Marketing may purchase up to 20,350 barrels per day for the supply of fuels to the terminals in Abilene and San Angelo, at a price that is a function of the price on the US Gulf Coast and the price in the Abilene region. This agreement is runs through December 31, 2017. The second agreement is with Magellan, and enables Delek Marketing to purchase up to 7,000 additional barrels of fuel products per day, to be supplied to terminals in Aldo, Odessa and Dallas, Texas, and is valid through December 14, 2015. The second agreement also stipulates Delek Marketing's right to use the pipeline infrastructure for transporting Magellan fuels at a tariff set in the agreement, which is a function of the price of the basic product in the Gulf Coast region. Delek USA is dependent on Magellan which owns, as aforementioned, the pipeline infrastructure and terminals used by Delek Marketing for its operations.

C. MAPCO

1. Suppliers of fuel and oil products - MAPCO purchases fuel products from suppliers in its areas of operation. The main fuel supplier in 2010 was Motiva, and in 2011, it was Valero, from which MAPCO purchased 20.4% and 17.0% of fuel consumption, respectively. Additionally, MAPCO purchases additional fuel products from other suppliers, including ExxonMobil, Conoco, Shell, BP and other independent suppliers. MAPCO's supply agreements are for an initial period of between one and 15 years, and generally include minimum monthly or annual purchase quotas.
2. Suppliers of retail products - In 2011, MAPCO purchased about 59.1% of the retail products it sells, including tobacco products and grocery items, from Core-Mark International, Inc. ("Core-Mark"). The engagement with Core-Mark is valid through December 31, 2013. In addition, MAPCO purchases significant amounts of retail products from Coca-Cola, Pepsi-Cola, Frito Lay and others. For details, see Section 1.7.19B below.

1.7.13 Working Capital

A. Inventory maintenance policy for crude oil and finished products

1. Delek Refining and Marketing

It is the policy of the refining sector to maintain an inventory of crude oil (the raw material) and fuel products (the finished product) at a level that ensures continuous supply of fuel products and fulfillment of its obligations to customers. The following are the main factors influencing the size of the inventory:

- Need for a minimal inventory required to fill the lower part of the tanks and pipelines.
- Need to maintain a large number of types of crude oil for the refining of various mixtures.
- Condition of the crude oil market and the oil products market and Delek Refining's estimate regarding the level of expected demand for its products and its production capability.

As part of its refining and marketing activity, Delek USA holds in the refineries, various terminals and third-party facilities, inventories of crude oil, fuel mixtures and distillates whose value changes according to the state of the global economy, the level of inventory on the local and global markets, and seasonal conditions. The following is a breakdown of the total inventories in the refining and marketing operations, including the average price at the end of 2010 and 2011:

	Dec. 31, 2011*			Dec. 31, 2010		
	Av. price per bbl (\$)	Quantity (in bbl M)	Total value (\$M)	Quantity (in bbl M)	Av. price per bbl (\$)	Total value (\$M)
Delek Refining ²¹	66.6	1.2	81	4.6	95.2	437.8
Delek Marketing ²	101.2	0.082	8.3	0.088	117.31	10.3
Total	68.9	1.282	89.3	4.688	95.58	448.1

*Including inventory balance at El Dorado as of this date.

2. MAPCO

Average inventory days for MAPCO is generally no more than five days for fuel products and 30 days for retail products. The value of the inventory as of December 31, 2010 and December 31, 2011 was USD 48.6 million and USD 45.0 million, respectively.

B. Credit Policy

1. Customer credit: Customers of the refining and marketing sector are given between 3 – 15 days' credit (10 days on average), except transactions for the sale of asphalt, in most of which they are extended credit of up to 30 days. Total credit to customers as of December 31, 2010 and December 31, 2011 was approximately USD 86 million and USD 253 million, respectively. MAPCO policy is not to extend credit to private customers. In certain cases, MAPCO has extended credit to its customers (mainly in out-of-station activity and car fleets), for insignificant amounts. The average term of credit to customers in 2010 - 2011 was 4 days.
2. Supplier credit:
 - A) Refining operation – at the Tyler Refinery, the total number of credit days Delek receives from its suppliers for the purchase of crude oil is 35 days on average (EOM + 20), usually accompanied by a bank letter of credit. Total credit from suppliers as of December 31, 2010 and December 31, 2011 was approximately USD 139 million and USD 190 million, respectively. In 2010 and 2011, supplier credit for Delek Marketing averaged 35 days.
 - B) In the refinery in Arkansas, the total number of credit days Delek receives from its suppliers ranges from minimal credit of only several days (regarding crude oil purchased through J. Aron, which undertook to provide the refinery with the credit required to purchase up to 100,000 barrels a day) and 35 days on average (EOM + 20), usually accompanied by a bank letter of credit (regarding other crude oil purchased directly from other crude oil suppliers). Total credit from suppliers as of December 31, 2011 was approximately USD 244 million about 30 days on average.
 - C) Delek Marketing - receives an average of 10-12 days' supplier credit for purchases of petroleum distillates. Total credit from suppliers as of December 31, 2010 and December 31, 2011 was approximately USD 16.3 million and USD 25.5 million, respectively. In 2010 and 2011, supplier credit for Delek Marketing averaged 12 and 13 days, respectively.
 - D) MAPCO - MAPCO receives credit from suppliers for periods of up to 30 days. In 2010 – 2011 the credit period from suppliers averaged between 13 to 20 days; however, there are some suppliers from which MAPCO receives no credit whatsoever. The credit MAPCO receives from its suppliers is more or less sufficient to finance inventory balances and customer credit.

1.7.14 **Financing**

- A. Delek USA finances its operations through bank credit, non-bank credit and independent resources.
- B. Credit facilities
 1. Delek Refining (the Tyler Refinery, including receivables of the El Dorado Refinery) - In February 2010, a new credit facility of USD 300 million (and under specific conditions up

²¹ Delek Refining's inventory contains both crude oil and fuel products for sale.

² Delek Marketing's inventory includes only fuel products for sale.

to USD 600 million) entered into effect, with a consortium of lenders headed by Wells Fargo Capital Finance ("New Credit Facility"). The New Credit Facility was increased on April 29, 2011 to USD 400 million, and validity was extended through April 2015. Its main purpose is to support the Tyler Refinery's working capital needs and the customers (receivables) of El Dorado. The New Credit Facility bears interest according to fixed, predetermined pricing grid, providing a choice between base rate loans or LIBOR-based interest plus a margin, with the initial margin set at LIBOR + 3% or Prime + 1.5%. The ability to borrow against the New Credit Facility is determined according to a calculation included in the credit agreement. As of December 31, 2011, Delek Refining had used USD 227.8 million for the issue of letters of credit for the purchase of crude oil. As of March 13, 2012, Delek Refining had used USD 218 million for the issue of letters of credit. To secure the facility, a charge was placed on the current assets of Delek Refining, including the receivables of the El Dorado Refinery.

2. Delek Marketing - Delek Marketing has a credit facility raised in December 2006 through an American bank (Fifth Third) and secured by assets, which it uses for current operations and for purchases of fuel products. The terms have been amended several times since. The credit facility is currently for up to USD 75 million (of which up to USD 35 million for letters of credit), valid through December 19, 2012. The credit facility bears interest according to a predetermined pricing grid and allows Delek Marketing to choose between LIBOR-based interest and interest based on the prime interest rate. Current interest at the end of 2011 had a weighted average of 3.9%. As of December 31, 2011, Delek Marketing had used USD 30.3 million (of the credit facility) and in addition issued letters of credit for a total of USD 10.5 million and as of March 13, 2012, Delek Marketing had used USD 32 million and in addition issued letters of credit for a total of USD 12 million. To secure the facility, a charge was placed on all Delek Marketing assets.
3. MAPCO - In 2010, MAPCO had a credit facility of USD 108 million from a consortium headed by a US bank (Fifth Third). In December 2010, the credit agreement was amended and extended through December 23, 2015, and the credit facility was increased to USD 200 million and, under specific conditions, up to USD 275 million. The facilities bear interest according to a predetermined pricing grid, which enable MAPCO to chose between base interest and LIBOR-based interest + interest of 2.25% - 4%, as stipulated in the agreement. The average interest rate as of December 31, 2011 was 4.3%. As of December 31, 2011, MAPCO had used USD 77.5 million of the aforementioned facility (including letters of credit amounting to USD 19 million), and as of March 13, 2012, approximately USD 96 million. (in addition to letters of credit amounting to USD 19 million). To secure the facility, a charge was placed on the assets of MAPCO Express and its subsidiaries.

C. Loans

Bank loans

Delek Finance - Delek Finance received two loans from an Israeli bank (Israel Discount Bank of New York), as follows:

1. A loan of USD 30 million, to be repaid on December 31, 2013, with interest of LIBOR + 4.5% or minimum interest of 5%.
2. A loan of USD 20 million, to be repaid on December 31, 2013, with interest of LIBOR + 4.5% or minimum interest of 5%.

As of December 31, 2011, the balance of the loans in respect of Delek Finance's two loans was USD 42 million and the average interest rate was 5.1%. Under the terms of the loans, payments on the principal of USD 2 million will be made quarterly, as of the end of the fourth quarter of 2011, and the balance of the consideration at the end of the term. The loans are secured by a charge on the shares of Lion Oil and a charge on two of Lion Oil's assets. As of the reporting date, the balance of the loan amounted to USD 42 million.

3. Delek USA was extended a loan of USD 50 million in November 2010 by an Israeli bank (Bank Leumi USA), following which the previous loans for the same total amount were canceled. Under the terms of the loan, payments on the principal of USD 2 million will be made quarterly, as of the end of the second quarter of 2011, and the balance of the principal at the end of the loan term, on October 1, 2013. The loan bears interest at the greater of a fixed spread over three-month LIBOR or an interest rate floor of 5%. As of

December 31, 2011, the debt balance was USD 42.8 million, with average interest of 5%. The loan agreement was amended on April 29, 2011, following the acquisition of Lion Oil, to allow said acquisition to be reflected in the securities and financial covenants. As of the reporting date, the balance of the loan amounted to USD 40.8 million.

The three aforementioned loans require compliance with financial covenants (see below), and to secure the loans, a charge was placed on Delek USA's shares in Lion Oil and a second charge on Lion Oil's assets, with the exception of payables and inventory.

4. Lion Oil was extended a loan of USD 100 million on April 29, 2011 from Israel Discount Bank of New York and Bank Hapoalim B.M. and Bank Leumi USA. As of December 31, 2011, the debt balance was USD 95.5 million. Under the terms of the loan, Delek USA must make four quarterly principal payments of USD 1.5 million as of June 30, 2011, followed by 16 more quarterly principal payments of USD 4 million. The maturity date of the loan is April 29, 2016. The loan is secured by all the shares and assets of Lion Oil (with the exception of inventory and receivables). The interest on the loan is LIBOR-based interest or prime interest, at the discretion of Delek USA, plus relevant interest spreads, provided that the rate is no less than 5.5% annually. As of December 31, 2011, average interest was 5.5%. As of the reporting date, the balance of the loan amounted to USD 95.5 million.
5. Loans from Delek Petroleum - The 2009 loan agreement with Delek Petroleum, the controlling shareholder in Delek USA (as was amended in September 2010 and April 2011) is for USD 44 million (after USD 21 million was repaid in July 2010). Under the amended agreement, the maturity date of the loan is January 1, 2013. The loan will bear interest, payable quarterly, of 8.25% annually (excluding withholding taxes). Delek USA will bear all taxes in respect of interest payments. The maturity date and interest payments may be subject to accelerated repayment in the event of violations, as set out in the agreement. Delek USA has the right to repay the loan early, without incurring any fine or premium. As of December 31, 2011, the loan balance was USD 26.5 million. As of the reporting date, the balance of the loan amounted to USD 26.5 million. Shortly prior to publication of this report, Delek USA repaid USD 14 million.
6. Subordinated note with Delek Petroleum - On April 28, 2011, Delek USA executed a Subordinated Note with Delek Petroleum in the principal amount of USD 40 million. As of December 31, 2011 and close to the date of the reporting, USD 40 million was outstanding under the secured subordinated note. The subordinated note matures on December 31, 2017 and is subordinated to the loan mentioned in Section 4 above. The maturity date may be accelerated by Delek Petroleum upon the occurrence events of default, as set out in the agreement. Interest is 7.25% per annum (net, without withholding taxes) and Delek US is responsible for the payment of withholding tax. Under the agreement, Delek is required to make quarterly interest payments commencing June 30, 2011 and annual principal payments of USD 6 million commencing June 30, 2012, with payment of the latter subject to meeting certain conditions set out in the agreement in effect between Delek Petroleum and the loan creditors, as described in Section 4 above.
7. Promissory note with Ergon Inc. ("Ergon") - On April 29, 2011, Delek USA entered into an agreement for a loan of USD 50 million with Ergon in connection with the acquisition of Lion Oil. As of December 31, 2011 and close to the reporting date, USD 50 million was outstanding under the secured subordinated note. Under the loan agreement, Delek USA is required to make annual payments of USD 10 million each, commencing April 29, 2013. The loan matures on April 29, 2017, and interest is 4.0% per annum.
8. Promissory note with Ergon Terminals Inc. - On December 19, 2011, Delek USA entered into a USD 25 million promissory note with Ergon Terminals Inc. in connection with the acquisition of Paline. Shortly thereafter, the promissory note was assigned to Ergon Inc. As of December 31, 2011 and close to the reporting date, USD 25 million was outstanding. Under the loan agreement, Delek USA is required to make quarterly payments of USD 2.1 million each, commencing March 31, 2012. The loan matures on December 19, 2014, and interest is computed at 6.0% per annum.
9. Variable interest credit

The following is a breakdown of the variable interest credit received by all entities of Delek USA from third parties (with the exception of Delek Petroleum), in accordance with

the current loan agreements as of December 31, 2011 (not including the aforementioned letters of credit):

Loan type	Change mechanism	Interest range Jan. 1, 2011 - Dec. 31, 2011	Average interest rate in 2011	Interest rate as of December 31, 2011	Loan as of December 31, 2011 (\$M)
Delek Refining credit facility - long term	LIBOR + 3.0% / Prime + 1.5%	4.75%-5.25%	5.12%	4.75%	-
Delek Marketing credit facility -	LIBOR + 2.75% / Prime + 1.75%	2.94% - 5.50%	3.87%	3.87%	30.3
MAPCO credit facility - long term	LIBOR + 3.75% / Prime + 2.75%	3.75% - 6.25%	4.48%	4.26%	77.5
Delek USA - long-term loan	LIBOR + 4.5%*	5.00%	5.00%	5.00%	42.8
Delek Finance - 2 long-term loans	LIBOR + 4.5%*	5.00%-5.08%	5.00%	5.08%	42.0
Lion - long-term loan - banks	LIBOR + 4.5%**	5.5% - 6.75%	5.54%	5.50%	95.5

*LIBOR floor of 0.5%

**LIBOR floor of 1.0%

D. Securing additional sources of finance

In light of the acquisition of Lion Oil, Delek USA increased its loans, in part by amending existing loans and also by taking new loans. Additionally, Delek Refining extended the maturity date of its credit facility by one year to finance working capital. Delek USA estimates that its current cash flow, including loans and credit agreements, will be sufficient for the next 12 months. Additional financing might be required to perform acquisitions, expenses or general financing. Should it be necessary to raise additional capital from various financing sources, Delek USA's ability will be able to raise additional financing or the terms under which it will be able to raise such is uncertain.

E. Credit restrictions

From time to time, the financial ratios of Delek USA and its subsidiaries (Delek Refining, Delek Marketing, Delek Finance and MAPCO) are close to non-compliance with the financial covenants stipulated and this, *inter alia*, due to fluctuations of Delek USA/subsidiary, amount of funds withdrawn as dividends by Delek USA, extent of leveraging of Delek USA/subsidiary and the relevant market conditions. Non-compliance with said financial covenants may lead to the significant amounts of credit Delek USA has to be called in for immediate repayment and may prevent the receipt of additional credit in accordance with the warranties of the lenders. Failure to comply with the financial covenants is therefore a risk factor for Delek USA. As of the report date, Delek USA is in compliance with all the financial covenants that apply to it and its subsidiaries, and there were no issues of non-compliance during the periods described in the report.

1. Delek Refining

Following are details of the main financial covenants with which Delek Refining is required to comply to secure the New Credit Facility described in Section 1.17.15(A)(1):

- Adjusted surplus of current assets less minimum of financial obligations ("Credit Margin") throughout the entire credit term. Delek USA provided a guarantee of up to USD 15 million to the consortium should Delek Refining fail to comply with the terms of the credit facility.
- If the credit margin is less than the higher of USD 15 million or 12.5% of the adjusted value of the base assets used as security for the loan (cash, trade receivables and inventory in transit), the following covenants shall come into effect: (1) Delek Refining must comply with a ratio (EBITDA less capital investments) / (interest expenses + planned payment of loan principal + income tax payments) greater than the amount set in Delek Refining's loan agreement; (2) There are various restrictions on the distribution of dividends and repayment of the loan to Delek USA.

- The assets of the Refinery were charged to the consortium, however should Delek Refining borrow over USD 100 million in respect of this equipment, the charge will be removed, with the exception of USD 50 million.

2. Delek Marketing

Following are details of the main financial covenants with which Delek Marketing undertakes to comply with respect to the credit facility described in Section 1.7.15(A)(2) above, short term, in the amount of approximately USD 75 million.

- Equity value will exceed USD 40.9 million.
- (EBITDA less current investments) / (interest expenses + planned payment of loan principal + income tax payments) will exceed 1.2.
- The ratio of financial debt to the cash flow from current operations EBITDA will be lower than 3.5.

3. MAPCO

In the credit facility and loans MAPCO received, as described in Section 1.7.14B.3, MAPCO warranted to comply with financial covenants, the highlights of which are as follows:

- (Total financial debt) to (EBITDA) will be lower than 3.60 from the first quarter of 2011 to the first quarter of 2012, 3.50 from the second quarter of 2012 to the third quarter of 2013, 3.40 from the fourth quarter of 2013 to the third quarter of 2014, 3.25 from the fourth quarter of 2014 to the first quarter of 2015 and 3.00 as of the second quarter of 2015.
- (EBITDA less current investments) to (interest expenses + planned payment of loan principal + income tax payments) will exceed 1.25 from the first quarter of 2011 and thereafter.
- (Total financial debt + 8 times rent) to (cash flow from current operations (EBITDA) plus rent) of MAPCO will be lower than 4.75 from the first quarter of 2011 to the third quarter of 2014, 4.50 from the fourth quarter of 2014 to the first quarter of 2015, and 4.25 as of the second quarter of 2015.
- Additionally, there are certain restrictions on MAPCO's dividend distribution, capital expenditures for growth and more.

4. Delek USA and Delek Finance

Following are details of the main financial covenants with which Delek USA and Delek Finance have warranted to comply in connection with Delek USA's and Delek Finance's credit facility and loans.

- Equity value will exceed USD 425 million.
- The ratio of equity to assets less liability to J. Aron will exceed 0.29.

In addition to said financial covenants, the credit agreements include numerous non-financial stipulations and restrictions, as is standard for such agreements, including restrictions on transfer of funds, distribution of dividends, investments, sale of assets, transactions with related parties and the like.

5. Lion Oil

Following are details of the main financial covenants with which Lion Oil has warranted to comply in connection with its credit facility and loans.

- Delek USA equity value will exceed USD 425 million.
- The ratio of equity to assets of Delek USA less liability to J. Aron will exceed 0.29.

In addition to said financial covenants, the credit agreements include numerous non-financial stipulations and restrictions, as is standard for such agreements, including restrictions on transfer of funds, distribution of dividends, investments, sale of assets, transactions with related parties and the like.

F. The following table presents the credit terms for the material loans

Loan	Lender	Original loan USD thousands	Loan as of December 30, 2011 USD millions	Interest rate	Final maturity date	Payment of interest	Annual repayment of principal (in foreign currency)	Security	Financial covenants	Financial covenants on date close to date of statement of financial position	Financial covenants on date close to date of report	Financial covenants on date examined by lender
MAPCO	Consortium	Credit facility of USD 200 million	77.5 in addition to letters of credit of USD 19 million	LIBOR + 3.75% / Prime + 2.75%	December 23, 2015	Quarterly	None	All company assets	Debt to EBITDA lower than 3.6	2.69	2.69	2.69
									Adjusted debt to EBITDA, plus rent is lower than 4.75	4.29	4.29	4.29
Delek Marketing	Consortium	Credit facility of USD 75 million	30.3 in addition to letters of credit of USD 10.5 million	LIBOR + 2.75% / Prime + 1.75%	December 19, 2012	Quarterly	None	All company assets	Debt to EBITDA lower than 3.5	1.32	1.32	1.32
									Minimum equity of 40.9 million	52.5	52.5	52.5
									Principal interest coverage and tax ratio higher than 1.2	2.91	2.91	2.91
Delek Finance	Israel Discount Bank	50.0	42.0	LIBOR + 4.5%, not less than 5%	December 31, 2013	Quarterly	USD 8 million	Lion Oil shares	Minimum Delek USA equity of USD 425 million	653.6	653.6	653.6
									Equity to adjusted assets of Delek USA is lower than 0.29	0.34	0.34	0.34
Delek USA	Bank Leumi	50.0	42.8	LIBOR + 4.5%, not less than 5%	October 1, 2013	Quarterly	USD 8 million	Lion Oil shares	Like Delek Finance	Like Delek Finance	Like Delek Finance	Like Delek Finance
Lion Oil	Bank Leumi, Bank Hapoalim, Israel Discount Bank	100	95.5	LIBOR + 4.5%, not less than 5.5%	April 29, 2016	Quarterly	USD 16 million	Lion Oil shares and assets, with the exception of inventory and receivables	Like Delek Finance	Like Delek Finance	Like Delek Finance	Like Delek Finance

Loan	Lender	Original loan USD thousands	Loan as of December 30, 2011 USD millions	Interest rate	Final maturity date	Payment of interest	Annual repayment of principal (in foreign currency)	Security	Financial covenants	Financial covenants on date close to date of statement of financial position	Financial covenants on date close to date of report	Financial covenants on date examined by lender
Delek Refining	Consortium	Credit facility of USD 400 million	Credit facility of USD 227.8 million	LIBOR + 3.0% / Prime + 1.5%	December 29, 2015	Quarterly	None	Tyler inventory, receivables and cash, and Lion Oil receivables	Adjusted credit spread less 20 million is higher than 0	80.6	104	104
Delek Refining									(EBITDA less capital investments) / (interest expenses + planned payment of loan principal + income tax payments) will exceed 1.	1.29	1.35	1.35

- G. Changes in the prices of commodities and future contracts (especially crude oil and fuels) and the interest rate are the main market risks faced by Delek USA. To protect against fluctuations in the prices of commodities, Delek USA, from time to time, enters into futures contracts. As of December 31, 2010 and 2011, the total of open contracts was not material. Additionally, Delek USA occasionally enters into interest rate swap contracts. As of December 31, 2010 and 2011, the total use of open contracts was not material. Entry into financial instruments for the performance of hedging involves exposure to financial losses should there be unexpected fluctuations or deviations in prices, and exposure to credit risk of the parties with who the contract is closed.

1.7.15 Liens

To guarantee Delek Refining's credit facility, Delek Refining placed a charge on all the inventories, receipts receivable from customers, including customers of the El Dorado Refinery, rights under letters of credit, equipment and more in favor of a consortium headed by an American bank. Additionally, Delek Refining has a negative charge on the Refinery's equipment.

To secure the loans Delek Finance and Delek USA took from Israel Discount Bank and Bank Leumi, as stated in Sections 1.7.14C.1 - 1.7.14C.3, a charge was placed on Delek USA's shares in Lion Oil and a charge was also placed on Lion Oil's assets, with the exception of trade receivables and receivables. To secure the Delek Marketing's credit facility, Delek Marketing placed a charge on all its assets in favor of an American bank. To secure the credit facility and loans as described in Section 1.7.14B.3, MAPCO charged all its fixed assets, including real estate, inventory, cash flow from customers and credit cards to a consortium headed by a US bank. To secure the loan the three Israeli banks extended to Lion Oil, all of Lion Oil's assets, with the exception of inventory and receivables, including Lion Oil shares.

1.7.16 Taxation

- A. Delek Refining, Delek Marketing and MAPCO are wholly owned subsidiaries of Delek USA, and therefore their financial statements for tax purposes are consolidated with those of Delek USA and are subject to the applicable tax laws, both at the federal level and at the state level in the states in which Delek USA operates (State income tax and franchise tax). For details of the tax laws to which Delek USA is subject, see Note 42 to the Group's financial statements.

The Group holds Delek USA through a wholly-owned Hungarian company, and consequently the tax rates on capital gains, interest and dividends are affected by tax treaties between Israel and Hungary and between Hungary and the USA.

- B. Delek USA has received final tax assessments through 2004.

1.7.17 Environmental protection

- A. Delek USA is subject to various federal, state and local environmental protection laws, regulation, ordinances and permits of the competent authorities in its segment of operation, and in particular the Environmental Protection Agency ("EPA"), U.S. Department of Transportation, the Pipeline and Hazardous Materials Safety Administration, the Texas Commission on Environmental Quality ("TCEQ"), Texas Railroad Commission, Arkansas Department of Environmental Quality and Tennessee Department of Environment and Conservation. Most of the environmental protection provisions applicable to Delek USA and the required permits are related to the refining activity, and particularly issues of air quality, quality of liquid waste, solid/toxic waste and prevention of ground pollution and pollution of ground water. Delek Marketing and MAPCO are also subject to environmental protection provisions, however given that they purchase finished fuel products, the degree of regulation applicable to them is significantly smaller. Said permits and approvals may be subject to changes, cancellation and renewals. Compliance with the foregoing requirements may involve changes to work procedures and capital outlays by Delek USA.

- B. Delek Refining and Marketing

1. The provisions of the Federal Clean Air Act ("CAA") - an air quality control law and state and local laws and regulations which govern the permitted level of emissions of certain substances which have a direct and indirect influence on refinery operations. CAA licensing requirements and/or control requirements relating to the permitted emissions levels of certain air pollutants can have a direct influence on refining operations. The CAA has an indirect influence on refining operations through comprehensive regulation of emissions of sulfur dioxide, nitric oxide and other compounds emitted by vehicles that use Delek Refining products. In addition, the unstable organic compounds emitted by the

Refinery or products manufactured are heavily regulated, including compounds such as benzene are described below.

- A) The CAA imposes strict limitations on the emission of substances, which require a Title V permit which enables the imposition of civil and criminal enforcement sanctions. The CAA also determines the final dates for implementation of the control standards and requirements based on the severity of air pollution in a specific geographic area. Consent decrees, to which Arkansas is party, were given to the El Dorado and Tyler Refineries on June 12, 2003 and September 23, 2009, respectively. None of said consent decrees claims violations due to the operation of the refineries by Delek USA, and the previous owners/operators bear liability for the violations, as aforementioned. However, the consent decrees require that changes be made in the operation of the refineries on an ongoing basis as well as adaptation of the practices they implement. Delek USA does not believe that the changes and costs involved in performance of these changes will have a material impact on its ordinary course of business. The EPA issued final regulations regarding changes to the formulation of gasoline that will require an average annual reduction in benzene content by January 2011 and maximum reduction in permitted benzene content by July 2012. In October 2010, Delek USA installed a device to reduce the amount of benzene in fuels at the Tyler Refinery. A similar project was initiated at the refinery in El Dorado in June 2011. In 2011, Delek Refining purchased credits points (to comply with the regulations) from other refineries. However, there is no certainty that it will be able to purchase such credit points in the future or that they will be available at reasonable prices. Additional projects for reduction of benzene content may be implemented to reduce or eliminate the need to purchase credit points for benzene, in accordance with the availability and costs of the credit points.
- B) Legislative initiatives and regulation (federal and state) to handle issues relating to climate change and greenhouse gas emissions ("GHG"), including carbon dioxide, methane and nitrogen oxides, are in various stages of discussion and implementation. In June 2009, the US Congress approved the American Clean Energy and Security Act of 2009, which limits the emission of greenhouse gas and increases the costs of using carbon-based fuels. The US Senate began work on its own legislation in this regard. Additionally, at the beginning of 2010, the EPA mandated reporting on emission of greenhouse gases and, at the beginning of 2011, started monitoring emissions of greenhouse gases at the refineries through Prevention of Significant Deterioration programs and Federal Operating Permit - Title V. Although these rules do not limit GHG emissions and do not impact on the operations of Delek USA, the data reported may serve as the basis for future regulation. Additionally, the EPA announced its plans to continue to regulate air emissions from refineries, including GHG emissions through New Source Performance Standards and National Emission Standards for Hazardous Air Pollutants to be published in 2012. Moreover, the EPA and Department of Transportation set final standards to increase Corporate Average Fuel Economy, which will impose federal restrictions on GHG emissions of cars and light trucks by 2016. Said standards were drafted in September 2011. In December 2011, additional decrees were proposed. They apply to 2017 and later models of cars, and their purpose is to reduce the fuel economy of vehicles to 54.5 mpg (miles per gallon) by 2025. It can be assumed that this will lead to increased costs and negatively impact on the viability of purchasing the Refinery's products. It is likely that as the number of electric cars and additional regulation on GHG emissions comes into effect, there will be a decline in demand for fuel products.
2. The Federal Clean Water Act 1972 ("CWA") influences refining operations by imposing restrictions on the discharge of liquid waste and rainwater into certain water reservoirs. Compliance with the stipulations of control, standards and regular reporting required by law is a precondition for the receipt or renewal of licenses which permit the discharge of liquid waste and rainwater into the water. The state of Texas has similar laws and regulations. The Tyler Refinery currently has the license required for the discharge of waste water in compliance with the National Pollution Discharge Elimination System Program. The waste water is transferred to the local authority for treatment in accordance with said program. Additionally, the Tyler Refinery operates in accordance with internal programs for oversight of efforts to comply with the aforementioned laws. In 2008, the El Dorado refinery signed a Consent Administrative Order that was in effect through 2009

with the State of Arkansas with regard to wastewater discharges. The El Dorado Refinery applied for and was granted a National Pollutant Discharge Elimination System permit for a combined discharge to the Ouachita River. The permit was contested by several environmental groups and other parties but ultimately upheld by the State of Arkansas Supreme Court in late 2010. The El Dorado refinery is party to an agreement with the other three dischargers to construct and jointly operate a 23 mile wastewater pipeline to convey the treated, commingled waste water to the Ouachita River. A number of environmental groups have threatened to file suit in an attempt to block construction of the system. It is expected that the pipeline will be completed in 2013. The EPA (Environmental Protection Agency) was not a party to the Consent Administrative Order, and in late 2011 petitioned the court with regard to historical discharges. As of the date of the report, Delek USA is in discussions with the EPA to settle the matter. Delek USA does not believe that such orders and fines, if handed down, would have a material effect on its business, financial condition or operations. In addition, at the federal level, the refineries are governed by the Oil Pollution Act, which amended the Clean Water Act. The Oil Pollution Act stipulates, *inter alia*, that in respect of public water reservoirs, owners or operators of a facility or tanker must have a contingency plan to deal with spills or leaks of oil and/or oil products. Delek USA has developed and implemented such a plan at each of its facilities to which the Oil Pollution Act applies. In addition, in the event of such a leak, the Act states that the companies responsible will bear the cleaning and purification costs and it imposes heavy civil fines as well as criminal sanctions for breaking the law. The State of Texas has passed legislation similar to the Oil Pollution Act.

3. Delek Refining is also subject to the Resource Conservation and Recovery Act ("RCRA"), which dictates how hazardous waste is to be treated, stored, removed and remediated. The state of Texas has similar law and regulations. The RCRA set standards and procedures for the treatment, removal, storage and transfer of hazardous solid waste. In addition to the current procedures for treatment, storage and removal of waste, the RCRA also relates to the environmental impact of removal of past waste, and the potential effects on ground water of the practices for current and historical waste management.
4. The Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), the RCRA and state laws impose liability on certain groups of people, regardless of the question of responsibility or legality of the original deed, in respect of the discharge or the possible discharge of hazardous materials into the environment. These people include the owner and/or operator of the site where the hazardous materials were discharged, and the companies that discharged or organized the discharge of the hazardous materials. Under CERCLA, these bodies may be jointly and severally liable for payment of the costs of cleanup of the hazardous materials discharged into the environment, payment of compensation for damage to natural resources, and cost of certain health studies. It is not uncommon for owners of neighboring lands or third parties to file actions for damage allegedly caused to body and property by hazardous materials or other pollutants discharged into the environment. In addition, state laws impose similar duties and responsibilities. Waste is produced as part of the ongoing operations at the refineries, and it may be considered to be a hazardous material that requires cleanup under this law. At this time, the El Dorado refinery has been named as a minor Potentially Responsible Party at one site for which Delek USA believes future costs will not be material. As of December 31, 2011, there is a recorded liability of USD 1256 million related to addressing certain environmental issues at the Tyler and El Dorado Refineries. This liability includes estimated costs for the investigation and remediation efforts, which were already being performed by the former operators of the Tyler and El Dorado refineries, for known contamination of soil and groundwater. Delek USA expects USD 1.4 million of this amount to be reimbursable by the previous owner of the El Dorado refinery and approximately USD 3.0 million of the liability is expected to be reimbursed over the next 12 months with most of the balance reimbursed by 2022. In the future Delek USA could be required to undertake additional investigations of the refineries, pipelines and terminal facilities or convenience stores, which could result in additional cost. Both of the refineries have consent decrees, as described above, referred to as Global Refining Settlements.
5. The Energy Independence and Security Act of 2007 ("EISA") increased the amounts of renewable fuel required by the Energy Policy Act to 32 billion gallons by 2022. Renewable Fuel Standard 2 implements EISA and requires Delek USA to blend increasing amounts of biofuels with refined products to approximately 7.8% in 2011,

increasing to 9.2% in 2012 and escalating to 18% in 2022. Alternatively, credits, called Renewable Identification Numbers ("RINs") can be used instead of physically blending biofuels. If adequate supplies of the different types of biofuels are unavailable in volumes sufficient to meet Delek USA's requirement or if RINs are not available in sufficient volumes or at economical prices, refinery production or profitability could be negatively affected. The rule could also cause decreased crude runs in future years and materially affect profitability unless fuel demand rises at a comparable rate or other outlets are found for the displaced products. The Tyler refinery began supplying a blend of gasoline and ethanol, E-10 (composed of 90% gasoline and 10% ethanol) in January 2008 and a 2% biodiesel blend in June 2011. The El Dorado refinery completed a project at the truck loading rack in June 2011 to make E-10 available. Delek USA is implementing additional projects that will allow blending increasing amounts of ethanol and biodiesel into fuel products in 2012.

6. In June 2007, the Federal Occupational Safety and Health Administration ("OSHA") announced a National Emphasis Program, addressing workplace hazards at petroleum refineries. As part of the program, OSHA conducted an inspection at the Tyler refinery and issued citations assessing an aggregate penalty of less than USD 100,000. Delek Refining is contesting the citations. Between November 2008 and May 2009, OSHA conducted an additional inspection of the Tyler Refinery in Tyler as a result of the fire and issued citations with an aggregate penalty of approximately USD 200,000. Delek Refining is also contesting these citations and does not believe that the outcome will have an adverse effect on it. In April 2009, OSHA conducted a National Emphasis Program ("NEP") inspection at the El Dorado refinery and assessed a penalty of less than USD 0.1 million, paid by the previous operator.

C. MAPCO

1. MAPCO's operations are subject to various environmental protection laws, regulations and orders which may be federal, state or regional and consequently differ from region to region. The various states issue permits for above and/or underground storage tanks. At the federal level, the Resource Conservation and Recovery Act requires that the Environmental Protection Agency ("EPA") prepare a comprehensive regulatory program for assessing, prevention and cleaning leakages from underground fuel storage facilities. The regulations published by the EPA enable the various states to develop, manage and enforce state regulatory programs, provided they adopt standards which are no less stringent than the federal ones. The EPA, as well as most states, set requirements regarding the installation of underground reservoirs, the upgrade and maintenance of existing reservoirs, measures to be taken to repair leaks, closing underground reservoirs and saving relevant data.
2. After a financial deductible, MAPCO is entitled to payments from state funds that share the responsibility for inspection, investigation and cleanup of certain environmental damage caused by leaks from underground storage facilities and/or other leaks of fuel at gas stations. Additionally, MAPCO purchased an insurance policy that covers its liability beyond the payments it is entitled to receive from the aforementioned state funds regarding certain environmental damage. In 2010 and 2011, MAPCO did not file any material claims against insurance companies. As of the date of the report, there were no claims beyond those covered by the state funds.
3. MAPCO's operations are also subject to CERCLA, as described in Section 1.7.17B.4 above. As of the date of the report, MAPCO is not party to claims under CERCLA.

D. Environmental protection policy

1. The Environmental Protection Department of Delek USA is responsible for handling all environmental issues. The Vice President of Delek USA is responsible for overseeing all environmental protection and regulation issues. Delek USA also calls on external consultants and attorneys on specific issues. The Vice President is responsible for quarterly examination of the handling of environmental protection issues in each of Delek USA's segments of operation and determined whether there has been a material change in Delek USA's liabilities in the field of environmental protection, in accordance with the procedures Delek USA implements in accordance with the Sarbanes-Oxley Act and GAAP. Delek USA's policy is to comply with all relevant environmental protection requirements. Furthermore, Delek USA is subject to the requirements of the Sarbanes-Oxley Act with respect to identifying environmental liabilities which may have a material

impact on Delek USA, and to do so quarterly and annually, and record this in the financial statements.

2. Delek USA's policy is to record environmental liabilities in its books that are not of a capital nature, when it is reasonable that the liability arose and its total can be reasonably estimated. Environmental liabilities present an estimation of the costs for testing and treating pollution. The estimate is based on internal and third-party estimates regarding the total scale of pollution, the technology to treat it, relevant regulation, generally factoring in all the activities and costs for the coming 15 years (unless they can be reasonably estimated for a longer term).
3. It should also be noted that Delek USA has environmental pollution policies that cover certain pollution damage claims and cleanup costs (but do not include, for example, cleanup costs in respect of historical environmental damage). As of the date of the report, no material claims have been filed in connection with these policies.

E. Liability and legal action on environmental protection

1. In October 2007, the TCEQ approved a consensual order with respect to the alleged violations of the provisions for the prevention of air pollution, which continued after acquisition of the refinery. In the consensual order, the Refinery was ordered to pay a fine and finance an environmental protection project for which Delek USA had previously earmarked funds. Additionally, Delek USA was required to and implemented additional amendments, as stipulated in the consensual order, that last of which was completed in 2010.
2. OSHA - See Section 1.7.17B.6 above.
3. The Chemical Safety Board ("CSB") and the EPA also demanded information regarding the fire at the Refinery in November 2008. The EPA is currently conducting an investigation under Section 114 of the CAA with respect to the company's compliance with the requirements for the prevention of chemical accidents under the CAA.
4. At this time, Delek USA is unaware of any ground or ground water pollution requiring investigation or clean-up near pipelines, but a need to perform assessments and clean-up of the pipeline area could arise in the future. Based on environmental assessments and inspections conducted by third parties when the two refineries were purchased and which were recently updated during the refinancing of the refinery in March 2010, as of December 31, 2011, Delek USA recorded in its books a liability of approximately USD 12.5 million in respect of estimated clean-up costs at both refineries, approximately USD 3.0 million in respect of the coming year, and the balance of USD 9.5 million by 2022. Current and future environmental protection regulations, as well as other situations requiring reporting and action, could necessitate significant additional investigation and cleanup expenses. Efforts to purify the groundwater at the Refinery are expected to continue in the foreseeable future.

F. Material investments in environmental protection

1. To comply with the regulation described above in Section 1.7.17(B)(1) on the restriction on the amount of benzene in gasoline, Delek Refining invested approximately USD 18.8 million in 2010 in the Mobile Source Air Toxics ("MSAT") II Compliance Project.
2. It is estimated that to comply with the new environmental standards, Delek USA's investments in this area will be approximately USD 8.9 million in 2012 and USD 80.7 million over the next five years.

This information regarding Delek USA's estimates for investments in environmental protection is forward-looking information. The information is based on the EPA requirements at this time, the extent of ground or water pollution of which Delek USA is aware at this time, and its estimates regarding the cost to handle environmental protection issues, in light of its experience. The information may not materialize, inter alia, if changes are made in the EPA requirements or other relevant regulation, if Delek USA finds new environmental protection issues that need to be handled and if while making the investments or prior to that time it is found that the costs of the investment are higher than expected. Delek USA estimates regarding investments in environmental protection and regulation depend on estimates and factors that are uncertain, including the complexity of the provisions regarding environmental protection and the various ways they can be interpreted, the possibility of discovering additional polluted areas and

estimating the precise scale of existing pollution or pollution that may be discovered considering, inter alia, that it is an old refinery, there is a lack of credible information regarding the extent of clean-up work required to repair and clean up the unknown pollution and the lack of certainty regarding the selection of the most appropriate cleaning method to clean up the pollution. Additionally, given the ongoing developments regarding environmental protection, the legislation and regulations for environmental protection change and are revised frequently, and stricter legal provisions may be added in the future with respect to Delek USA operations, and they may impact on the above assessment. As of the date of the report, to the best of its knowledge Delek USA is in material compliance with environmental protection requirements.

1.7.18 Restrictions, oversight and legislation

A. Delek Refining and Marketing

1. Business licenses - Delek Refining and Delek Marketing operate under many licenses they have obtained for their operations, such as licenses under various environmental laws (waste disposal licenses), pipeline operator license for the transportation of fuel, etc.
2. Delek Refining is subject to the Federal Occupational Safety and Health Act ("OSHA") and other similar state laws that regulate safety and health conditions for employees, including how hazardous materials are handled.

B. MAPCO

MAPCO's operations are subject to laws and regulations including, inter alia, labor laws, regulations governing the sale of alcohol and tobacco products, minimum wage, work conditions, public access roads and additional laws, including:

1. Licensing of gas stations and fuel and oil sales – An annual permit for the sale of fuels and oils is issued by the various states in which MAPCO operates (Regulatory Services Permit). The permit is annual. In addition, states also issue an annual permit for above and/or underground storage tanks.
2. Lottery license - MAPCO is licensed to issue computerized lottery tickets and scratch cards in certain states, under the license it received.
3. Alcoholic beverages license - State or local laws restrict the hours during which certain products may be sold, the most significant of which are alcoholic beverages. State and local authorities have the power to approve, cancel, suspend or deny applications for the issue or renewal of licenses for the sale of alcoholic beverages, or to impose various restrictions and sanctions.
4. Cigarette license – The license to sell cigarettes is issued separately by three authorities: state, county and municipal. This license is granted annually, and in addition, MAPCO must obtain permits for the sale of other tobacco products.
5. License to operate convenience stores - Convenience stores are subject to various federal and state regulations governing health and sanitation, safety, fire, and planning and construction.

- C. Additionally, Delek USA is subject to federal and state legislation on wage protection, overtime, work conditions and civic affairs. It should be noted that to the best of Delek USA's knowledge, from time to time there are federal bills proposing to increase minimum wage and obligating employers to provide their employees with health insurance. Should these bills become law, they may adversely affect Delek USA's results.

1.7.19 Material Agreements

A. Delek Refining and Marketing

The agreements with Noble Group and Magellan are material. For additional information, see Section 1.7.12(B) above.

B. MAPCO

1. Core-Mark International Inc. ("Core-Mark") was the main supplier of retail products in 2010 and 2011, and purchases from it amounted to close to 59.4% and 59.1%, respectively. On August 23, 2010, MAPCO extended the supply agreement with Core-Mark through December 31, 2013. Under the agreement, among other things, Core-Mark will continue to be the main supplier of food and retail products for all MAPCO stores.

1.7.20 Legal Proceedings

Delek Refining and Delek Marketing are not party to any material legal proceedings. MAPCO is party to various legal claims and proceedings stemming from its ordinary course of business. MAPCO believes the final decision in the aforementioned matters known to it at present will not have a materially adverse effect on its financial condition or on its future operating results. For further information about legal proceedings on matters related to environmental protection, see Section 1.7.17E above.

1.7.21 Goals and Business Strategy

The companies in the Delek USA group review their plans and strategic goals from time to time and revise them in accordance with the developments in the fuel market, the competition map and macro-economic influences on its area of operation. In the coming years, Delek USA may focus on the following operations:

- A. Since its establishment, Delek USA's growth strategy has been through acquisitions. In the coming years, Delek USA is expected to examine potential acquisitions, including acquisition of additional refineries, gas stations and convenience stores or other supplemental assets, such as pipelines or terminals. Acquisition of such additional assets may be in the regions of Delek USA's operations or in other regions of the USA. Certain assets, such as gas stations and convenience stores with poor performance or an asset value that is very high relative to their profitability, may be sold or converted to operation by third parties.
- B. Increasing the refining capacity of the refineries, the marketing efforts to expand the customer base and obtain better terms of engagement, and reducing production costs.
- C. Expansion of retail activity and range of the products sold in the convenience stores, particularly ready-to-eat food. As part of this move, MAPCO intends to also sell premium products in its stores which it believes will also attract a new target audience, to expand sales of private label food products and present a large product offering. The range of products to be sold at each convenience store will be determined in accordance with a unique sales strategy for each convenience store, which will take into account its location and customer profile.
- D. MAPCO is working to strengthen its brands and their recognition as leading brands in the southeastern USA, and to refurbish and redesign its convenience stores, with the goal of enhancing the customer shopping experience. As aforementioned, as of 2007, MAPCO began the rebranding of some of its convenience stores under the name Mapco Mart. Between 2009-2011, 85 stores were refurbished, and in 2012, Delek USA plans to refurbish 20 more stores and build 10 new ones. MAPCO believes that this move will expand its customer base.
- E. Attainment of said goals and strategy depends on various external factors which might prevent their realization or lead to changes in them. In addition, Delek USA customarily reviews and revises its goals in accordance with developments in the fuel market, the competition map and macro-economic influences.

1.7.22 Development Expected over the Coming Year

In the fourth quarter of 2011, the refinery in El Dorado processed 25,000 barrels of oil a day, relatively more cheaply than oil originating on the Gulf Coast (including local oil), and about 50,000 to 55,000 barrels a day of oil originating on the Gulf Coast, sold at a premium compared to oil originating in West Texas. In 2012, Delek USA plans to work to find sources for the supply of inexpensive oil from the refinery in El Dorado, such that in 2013 it will be possible to process close to 50,000 barrels a day of oil that is less expensive than oil from West Texas at the El Dorado Refinery and, additionally reducing the premium paid for some of the barrels currently purchased for the refinery in Tyler, Texas.

Additionally, in 2012 Delek USA intends to complete two projects at the Tyler and El Dorado refineries at a cost of 5 million and 16 million, respectively, and which are expected to increase the profitability of the refining segment by transferring up to 2,000 barrels of asphalt a day from the refinery in El Dorado to the Tyler Refinery and converting them into white products and coke, and reducing amortization in production of end products in El Dorado by using natural gas, which is relatively inexpensive.

Said forecast for development in the coming year is forward-looking information based on Delek USA's plans for the coming year, and it may change should there be changes in the investment plan, regulatory delays in receipt of the required permits and approvals and the like.

Risk factors

- A. **Macroeconomic conditions and the economic crisis** - A global or local economic downturn, particularly in the southern US, may have an adverse effect on Delek USA's business, operating results, and sales turnover of fuel and retail products due to a decline in consumption. Some of the factors that impact on a decline in consumption are macroeconomic and geopolitical conditions (particularly in oil producing areas), unemployment, consumer debt, depreciation in net value based on sharp declines in markets, real estate value, mortgage markets, taxation, energy prices, interest rates, consumer confidence and additional macroeconomic factors. During a period of economic uncertainty, consumers may travel less, consume less, etc.
- B. **Exposure to fluctuations in crude prices and irregular supply** - historically, global prices of crude oil fluctuate and are dependent on factors not under Delek USA's control such as the geopolitical (including wars and terror) and economic situation, as described in Section 1.7.1(B). Fluctuations in (crude) oil prices may reduce demand for crude oil products and have a detrimental effect on the profitability of Delek USA (especially on products, the prices of which are not correlated with the fluctuations in the prices of crude oil, such as asphalt, propane and other products produced by Lion Oil. From time to time, Delek USA conducts hedging transactions through derivatives to reduce its exposure to these risks, but the scale of these transactions changes from time to time, and they themselves entail various risks. Additionally irregular supply of fuels and retail products may impact negatively on Delek USA's operations.
- C. **Exposure to changes in the prices of raw materials and products** - Changes in the prices for the purchase and sale of raw materials, crude oil products and retail products from Delek USA's suppliers and to its customers may impact adversely on Delek USA. It should be noted that Delek USA's competitors also include integrated, multinational companies that are substantially larger than Delek USA, which because of their size, integration of operations and more complex refineries may be better able to withstand volatile market conditions.
- D. **Competition** - High competitiveness, including competition against supermarket chains in the field of fuels, may lead to a drop in prices, expressed in relatively low margins and lost of market share that translates into a decline in revenues.
- E. **Alternative products** - Accelerated consumption of alternative or renewable energy such as ethanol or biodiesel may lead to a decline in the prices of the fuels and/or demand for fuel products. The use of electric vehicles may also lead to decreased demand for fuel products and may have a negative impact on the profitability of Delek USA.
- F. **Changes in margins** - changes in the refining margin, including a change in the margin between crude oil originating in West Texas and crude from the Gulf Coast, as described in Sections 1.7.1C and 1.7.7, and the risk of erosion *inter alia* due to an increase in crude oil prices and difficulty in fully adjusting the prices of fuels sold to consumers, may lead to a decline in profitability. Upon acquisition of all the holdings in the refinery in El Dorado, Delek USA's exposure to this risk factor increased substantially.
- G. **Dependence on two assets** - Given that all the refining activities are concentrated at the Tyler Refinery and the refinery in El Dorado, major disruptions in the operations of one of the refineries could have an adverse effect on Delek USA. Said risk factor materialized on November 20, 2008, with the explosion at the Tyler Refinery, following which its operations were shut down through May 2009 and for unexpected repair work for about two weeks in the third quarter of 2010. The dependence on the refineries may also be seen in the event of incidents such as natural disasters, work accidents, loss of licenses and the permits required for the facility's activity, maintenance, etc.
- H. **Operational and external risks** - Delek USA's operations are subject to risks inherent to the refining of fuels and supply of fuel products. These risks include, among other things, natural disasters, severe weather conditions, seasonality, war, terrorism, fires, explosions, pipeline leaks, accidents involving the fleet of trucks for transport of the fuels, maintenance faults, problems with information technology, third-party intervention and other events that are beyond the control of Delek USA and that could disrupt the operations of the refineries, pollute and harm the environment and damage third-party property, cause injury suits and even death. In the incident at the Refinery on November 20, 2008, two employees were killed and several other people were injured. All of the related proceedings are still not complete, and Delek USA may be exposed to various proceedings in the future as well.
- I. **Limited pipeline infrastructure** - The pipeline transporting crude oil to the Tyler Refinery has limited capacity, which could become insufficient if the refinery increases its output

significantly. Moreover, the Tyler Refinery does not have an outbound pipeline for distribution of its fuel products, and in 2010, virtually all of its sales were made through its own terminal. This could make it difficult to attract new customers for the Tyler Refinery and have an adverse effect on the refinery's results if demand for its products in northeastern Texas falls significantly. The refinery in El Dorado is dependent upon a third-party pipeline for the distribution of fuels as well as two main pipelines owned by a different third party, through which the refinery receives most of the oil it processes.

- J. **Decline in cigarette consumption** - A decline in the consumption of cigarettes (MAPCO's best selling retail item) and the difficulties of the US tobacco companies or a problem in the pricing mechanism of cigarettes for MAPCO may have an impact on the prices and marketing of cigarettes. Future legislation concerning tobacco products, such as an rise in cigarette prices or higher taxes on tobacco products and negative advertising on tobacco products, may have a negative impact on cigarette consumption.
- K. **Existing debt, financing of activity and credit restrictions** - Delek USA has significant debt and credit facility. It is not certain that Delek USA will be able to refinance its loans, renew credit facilities and secure new financing at the time required and with good terms. Extensive leveraging has various negative implications, including significant exposure to negative conditions in the market and industry, the need to use cash flow to pay debt and restriction of business flexibility in existing activity and entry into additional activities. Difficulties in servicing the existing debt and financing the activity may hurt relations with suppliers, lead to poorer conditions in the contracts with them, and hurt Delek USA's business operations (such as acquisitions). In this regard it is important to emphasize that the ongoing economic and financial crisis may have a materially adverse effect on banks and restrict the accessibility required to raise capital and debt.
- L. **Compliance with financial and other covenants** - Current and future credit agreements that include financial covenants may negatively impact on the ability to finance future activity, conduct business and may mandate early repayment of loans in significant amounts and make it difficult or prevent receipt of additional financing. At times, Delek USA is close to non-compliance with the financial covenants that apply to it. Compliance with financial covenants depends, among other things, on factors such as level of leverage, profitability, relevant market conditions and more, such that deterioration of various parameters may hurt Delek USA's ability to comply with the financial covenants or to remedy them if necessary. This is, *inter alia*, due to the current crisis in the credit market and the general deterioration of market conditions. Additionally, by virtue of the credit agreements, various stipulations and limitations apply to Delek USA and may impact negatively on its ability to perform various operations such as distribution of dividends, sale of assets, entry into new activities, investments, etc.
- M. **Insurance** - Delek USA has insurance policies, including property policies with coverage of up to USD 1 billion for each refinery. Nevertheless, Delek USA could sustain damage that is not insured, or which cannot be insured under its policies, or that is higher than the sums insured by the policy. For example, the business interruption policy does not apply unless the interruption extends beyond 21-45 days. Delek USA cannot ensure that the terms of the insurance policies will not change for the worse or if they will be renewed by its insurers.
- N. **Legislative developments and changes and environmental issues** - Delek USA is subject to various laws, regulations and standards related to its operations, particularly as concerns environmental protection. Delek USA is therefore exposed to legislative developments, changes and new requirements, and the possibility that in the future, material deviations will be discovered or new and more stringent legal provisions will be added, thus leading to expenditures. It is estimated that to comply with the new environmental standards, Delek USA's investments in this area will be approximately USD 8.9 million in 2012 and USD 80.7 million over the next five years.
- O. **Dependence on employees** – As of December 31, 2011, Delek USA employed 272 and about 580 people at the refineries in Tyler and El Dorado, respectively. 202 employees of the Tyler Refinery (including 40 truck drivers) and about 168 employees at the El Dorado refinery are represented by unions. These employees are covered by collective bargaining agreements that expire on January 31, 2015 and August 1, 2014, respectively. Although these collective bargaining agreements contain provisions to discourage strikes, there is no assurance that strikes or work stoppages will not occur. A strike or work stoppage could have a material adverse effect on Delek Refining's operations.

- P. Dependence on major suppliers - Delek USA is dependent on major suppliers such as Magellan and Noble in marketing and Core-Mark in the retail field. Changes in suppliers, supplier relations, agreements with major suppliers, their compliance with terms of payment and delivery or interruptions in supply for any reason whatsoever may have an adverse effect on Delek USA.
- Q. **Changes in the dollar interest rate** - As of December 31, 2011, Delek USA had credit debt with variable interest of USD 288.1 million and total credit debt of USD 432.6 million. It is exposed to changes in the interest rates paid by said companies on these loans and in the future.
- R. **Risks as a result of the purchase of control in Lion Oil** - The acquisition of control in Lion Oil involves several risks, including increasing the dependence on the refining activity and specifically on the results of Lion Oil; increasing the Delek USA's total credit; difficulty integrating the new activity with the existing activity; exposure to liabilities that were unknown on the date of entry into the agreement such as liabilities in respect of environmental protection, regulation and legal proceedings; increase in total investments Delek USA will be required to make in the future, and more.

Following is a summary of the aforementioned risk factors by type (macro risks, sector risks, risks specific to Delek Refining and Delek Marketing) which have been rated based on an estimate by Delek USA, according to their impact on Delek USA – as major, moderate or minor:

	Impact of the risk factor on Delek USA		
	Major impact	Moderate impact	Minor impact
Macro risks		• Macroeconomic conditions and the economic crisis • Insurance	• Changes in dollar-denominated interest
Sectoral risks	• Exposure to fluctuations in the price and irregular supply of crude oil • Competition • Changes in the refining margins, including that between oil originating in West Texas and oil from the Gulf Coast. • Legislative developments and changes and environmental issues	• Exposure to changes in the prices of raw materials and products • Operational and external risks	• Alternative products • Decline in cigarette consumption • Negative publicity
Risks specific to Delek USA	• Compliance with financial and other covenants • Risks arising from the acquisition of control in Lion Oil • Decline in asphalt prices	• Dependence on the two refining assets • Limited pipeline infrastructure • Existing debt, financing of activity and credit restrictions • Dependence on major suppliers	• Dependence on employees

The degree to which Delek USA's risk factors impact is based solely on estimates. In reality the actual impact may be different.

1.8 **Fuel Product Segment in Israel**

The Group's operations in the Israeli fuel products segment are conducted through Delek, The Israeli Fuel Corp, Ltd, and companies and partnerships under its ownership (Delek, The Israeli Fuel Corp Ltd and its subsidiaries are hereinafter referred to as: ("**Delek Israel**") In August 2007, Delek Israel completed an IPO of shares, options exercisable for Delek Israel shares, and debentures for total proceeds of NIS 940 million (gross) under a prospectus dated August 5, 2007 Delek Petroleum's profit from the issue of Delek Israel shares was NIS 75 million. Under a shelf

prospectus dated May 29, 2009 ("**the Shelf Prospectus**") and shelf tender offer dated June 16, 2009, Delek Israel issued debentures to the public for total proceeds of NIS 814 million (gross). Moreover, under a shelf prospectus and shelf tender of May 5, 2011, Delek Israel issued debentures to the public in return for NIS 328 million (gross).

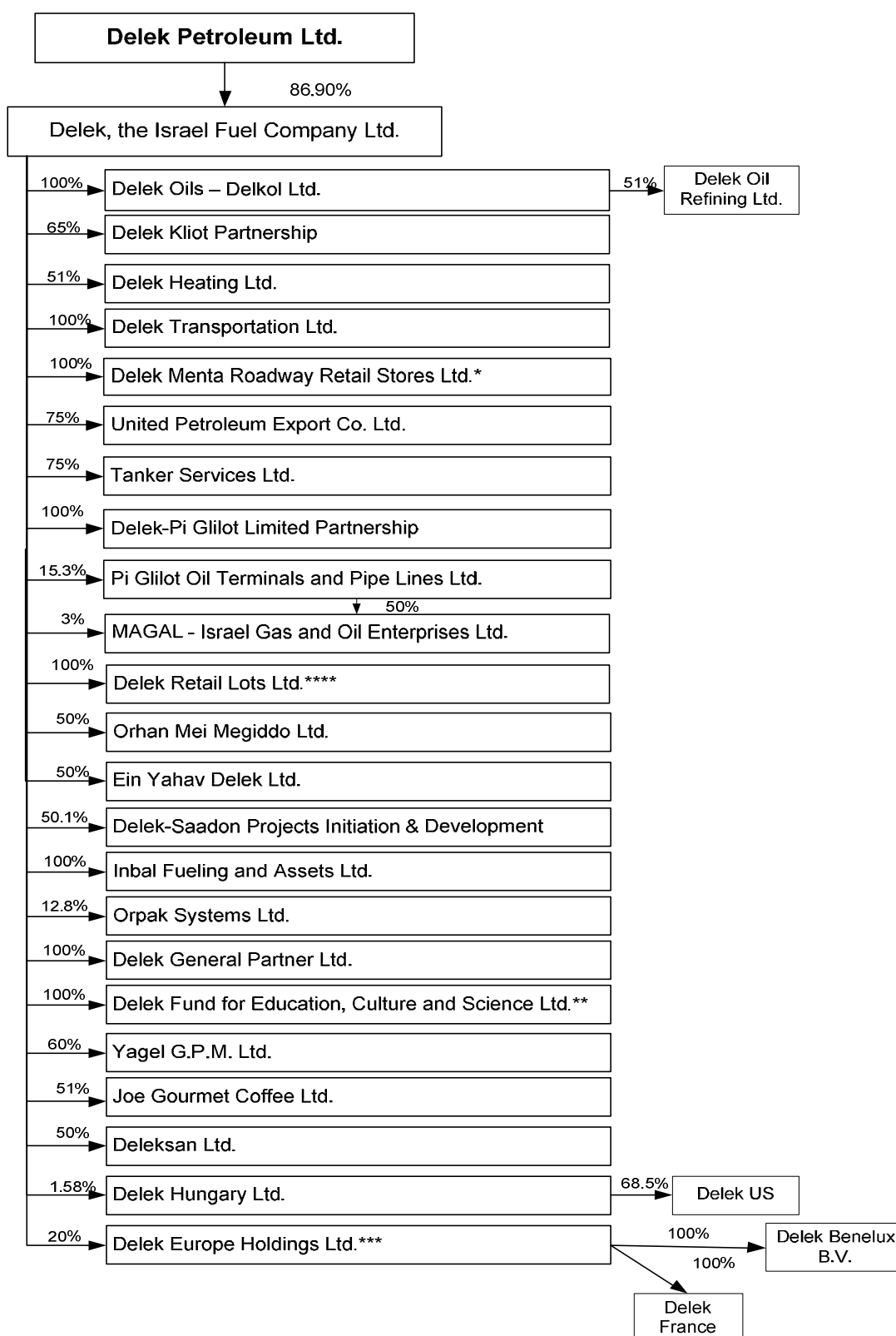
On July 12, 2011, Delek Petroleum published a tender offer for Delek Israel shares, which was amended on July 26, 2011 ("**the Tender Offer**") Under a tender offer of August 4, 2011, Delek Petroleum acquired 1,099,699 ordinary Delek Israel shares, representing 9.69% of its issued and paid up share capital and voting rights, in return for NIS 111.07 million. As of the reporting date, the Group, through Delek Petroleum, holds 86.9% of Delek Israel shares.

Delek Israel is active in the Israeli fuel products industry, including selling fuel products at public gas stations (including selling to gas stations operated by third parties) and operating convenience stores located at most of these gas stations ("**Gas Station and Commercial Compounds**"), initiating setting up and operating public gas stations and convenience stores, direct marketing and distribution of fuel products outside the gas station and commercial compounds ("**Direct Marketing**"), and storing and dispensing fuel for itself and others. Delek Israel also holds approximately 1.58% of the shares in Delek Hungary Ltd., ("**Delek Hungary**"), which holds 68.5% of Delek USA shares . Delek Israel also holds 20% of the shares in Delek Europe.

End December 2011, Delek Israel completed the acquisition of 51% of the issued and paid up capital of Joe Gourmet Coffee Ltd.. For further information, see sections 1.8.2B and 1.8.4.

On February 21, 2012, Delek Israel completed the acquisition of Delek Natural Gas - Marketing & Distribution Ltd., a wholly owned company of the Group ("**Delek Gas**"). For further information, see section 1.8.6B(3) below.

Following is a diagram of the main structure of the Group's holdings in the Israeli fuel products segment as at the reporting date:



- * In 2010, Delek Retail Registered Partnership merged with Delek Menta Roadway Retail Stores Ltd., when in January 2012, the merger was completed following approval of the Tax Authority and Registrar of Companies.
- ** Delek Israel intends transferring its holdings in Delek Foundation to the Group.
- *** The holding is through Delek Europe B.V., a wholly-owned subsidiary of Delek Europe.
- **** This company has the following holdings: M. Rosenfeld – Delek Gas and Business Center Ltd. (50%), Damak - Pinto Commercial and Fuel Center Ltd. (50%).

Details relating to the investment of Delek Israel's equity in the two years preceding the date of the report

Date	Transaction Type	% of Delek Israel's issued capital ²²	Capital investment in NIS thousands
2010	Exercise of options to shares	0.2%	25
2011	-	-	-

To the best of Delek Israel's knowledge, in the past two years no material transactions were made in Delek Israel shares by interested parties in Delek Israel outside the stock exchange, except for the following:

7. On January 5, 2011, in a private transaction Elad Sharon (Tshuva) acquired 41,400 ordinary NIS 1 par value shares representing 0.36% of Delek Israel's issued and paid up share capital and voting rights in return for NIS 5.928 million.
8. On August 4, 2011, Delek Petroleum acquired (under a tender offer) 1,099,699 ordinary Delek Israel shares, representing 9.69% of its issued and paid up share capital and voting rights, in return for NIS 111.07 million.
9. On August 4, 2011, Elad Sharon (Tshuva) acquired 45,317 ordinary Delek Israel shares under a tender offer, representing 0.40% of its issued and paid up share capital and voting rights and 0.38% fully diluted, in return for NIS 4.577 million.
10. On August 4, 2011, Clal Insurance Enterprises Holdings Ltd. (nostro account, participating insurance account and provident funds) ("**Clal Insurance Enterprises Holdings**") sold 335,309 ordinary Delek Israel NIS 1 par value shares under a tender offer, representing 2.96% of Delek Israel's issued and paid up share capital and voting rights and 2.79% fully dilutes, in return for NIS 33.866 million. With the sale, Clal Holdings ceased to be an interested party in Delek Israel.

1.8.1 General information about the areas of operations

A. Structure of areas of operation

Annual consumption of gasoline, diesel oil and kerosene fuels in Israel in 2011 and 2010 was approximately 7.2 tons (9 million kiloliters ("kl")) and 6.9 million tons 8.4 kl)²³, respectively. The source of all the fuel is the refineries in Ashdod and Haifa, excluding an immaterial quantity which was imported in 2011.

In Israel's fuel industry, there are infrastructure companies providing infrastructure services such as unloading, storage, dispensing and piping of fuel and fuel companies involved in marketing, distributing and selling fuel products and oils in the gas station and commercial compounds and in initiating the establishment and operation of gas stations and convenience stores. The four main fuel companies: Paz, Delek Israel, Sonol and Dor-Alon own about 918 public gas stations in Israel. There are also other fuel companies which together own about 162 public gas stations²⁴.

Delek Israel's operations include the marketing fuel and oil products to gas stations (including those operated by third parties) and operating the gas stations, including refueling services using an electronic identification refueling system ("**Dalkan**") designed mainly for fleets, oils and other products at the public gas stations, and initiating the establishment and operation of gas stations and convenience stores. At some of the compounds, Delek Israel leases out areas to third parties for commercial purposes ("**Retail Areas**"). Delek Israel also engages in marketing, distributing and supplying various oil products (fuels) outside the public gas stations directly to the customers' sites which are not open to the general public. Delek Israel also provides fuel products storage and dispensing services from the three terminals Ashdod, Beer Sheva and Jerusalem purchased from Pi Gilot in July 2007. Additionally, Ionex operates a diesel fuel and fuel oil distribution facility in Ashdod used to issue them to direct marketing customers.

²² Calculated according to the issued and paid up capital known on the date of this report.

²³ This information is taken from data of the Ministry of Energy and Water. The data includes kerosene and diesel oil to IEC.

²⁴ Based on the Ministry of Energy and Water's information of December 21, 2011.

As of the report publication date, Delek Israel markets fuel products to 247 public gas stations²⁵ under the Delek and Gal brands deployed nationwide, including 178 where convenience stores operate and 31 where retail areas operate. Delek Israel also has 10 convenience stores operating outside the gas station compounds. As of the report date, Delek Israel is Israel's second largest fuel company in quantity of gas stations.

At the end of 2011, Delek Israel marketed fuel products to 246 public gas stations, of which 176 where convenience stores operate and 31 which have retail areas. At the end of 2010, Delek Israel marketed fuel products to 246 public gas stations, including 160 where convenience stores operate and 31 where retail areas operate.

As of December 31, 2011, of the gas stations where Delek Israel markets its products, 55 are owned by Delek Israel or leased under primary lease from Israel Lands Administration (compared to 52 on December 31, 2010), 171 it sub-leases or leases (the same number as on December 31, 2010) and 20 are not owned and/or leased by Delek Israel and are operated by third parties which Delek Israel has contracts with for the supply of fuel products and oils (compared with 23 stations on December 31, 2010).

As of December 31, 2011, Delek Israel operates 202 gas stations (compared with 195 on December 31, 2010), 17 gas stations are operated by other companies on behalf of Delek Israel (compared with 20 on December 31, 2010) and 27 gas stations are operated by others not on behalf of Delek Israel (compared with 31 on December 31, 2010).

Furthermore, as of the report date, Delek Israel has 21 initial contracts in initiating, planning and setting up gas stations, of which 9 projects are in the advanced stages of obtaining building permits and Delek Israel estimates the construction of 3 of them is expected to begin in 2012. Delek Israel estimates with respect to when the construction of the gas stations will begin is forward looking information based on assessments concerning obtaining the permits and approvals required to set up the stations. This information may not materialize, *inter alia*, due to failure to receive approvals and permits in the anticipated time for reasons beyond Delek Israel's control. In this matter, it should be noted that the average time to set up a gas station compound is between three to five years. Most of the time is to obtain approvals and permits to establish the compound. In the five years preceding the periodic report date, the average construction time required by Delek Israel to set up a standard gas station compound is around six months from obtaining the approvals and permits, if no exceptional problems are encountered. The average cost to establish a gas station compound (as was taken into account in Delek Israel's budget for 2012) is between NIS 4-5 million.

Following is a description of the Israeli fuel industry structure, which also addresses the importation, transportation, storage, dispensing and trucking to the gas stations of crude oil and fuel products.

Importation, purchase, transportation and storage of fuel products

Fuel companies are permitted to import crude oil and crude oil products to Israel. In practice, as of the reporting date, the oil refineries import crude oil to Israel and refine it into products. Until the privatization of ORL, selling prices of distillates (oil products) sold by the refineries to the fuel companies were controlled. After the privatization and the splitting up of the oil refineries, ex-ORL price control was lifted, excluding the price of two types of bitumen (PG-68 and non-blown) and LPG. Delek Israel does not import crude oil²⁶, but in 1999 it began importing fuel products (mainly gasoline and diesel oil) and since 2008 the quantities are immaterial.

Nevertheless, the quantity imported in 2011 and 2010 was very small (negligible amounts only) due to Delek Israel's fuel product purchase agreement for these years with the Haifa refinery under which more attractive fuel price are fixed.. As of the report date, Delek Israel has an agreement with ORL for the purchase of most of the fuel for 2012. Delek Israel may

²⁵ Excluding 170 internal gas stations which, as at the report date, are part of the direct marketing segment.

²⁶ Delek Israel maintains an emergency stock of distillates for the State under the provisions of the State Economy Arrangements (Legislative amendments to achieve the 2001 budget and economic policy targets) (Holding reserves and security reserves of fuel) Regulations, 2001. For additional details, see section 1.8.19.A1 below. Delek Israel also maintains a small quantity of crude oil under the same regulations. This quantity is maintained for several years due to a dispute between PEI and Israel Fuel Authority concerning a financial debt between them. The dispute recently ended by Delek Israel's conduct vis-a-vis PEI and Israel Fuel Authority as part of which the inventory will be sold and the proceeds thereof will be transferred to Delek Israel as its share and the remainder will go to the State.

also examine importing different amounts of fuel. Its decision concerning the import of fuel products is affected by the economic feasibility of importation (the import price versus ORL ex-refinery price) and the cost of the infrastructure involved in sea freight, unloading, storage and piping from the port to the supply facilities.

Imported fuel products (as opposed to crude oil) may currently be offloaded at the following sites: A) Haifa Port by PEI²⁷ (B) Ashkelon Port by PEI and EAPC²⁸ (C) IEC dock in Ashdod to a limited extent.

Oil products are stored at infrastructure company terminals and the major fuel companies' facilities (Paz, Delek Israel and Sonol). The terminals / facilities are operated by their owners. The infrastructure companies which provide storage and dispensing services are: (1) PEI, which owns storage facilities throughout Israel and a storage and dispensing facility near Beer Sheva; (2) EAPC, which has a storage and dispensing facility in Ashkelon; (3) Ashdod Oil Refinery (AOR), which has storage and dispensing facilities in the Ashdod oil refinery compound; (4) ORL, which has a storage and dispensing facility in the Haifa oil refinery compound; and (5) Delek Israel, which owns storage and dispensing facilities in Ashdod, Beer Sheva, Jerusalem and Haifa²⁹. Fuel products are mostly transported to the storage and dispensing terminals along a pipeline owned by Fuel Products Line Ltd.³⁰ ("FPL"). Delek Israel's central storage facilities are located Haifa and Ashdod (which it owns). The pipeline which usually carries the oil products to Delek Israel's storage and dispensing terminals in Haifa is owned by ORL. The infrastructure service rates (unloading, storage and transporting) of oil products were set in the Commodity and Service Price Control (Infrastructure rates in the fuel economy) Order, 1995 ("the Infrastructure Price Control Order").

Transportation, issue and trucking

Oil products manufactured at the Haifa or Ashdod refineries and imported oil products are transported to the various storage facilities through a national distillate pipeline primarily belonging to FPL. The transportation of oil products to several major consumers in the Haifa area is by means of the pipelines owned by ORL and IEC. The fuel products are dispensed at the dispensing sites to road tankers or directly to institutional customers' end facilities. The fuel companies select a storage site and the method of transporting the oil products from time to time, based on their business considerations.

Oil products are carried from the dispensing sites by road tankers, some of which carry only "white" products (gasoline, diesel oil and kerosene) while others carry only fuel oil or bitumen.

As of the reporting date, over 80% of the oil products sold by Delek Israel are transported by Delek Transportation Ltd. ("**Delek Transportation**"), a wholly owned subsidiary of Delek Israel. The rest of the fuels (about 20%) are transported by subcontractors hired by Delek Israel or by customers using their own fleet of tankers or by parties acting on their behalf³¹.

Marketing of oil products

To the best of Delek Israel's knowledge, over 40 fuel companies are registered with the Fuel Administration and licensed to purchase oil products directly from the refineries. Delek Israel estimates that additional entities operate in this market (companies, agents, distributors, and wholesale customers), purchasing oil products from the licensed fuel companies and selling them to customers.

B. Material changes in the segment

1. ORL privatization – based on the decision of the Ministerial Committee on Privatization of December 26, 2004 ("**the Ministerial Committee's Decision**"), Oil Refineries Ltd. ("**ORL**") was split into two refineries (one in Ashdod, one in Haifa) and then sold by the State. The Ashdod oil refinery was acquired by Paz on September 28, 2006, while the

²⁷ A company wholly owned by the State of Israel.

²⁸ A company owned by the State of Israel (50%) and a third party.

²⁹ It is noted that most of Ashdod refinery's storage and distillation services are primarily for its own use since most of the derivatives which it produces are used by Paz and the Palestinian Authority. It is also noted that the Haifa facility is used mainly for Delek Israel's use. It is further noted that EAPC has recently substantially increased its storage capacity aimed at leasing it mainly to international fuel traders.

³⁰ A subsidiary wholly owned by PEI.

³¹ Some of the agreements with third parties grant them the right to carry the fuel products they purchase.

controlling stake in ORL was sold on February 19, 2007 to a company owned by the Ofer-Federman Group.

The Ministerial Committee's Decision prescribed that the Commodity and Service Price Control (Maximum ex-works prices for ORL oil products) Order, 1992 would be amended so that after the split of ORL and the privatization of Oil Refineries Ashdod ("ORA"), control of ex-works oil distillate prices of at the refineries would be lifted, excluding the prices of oil products, of which over 50% of the local market consumption is sold by one of the two refineries while less than 15% is sold by the other refinery. As of the reporting date, LPG and bitumen (PG-68 and non-blown) are still under price control. The trading terms of Delek Israel with the refineries in 2011 were similar to those in 2010.

2. Pi Gllilot Tender (storage and supply operations) – as set out above, on July 31, 2007, Delek Israel acquired the three Pi Gllilot terminals for NIS 806 million once the provisions of the sales procedure were fulfilled and approval from the Antitrust Commissioner was obtained.
3. Increased competition – The increased competition in marketing fuel products to the end customers is expressed in an ongoing increase in the number of gas stations and convenience stores, granting of discounts on fuel prices at the gas stations, competition over customer credit terms, the level of discounts for fleets and the service quality improvement, which require investments in improving the gas station infrastructures and appearance. The increasing competition in the direct marketing segment is expressed mainly in lower marketing margins. Furthermore, the structural changes described in sections 1.8.1B.1) and 1.8.1B.2) above have increased competition in the fuel storage and supply segment, which is primarily affected by the location of each company's storage facilities operating in this segment and the costs involved in transporting the fuel to the end user.
4. Changes in the fuel supply segment – Between 2001 and 2003 material changes occurred in the fuel supply segment. Since 2001, ORL (at the Haifa and Ashdod refineries) started providing fuel supply services directly from its facilities, and in 2002 it started supplying fuel at the PEI facility located in southern Israel. In 2003, the Pi Gllilot facility in Herzliya shut down and Delek Israel began supplying fuel from the Pi Gllilot facility in Ashdod, the EAPC facilities in Ashkelon and the ORA facility in Ashdod.
5. Regulatory developments in the fuel segment – regulatory changes have recently been made concerning the State's control policy of fuel products purchases by the fuel companies after the privatization of ORL; the control policy of fuel product selling prices to consumers (currently the 95 octane (unleaded) gasoline prices are controlled), including fixing the marketing margin; the Fuel Economy Bill, 2011; the Fuel Economy Regulations (Promotion of Competition) (Including the universal automatic fueling device issue), 2011 ("**Universal Refueling Device Regulation**"); control of the price of diesel oil for transportation; control of the infrastructure rates; the gradual conversion of some of the gas pumps at the gas stations to self-service; and the passing of Amendment 4 of National Outline Plan 18, which will enable the setting up "miniature" city gas stations, expedited approval processes, and planning relief. Environmental protection requirements have become more stringent.

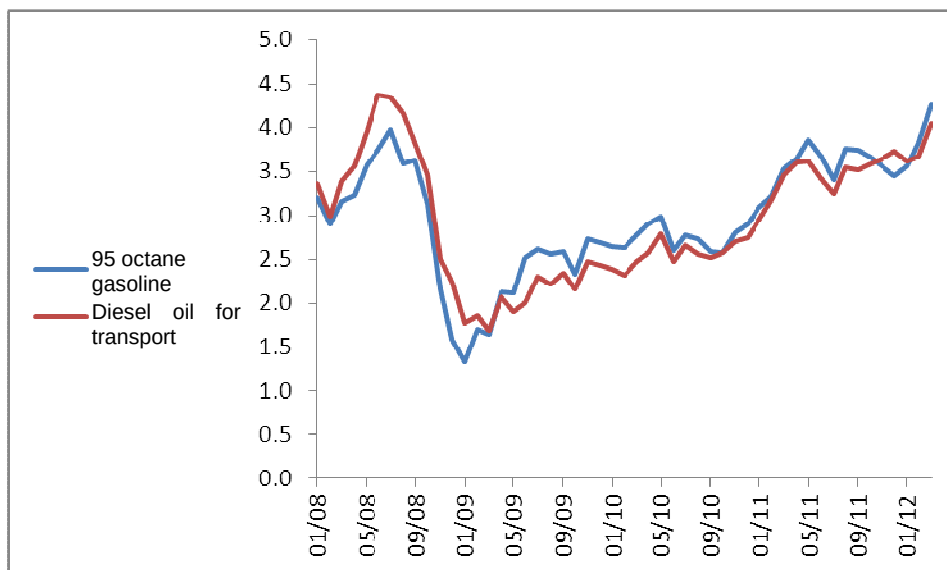
C. Restrictions, legislation and standardization

The fuel companies' operations are subject to various legislative and regulation limitations. For details see sections 1.8.18 and 1.8.19 below.

D. Changes in the volume and profitability of operations in the segment

Global fuel prices directly affect the price of the fuel products marketed by Delek Israel. When crude oil prices decrease, Delek Israel's profitability declines due to the reduction of its fuel product inventory value and erosion of profits, impairing its gross profitability. On the other hand, when global crude oil prices rise, Delek Israel's profitability could improve due to selling its fuel product inventory at higher prices and an indirect increase in marketing margins, while a possible consequence is decreased demand, fiercer competition and increased discounts and financing costs. It is also emphasized that the higher the fuel prices raise, the higher the need for working capital and increased financing costs resulting from the rise in financial liabilities.

The graph below illustrates the volatility of ORL ex-refinery oil distillate (gasoline and diesel oil) prices (which are directly affected by the global distillate prices) from January 2008 until close to the reporting date (Brent crude oil in USD per barrel):



In the graph, it is clear that in mid 2008, the gasoline and diesel oil prices peaked and from then they descended to a low in January 2009. Since early 2009, fuel prices have been climbing steadily and the gasoline and diesel oil prices ascended according, reaching NIS 3 towards the beginning of 2010. In 2011, the price increase continued primarily due to the governmental instability and revolutions in the different Arab countries and the nuclear threat from Iran. The result is that in the beginning of 2012, the prices are continuing to rise and have recently crossed the NIS 4 mark.

From early 2009 until the reporting date, we have been witnessing sharp fuel price rises, which have surpassed NIS 4,000 per ton. The fuel price increase began mainly due to the policy/political changes in the various Arab countries. This continual ascent brought about a growth in customer credit accordingly, increasing Delek Israel's exposure because of it. In 2011, the fuel prices rose by over 45% (December 2011 compared to December 2010), causing the customer credit to rise by NIS 108 million.

Changes in Israel's policy which included an obligatory increase of emergency inventory could affect the volume of storage operations. In this case, the impact on Delek Israel could be negative and the storage fees paid by the State will be lower than the market price, making it less economically viable. Moreover, the Pi Giliot tanks are currently full from the storage area aspect and if the fuel companies and Delek Israel are forced to increase the emergency inventories, which will be stored at the Pi Giliot facility at lower prices than those of the market. This could impair Pi Giliot's business results. However, increasing the emergency inventory could have a positive effect on the fuel storage and supply segment, if the price policy changes.

E. Developments in markets and customer characteristics

Delek Israel's operations are affected by various market developments, including the Israeli economic situation and global fuel prices. Below are material market and customer characteristic developments:

Development of fuel stations into retail areas – In recent years, there is a growing trend of fuel companies, including Delek Israel, developing and expanding their fuel stations into retail areas which, in addition to fuel products and lubricants, also offer a range of services such as convenience stores, restaurants, cafes, car wash services etc. For further information, see sections 1.8.2B and 1.8.6B below.

Self-service expansion – In a gradual process until April 2006, the fuel companies were required to install self-service gasoline (whose price is controlled) pumps in their public gas stations. The selling price of gasoline products is lower at the self-service pumps and no service fee is collected. Furthermore, following the introduction of self-service there has been

a drop in the sales of “island products”³² in the pump area. On the other hand, as a result of self-service the cost of employing gas station attendants has dropped and the transition to self-service is also in line with the trend to expand the use of the convenience stores. As opposed to previous years, the introduction of self-service at Delek Israel's gas stations impaired its results in the last year. Recently, because of the reduction in staff at the compounds and the streamlining measures taken by Delek Israel as a result of the reduced marketing margin, we are witness to a reduction in the volume of sales compared to the small fuel companies operating in the industry, which provide full service at the self-service pumps with the discount prices. It is also emphasized that the move to reduce the marketing margin led the customers to change their consumption habits, which are reflected in purchasing fuels in the discount lane. Also see Section 1.8.19B(2) below.

Fleet customers – In recent years, there has been an increase in the number of fleet customers signing agreements with fuel companies for the supply of oil products. The number of fleet customers and their proportion of the total number of customers at Delek Israel's public gas stations have grown in recent years. The oil product sales and marketing for fleets is performed through the Dalkan system, which enables computerized refueling and payment on credit. The competition between the four major fuel companies (Paz, Delek Israel, Sonol and Dor Alon) has led to increased discounts for fleet customers. Due to the global economic crisis which began to affect the Israeli economy at the end of 2008, fleet sizes started decreasing towards the end of 2008 and early 2009, resulting in a decline in fuel sales to existing fleets. In the reporting year, there were no material changes in fuel sales to fleets. Of course, because of the marketing margin reduction, inter alia, the refueling discounts granted to Delek Israel's customers have begun to decrease. On October 23, 2011, the Universal Refueling Device Regulations were published concerning coercing the fuel companies to install a universal refueling device system to enable the consumer to sign an agreement with various fuel companies and refuel at other fuel companies using the same device. For further information, see section 1.8.19A.8 below.

F. Key success factors in this segment and the changes in them

Delek Israel estimates that the key success factors in the segment are:

1. Nationwide fuel station deployment.
2. Financial strength which allows Delek Israel to invest in constructing new gas stations owned by the Company, refurbishing and expanding existing station, including financing working capital, and purchasing or setting up storage and supply facilities as well as to invest in the existing facilities.
3. Capacity to raise capital from banking and non-banking sources.
4. Setting up a chain of convenience stores and retail areas.
5. Capacity to provide customer credit, including to fleets refueling with the Dalkan electronic identification system.
6. Proprietary rights in properties that gas stations are built.
7. Terms of agreements with the station operators.
8. Attractive agreement terms with fuel suppliers.
9. Attractive agreement terms with convenience product suppliers.
10. Availability and storage capacity of fuels and various products.
11. Competitive prices offered in the tenders of major institutional clients.
12. State-of-the-art marketing and logistics systems.
13. A developed collection and credit control system.
14. A cutting-edge compound control system.
15. Substantial branding of Delek Israel's products compared to its competitors.
16. Equipment and professional services provided by Delek Israel to its customers, including fleets.

³² Products found on the gas pump islands, such as mineral water, children's toys, oils, etc.

17. Successful integration of the commercial operations alongside the fuel operations, such as integrating the Joe coffee shop chain in Delek Israel's compounds, including the sale of Joe coffee products in the convenience stores.
18. Collaboration with retail chains to utilize joint logistics platforms and obtain better purchasing terms, e.g. Israel Postal Services, ACE, Auto Depot and customer membership clubs.
19. Diverse marketing and distribution channels throughout Israel, including an independent marketing system and independent agents.
20. In the Direct Marketing branded products (like Delek oils), the important success factors are reputation, know-how and professionalism, quality control systems and human capital.
21. Geographic location of storage and supply facilities where the oil product pipeline is located.
22. Obtaining the required statutory permits for the foregoing operations.

G. Changes in the segment's supplier and raw materials array

There are two oil refineries in Israel – one in Haifa (ORL) and the other in Ashdod (ORA), which were State-owned until the ORL privatization. Since the ORL privatization, Delek Israel has two potential local suppliers of fuel products (ORL and ORA). At the same time, it should be noted that due to the fact that ORA supplies fuels mainly for Paz Oil Company Ltd. (the parent company of ORA) Delek Israel's primary potential fuel supplier is ORL and import sources overseas. For further details see Section 1.8.13B below.

H. Main entry and exit barriers in the fuel segment

The main entry barriers in the segment:

1. The high costs involved in locating and setting up gas stations, which are affected by the high gas station construction standards; establishing the production facilities, purchasing and developing know-how and technology and the need to obtain regulatory permits required to enter the direct marketing compound segment; or constructing storage and supply facilities.
2. A key entry barrier into the direct marketing segment is the financial strength required from a marketing company selling the products which it produces due to the need to extend high customer credit, because of the high fuel prices and diesel oil excise tax.
3. A key entry barrier into the fuel storage and supply segment is ownership of the storage facilities in geographical locations where the oil product pipeline is situated
4. The long period required to obtain a permit to construct and operate gas stations.
5. Existing regulatory restrictions in the storage and supply segment, including legislation and regulation relating to planning, construction and environmental protection.
6. Competition with other old-established fuel companies in all segments.
7. The need for substantial credit resources to finance purchasing oil products and granting credit to the station operators and fleet customers.

The key exit barrier to the fuel storage and supply segment is rental contracts/leases/operating contracts with land/station owners. The key exit barriers in the storage and supply segment are the material investments made in facilities and the liabilities and restrictions which Delek Israel assumed as part of acquiring the terminals (see section 1.8.20D below).

I. Substitutes for existing products and the changes in them

In 2003, the Israeli Government approved Amendment No.3 to National Outline Plan No.18 permitting the use of LPG to refuel vehicles in gas stations ("**Automotive LPG**"). As of the reporting date, Delek Israel has four gas stations where vehicles may refuel with LPG and in 2012, through a subsidiary, it is expected to install such LPG refueling points at another 10 stations. This information is forward-looking information as defined in the Securities Law, based on Information at Delek Israel on the report date and includes its assessments or intentions as at the report date. This information may not materialize, *inter alia*, due to incidents occurring contrary to its expectations and intentions. Moreover, in recent years hybrid vehicles with a combined gasoline and electric motor have been begun selling resulting

in less gasoline is consumed. Delek Israel estimates that as of the reporting date, the number of vehicles in Israel suited for automotive LPG, or the number of hybrid vehicles, is negligible. Elements in the auto industry and other entities have recently been involved in developing cars that run only on electricity. In this regard, it is noted that the company, Better Place, is currently establishing electric car charging stations and battery replacement points as infrastructure for selling battery -powered electric vehicles which are charged while traveling and at such charging stations. To the best of Delek Israel's knowledge, Better Place has dozens of parking lots with suitable infrastructure for loading, but has only sold several hundred electric cars. Delek Israel considers the development of alternative vehicles to those powered by fuel a threat to the fuel sales at gas stations. However, it is unable to estimate the extent of the impact, if at all, this may have on its fuel sales at gas stations and its profitability from such sales. In the fuel storage and supply segment, the transition to using alternative energy sources which are not oil may materially affect fuel consumption in the market and as a result, also this segment.

J. Structure of the competition and the changes therein

There are four large competitors in this market (including Delek Israel). To the best of Delek Israel's knowledge, Paz holds 27% of the country's gas stations while Delek Israel holds 23%, Sonol holds 21% and Dor Alon holds 18%³³. Delek Israel believes that each of its three main competitors has a nationwide gas station chain and the capability to provide fleet services.

There are also numerous smaller companies which together, at the reporting date, operate 9% of the public gas stations in Israel

The competition for private consumers is mainly reflected in price, range of services and the sale of related products at the gas stations.

The competition for fleet customers is expressed in price, credit terms and providing value-added services (such as fuel consumption analysis reports, car wash services, etc.).

The competition between the fuel companies is expressed by the renewal of existing contracts with gas stations owners and competition for the location of new gas stations, while the demand for gas stations in specific potentially lucrative locations leads to higher rent or higher purchase prices payable to land owners and erodes the profitability of the fuel companies.

Competition in the direct marketing segment is also intense, and is reflected in discounts, favorable customer credit terms and competition for the quality of service provided. Competition in this segment exists among all the fuel companies, large and small alike.

Infrastructure companies and the three major fuel companies (Delek Israel, Paz and Sonol) operate in the fuel storage and supply segment. The geographical location of the storage and supply facilities of each of these companies is different. Competition in this segment is affected primarily by the location of the facilities of each of the companies operating in it, the costs involved in transporting the fuel to the end user, and the price for fuel storage and supply services, which is partly controlled.

1.8.2 **Products and Services**

The products marketed by Delek Israel and the services it provides in this segment are mainly the following:

A. Fuel products and other services

1. Distillates ("White Products")

Various types of gasoline	– used as fuel in vehicles with a gasoline engine and sold mainly at gas stations.
Diesel oil	– used mainly as fuel in vehicles with diesel engines, for heating and in industry.
LPG	– used as fuel for vehicles powered by gas.
Kerosene	– used mainly for heating in industry and in the home.
Jet fuel	– used for refueling aircraft.

³³ These data are taken from the websites of the major fuel companies as at the reporting date.

2. Residues ("Black Products")

Fuel oil	–	used mainly as a fuel for industry, ships and producing electricity.
Bitumen (tar)	–	used mainly as a raw material in the manufacture of asphalt and as a sealant and sold mainly to earthworks contractors.

3. Industrial Products

Delek Israel sells automobile and industrial oils and byproducts from its own production and from imports. The industrial products, such as engine oils, lubricants, greases, water paints, fuel oil and oil products (including diesel oil) for industry are sold to industrial plants, garages, business customers, agriculture and to other entities. Until January 3, 2011, Delek Israel also engaged in producing and marketing insulation and sealing products for the building industry and bitumen products for the infrastructure companies through Bitum Industries Ltd. (. "**Bitum**"), a subsidiary in which Delek Israel held 60% of the shares. On January 3, 2011, Delek Israel sold all its shares in Bitum to a third party for NIS 17.3 million. Moreover, Delek Oils has a partnership with Sano-Intertrans called Deleksan Partnership ("**Deleksan**"), which was established on September 1, 2010 with the purpose of recycling industrial solvents by performing a range of separation and purification of wastes processes, all aimed at salvaging the greatest percentage of materials possible from the wastes. The recycling process is performed through dedicated facilities. As of the reporting date, Deleksan operates two solvent recycling facilities.

4. Ship services

Delek Israel provides services for ships anchored in Haifa, Ashdod and Eilat ports, including port, electricity and cash withdrawal services, as well as referrals to local offices and payment of fees, etc.

B. Retail products

Delek Israel sells a selection of retail products such as food products (sandwiches, baked goods, snacks, etc.), beverages, cigarettes and other products at its Menta convenience stores. In 2010, Delek Israel, together with Israel Posy Company, began establishing postal service points at Delek Israel's convenience stores. As at publication date, Delek Israel operates 25 service points, while in 2012 Delek Israel anticipates establishing further service points. Most of the basic services provided by the postal agencies are carried out at these points. Together with Israel Post Company, Delek Israel is examining expansion of the basket of services provided at these points. In addition, most of its gas stations sell car-related accessories. The majority of Menta stores operate 24/7. As at December 31, 2011 and December 31, 2010, 190 and 173 Menta stores operated at Delek Israel gas stations respectively. As of the report publication date, Delek Israel operates 10 convenience stores outside gas station and commercial compounds; seven convenience stores operate at train stations, one at a hospital and two at academic colleges in central Israel.

Most Menta stores are operated by Delek Israel and it plans expanding their nationwide deployment at additional gas stations. It also plans increasing the range of products and services offered in some of the stores. In the latter half of 2008, Delek Israel also began operating convenience stores by means of franchisees and currently 12 convenience stores are operated by this method.

At end December, Delek Israel completed the acquisition of 51% of issued and paid up share capital of Joe Coffee Gourmet Ltd. ("**Joe Chain**") under an agreement dated September 22, 2011 signed between Delek Israel on the one part and Joe Chain and Joe Chain shareholders on the second part. At the same time, it also signed a franchise agreement with Joe Chain under which the coffee and food sales points currently operated at its convenience stores will gradually be converted to a store-in-store and branded under Cup-O-Joe.

C. Supply services

Delek Israel provides supply services of various fuels from its four facilities: gasoline, diesel oil and kerosene are supplied from the Ashdod facility, 95 octane gasoline, kerosene, diesel oil (transport and heating), light fuel oil and brown fuel from the Haifa facility, and only diesel oil and kerosene from the Beer Sheva and Jerusalem facilities. The supply service is provided to road tankers which carry the fuels to the fuel companies (including Delek Israel) that either

transport the fuels to their customers or supply them by direct piping to the customer's premises. In Haifa, Delek Israel also stores distillates from ORL and the distillate port at its Haifa facility. In 2010 and 2011, the three terminals and the Haifa facility supplied 2,610 thousands kl and 2,570 thousands kl of fuel products respectively. In 2011, 40% of the supply at the Ashdod, Beer Sheva and Jerusalem facilities and 93% of the supply at the Haifa facility were for Delek Israel.

D. Storage services

The storage services include operational storage for the fuel companies receiving supply services from Delek Israel (including Delek Israel itself), storage of a State defense stock through the fuel companies, commercial storage through leasing of storage tanks to Delek Israel's customers (IEC, ORL and other commercial entities) and temporary storage ("in transit" storage) in five transit tanks at the Ashdod facility of fuel piped directly to FPL's customers throughout Israel.

Delek Israel also sells fuel additives for the fuels to meet the Standards Institution of Israel standards and provides a additives adding service for the fuel that it supplies.

1.8.3 Breakdown of revenues

The following is the amount and proportion of Delek Israel's income of total Group revenues, divided by product or service groups for which the total revenues account for at least 10% of the revenues of the Delek Group in 2011, 2010 and 2009 (including excise taxes):

	Product	Total sales NIS millions		% of segment revenues		% of Group's revenues	
		Less excise	Including excise	Including excise	Less excise	Including excise	Less excise
2011	Fuels and oils	5,888	3,131	95.5%	91.9%	10%	5.3%
2010	Fuels and oils	5,384	2,628	95.9%	92.1%	12.6%	6.1%
2009	Fuels and oils	4,537	2,132	96.5%	92.7%	12.2%	5.8%

It is noted that the revenues from the oils sales are not material and the profit margin from them is higher than from the fuel sales.. Delek Israel's revenues from the retail products sales at its convenience stores in 2011, 2010 and 2009 were not material and the profit margin from them is higher than from the fuel sales.

Gross profit stemming from oil products in Israel in 2011, 2010 and 2009 amounted to NIS 762 million, NIS 735 million and NIS 736 million, respectively.

1.8.4 New products

Delek Israel plans to increase the diversity of the products and services offered at its convenience stores. Currently, the products and services at the convenience stores include, *inter alia*, postal services (in cooperation with Israel Post), products such as easy-park devices and device loading services, ACE products, and cellular products. In this context, it is noted that at the end of December 2011, Delek Israel completed the acquisition of 51% of the issued and paid up capital of the Joe chain, in which Delek Israel contracted with the Joe chain in a franchise agreement dated September 22, 2011 under which the coffee and food product selling points currently operated at Delek Israel's convenience stores will gradually be converted to a store-in-store model which will be branded under Cup-O-Joe. Under the franchise agreement, as part of converting the existing points, Delek Israel will purchase equipment and coffee machines from the Joe chain to prepare coffee in the usual Joe chain quality as determined by the Joe chain (while Delek Israel will determine the number of machines required at each point). A brand experience will be built in agreement based on the brand policy prescribed by the coffee house chain for the sale of Cup-O-Joe products throughout Israel. The franchise agreement stipulates that the existing points will be converted by Delek Israel gradually in a process beginning upon signing the agreement and ending in 2014. Under the franchise agreement, the Joe chain granted Delek Israel and anyone on its behalf operating a store-in-store a license to use the trademarks, including the name Cup-O-Joe in the convenience stores operated by Delek Israel, all under the terms stipulated in the agreement. The franchise agreement also stipulates that in return for the license to use the trademarks and Cup-O-Joe brand (in this section: "the **Brand**"), Delek Israel will pay the Joe chain a fixed one-time amount for each Menta store converted to use the brand as well as a monthly amount equal to the percentage stipulated in the agreement of the monthly turnover of all the convenience stores using the brand. This agreement is valid for 10 years. Delek Israel is also granted a five option periods of

two years each, providing it with the right to extend the agreement for a cumulative period of a further ten years, subject to prior written notice 90-days before the expiry date of the agreement and the relevant option period. Despite this, it is prescribed that Delek Israel will be entitled to terminate the agreement three years after signing the agreement (including in the option period) by six months prior written notice.

Until the end of 2011, Delek Israel took steps to complete Cup-O-Joe chain's work plan (with respect to the Menta chain and the Cup-O-Joe coffee shops not connected to the Menta chain) and also completed its plan to assimilate Cup-O-Joe (coffee and food) at the gas station and commercial compounds belonging to the Menta chain. As of the reporting date, a pilot is underway to examine the manner of assimilating these solutions at Delek Israel's compounds, as part of which, a variety of Cup-O-Joe brand products in the following segments have been deployed at compounds: Coffee, pastries, sandwiches, and various meal solutions. Suitable equipment, visible accessories and branding complying with the Cup-O-Joe brand have been placed at the compounds participating in the pilot. Delek Israel intends assimilating Cup-O-Joe in all gas station and commercial compounds. In 2012, it plans doing so in 100 compounds.

Deployment throughout the chain will bring about an annual investment of millions of NIS from Delek Israel's ongoing investments, while such ongoing investment budget is not expected to increase this year compared to the previous two. Moreover, as at the report date, Delek Israel has established 10 new stores in the ministore concept under the Menta Market brand. This convenience store differs from the others both in size and offering a wider range of products.

1.8.5 Customers

A. Delek Israel's customers may be classified into groups as follows:

1. Gas station and convenience store customers, divided into two main groups:

- A) Private customers who buy fuel products, lubricants or retail products at the gas stations and convenience stores operated by Delek Israel. Delek Israel sets the selling prices to the end user at the stations that it operates, while the selling price of 95 octane gasoline is limited as it is government controlled. The difference between the selling price to end users and the cumulative ORL ex-refinery gasoline price, including excise taxes and infrastructure service payments is called the "Marketing Expenses Basket" or "marketing margin". The selling price at stations operated by an external operator is set in an agreement between the parties, while the operator sets the price for random customers.
- B) Corporate customers, including fleets subscribing to the Dalkan service, tender customers ("Dalkan customers") and gas stations associated with Delek Israel under operating contracts on behalf of Delek Israel and supply contracts for the purchase of fuel and oil products. These customers differ from the private consumers mainly in the credit terms (which are longer) and discounts which they receive.

It should be noted that during the ordinary course of business, and as is customary in the fuel segment, Delek Israel extends credit to its customers at the gas station and commercial compounds for several purposes: (a) Enterprise loans – as part of a third party (that is not Delek Israel) agreement with a landowner for the development and construction of a gas station by the third party or Delek Israel, where the gas station is subsequently leased to Delek Israel and Delek Israel provides the third party (the land purchaser) with a loan to purchase the land. These loans are generally repaid by offsetting the future rent which the gas station owner is eligible for; (b) commercial loans given for the renewal of a contract – occasionally, in the agreements to renew the contractual arrangement with a gas station owner under a rental or supply agreement, Delek Israel provides the gas station owner with a loan. These loans are repaid by offsetting the current rent which the gas station owner is eligible for or against current cash receipts from the borrower under a predetermined schedule; (c) agreements for scheduling a debt of those who operate gas station on behalf of Delek Israel or independent gas station operators. Occasionally, due to cash flow or other reasons, these operators request converting part of their debt balance into a loan, with this loan being spread out over several periods which cumulatively do not exceed the remaining term of the agreement between Delek Israel and the operator. Most of the enterprise and commercial loans are backed by a charge on the land where the gas station is located and most of the debt scheduling loans are without collateral.

The total balance of these loans at December 31, 2011, is NIS 158 million, of which NIS 8 million are in respect of enterprise loans, NIS 108 million in respect of commercial loans and NIS 42 million in respect of debt scheduling agreements.

The marketing margin is the difference between Delek Israel's selling price to its customers and the accrued amount of the ORL ex-refinery fuel price plus excise taxes. The maximum margin element for 95 octane lead-free gasoline is a fixed amount (due to government control) which is not materially affected by ORL ex-works fuel price fluctuations (whether controlled or not) and changes in excise tax values and infrastructure rates. It is noted that in circumstances where the global market fuel prices and the taxes thereon increase, a situation arises where there is no built-in compensation for financing and credit risk costs when the customer credit increases.

2. Direct marketing customers: These include private customers, tender customers (both government companies and commercial companies), and corporate customers such as industrial plants, sea craft, infrastructure contractors, etc.
 3. Fuel storage and supply customers: These are private customers, including the fuel companies (including Delek Israel), and governmental customers, including FPL, the Ministry of Defense and IEC.
- B. Below is a breakdown of sales in the gas station and commercial compounds (including excise) in 2011 and 2010 by type of customer (in NIS millions and as a percentage of the total revenues in the segment in that year):

Type of customer	2011		2010	
	NIS millions	% of total segment revenue	NIS millions	% of total segment revenue
Corporate (incl. tenders and Dalkan)*	1,983	20%	1,765	20%
Operating/supply stations	1,436	14%	1,426	16%
Private	2,745	27%	2,420	28%
Total	6,164	61%	5,611	64%

* The operational profit percentages from sales to tender and Dalkan customers are similar.

1.8.6 Marketing and distribution

Below is a brief description of Delek Israel's marketing methods:

A. Marketing at gas stations

Marketing to the public – Delek Israel promotes its products and services in several ways: discounts, national or station-specific special offers and using sales promoters (e.g. distributing newspapers free or at discounted prices to customers buying gas for more than a certain amount, car wash at discounted price), and advertising in the media. Delek Israel also invests in maintenance and upgrading its gas stations and the services provided there, refurbishing old stations and improving their exteriors and is also working to expand the range of services provided at the stations.

Marketing of the Dalkan electronic identification system – Delek Israel employs marketing staff and hires outside sales promoters to recruit new Dalkan customers. Delek Israel also participates in tenders published by companies and bodies with large fleets seeking collective gas service arrangements

Moreover, Delek Israel operates a fueling service through a network card ("**Station Owner Card**"), which allows private firms to obtain credit and discounts on fuel purchases at gas stations in the vicinity of their business.

B. Expanding deployment of gas stations, convenience stores and retail areas

1. Delek Israel employs an enterprise manager to identify potential locations and entities interested in partnering with the company to set up gas stations. In the forthcoming year, Delek Israel estimates that it will reach deployment of over 210 convenience stores, i.e. to

set up 20 additional stores (whether operated by the Company or through franchises). This information concerning expansion of the convenience store chain is forward-looking information, which may not materialize, *inter alia*, due to the need to obtain the approval of the holder of the rights in the gas station, difficulties in obtaining the necessary approval to establish retail areas (to set up a retail area, Delek Israel is sometimes required to change the urban building plan applicable to the retail areas, obtain building permits, etc.), regulatory changes which might impede the construction of additional outlets, economic viability, heightened competition among convenience stores, an economic recession which would weaken sales at convenience stores, etc.

2. Delek Retail Lots Ltd. ("**DRL**"), a wholly owned subsidiary of Delek Israel, specializes in identifying and purchasing 50% or more of the ownership in land where it will initiate, plan, build and operate real estate enterprises which include gas stations and commercial centers. As of the reporting date, DRL has acquired fourteen plots where it plans to operate in this manner (two already had active gas stations and commercial centers when they were acquired, four have begun operating by the reporting date and eight are in advanced planning stages, which are expected to be built between 2012 and 2015).

C. Marketing and distribution in direct marketing

In the direct marketing operation, Delek Israel has a marketing and sales system, either alone or through investee corporations, to market the products to the end customers. Delek Israel also has contractual arrangements with fuel agents (third parties), selling fuel to end customers, who are the agents' customers. The transportation of oil products marketed by Delek Israel in the direct marketing segment is mainly through its subsidiary Delek Transportation, through various subcontractor carriers and by direct piping to the customer. Delek Israel is not dependent on any single agent marketing the fuel products, but the entire marketing array is material for it. On February 21, 2012, Delek Israel completed the acquisition of Delek Gas' operation including 600 NIS 1 par value shares of Delek-Yagel G.P.M Ltd. ("Delek-Yagel"), representing 60% of its issued and paid up capital, Delek Gas' share of the shareholders' loans granted to Delek-Yagel, agreements which Delek Gas is engaged in for the supply of gas consumption, import of equipment and establishment of a natural gas compression and trailer filling facility on land rented to it, and Delek Gas's vehicles, in return for NIS 2 million. The remaining Delek-Yagel shares (40%) are held by Gaz Yagel Marketing & Distribution Gas (1996) Ltd. ("**Gaz Yagel**"). LPG is supplied by Delek-Yagel through Gaz Yagel.

D. Exclusive agreements

Delek Israel has an exclusive representation agreement, which is not material, with international corporation Exxon Mobile to market the latter's oils in Israel. The agreement is effective through December 31, 2011, and can be canceled under the customary terms in such agreements.

Moreover, most of Delek Israel's supply agreements with gas stations are for exclusive supply of fuel products during the contract period. For information of the supply contracts, see section 1.8.10C below.

1.8.7 Competition

- A. According to data published by the authorities, there are over 40 fuel companies registered in Israel and licensed to purchase oil products from ORL. Together, the four major companies hold the major market share in Israel. Delek Israel estimates that it is the second largest fuel marketing company in Israel, its main competitors being Paz, which markets fuel products to 280 gas stations (26% of all gas stations), Sonol, which Delek Israel estimates markets to about 232 stations (21%) and Dor Alon which Delek Israel estimates markets to about 195 stations (19%).
- B. The Israeli fuel economy is currently characterized by fierce competition in all of Delek Israel's areas of operation, as follows:
 1. Expansion of the fuel companies' gas station deployment and location, whether by identifying new locations and setting up new stations or through agreements with old-established gas stations whose operating/supply contracts have expired.
 2. Marketing to end consumers and increasing sales at gas stations. This competition is reflected in the erosion of marketing margins, granting discounts, holding various sales

promotions, the service provided at the stations, and the range of services offered to the customer.

3. Entry of fuel and retail companies into retail operations on the gas station premises
 4. Competition in marketing to fleets, which is primarily between the major fuel companies, is reflected primarily in competition over the prices offered to the fleets and the additional services provided by the fuel companies, such as electronic reports and media, fleet management software, car-wash services, etc.
 5. The direct marketing competition has become extremely aggressive, due to both the factors driving competition in the fuel industry in general and issues that are unique to this segment. Since the bulk of supply is carried out directly to the customer, independent of the physical location of the marketer (i.e. the gas station), and no major financial investment in facilities is necessary, there is fierce competition among all the rival parties for each and every customer, with none of them having any comparative advantage. The competition is reflected in the price and credit terms granted to the customers. The fierce direct marketing competition arises, *inter alia*, from the fact that some of the oil products are generic with limited importance as to their origin and/or quality and from the low transfer costs (for both the customers and the fuel companies) and the terms of the arrangements with customer made in the framework of tenders or short-term contracts.
 6. Competition in the fuel storage and supply segment is affected mainly by the location of the storage facilities of each of the companies (the infrastructure and fuel companies), the costs of transporting the fuel to the end consumer and fuel storage and supply service price, which is partially controlled.
- C. Below are the key ways that Delek Israel deals with competition and the factors affecting its competitive status:
1. Delek Israel is acting to expand deployment of the gas stations that it is associated with and estimates that nationwide gas station deployment increases their accessibility and gives it a competitive edge with private and Dalkan customers for whom a wide distribution of gas stations is especially important.
 2. Expansion of marketing additional products and services in gas stations based on the existing infrastructure.
 3. Delek Israel is taking measures to streamline the ongoing operation of all segments, to strengthen its capacity to grant customer discounts and thus increase sales.
 4. Improving the appearance, atmosphere and service at gas stations.
 5. Improving the stations' operating structure.
 6. Capacity to grant customer credit bearing in mind that credit exposure is a risk factor.
 7. Financial strength and a developed, supervised marketing array with a high-level command and control capacity.
 8. Levels of readiness to manufacture and supply large quantities when necessary.
 9. In the fuel storage and supply segment, the key manner that Delek Israel deals with competition is providing better service and more competitive prices. The costs differences versus the other infrastructure companies and the different storage capacity of each company operating in this area affect Delek Israel's competitive status in this segment.

1.8.8 Seasonality

Delek Israel is generally not affected by seasonality. Nevertheless, it is noted that in recent years summer gas station fuel sales have grown substantially. Delek Israel believes that this stems, *inter alia*, from increased car travel to vacation destinations and the use of air-conditioning in cars, which increases fuel consumption. During Jewish holidays (usually one or two days), fuel consumption decreases substantially, especially in the business and industrial segments, while sales of retail products increase compared to the rest of the week.

Seasonality does not exist for most direct marketing products. However, diesel oil and kerosene sales for domestic heating and sales to industrial customers increase during the winter, i.e. in the first and fourth quarter of each calendar year.

The effects of seasonality on the fuel storage and supply activity are immaterial.

1.8.9 Direct marketing production capacity

The maximum potential production capacity at the plant manufacturing oils and auxiliary products for vehicles and industry ("Delek Lubricants Plant") is 40,000 tons annually. The annual oil production capacity utilized at this plant is around 15,000 tons.

For a description of the maximum and utilized capacity of the storage and supply facilities, see section 1.8.10G below

1.8.10 Property, plant and equipment, and facilities

- A. As of December 31, 2011, Delek Israel owns or leases from ILA 55 gas stations (including 10 jointly owned with third parties) and 171 stations nationwide leased or rented under long-term agreements. Delek Israel also has fuel storage and supply depots in Ashdod, Beer Sheva and Jerusalem, a fuel supply depot in Haifa, a fuel oil supply depot in Ashdod, and a lubricant manufacturing and mixing plant in Lod.

As at December 31, 2011, Delek Israel operates 202 of the above gas stations, while 20 are operated by third parties on behalf of Delek Israel under operating agreements and 27 are operated by third parties under supply agreements. All the gas stations are branded Delek or Gal and sell Delek Israel products exclusively.

Below are Delek Israel's gas stations, classified according to proprietary rights in the land and terms of station operation, at December 31, 2011:

Type of station	Self operation (Delek Retail)	Operated by Delek-appointed operator	Operated by contractor (supply)	Total
Ownership and ILA lease	47	8	-	55
Disabled IDF veterans	20	1	4	25
Rent under three years	31	1	-	32
Rent above three years	107	4	3	114
No proprietary rights (supply)	-	-	20	20
Total	205	14	27	246

B. Proprietary rights in station land

Delek Israel's gas stations are divided into four categories from the aspect of ownership of the land where the stations are located as follows:

- Stations owned by Delek Israel or leased from Israel Land Administration (ILA) include stations where the land is owned by Delek Israel or leased from ILA, with some stations jointly owned with a third party.
- IDF veteran stations, which were established pursuant to an interministry agreement between the State and the fuel companies. This arrangement stipulates that ILA land would only be allocated for establishing gas stations if the right to operate them is awarded to a disabled IDF veteran selected by the Rehabilitation Department of the Ministry of Defense for his rehabilitation. This guideline was modified in the 1990s and currently ILA allocates land for gas stations directly to the fuel companies, and not under the disabled IDF veteran rehabilitation agreement. Under this agreement, the disabled IDF veteran is granted primary leasing rights for 49 years with an option for extension for a further 49 years. Concurrently, the fuel companies are granted secondary leasing rights for the same term in return for leasing fees equal to the leasing fees paid by the veteran to ILA. Delek Israel would lease the land for establishing the gas station, install the equipment needed for its operation and maintain its systems. After establishing the station, Delek Israel appoints the veteran as an operator on its behalf, so that he must purchase all oil products exclusively from Delek Israel, and the oil product prices to the station (i.e. the sale prices to the veteran) are determined by Delek Israel. Under the agreements, in some cases the veterans have undertaken to pledge the station land to Delek Israel to secure their obligations, but in most cases this pledge has yet to be registered and only the contractual obligation exists. In this context it should be noted that under new Ministry of Defense guidelines pertaining to gas stations and the rehabilitation of veteran soldiers, approval must be received from the Rehabilitation Department of the Ministry of Defense for any transfer of operating rights for the said gas station to a third

party, including Delek Israel, requiring Ministry of Defense consent and approval (this requirement appears, *inter alia*, in the gas station leasing agreement). The Ministry of Defense emphasizes that its principle policy is that the station is designated for the veteran's occupational rehabilitation and therefore cannot be transferred to a third party. The Rehabilitation Department sent a letter to Delek Israel requesting details pertaining to stations owned by veteran soldiers which has contracts with Delek Israel, and Delek Israel provided this information. It should be noted that if the Rehabilitation Department does not approve operation of the veteran stations by Delek Israel, it will order the termination of the operating agreement between Delek Israel and the veteran and Delek Israel will only be permitted to supply fuel to those stations. As of the reporting date, the status of the above investigation conducted by the Rehabilitation Department of the disabled IDF veteran stations operated by Delek Israel has not changed. If Delek Israel's rental agreements with the 21 disabled IDF veteran stations are terminated, this will not affect it materially.

- Rented stations include those where Delek Israel is sub-lessee or lessee from a third party which is not ILA and stations under long-term or short-term rental. Delek Israel usually commits to establish the station at its own expense, to install most of the equipment required for normal operation, and to maintain all its systems. At these stations, the operator is obligated to purchase all oil products exclusively from Delek Israel and their prices to the station operator are determined by Delek Israel. By the end of 2012, rental rights of Delek Israel in 5 gas stations are expected to expire. However, based on past experience, Delek Israel estimates that a rental agreement will be signed for most of these stations for a further period, although it is uncertain that such agreements will be signed or that the rent will not change when renewing those contracts.
- Stations where Delek Israel has no proprietary, possession or usage rights are those where it has signed agreements with station owners usually granting it exclusivity in supplying fuel products for a one-year term, with the owner alone having the option to demand renewal of the agreement for a further one to three years; the remaining cases include provisions with regard to commercial terms. In many of these agreements there is no collateral for the supply of fuel product. The supply agreements for these stations will end by end of 2014. Nevertheless, in view of past experience and relationships with the owners of these stations, Delek Israel estimates that in most of them, supply will continue after expiration of the supply agreement. This estimate by Delek Israel is forward-looking information which may not materialize, *inter alia*, if the supply agreements are not renewed or if margins do not change upon their renewal. If the agreements are not renewed, Delek Israel foresees no material impairment of its business. For information of restrictions in antitrust laws applicable to Delek Israel's contracts with the owners of rights in gas stations, see section 1.8.19E.3.J) below.

C. Gas stations are operated in several ways:

- By Delek Israel through Delek Menta Roadway Retail Stores Ltd.³⁴ (“**Delek Menta**”).
- By a third party appointed by Delek Israel. Gas stations in this arrangement carry Delek Israel signage and purchase all products exclusively from it. The operator is obliged to operate the station under Delek Israel procedures which include, *inter alia*, criteria for opening hours, uniform exterior appearance, maintenance standards and quality of service. Usually, the operator bears most of the gas station operating cost, including staff hire and purchase of inventory from Delek Israel. In some cases Delek Israel contributes to operating costs (property tax, station maintenance, leasing fees if the station is leased, participation in discounts to Dalkan or refueling card customers). In other cases, it does not participate in the operators' costs, but grants discounts on the prices of the fuels sold to them. The operator is responsible for obtaining the licenses and permits required to operate the station, but in some cases Delek Israel processes and pays for compliance

³⁴ On December 31, 2009, a merger agreement was signed between Delek Retail and Delek Menta under which in the first stage Delek Retail would transfer all its assets to the new company set up especially for this purpose, in return for allotment of shares in the new company and against liabilities and/or trade receivables and payables, and in the second stage (immediately following the first stage), the new company would merge with Delek Menta so that all its assets and liabilities would be transferred to Delek Menta and the new company would be dissolved without liquidation. On December 29, 2010, the Tax Authority approved this merger and in January 2012, the merger was completed after receiving approval from the Registrar of Companies.

with regulatory requirements applicable to the gas station. The operator pays Delek Israel fixed and/or variable rent, based on sales volume at the station.

- By an independent third party not appointed by Delek Israel. In these stations there are actually short-term supply agreements of a year, with the operator alone having the option to request renewal of the agreement for another year, for up to three years. The supply agreements require operators to purchase fuel and lubricant products from Delek Israel at agreed prices and credit terms and sell them under Delek Israel trademarks, under its name, within price control restrictions and under Delek Israel's instructions concerning safety procedures, marketing, the gas station's exterior appearance etc.

Delek Israel usually owns the gas station equipment and lends it to the station operator. Delek Israel installs the equipment required to operate the station and provides the owner of the rights with maintenance services and professional training under the contractual agreement. In most cases there is no collateral for selling fuel to stations. In some cases, Delek Israel has no exclusivity in supplying fuel products.

- D. All Menta convenience stores are operated by Delek Israel through Delek Menta, except for 10 stores operated by franchisees. All Menta store employees are Delek Menta's employees. Delek Menta purchases the inventory and bears the risk involved in operating the convenience stores. In 2008, Delek Israel began operating convenience stores through franchisees who run them with their own employees. The franchisees purchase the inventories and bear all the risk involved in operating the stores. Delek Israel will decide in each case, based on business considerations, whether to operate the convenience store through franchisees, if at all. Cup-O-Joe will be introduced at Menta stores in the store-in-store concept, while Cup-O-Joe is responsible to supply and continually maintain equipment and supply Cup-O-Joe products for sale.
- E. Delek Israel's property, plant and equipment in gas stations and convenience stores operations include the buildings and equipment in most public gas stations where it has ownership rights. It also has equipment installed in all its stations where it has no ownership rights or where it has short-term lease agreements. At some of these stations, Delek Israel also has property, plant and equipment in station buildings constructed many years ago, when it had ownership rights (including long-term lease contracts) there. Delek Israel's equipment in its stations includes everything needed to operate them and the convenience stores, including tanks, pipes, pumps, computer and communication systems, office equipment, store furniture and accessories, electrical systems and generators if required, fire extinguishers and public toilets. It also has vehicles and trucks to transport the fuel products, paint and oil.
- F. Delek Israel's property, plant and equipment in the direct marketing segment includes the equipment on customer premises and in their facilities (mainly designated tanks and pumps) and equipment at the interior stations, including infrastructure, tanks, pipelines, electronic pumps, electronic refueling control systems.

Delek Israel also has a fuel supply depot in Ashdod, which it leases from Ashdod Port Ltd. ("**Ashdod Port**") until June 1, 2013.

Delek Israel has a 4.9 hectare plant in Lod, of which 4.7 hectares are owned by Delek Israel and the rest is leased from ILA. The plant contains lubricant mixing, filling and packing facilities, a lubricant re-refining installation, solvent manufacturing and recycling facilities, a central sewage treatment plant, warehouses, laboratories, various buildings, a water-based paint manufacturing plant and offices.

- G. Delek Israel's property, plant and equipment in the storage and supply operation includes four facilities: three in Ashdod, Beer Sheva and Jerusalem for providing storage and supply services for Delek Israel and third parties and the fourth in Haifa, for Delek Israel's own use. The Ashdod facility, Delek Israel's main storage and supply facility in Israel, is located on 32.9 hectares in the city's northern industrial zone. Delek Israel is entitled to be registered at ILA as owner of leasing rights in this land through June 30, 2019, with an option for a further 49 years. The Ashdod depot has 26 above-ground tanks with a maximum capacity of 506,000 cu.m. as well as six additive tanks and three water tanks. In practice, in 2011, 100% of the total above-ground tank capacity was utilized. Adjacent to the tank farm is an operating area which includes an administrative building, an office building and technical and special-purpose buildings. The Beer Sheva facility is situated on 7.9 hectares of land next to the Hatzerim road. Delek Israel is entitled to be registered

at ILA as owner of leasing rights in this land until July 31, 2015³⁵ with an option for a further 49 years. This facility has 10 above-ground tanks with maximum capacity of 72,000 cu.m. as well as two additive tanks and two water tanks. Adjacent to the tank farm is an operating area which includes an administrative building with restrooms and technical and special-purpose buildings. In practice, in 2011 a total of 69,000 cu.m. of the total above-ground tank capacity was utilized at this facility. The Jerusalem facility is located on the southern slopes of the Har Nof neighborhood, on 5.9 hectares of land on three levels, of which FPL holds 0.3 hectares under a separate leasing agreement. A plan was approved conditionally for filing by the Planning and Construction Subcommittee on March 25, 2002, whereby this land will be re-zoned for residential use. The plan has not progressed due to the opposition of green organizations to the location of the alternative site designated at the time, and the plan is no longer being processed. Delek Israel is entitled to be registered at ILA as owner of leasing rights in 5.5 hectares of land through March 19, 2015, with an optional extension for a further 49 years. ILA announced that it intends to renew the lease from April 1, 2008 for a further 49 years. In October 2011, the land rights at the Jerusalem facility were recorded at ILA in Delek Israel, name such that it took over from Pi Gllot. The Jerusalem facility has eight above-ground tanks with a maximum capacity of 33,500 cu. m as well as three additive tanks and one water tank. The operating area includes two office buildings and technical and special-purpose buildings. In practice, in 2011 a total of 10,000 cu. m out of the total above-ground tank³⁶ capacity was utilized. The Haifa facility is in the Haifa Bay area (Hof Shemen) on 3.1 hectares of land and is owned by Delek Israel. It has 14 tanks with maximum capacity of 20,000 cu. m, five additive tanks and water tanks. In practice, in 2011 Delek Israel used approximately 12,000 cu. m of the maximum tank capacity. Delek Israel also has the equipment required for the storage and supply operation.

1.8.11 Intangible assets

Delek Israel operates under several well-known, protected brands: "Delek" and "Gal" (gas station brands), "Menta" (convenience store brand), "Delkol" (oil brand) and "Dalkan Delek" (electronic refueling service brand). The Company also markets products under various brands, such as export lubricants under the Desko and Mapco brands, and is the exclusive importer of Exxon Mobil products in Israel.

1.8.12 Human resources

A. Delek Israel employees at December 31, 2011 and December 31, 2010:

Segment	No. of employees as of December 31, 2011	No. of employee as of December 31, 2010
Gas station and commercial compounds	2,149	2,069
Direct marketing	198	228
Storage and supply	90	106
Other	60	60
Total	2,497	2,463

- B. Most of Delek Israel's employees are hired under personal employment contracts and not subject to a special collective agreement, while special or general collective agreements apply to some by virtue of membership of the companies in employers organizations or by virtue of expansion orders. Delek Israel customarily grants its employees bonuses, based on performance and subject to the approval of the Board of Directors.
- C. It only employs road tanker drivers who are licensed to transport hazardous materials. Moreover, employees who work in the gas stations or come into contact with fuel materials, undergo fire fighting and hazard prevention training and environmental protection courses.
- D. Officers and senior management staff at Delek Israel are employed under personal employment contracts which include contributions to managers insurance. On November 5, 2007, Delek Israel adopted a stock options plan for 2007, under which Delek Israel granted, free of charge, to employees, officers and consultants up to 442,624 unlisted options ,

³⁵ The aforesaid date is according with Rights Confirmation issued by ILA. Under the leasing contract, the leasing rights are through August 20, 2015.

³⁶ Delek Israel is currently reviewing the option of changing the future use of the property at the Pi Gllot compound in Jerusalem, including taking steps to re-zoning the land for residential use.

exercisable for ordinary Delek Israel shares ("**the 2007 Plan**"), of which 109,483 options were granted to Mr. Moshe Amit, Chairman of Delek Israel's Board of Directors, and the remainder to employees, consultants and officers of Delek Israel and/or corporations which it controls. By December 31, 2011, 96,309 options expired due to termination of the employment of the employees who were allocated these options and 22,020 options were exercised for shares. The options will vest over a 5-year period, with the exercise price varying at each grant date. Exercise of options for shares by employees who are not senior officers is by means of cashless exercise, whereby the employee is eligible to receive shares reflecting the benefit component inherent in the exercised options, based on a formula set out in the Plan, in consideration of payment of the par value of the shares only. Employees who are senior officers can choose to exercise the options granted to them either by cash payment of the exercise price or by means of the above mechanism. The option can be exercised for shares, subject to their vesting schedule, through May 31, 2013, or prior to that date in the event of termination of employment or provision of services, as described in the Plan. The right to exercise is subject to adjustments described in the 2007 Plan. Senior Delek Israel officers are entitled to receive a loan to exercise the options, at annual interest of 4% linked (principal and interest) to the CPI known on the loan grant date. The loan will be a non-recourse loan secured only by a fixed senior lien on the underlying shares. Based on the Black & Scholes model, the theoretic financial value of a total of 324,295 options allocated to employees which have not expired as of December 31, 2011, amounts to NIS 12.897 million, based on the following parameters: price per ordinary share at the date of the Board's resolution concerning the allocation; exercise prices as aforesaid; annual standard deviation of 35.29%; option expiry date for the purpose of this calculation was calculated as an average of the purchase date of each tranche and the formal contractual expiry date; annual discount rate of 4%; rate of employee churn of 3% per year; the expected expiry date of non-recourse loans was calculated as the average between the expected contractual option expiry date and extension of the options by six months from the original expiry date. It is noted that after December 31, 2011, 43,792 options expired due to termination of employer-employee relations.

Below is further information of Delek Israel's employee stock options under the 2007 plan:

	Number of shares exercisable under the plan (fully diluted)	Value of benefit in options granted under the plan (NIS in thousands)	Expenses recognized in 2011 (NIS in thousands)
Employees (non-officers)	86,820	2,185	291
Officers	127,993	5,907	402
Chairman of the Board	109,483	4,805	-
Total	324,296	12,897	693

On August 31, 2009, Delek Israel adopted a plan to allocate options for 2009 under which Delek Israel awarded, free of charge, to employees of Delek Israel and/or companies under its control, 69,600 unlisted options are exercisable for ordinary Delek Israel NIS 1 par value shares ("**the 2009 Plan**"). The 2009 Plan was submitted for approval of the income tax authorities as required under the provisions of the Israeli Income Tax Ordinance (New Version) -1961 ("**the Ordinance**"). As of December 31, 2011, 23,000 of the options allocated under the 2009 plan expired due to termination of employment of the employees who were allocated these options. The table below presents particulars of the 2009 plan:

	Number of shares exercisable under the Plan (fully diluted)	Value of benefit in options granted under the plan (NIS in thousands)	Expenses recognized in 2011 (NIS in thousands)
Employees (non-officers)	16,600	679	186
Officers	30,000	1,249	293
Total	40,600	1,928	471

On August 1, 2010, after receiving the approval of the Audit Committee, Delek Israel's Board of Directors approved the allotment to Mr. Ben Assayag under the terms of his employment as Delek Israel's CEO of 283,099 unlisted options exercisable for up to 283,099 ordinary Delek Israel shares, free of charge, in work income track in accordance with section 102B(1) of the

ordinance, under the 2010 option plan ("the 2010 Plan"). The underlying shares represent (assuming full exercise) up to 2.43% of Delek Israel's issued and paid-up capital and up to 2.37% fully diluted³⁷. The options are exercisable into Delek Israel shares, in full or in part, from time to time, subject to the vesting dates, the other terms of the 2010 plan and the option agreement between Delek Israel and Mr. Ben Assayag as specified below:

Share no.	No. of options granted on each vesting date	Vesting date	Exercise price (NIS)	Latest exercise date
1	94,367	August 22, 2012	175.70	February 22, 2014
2	94,366	August 22, 2014	184.49	February 2, 2015
3	94,366	August 22, 2015	193.71	February 22, 2016

Exercise of options for shares is by means of cashless exercise, whereby Mr. Assayag is eligible to receive Delek shares reflecting only the benefit component inherent in the exercised options, in return for payment of the par value of the shares only. The right to exercise is subject to adjustments described in the 2010 plan. The economic value of the options allotted to Mr. Ben Assayag amounts to NIS 6.7 million. As of December 31, 2011, Delek Israel recorded an expense for these options of NIS 1.664 million. On August 22, 2010, these options were allocated.

The underlying shares resulting from exercising 610,202 options allotted under this plan (including options granted to Mr. Avi Ben Assayag), which had not expired and/or been exercised as at the report date represent (assuming full exercise by all the employees) up to 3.2% of Delek Israel's voting rights and issued and paid up capital³⁸.

- E. For a description of Delek Israel's Chairman of the Board, Mr. Moshe Amit's employment terms, see breakdown under article 21 in Part D of the periodic report.

1.8.13 Fuel and oil product raw materials and suppliers

A. The main oil products used by Delek Israel

The main fuel products used by Delek Israel in both fuel marketing at public stations and direct marketing are oil distillates produced from crude oil purchased and traded on global exchanges. The oil distillates are purchased primarily from ORL, a small quantity from ORA and the rest are imported from overseas suppliers on the basis of financial considerations. It is noted that the oil distillate prices are exposed to currency exchange rate and global commodity market fluctuations. In most of the direct marketing operations (excluding oils and products manufactured by Delek Oils) Delek Israel purchases finished fuel products and not raw materials.

The main raw materials used by Delek Israel to manufacture oils and lubricants is basic oil purchased from Haifa Basic Oils Ltd. and overseas suppliers and additives purchased primarily from various suppliers overseas. Delek Israel also imports oils and finished products from overseas suppliers (Exxon Mobil) to supplement its product range.

In 2010 and 2011, Delek Israel purchased over 95% of its fuel products from ORL and the rest from ORA, apart from a negligible amount which was imported. Delek Israel's decision concerning the source of fuel purchases derived purely from financial feasibility considerations.

Delek Israel is dependent on ORL. In 2011 and 2010, Delek Israel's purchases from ORL amounted to 88% and 86% of its total sales cost respectively.

³⁷ Assuming full exercise of the 283,099 unlisted options allotted to Mr. Ben Assayag and 327,103 options allotted to Delek Israel employees, consultants and officers under memorandums dated November 8, 2007, April 9, 2008 and September 3, 2009 ("the Memorandums").

³⁸ It is noted that the said amount of shares was calculated theoretically assuming exercise of all the options allotted for a quantity of underlying shares reflecting the number of exercised options (i.e. that each option is exercisable for one ordinary share, which is a total of 610,202 shares). Since senior officers are entitled to exercise the options allotted to them in cash or by cashless exercise while the options of employees who are not senior officers are exercisable for ordinary shares only by cash exercise, it is possible that the number of underlying shares for exercise of all the options allotted is lower than the number of options offered.

B. Agreements with major suppliers

1. Local suppliers

As of the report date, Delek Israel's primary fuel product supplier is ORL. The purchases from ORL are made under a renewable annual agreement dated November 8, 2010 starting January 1, 2010 under which ORL will sell and supply fuel products to Delek Israel. This agreement stipulates that fuel products will be purchased from ORL on the basis of monthly orders. With respect to 95 octane gasoline and diesel fuel, the monthly order will be placed on the basis of an annual plan (listed by month) which was submitted to ORL, while Delek Israel is permitted to update the volume of monthly and annual purchases by the deviation specified in the agreement. The price of fuel products purchased from ORL is determined according to the **CIF Lavera** prices. The relevant Lavera price used to determine the price will be five consecutive published prices, the last being two working days in Israel of the month preceding the supply month under the mechanism fixed in the agreement. The credit extended to Delek Israel is EOM + 15 days. Delek may also make pre-payments to ORL, subject to prior request and ORL's consent, against interest credited at a percentage to be agreed between the parties. The agreement includes, *inter alia*, provisions concerning ORL discounts based on quantities purchased by Delek Israel, financial collateral that Delek Israel must provide for the purchases, etc.

Delek Israel also purchases small quantities of fuel products from ORL under an agreement whereby the fuel product purchases are made by means of monthly orders in exchange for prices set in the agreement and calculated using a price formula derived from the Mediterranean Basin fuel price, while under the agreement ORL is permitted to update the price structure from time to time at its own discretion. Fuel product purchases beyond the quantities noted in the above agreements are made on the basis of agreed terms between Delek Israel and oil product suppliers with respect to each and every purchase.

2. Import of oil products

In the past, Delek Israel imported oil products from global oil suppliers when the cost of imported oil products was lower than local supply. In 2008, Delek Israel imported negligible quantities of oil products from international suppliers and in 2009 and 2010 it did not import oil products, because ORL's oil product purchase terms were better than the cost of importation and infrastructure, which includes unloading, storage and piping to Delek Israel's storage facilities. In 2011, Delek Israel imported a negligible amount. The import price for international trade companies is determined by a formula based on the local rate. Delek Israel is continuing its efforts to review import alternatives for oil product purchases, including the option to reduce the unloading and piping costs of oil products to the Pi Giliot facilities in Ashdod.

1.8.14 **Working capital**

A. Credit policies

1. Customer credit:

To promote its business, Delek Israel provides customer credit in all operations based on the nature of their operations and market conditions. In the gas station and commercial compound operation, Delek usually extends credit to fleet customers of between EOM and EOM + 60 days, based on the product type (gasoline or diesel oil). The remaining sales are either cash sales or by ordinary credit card transactions. In direct marketing, the customer credit outside the gas station fluctuates between EOM + 30 days and EOM + 90 days, for the oils customers, it is up to EOM + 120 and for refueling of marine vessels, the credit is up to EOM + 30 days. In practice, the storage and supply customer credit is EOM + 15 days.

The average customer credit period in 2010 and 2011 was 52 days and 53 days respectively. Average customer credit amounts in 2010 and 2011 were NIS 1,500 million and NIS 1,610 million, respectively.

2. Supplier credit:

The supplier credit extended to Delek Israel for fuel purchases fluctuates between cash payment (with respect to some of the purchases) and credit of EOM +15 days. The payment terms for the convenience products fluctuate between credit of 10 days and EOM + 60 days.

The average supplier credit period in 2010 and 2011 was 34 days and 33 days respectively. The average supplier credit amounts in 2010 and 2011 were NIS 490 million and NIS 548 million respectively.

3. Excise taxes (which are a significant part of the fuel cost) are paid by Delek Israel in accordance with the law within ten days after supply of the fuels.
4. The material difference between the supplier and customer credit arises, *inter alia*, from the high excise imposed on the fuel distillates sold by Delek Israel, the fierce competition in the fuel economy and the short credit periods from the distillate suppliers, which on average does not exceed 30 days.
5. The differences between the customer, supplier and excise credit compel Delek Israel to take short-term loans to finance them. Delek Israel's strategy to finance these differences. Delek Israel's strategy in this regard is to shorten the customer credit period and replace short-term credit with long-term credit. Also see section 1.8.23AE below.

B. Inventory maintenance policy

Delek Israel's policy is to maintain minimal inventory and adapting it to the ongoing supply requirements. The inventory days of fuels are up to 14 days consumption, of oils (raw materials and finished products) are up to three months supply and of convenience products are an average of 90 days. Product returns are extremely rare in Delek Israel's operations. It is obligated to supplying standard quality products which are based on the suppliers' liability for the supply of these products. In cases of product quality which fails to meet the standards and cases where damage was caused to customers from use thereof, the product is examined and handled accordingly. It is emphasized that Delek Israel has an insurance policy dedicated to product liability.

C. Financing of working capital

Generally, Delek Israel finances the customer credit plus inventory less supplier credit by short-term bank credit. However, its working capital is negative, primarily due to its preference to finance investments and long-term debit balances through short-term bank credit and repayment of long-term liabilities through short-term bank credit. From time to time Delek Israel reviews taking long-term financial credit, subject to the market conditions, and availability and cost of this credit.

1.8.15 Investments

- A. Delek USA - Delek Israel holds 1.58% of the share capital of Delek Hungary, which holds 68.5% of Delek USA. For information of Delek USA's refining and fuel product operations in the USA, see section 1.7 of the report.
- B. Delek Europe – Delek Israel holds 20% of the shares of Delek Europe Holdings Ltd. ("**Delek Europe**"), which holds 100% of shares of Delek Benelux B.V. ("**Delek Benelux**"), through a wholly-owned foreign subsidiary. On October 1, 2010, Delek Europe acquired the fuel and convenience store operation of BP France SA, through Delek France Finance SNC ("**Delek France**"), a wholly-owned subsidiary of Delek Europe held indirectly through Delek France B.V (a wholly-owned subsidiary of Delek Europe). For information of Delek Benelux's marketing operations in Benelux countries (Belgium, Holland and Luxembourg) and the fuel marketing operation in France, see section 1.9 of the report.
- C. Pi Gllilot – Delek Israel holds 15.3% of Pi Gllilot, a mixed company as defined in the Government Companies Law, together with Paz, Sonol, Sonefco Bank Street Corporation and the State of Israel (21.5%, 13.2% and 50%, respectively). Until July 31, 2007, Pi Gllilot held real estate rights in the storage and supply facilities in Ashdod, Beer Sheva and Jerusalem. Following the privatization of Pi Gllilot, Delek Israel acquired these storage and supply facilities and the associated storage and supply operations on July 31, 2007, in consideration of NIS 806 million. Currently, Pi Gllilot owns real estate rights in the 17-hectare Pi Gllilot site in Ramat Hasharon which used to house a storage and supply depot. As of the report date, Pi Gllilot contracted with third parties to lease some of the land. As of the reporting date, to the best of Delek Israel's knowledge, ILA is promoting an urban building plan to develop the area, including the Pi Gllilot site at the Gllilot junction, for housing, commerce and employment purposes. Based on an assessor's valuation obtained for participation in the Pi Gllilot tender, Delek Israel believes that the property value may increase if these land zoning changes are completed. This is forward-looking information, based on the assessor's valuation,

assumption that the urban building plan will be accepted, demand for real estate in the compound and other reasons, and might not materialize.

Under a district court decision of June 11, 2002, Pi Gllot ceased all business activity relating to the supply of fuel products from the Pi Gllot site in Ramat Hasharon in 2004. The privatization agreement prescribes that on completion of the privatization proceedings, the Ramat Hasharon facility would be transferred to Pi Gllot shareholders and Pi Gllot will enter into voluntary liquidation, ending all operations.

Under the agreement, due to the privatization process, it was supposed to enter into voluntary liquidation soon after completion of the privatization process. This agreement was secured in an agreed order which received the validity of a ruling in the Antitrust Court.

The fuel companies, Governmental Companies Authority and Antitrust Authority reached an agreement, which has not yet been approved by the court, with respect to amending the privatization agreement and the agreed order to postpone liquidation of Pi Gllot.

1.8.16 Financing

- A. Below are the average effective interest rates on loans from bank and non-bank sources effective in 2011 and not intended exclusively for specific use by Delek Israel:

		Average interest rate	
		Short-term credit	Long-term credit
Banking sources	NIS loans	3.96%-6.96%	5.10%-5.95%
	CPI-linked loans	-	-
	Foreign-currency-denominated loans	1.85%-3.29%	-
Non-banking sources	NIS loans	-	4.75%
	CPI-linked loans	-	5.60%
	CPI-linked issued debentures	-	5.55%
	NIS-linked issued debentures	-	4.58%-6.58%

- B. Financial covenants – in receiving the bank loans and credit facilities, Delek Israel undertook to maintain the following financial covenants:

- Delek Israel is obligated to some of the banks not to encumber its property, plant and equipment in any form without the prior written approval of the banks (excluding property, plant and equipment encumbered in favor of the entities that financed the purchase of those items).

Its subsidiary committed to a bank to maintain an equity to balance sheet ratio of 30% in the subsidiary. At December 31, 2011, the ratio in the subsidiary was 37%. The subsidiary also committed to the same bank not to place a lien on its existing assets and those it will have from time to time without the bank's consent. As of December 31, 2011, the liabilities to the bank were NIS 78 million.

- A bank agreement of 2002 between eight banks (which Delek Israel is not party to) to regulate the relationship among them concerning exercise of the floating lien given to them on Delek Israel's inventory and its consideration stipulates that if one of the banks enforces and/or exercises the charge generated for its benefit that leads to appointing a receiver or receiver and manager of the charged property (as defined in this agreement), the other banks are entitled to exercise the charge given in their favor by Delek Israel.
- Two indentures dated May 2, 2011 signed between Delek Israel and Gafni Trusts Ltd. concerning debentures (series C and G) (in this section: **"the Debentures"**) issued in May 2011 defined events which, should they occur (subject to defined periods to amend the breach in certain cases), grant the trustee rights to call for immediate repayment of the unsettled balances of the debentures. These events include, *inter alia*, the following: (1) if another series of the Delek Israel's debentures is called for immediate repayment by the trustee and/or the debenture holders of that series; (2) if the financial ratio changes

such that the equity to balance sheet ratio³⁹ is below 12% and Delek Israel's⁴⁰ equity is below NIS 600 million (in this section: "**the Lowest Level**") and the said financial ratio remains below the lowest level under three consecutive Delek Israel financial statements; (3) In the event of sale of most or all of Delek Israel's operations in the gas station and commercial compounds and direct marketing segments, following which the percentage profit of Delek Israel's ordinary operations in these segments (cumulatively) falls below 25% of the total consolidated profit of its ordinary operations in all its segments, as appearing in the first financial statements published following the sale of such operations.

Below is information concerning Delek Israel's compliance with the relevant financial criteria fixed in the above immediate debenture repayment events:

Financial criteria	Reviewed ratio As of December 31, 2011
Equity to balance sheet ratio exceeding 12% and equity exceeding NIS 600 million.	Total equity = NIS 1,097 million Total balance sheet = NIS 5,006 billion Equity to balance sheet ratio = 21.9%
Sale of all or most of Delek Israel's operations in the gas station and commercial compounds and direct marketing segments, following which the percentage profit of Delek Israel's ordinary operations in these segments (cumulatively) falls below 25% of the total consolidated profit of its ordinary operations in all its segments, as appearing in the first financial statements published following the sale of such operations.	No operation was sold.

As of the report date, Delek Israel complies with all the above financial covenants.

- C. Credit facilities – As of December 31, 2011 and the date of publication, Delek Israel's bank credit facilities (separate) totaled NIS 1,660 million, of which it has utilized NIS 1,205 million. However, it is emphasized that at December 31, 2011, Delek Israel's cash balances and cash equivalents were NIS 6 million.
- D. Credit rating – On January 6, 2011, Standard & Poor's Maalot ("**Maalot**") updated the rating outlook of Delek Israel's debentures (Series A and B) from stable to negative and at the same time confirmed the rating of iIA. On January 17, 2011, Midroog Ltd., ("**Midroog**") announced a decline in the rating of Delek Israel's debentures (Series A and B) from A1 to A2 with stable outlook. On March 2, 2011, Maalot announced that there is a change in rating or outlook of Delek companies, including Delek Israel, in view of public pressure to lower fuel prices and that it would continue monitoring whether this pressure will lead to a drop in the marketing margins or whether to adopt a stricter marketing margin update model. Maalot believes that a decision to reduce the marketing margins by over 10% may in the mid-term be accompanied by negative rating measures. On February 8, 2011, April 14, 2011 and May 1, 2011, Midroog announced setting an A2 rating with a stable outlook for debentures totaling up to NIS 400 million issued by Delek Israel through a shelf offering of May 5, 2011. At the same time Midroog announced placement of Series A and B and the new series issued in the watch list following the Fuel Administrations investigation concerning the 95 octane gasoline marketing margin, including changing the method of updating it. On June 12, 2011, Maalot announced that it was lowering the rating of Delek Israel's Debentures (Series A and B) from iIA to -iIA and revised the outlook from negative to stable. On July 14, 2011, Maalot announced no immediate change in rating or outlook of Delek Israel (iIA-/Stable) following the Delek Petroleum tender offer. On February 8, 2011 Midroog announced placing Delek Israel's Debentures (Series A and B) in CreditWatch with negative implications. On October 9, 2011, Midroog announced removing Delek Israel's Debentures (Series A, B, C and D) from the watch list while leaving the A2 rating in place and changing the outlook from stable to negative. On December 14, 2011, Maalot announced lowering Delek Israel's Debentures (Series A and B) rating to iBBB from -iIA and at the same time removed these debentures from CreditWatch with negative implications, which they were placed i on August 2, 2011. Midroog's outlook remained negative.

³⁹ The ratio between the total equity attributed to the shareholders, excluding non-controlling rights, and Delek Israel's balance sheet total in its audited or reviewed consolidated financial statements.

⁴⁰ Delek Israel's equity, excluding non-controlling rights, as appearing in its audited or reviewed financial statements.

E. Variable interest credit:

Details of variable interest credit obtained by Delek Israel as of December 31, 2011 and at the reporting date are as follows:

Interest rates proximate to report date	Range of interest rates as at December 31, 2011	Track
4.35%-5.95%	4.35%-5.95%	NIS
1.98%-3.50%	2.08%-3.58%	USD
3.50%-6.25%	3.75%-5.00%	On Call

- F. Buyback of debentures Under a buyback plan of December 18, 2011 totaling up to NIS 50 million, by the report publication date, Delek Israel acquired 2,431,168 Delek Israel debentures (Series A) at a total cost of NIS 2.553 million, 2,704,862 Delek Israel debentures (Series B) at a total cost of NIS 2,543 million, 1,117,907 Delek Israel debentures (Series C) at a total cost of NIS 804 thousands and 937,408 Delek Israel debentures (Series D) at a total cost of NIS 795 thousands. These debentures were removed from trade upon acquisition.

- G. Liens – To secure debt to banks amounting to NIS 1,200 million as at December 31, 2011, Delek Israel placed an unlimited floating lien on the inventory in its possession, its proceeds and the rights thereof as defined in the lien documents. Delek Israel also guaranteed Delek Petroleum's debenture-raising (Series A) from institutional investors, and the proceeds from were provided as a loan under the same terms to Delek Israel, excluding the interest rate collected from Delek Israel, which was 0.05% higher than interest on the debentures and several additional terms which were laid down between Delek Israel and Delek Petroleum. The total balance of the loans extended to Delek Israel as at December 31, 2011, amounted to NIS 69 million.

In January, 2004, in a debentures issue by Delek Petroleum, Delek Israel encumbered under a senior fixed lien unlimited in amount, all of its rights in respect of the loans extended by Delek Israel to the Company.

As of December 31, 2011, the Group's balance for these loans was NIS 293 million.

For long and short-term loans taken by Delek Israel's associated companies, their property and rental contracts signed with respect to this property were mortgaged.

1.8.17 Taxation

The primary tax rate applicable to Delek Israel is different to the effective tax rate, due mainly to the timing differences between expenses, unrecognized discounted expenses, exempt income and affiliated company losses.

Besides the regular corporate tax laws, it is noted that under the Fuel Excise Law, 1958 and the Fuel Excise Order, 1980, a defined amount of tax is imposed on the fuel products listed in the Order, which is updated every three months, based on CPI changes. In January 2005, an order was issued whereby the diesel fuel and kerosene excise tax rates would be raised gradually to equal that on gasoline over a period between 2005 and 2009. The excise tax component in fuel prices is highly significant. Fuel companies are charged excise tax directly upon issuing the fuel, with 10 days' credit, whereas the number of credit days granted by Delek Israel to its customers is significantly higher, especially for diesel fuel sales.

1.8.18 Environmental risks and manner of handling them

Delek Israel's operations are regulated under various environmental laws, regulations and directives. It takes constant measures to minimize and prevent possible damage to the environment, investing considerable resources to do so, and has increased its investments in this area since Water (Prevention of water pollution) (Gas stations) Regulations, 1997 were promulgated, including comprehensive provisions aimed at regulating this issue and preventing soil and water pollution. A trend of stricter enforcement of environmental laws is evident in recent years. For information of pending indictments in this matter, see section 1.8.18I below.

The principal provisions concerning environment laws applicable to Delek Israel and their impact are specified as follow:

A. Maintenance of Cleanliness Law

The Maintenance of Cleanliness Law, 1984 ("**the Maintenance of Cleanliness Law**") imposes criminal liability on whoever dirties and/or disposes waste (including fuels) in the public domain. This law also grants authority to levy fines, issue an order requiring the polluter to restore the polluted area or impose double the expenses for restoration of the site by the authorities.

B. Water Law and Regulations

The Water Law, 1959 ("**the Water Law**") imposes liability for polluting water sources. It grants State authorities extensive powers, including the authority to demand termination of the pollution, restoration, levy fines and charge expenses.

The Water (Prevention of water pollution) (Gas stations) Regulations, 1997 ("**the Water Regulations**") promulgated by virtue of the Water Law, include comprehensive provisions aimed at regulating this field and preventing soil, water or air pollution.

The Water Regulations include, inter alia, provisions requiring gas station operators to install various means of protection for various matters, including the construction of a sealed floor and a drainage system, regular periodic inspections, to fix leakages and report them immediately, and to adapt old gas stations to the current standards.

The gas station operator is defined in the Water Regulations as the business license holder, or the person under whose supervision, management or control the station operates. It is noted that in the supply contracts, the liability for handling this matter is imposed on the gas station owner or its operator. As noted above, at December 31, 2011, Delek Israel operates, itself and through its operators, 219 gas stations (of which 130 are stations established before 1997 ("the Old Stations"), where liability for pollution control and treatment is imposed on Delek Israel. Most of Delek Israel's gas stations are located in high risk areas for groundwater pollution. Under a multi-annual contract with the Ministry for Environmental Protection and the Ministry's requirements prior to the signing this contract, Delek Israel ran about 100 tests at its gas stations. At 54 stations soil and groundwater pollution was found from past violations and fuel infrastructure leakages for which Delek Israel made provisions in its books. Soil surveys and groundwater monitoring bores were carried out at these stations in order to characterize the type of pollution. At the other stations where no pollution was found, Delek Israel was required by the Ministry for Environmental Protection and the Water Commission to conduct annual monitoring tests. After receiving clear idea of the condition, treatment using standard technologies to restore the soil and water will begin in cooperation with the Water Commission and the Ministry for Environmental Protection.

The cost estimate for cleaning soil and water contamination depends on the size of the contaminated area and severity of the contamination. At the report date, 25 gas stations completed soil surveys and groundwater monitoring bores and Delek Israel began the soil restoration process in them.

C. Monitoring means at old gas stations

Under the Water Regulations, Delek Israel is required to install monitoring means in all old gas stations to detect fuel leakage into soil there. As of the report date, Delek Israel has 130 old gas stations where it has installed the required monitoring means as required.

D. Permeability tests

The Water Regulations require that regular permeability tests (once every five years) be conducted on the pipes and tanks at all gas stations or more frequently, depending on the circumstances. As of the report date, one round of tests was completed at all Delek Israel gas stations. The cost of these tests is immaterial to Delek Israel and will not significantly affect its results unless soil or water pollution resulting from defective sealing is detected which will lead substantial repairs. It should be noted that in 2011, insulation faults were discovered in a small portion of the infrastructures tested. In Delek Israel's estimation and as at the report date, the anticipated rehabilitation costs incurred due to these faults are NIS 1 million.

The information in this section and all the subsections about Delek Israel's future operations for compliance with the provisions of the water regulations and with respect to protection means to prevent leakage in the old stations, installation of monitoring means, conducting of periodic permeability tests and the anticipated investments and costs is forward looking information as defined in the Securities Law, based on existing information as at the report

date. It is possible that compliance with the water regulations will take longer than set out above, due to possible technical delays preventing completion of the treatment or due to other external restrictions which may delay meeting the provisions of the water regulations in full. It is also possible that in practice Delek Israel will be required to make larger investments, *inter alia*, because pollution could be discovered at other stations and because of additional requirements from the Ministry of Environmental Protection and/or the Water Authority.

E. Clean Air Law, 2008

On July 22, 2008, the government adopted the Clean Air Law, 2008, which is aimed at improving the air quality and preventing and reducing air pollution with a series of treatments under a single legislative procedure. For the most part, the law entered into effect on July 1, 2011. A gradual transition period ending on March 1, 2015 was also determined to enforce the obligation to obtain a permit for emission sources requiring a permit under the law, including *inter alia*, the energy industries in general and the gas and fuel refining industry in particular. As of the report date, Delek Israel has no stack emissions. However, under this law, the Ministry of Environmental Protection is permitted to order Delek Israel to take steps to prevent air pollution generated while refueling vehicles, in addition to similar provisions usually arising from the business license issuing process for the gas stations.

F. The Environmental Protection (Polluter Pays) (Legislative Amendments) Law, 2008

On July 29, 2008, the government adopted the Environmental Protection (Polluter Pays) (Legislative Amendments) Law, 2008, which entered into force on October 10, 2008. The objective of this law is to protect, maintain and improve the environment, prevent damage to the environment or public health, and negate the economic viability of causing harm to the environment, *inter alia*, by means of punishment which takes into account the value of the damage caused and the benefit or profits gained by committing environmental crimes. In addition to stricter penalties for environmental violations, the courts are authorized, for a violation by a person resulting in that person gaining a benefit or profit, to impose a fine to the value of the benefit or profit in addition to any other punishment.

G. Environmental bills

In recent years, several environmental bills have been proposed which may impact Delek Israel if adopted, like: the Reduced Greenhouse Gas Emissions Bill, 2008, which defines goals for significantly reducing greenhouse gas emissions and promoting a national multi-annual plan to reduce greenhouse gas emissions; the Restoration of Contaminated Soil Bill, 2007, to solve the problem of soil and groundwater contamination to protect the environment and public health in Israel from pollution resulting from the presence of hazardous substances in the soil.

H. Additional environmental requirements

1. In November 2005, the Ministry of Environmental Protection published framework terms for gas stations, enabling the authorities, under certain conditions, to demand implementing further station infrastructure improvements excluded from the water regulations published in 1997, e.g. sealing beneath the pumps, installing overfilling limiters and installing means of preventing cathode protection spillovers and gas vapor retrieval systems (stage 1 and 2). The total cost of meeting these requirements is NIS 150 thousand per station.

As of the report date, Delek Israel was required to conduct tests in 130 old stations as described above. The cost of these tests and treatment is estimated at NIS 30 million spread over 2012-2014. As of the report date, Delek Israel has carried out tests and treatment at 100 stations, while in practice, in 2009-2011 the costs amounted to NIS 20 million.

Delek Israel reached an agreement with the Ministry of Environmental Protection to install Stage 2 vapor retrieval systems at 70 of its old stations over the next six years as of 2008 at an overall cost of NIS 14 million, in addition to installation of this system at its new stations under construction. To date, such retrieval systems have been installed at 60 stations (most of which are old stations). On May 31, 2010, the Minister of Environmental Protection sent a letter to the gas companies informing them of its intention to compel all the gas stations in Israel to install vapor retrieval systems and that this obligation will be included in the business licenses for all stations. The timetables include mainly the installation of the vapor retrieval systems in 20% of the stations in each of the forthcoming years until the installation is complete in all the stations within five years. In 2011, the Ministry of Environmental Protection updated the business license terms of

some of the gas station and will continue to do so in 2012, including integrating updated requirements concerning the installation of vapor retrieval systems. The Ministry of Environmental Protection also requires installing systems meeting more up-to-date standards and thus Delek Israel will be required to invest a higher amount to purchase them. In 2012, Delek Israel anticipates installing such systems in over 30 of its stations at an investment of NIS 6 million.

2. In February 2008, Delek Israel received draft framework terms for fuel tank farms from the Ministry of Environmental Protection determining benchmarks and requirements applicable to Pi Gllot concerning operation of the tank farm, in order to protect the environment. The draft contains provisions dealing with soil and water pollution prevention, including the manner of discharging industrial wastes, the installation of a waste treatment facility, determination of the quality of wastes to be discharged into the sewerage system, tank testing, pipe testing, installation of means for locating leaks in tanks, as well as testing and treatment of contaminated soil and water. As of the report date, the draft had not entered into force, but some of its requirements were included as additional terms for a business license.

I. Legal and administrative proceedings relating to environmental protection

Failure to comply with the provisions of the Water Law and Water Regulations could constitute a criminal offense, carrying a one-year prison sentence or a fine of up to NIS 350,000⁴¹, and heavier penalties in the event of an ongoing offense. An indictment concerning environmental issues was filed against Delek Israel and its managers, alleging contamination of soil and groundwater, and was filed against Delek Israel's then CEO, its VP Sales and several of its marketing staff. The indictment was amended and the case is was closed with a plea bargain including, *inter alia*, fees of NIS 250,000 and liability of NIS 500,000 which will remain in force for three years in which the same offence will not be repeated at the gas station subject of the indictment. A second indictment was filed at the end of 2010 against Delek Israel and its former officers concerning, *inter alia*, alleged violations of the Water Law and the Regulations by virtue thereof concerning fuel leakage from tanks and pipelines and the reporting thereof. A reading meeting of the indictment was scheduled for April 5, 2011. As of the report date, this case was fixed for reminder on May 1, 2012. A ruling has not yet been handed down concerning the preliminary claims raised. Moreover, several hearings against Delek Israel and its senior officers are pending with respect to claims of environmental protection law violations in a minimal number of stations. Delek Israel cannot estimate at this stage whether the hearings will lead to enforcement measures against the invitees or not.

J. Stricter enforcement of the prevention of diluted fuel sales

In April 2008, the Knesset adopted an amendment to the Vehicle Operation Act (Engines and fuel) Law, 1960, aimed at minimizing the sale and supply of gasoline blended with diesel fuel, naphtha and other substances, for which the prices and taxes payable are significantly lower than the price of the fuel.

Under the amendment, every gas station operator is required to conduct at least six annual tests to have product quality verified by an authorized laboratory. Sanctions against nonstandard oil products will be increased substantially, including possible administrative closure orders, publication of the names of gas stations selling nonstandard products, and significantly higher fines. The provisions of the amendment entered into force on October 10, 2008. Delek Israel cannot evaluate the exposure in claims concerning the October 2006 fuel dilution issue, if any.

K. Fuel supply facilities

The Ministry of Environment requires installing a vapor retrieval system at supply facilities issuing gasoline to treat gasoline vapors collected from stations' petrol tanks when they are being filled. The Ashdod facility already had such a system when was acquired by Delek Israel in July 2007. The Beer Sheva and Jerusalem facilities have no such systems, hence no gasoline is supplied from these facilities. The installation and operation of the system at the supply facility in Haifa was completed at the end of April 2007 at a cost of NIS 3 million

⁴¹ The fine is in addition to the expenses involved in treating the contamination.

L. Bottom filling system

Under the Ministry of Transportation regulations, Delek Israel is required to install a bottom filling facility in its petrol tankers of 14,000 liters volume and above to prevent environmental pollution when the tankers are filled. As of the report date, Delek Israel has completed the installation at its distribution facility in Haifa and in all its tankers. Delek Israel acquired the Pi Gllot supply facilities including such systems, except for the Jerusalem facility which has no such system since supply at this facility by gravitation. Since investment in construction of a system to change the current supply method, adapting it to requirements concerning vapor retrieval and bottom filling was found to be economically unfeasible in all aspects, considering future fuel supply volume at the facility and the supply rate compared with the required investment, no bottom filling system has been installed and gasoline supply has been completely discontinued from this facility.

M. Ashdod fuel oil distribution facility

Ionex (a Delek Israel subsidiary (75%)) operates a fuel oil distribution facility for which it has a lease from Ashdod Port until May 31, 2013. As of the report date, Israel Ports Company ("IPC"), owner of this distribution facility, published a tender to lease the facility for a period beginning June 1, 2013. Ionex is studying the details of this tender. At the demand of the Ministry of Environmental Protection, the soil in this facility was surveyed three years ago, with no adverse findings requiring treatment. Ionex and the Ministry of Environmental Protection discussed adding terms to the Ashdod supply facility business license relating to the need for special investment to prevent future contamination. Ultimately, the parties agreed on the special terms which were added to the business license while others were deleted and will be added to the business license of the winning bidder in the tender for operation of the supply facility which will be issued by IPC. At the end of February 2011, a leak was discovered in the pipelines transporting fuel from the Ionex facility in the area of the Ashdod Port fueling dock. The leak seeped into the soil and reached groundwater. Ionex management reported it to the Ministry of Environmental Protection, the Cities Association and the Port authorities as required and is currently working to repair these faults in cooperation with the Ministry of Environmental Protection and IPC. It is noted that Ionex and IPC are in disagreement concerning responsibility for the leak.

N. Hazardous materials

Under the Hazardous Materials Law, 1993 ("**the Hazardous Materials Law**"), oil distillates are defined as hazardous materials. The law prescribes a duty to hold a "poisons permit" from the supervisor authorized to issue such by the Environment Minister. Delek Israel has permits to hold hazardous materials as defined therein, and to trade in fuels without storing them.

O. Green tax reform

The green tax reform entered into force as from August 2009, prescribing vehicle tax incentives based on their pollution emission level aimed at encouraging the purchase of more environmentally friendly vehicles. The main point of the reform is changing the mechanism of imposing tax on new vehicles weighing under 3.5 tons. Under the reform, the purchase tax of a new vehicle sold in Israel will be determined according to the air pollution emissions from the vehicle. Delek Israel estimates that the impact of the green tax reform on its operations and results in the short-term are expected to be negligible only. This sections includes forward looking information as defined in the Securities Law which are beyond Delek Israel's control and uncertain. Delek Israel's assessments may not materialize and the actual results may be different to that set out above if any of the assumptions used by Delek Israel in their assessment change.

P. Projected significant costs and investments in environmental issues

In 2011 and 2010, Delek Israel's total investments and costs in gas station and commercial compounds for compliance with statutory and official environmental requirements amounted to approximately NIS 10 million and NIS 10 million, respectively (excluding investment in the construction of new gas stations in compliance with statutory environmental requirements).

Since Delek Israel's old stations 130 in number) were built to standards predating the Water Regulations and since accumulated knowledge indicates that the required standards of that period cannot ensure soil and/or water damage prevention, Delek Israel cannot estimate which of its old stations have polluted the soil or the water surrounding them. Tests conducted detected several stations where the soil and/or groundwater is contaminated. Delek Israel has begun implementing a soil and/or groundwater rehabilitation plan at the stations where the

survey was completed and contamination was discovered. In this matter, Delek Israel is in compliance with the arrangement signed with the Ministry of Environmental Protection in 2008 with respect to the timetables for locating and rehabilitating contaminated soil at old gas station. This arrangement does not contradict any other law applicable to Delek Israel. However, under the agreement, as long as it operates according to the rehabilitation plan, this will be taken into consideration in decisions of the authorized entities when they have to rule with respect to the legal and public justification of enforcing this matter. As stipulated above, if additional pollution which is unknown at the date of this report is identified, it could be required to allocate substantial investments to that end.

Delek Israel has submitted to the Ministry of Environmental Protection a work (rehabilitation) plan for locating, monitoring and surveying soil and water at its old stations (established prior to January 1, 1998) operated by or on behalf of Delek Israel. Under the plan, all surveys will be completed within 3-10 years from start of the plan, with at least 15 gas stations surveyed and completed in each calendar year. After these surveys, Delek Israel will prepare an individual soil rehabilitation plan for each station found to be contaminated, which will be submitted for review by the Ministry of Environmental Protection. Once the results of the review are known, Delek Israel will start rehabilitation work in the relevant station, with such work on the final station to start no later than in the seventh years after the start of the rehabilitation plan. The Minister for Environmental Protection indicated to Delek Israel that the Ministry regards favorably formulation of a plan for cleaning up contamination from gas stations, and action based on such plan in coordination with the Ministry. Nevertheless, it is Ministry policy to enforce provision of environmental protection laws, and execution of the plan would not grant immunity from enforcement of the law where its provisions were violated or result in the cancellation of indictments already filed. However, when considering the legal and public justification of prosecution, all circumstances of the matter would be taken into account, including actions taken by the violating entity. It is also noted that to the best of Delek Israel's knowledge, several fuel companies have submitted similar plans to the Ministry of Environmental Protection.

Details of costs (expenses involved in ground- and underground water treatment) and investments (in equipment and means to prevent and alert to such contamination) estimated for the coming years in gas station and commercial compounds are as follows:

	2012 (NIS thousands)	2013 (NIS thousands)	2014 onwards (NIS thousands)
Anticipated significant costs	6,500	7,000	7,000
Anticipated significant investments	7,000	8,000	7,000
Total	13,500	15,000	14,000

This information on the estimated costs and investments is forward-looking information that may not materialize if Delek Israel is found to be in breach of regulations or if new regulations issued by the Ministry of Environmental Protection enter into force obliging Delek Israel to allocate additional funds.

- Q. Under the understandings and agreements with the Ministry of Environmental Protection, Delek Israel began implementing a plan to install vapor retrieval systems at some of the stations, as noted in section 1.8.18H.1 above, at a total cost of NIS 40 million until 2015.
- R. Delek Israel's direct marketing operation at internal gas stations located on customer premises is also subject to the provisions of the Water Regulations, as described in section 1.8.18B above. The gas station operator as defined in the Water Regulations is held responsible for implementing these provisions. If the matter is brought for its decision, a court may rule that in view of the terms of the agreement between Delek Israel and the internal station owner, Delek Israel is also considered to be a "station operator". For information of the responsibility of a "station operator," see section 1.8.18B above.
- S. A subsidiary of Delek Israel (Delek Oils Ltd. – "Delkol"), removes industrial waste under the provisions of environmental laws.
- T. In 2011 and 2010, Delek Israel's total costs and investments in direct marketing and storage and supply operations for compliance with statutory provisions and official environment requirements were negligible. Delek Israel does not foresee any material costs in these areas of operation, which are expected to total NIS 2 million in 2012. This information on estimated

costs and investments is forward-looking information that may not materialize if serious deviations are found in Delek Israel's operations or if new environmental requirements enter into force necessitating material expenditure.

1.8.19 Limitations and supervision of Delek Israel's operations

Below is a description of the main limitations and supervision applicable to Delek Israel, in addition to the above environment supervision:

A. Legislation specific to the fuel economy:

1. The State Economy Arrangements (Legislation amendments to achieve 2001 budget and economic policy targets) Law, 2001 ("the State Economy Law") – This law states that a fuel company must be registered before commencing operation and may continue to operate as long as it is registered in the register maintained by the Fuel Administration. Delek Israel and Gal Fuel Co. Ltd. (a Delek Israel subsidiary) are registered at the Fuel Administration Register as fuel companies. It should also be noted that the State Economy Law prescribes that a fuel company must maintain, at its own expense, such fuel stock as is determined by the Energy and Water Minister in consultation with the Ministers of Defense and Finance, and that the State has promulgated regulations⁴² by virtue of the State Economy Law that regulate this matter. In November 2002, the High Court of Justice approved an interim arrangement requiring the maintenance of security inventory, but the State can change the present status to require also the maintaining of a civil inventory.
2. Fuel Economy (Promotion of competition) Law, 1994 – The law prescribes, *inter alia*, limitations on opening new gas stations near stations marketing the products of the same fuel company or operated by the same operator. The section in the law dealing with the limitations concerning a regional engagement between gas stations of one fuel company is in force through the end of July 2018. In December 2007, the Fuel Economy (Promotion of competition) (Amendment No. 2) Law, 2007 designed to regulate the advertising of prices at gas stations to increase competition and prevent deceit in prices was enacted. On March 5, 2012, the Fuel Economy (Promotion of competition)(Temporary order)(Amendment-Zoning changes for establishment of gas stations) Bill, 2012 was submitted to the Knesset Speaker and Deputies. This private bill proposes reinstating the provision which expired on July 29, 2008 concerning the rights of a land owner as lessor or authorized entity under the contract with ILA to establish a gas station on the land without being obligated to return the land to ILA for this. Delek Israel estimates that approval of the current version of the bill, if at all.
3. Fuel Economy (No sale of fuel to specific gas stations) Law, 2005 – This law bans the sale and supply of fuel to gas stations unless they are on the list maintained by the Fuel Administration. As of the reporting date, most of Delek Israel's public gas stations are included in the list published by the Fuel Administration.
4. Excise – Under the Excise Law, no person shall manufacture fuel nor deal in its sale without a license from the Customs and Excise Administration. Delek Israel has been issued such a manufacturing license, which it renews annually. Excise is levied on fuel when it is issued at a supply facility or released from customs in the case of import. As a result, only companies holding such a manufacturing license may purchase oil distillates directly from refineries in Israel or import them.

The Excise on Fuel (Levying excise) Order, 2004 ("the Excise Order") sets specific excise rates for every oil product. In January 2005, the Excise on Fuel (Amendment No.3 and temporary order), 2004 and the Excise on Fuel (Exemption) Order, 2005 entered into force, raising the excise rate on diesel fuel and kerosene gradually from 2005 to 2009, to equal that levied on gasoline. As of the report publication date, the excise on naphtha was the same as that applicable to gasoline and the excise applicable to diesel fuel and kerosene is 14 agorot (including VAT) lower than on gasoline. Furthermore, the Excise on Fuel (Exemption) Order, 2005 prescribes, *inter alia*, that fuel used by civilian commercial marine vessels transporting passengers or cargo is exempt from excise payment, provided that after fueling the vessel departs from an Israeli port for a destination outside Israel. On June 20, 2010, the Excise Tariff and Exemptions and

⁴² The State Economy Arrangements (Legislation amendments to achieve 2001 budget and economic policy targets) (Maintaining inventory and security inventory of fuel) Regulations, 2001.

Purchase Tax on Merchandise (Amendment No. 19) Order, 2010 and Excise on Fuel (Imposition of excise) (Amendment) Order, 2010 were published under which the excise will be updated every four month and not every three months as it was until now.

On July 21, 2010, as part of the Economic Plan for 2011-2012, Structural Change, Budget Aggregate and Budget Composition - Government Decision No. 2059 dated July 15, 2010 ("**the Government Decision**") was published imposing another 20 agorot per liter excise on gasoline, diesel oil, kerosene and fuel mixtures will be increased in 2011, and imposing another 20 agorot per liter in 2012. On February 13, 2011, following the public outcry against increasing the excise on gasoline, the government canceled it shortly before it was to be implemented. Based on the Government Decision, Excise Tariff and Exemptions and Purchase Tax on Merchandise (Amendment No. 22) Order, 2010 was published prescribing that as from October 3, 2010, tax of NIS 2.5 per liter will be imposed on biodiesel which is similar to that applicable to diesel fuel. Despite the above, on March 1, 2012, Excise on Fuel Order (Imposition of excise tax)(Temporary order), 2012 was published stipulating that between March 1,2012 and April 30,2012, the excise tax rate imposed on naphtha and gasoline will be reduced by 3%. Increasing the excise on fuel sold by Delek Israel significantly increases the credit extended to customers purchasing them, its exposure to this credit, and its dependence on banks and other financing sources to finance this credit

5. Hours of Work and Rest Law, 1951 – Under Section 9 of this law, employing Jewish employees on Saturday, which is part of the statutory weekly rest period, must be approved by the Minister of Labor. The Hours of Work and Rest Law also stipulates, *inter alia*, that on rest days defined in the Law and Administration Ordinance, 1948, no store owner shall conduct business in his store. This law lays down a fine or up to one month's imprisonment or both for whoever employs staff in breach of the law. Most of Delek Israel's public gas stations and some of its convenience stores operate on Saturdays. To date, the restrictions imposed by these laws have had no materially impaired Delek Israel's business results, and based on past experience it estimates that they will not do so in the future either. This estimate is forward-looking information which may not materialize, *inter alia*, due to stricter enforcement of provisions of the Hours of Work and Rest Law all over Israel, which could lead to convenience stores being closed on Saturdays. At the reporting date, investigations were conducted in the past against Delek Israel in connection with convenience stores and gas stations operating on Saturdays. All the foregoing investigations were concluded without any legal / criminal proceedings instituted against Delek Israel.
6. Vehicle Operation (Engines and fuel) (Supply of fuel by tanker) Order, 2007 ("the Fuel Supply Order") - was enacted pursuant to the Vehicle Operation (Engines and fuel) Law, 1961 ("**the Vehicle Operation Law**"). The order states that a motor vehicle will run on gasoline, diesel, LPG or other fuel prescribed under the Vehicle Operation Law, provided it meets standard requirements for the product and requirements laid down in the order, if any. The order imposes liability on fuel companies supplying gas stations, owners of a supply facility, the owner of a gas station and transporters of fuels to gas stations, requiring them to take all reasonable precautions to ensure that every fuel product supplied meets the requirements of an official Israeli standard as defined in the Standards Law, 1953 ("**the Standards Law**") and regulations pursuant to the Vehicle Operation Law by means of duties imposed on each such entity within its area of responsibility. In January 2011, an amendment was published to the Vehicle Operation (Engines and fuel) (Supply of fuel by tanker) Order, 2007 ("**the Order**") under which by the end of June 2012, an electronic seal (a device designed to control opening of the tanker and the quantity of fuel therein) must be installed on every fuel tanker, according to the definitions in the order. Delek Israel disagrees with the price which the sole authorized supplier in Israel of the electronic sealig system demands and is taking steps in this regard with the supplier and the Fuel Administration.
7. Fuel Economy Bill, 2007 ("the Fuel Economy Bill") – At the beginning of 2007, a draft of the Fuel Economy Law, 2007 ("**the Draft Fuel Economy Law**") was announced. The aim of the draft, according to its memorandum, is to regulate all the operations in the fuel economy, from the financial, safety and consumerism aspects, by setting an appropriate licensing and regulatory regime. On January 30, 2011, the updated Fuel Economy Bill, 2011 was received from the Fuel Administration and Delek Israel was given the opportunity to respond. Delek Israel submitted its response to the updated bill which it received on February 28, 2012. On March 15, 2012, the Fuel Administration distributed

an updated draft of the bill (Fuel Economy Bill, 2012) and submitted it to the Ministerial Legislative Committee on March 18, 2012. Delek Israel cannot assess whether the Fuel Economy Bill will pass or not, and if so, to what extent and when. It estimates that approval of the Fuel Economy Bill in its current version, if at all, may materially affect its results, while the extent of the impact will derive from the wording of the law that is approved in the long run, if at all.

8. Universal Refueling Device Regulations: On July 21, 2010, an amendment to section 7B of the Fuel Economy (Promotion of competition) Law, 1994, ("**the Fuel Economy Law Amendment**") was published. Under the Fuel Economy Law Amendment, *inter alia*, the definition of "a universal automatic fueling device" was changed so that under the new version it is a device which may be used to purchase fuel from any fuel company independent of the identity of the fuel company that installed it. This amendment also stipulates that regulations pursuant to the amendment will be brought before the Knesset Economic Committee for approval. On October 23, 2011, the universal refueling device regulations were published in the Official Gazette requiring fuel companies to install a universal refueling system which will allow consumers to contract with different fuel companies, and use the same system to refuel in gas stations operated by different fuel companies. Under these regulations, the universal refueling device system will be based on specifications for a universal automatic refueling device ("**the Universal Device**") to be approved by the Fuel Administration (in this section: "**the Administration**") These specifications will define, *inter alia*, technical and functional requirements for the universal device. To produce these specifications, the regulations prescribe a two-phase process: A) Phase 1 - SII will enact suitable standards in the time frame prescribed in this standard. If standards are prescribed in this time frame, they will constitute the specifications; Phase 2 - If SII does not manage to enact standards in the time frame set, the Administration will select specifications in a competitive, equal process. A year from approval of these specifications, it will not be possible to sell fuel at a station using a refueling device unless it has at least one refueling nozzle for each fuel product which fuel may be purchased with using a universal device and 18 to 36 months from approval of these specifications, at least three refueling nozzles for each product or two thirds of the refueling nozzles, whichever is less. Three years from approval of these standards or specifications, Delek will not be able to sell fuel at stations using a refueling device which is not universal. Delek Israel estimates that the universal refueling device provisions may cause Delek Israel to incur expenses, *inter alia*, to convert existing refueling devices to universal refueling devices and to carry out computer adaptations whose scope will be determined from the above specification or standards to be prescribed. Moreover, converting the refueling devices to universal devices will increase the number of stations where customers may purchase fuel products, which may lead to a reduction in the number of customers purchasing fuel products through its automatic refueling system.

B. Price control

1. Supply of fuel products by ORL to the fuel companies - ORL was declared a monopoly at the time in the refining of crude oil in Israel. Currently, only two types of bitumen are sold by ORL, subject to maximum ORL ex-works prices and set under the Commodity and Service Price Stability Order (Temporary Order) (Maximum ORL ex-works Prices for Oil Products) 1992 ("**the ORL Ex-Works Price Order**"), which sets the maximum ORL ex-refinery prices for the various fuel products (see section 1.8.1B.1) above). The ORL ex-works price is updated on the first of every month, based on the external fuel product price plus or minus an amount set by the Fuel Administration Director, with the approval of the Ministers of Energy and Finance. As of the report date, after privatization of the oil refineries, the price setting mechanism has not changed. Of Delek Israel's fuel product purchases, its purchase price for controlled price products in 2011 and 2010 amount to 0.8% and 1.88%, respectively.
2. Consumer price - Commodity and Service Price Control Order (Maximum prices at gas stations, 2002 - under this order, the maximum price for lead-free 95 octane gas sold at a public self service pump is fixed, as are the date and methods of its update. In this context, it is noted that since 2008, the Fuel Administration began conducting reviews with the fuel companies concerning marketing margin analysis, including changing the method of updating it. On February 15, 2011, the Fuel Administration sent the fuel companies a marketing margin analysis report on its behalf. On August 31, 2011, the Ministry of Energy and Water published and the Commodities and Services Price Control Order (Maximum prices at gas stations)(Amendment), 2011, duly signed by the Energy

and Water Minister and Finance Minister ("**the 2011 Price Control Order**") under which, *inter alia*, as from September 1, 2011, the self-service 95 octane gasoline marketing expenses basket will be NIS 589,000 per thousand liters (in Eilat NIS 279,080 per thousand liters) and the surcharge for full service will be NIS 173,000 per thousand litres. The 2011 Price Control Order also includes, *inter alia*, changes relating to the manner of updating the expenses basket and full service surcharge components. It also proposes that the expenses basket and full service surcharge component be updated according to the CPI and not the European marketing margin as is customary. On that date, Delek Israel petitioned the Supreme Court, sitting as high Court of Justice, to issue an order nisi and interim order against the 2011 Price Control Order (in this section: "**the Petition**"). On September 19, 2011, deliberations were held at the Supreme Court, sitting as high Court of Justice, on the matter of the petition of Delek Israel and other fuel companies in which it was decided to return the marketing margin matter for a repeat hearing based on an updated database to which 2009 and 2010 information will be added. As of the report date, Delek Israel is in the additional hearing process held for the fuel companies following the above deliberations at the High Court of Justice and is waiting to receive the hearing results from the Price Committee.

3. Price control of diesel oil for transportation – In 2011, the Knesset Economic Committee held several meetings concerning the prices of diesel oil in Israel and the question of imposing price control on these prices. On September 25, 2011, the committee announced on behalf of the Ministry of Energy and Water that "the Minister of Energy and Water, Uzi Landau, has decided to take steps to reinstate price control on diesel oil prices." On the same day, the Ministry of Energy and Water contacted the chairperson of the interministerial Price Committee (composed of representatives of the Ministries of Finance and the Energy and Water) (in this subsection: "**the Price Committee**") to convene the committee to discuss application of the Commodities and Services Price Control Law, 2006 ("**the Price Control Law**") to diesel oil. At the same time, the Trachtenberg Committee succeeded in reinstating control of the ex-refinery and ex-gas station price of diesel oil for transportation, similar to the price control mechanism in the gasoline market. Moreover, two Commodities and Services Price Control Bills (Amendment – Price control of diesel oil for transportation), 2011 were submitted to the Knesset; the first on May 23, 2011 by MKs Ophir Akunis and Zion Pinyan and the second on November 28, 2011 by MK Carmel Shama. These bills, which are similar in content, propose obligating the ministers to prescribe the maximum permitted price for diesel oil for transportation in the order. Delek Israel believes that approval of these bills in their current wording, if at all, may impair its business results. On December 21, 2011, Delek Israel received a letter from the Price Committee that it intends to examine imposing control on the marketing margins of diesel oil for transportation at gas stations. According to the letter, the control level under examination at this stage is that set out in chapter G of the Price Control Law under which the reporting entity is required to report profitability and prices to the Price Control Supervisor. On February 2, 2012, Delek Israel sent the Price Committee the response to its letter on the matter stipulating that there is no room (or authority) to impose such control. If Delek Israel's viewpoint is rejected, the Price Committee is likely to recommend the ministers impose control of the marketing margin of diesel oil for transportation at gas stations. Even if this recommendation is adopted by the ministers, this will not impair Delek Israel's business results since as at the report date, the control is on the reporting level only. As at the report date, Delek Israel cannot estimate the scope of the direct and indirect implications of the decision to reinstate price control on diesel oil, if adopted, but it may have an adverse impact when the scope of the impact will ultimately derive from the exact wording of the decision adopted.
4. Control of infrastructure tariffs - Infrastructure services relating to fuel products in Israel, include, *inter alia*, unloading, transportation, storage and distribution of fuel products. The Commodity and Service Price Control Order (Fuel Economy Infrastructure Tariffs) 1995 (in this section: "**the Order**") aims to ensure obtaining the maximum price for the various infrastructure services. In 2004, a committee was appointed to examine the prices of infrastructure in the energy sector (in this section: "**the Price Committee**" or "**the Committee**"). The committee contacted Delek Israel to obtain data to conduct an updated survey of the prices, as aforesaid, and even distributed a draft report in March 2010 concerning its recommendations for the various infrastructure prices ("**the 3/2010 Draft Report**"). A hearing was held for Delek Israel before the Price Committee where it sought to reject the recommendations of the 3/2010 draft report. In September 2011,

Delek Israel received a letter from the Ministry of Energy and Water with an updated draft report attached for a committee hearing to examine the energy economy infrastructure prices ("**the 9/2011 Draft Report**"). In the above letter, the Ministry of Energy and Water invited Delek Israel to send its written response to the 9/2011 draft report and the recommendations included therein. The 9/2011 draft report examines the current controlled prices in the energy economy infrastructure services and recommends, *inter alia*, a new price structure and a price updating mechanism. This draft updates (with respect to the 3/2010 draft report) most of the infrastructure prices, while those relevant to the Company are: Oil product storage and oil product storage tank leasing prices⁴³. It is noted that the oil product supply prices remained unchanged in the 9/2011 draft report compared to the 3/2010 draft report. However, the storage tariff in the 9/2011 report was slightly improved compared to the 3/2010 report, but this improvement does not satisfy Delek Israel. On November 2, 2011, Delek Israel submitted its response to the 9/2011 draft report requesting to reject its recommendations concerning, *inter alia*, the storage and leasing prices. On January 31, 2012, a hearing was held at the Ministry of Finance where Delek Israel presented its reservations to the committee's recommendations, *inter alia*, with respect to the infrastructure costs for imported distillates from the unloading ports in Israel. As of the report date, the committee has not yet published its conclusions and recommendations with respect to the foregoing. Adoption of the committee's recommendations, primarily those concerning the storage and leasing prices may materially impair Delek Israel, while the scope of impact will be derived from the recommendations adopted, if any.

- C. Essential Operations - Delek Israel, its gas stations and storage and supply terminals have been declared an Essential Operation as approved by the Ministry of Industry, Trade and Labor. Under this approval, in an emergency, Delek Israel's fleet and fuel storage and supply installations are mobilized for national emergency to enable the regular supply of fuel and gas.
- D. Weights and Measures Ordinance, 1947 ("**the Weights Ordinance**") - the Weights Ordinance sets standards for weights and measures, including the liter as the measure of volume. The weights ordinance describes several offenses, among them refusal to cooperate with the inspector and possession for use in commerce or for commercial use of instruments not certified by the inspector, or instruments which have been tampered with. The weights regulations were established under the weights ordinance, laying down, *inter alia*, how liquid fuel pumps must be tested and calibrated and the obligation to place a calibration seal on the pumps after they are tested and calibrated. The weights regulations also prescribe provisions for instruments which measure oil products assembled on tankers, including installing a calibration seal on these instruments.

The weights ordinance prohibits the use of such instruments unless they have been calibrated and sealed in accordance with the weights regulations. All Delek Israel storage and supply terminals, other than that in Haifa, have calibration certificates for their measuring instruments through to August 1, 2012. Final calibration tests of the equipment at the Haifa terminal are currently being carried out.

- E. Gas station operating licenses

The licensing procedures for new gas stations are long and complicated and require large investments involving obtaining approvals and licenses from numerous entities. This procedure is regulated under many laws granting licensing powers to various governmental authorities. Furthermore, on November 18, 2010, an amendment to the Business Licensing Law (Amendment 27) was recently published, prescribing, *inter alia*, an expedited procedure for receiving a temporary license valid for one year only, under the terms laid out in the amendment. Below are the main legislature granting licensing powers to the various governmental authorities.

- 1. Planning and Construction Law, 1965 ("**the Planning Law**") and its regulations - Under this law, the National Planning Council approved the National Outline Plan for Gas Stations, setting conditions and criteria for the establishment of gas stations. Under the Planning Law and its regulations, a permit is required for any use of land - for erecting a structure and the use of any structure, etc. A building permit for the construction of a gas station often requires rezoning the land.

⁴³ Currently, the leasing services are not controlled.

During the first half of 2006, Amendment No. 4 of the National Outline Plan No. 18, entered into force aimed at adapting the gas station system to the needs of the Israeli population while ensuring appropriate service for consumers and preventing transportation, safety, visual or environmental nuisances. Most of the change is that local Planning and Construction Committees are authorized to approve construction of a gas station in any built-up area, including areas zoned for residential, office, commercial or industrial and commercial areas. Another change in the plan is the possibility of setting up mini gas stations, an option not available under National Outline Plan No. 18. Mini stations require smaller capital investment than that required for public gas stations. A mini gas station is any station which can serve up to four 4-ton vehicles simultaneously and no structure can be added to such station other than a roof over the gas pumps.

2. Business Licensing Law, 1968, ("**the Business Law**"), and its regulations and orders
 - A) Business Licensing (Businesses requiring a License) Order, 1995 - Under this order, a gas station is a business that is required to be duly licensed. The licensing authority is the local authority in whose jurisdiction the gas station is located. To operate a gas station, *inter alia*, approval is required from the following authorities: Israel Police, the Ministry for Environmental Protection, Ministry of Industry, Trade and Labor, Israel Fire and Rescue Services and the relevant Planning and Construction Committee.
 - B) Business Licensing (Fuel Storage) Regulations, 1976, ("**the Fuel Storage Regulations**") - Regulations promulgated under the Business Licensing Law, setting out detailed provisions for obtaining a gas station business license. These regulations describe, *inter alia*, the fuel safety and storage conditions to obtain a license
 - C) Business Licensing (Sanitary Conditions at Gas Stations) Regulations, 1969 - These regulations set out, *inter alia*, provisions concerning the sanitary conditions and facilities required at gas stations.
 - D) Business Licensing (Hazardous Plants) Regulations, 1993 - Under these regulations, a business that stores, produces, processes or sells hazardous materials must have a special license to do so and must comply with the safety provisions laid down in or under any law.
 - E) On July 29, 2010, an amendment to the Business Licensing Law, Amendment No. 26 (Temporary Order), 2010 ("**the Business Licensing Law Amendment**"), pursuant to which, *inter alia*, a business where alcoholic beverages are sold or served, including food chains, kiosks and convenience stores are prohibited from serving or selling alcoholic beverages between the hours 11:00 p.m. through 6:00 a.m.
3. Supervision of Commodities and Services (Garages and Vehicle-related Plants) Order, 1970 issued under the Supervision of Commodities and Services Law, 1957 prohibits opening or operating a gas station without a license from the Ministry of Transport Division of Vehicles and Maintenance Services.
 - F) Most of Delek Israel's public gas stations and convenience stores have received business licenses or temporary permits pending receipt of permanent permits. With respect to other gas stations and convenience stores, Delek Israel or the station owner are taking necessary measures to obtain business licenses or temporary permits, and Delek Israel believes there is nothing material preventing receiving them.
 - G) As of the reporting date, ten indictments are pending against Delek Israel relating to the operation of gas stations and/or convenience stores without a business license or deviation from a permit or in contradiction to the planning and building provisions. Some of the indictments were filed, *inter alia*, against Delek Israel's CEO, several of its senior managers and station owners/operators. Delek Israel estimates that apart from insignificant fines, it has no other material exposure in this regard. Delek Israel's assessment concerning such exposure is forward-looking information based on Delek Israel's past experience. This forward-looking information may not materialize, *inter alia*, due to the occurrence of events contrary to Delek Israel's expectations.

- H) Business licenses are required for the Ionex supply facility and for Delek Oils. As of reporting date, the Ionex supply facility at Ashdod and the Delek Oils plant have permanent business licenses, issued in perpetuity.
- I) The storage and supply operations require business licensing. Some of the conditions for issuing a business license require additional approvals such as permits from the Fire Department and the Ministry of Environmental Protection. The supply facilities in Ashdod, Beer Sheva and Jerusalem have permanent valid business licenses. The Haifa facility has a temporary license, subject to compliance with certain conditions, valid through June 30, 2012, and Delek Israel is taking steps to obtain a permanent business license.
- J) With regard to the internal gas stations at kibbutz or moshav settlements, ILA Agricultural Division provides that an internal non-commercial gas station may be set up within the area of the agricultural settlement without requiring payment to the ILA, under certain conditions. The establishment of an internal station requires obtaining a building permit and operating approvals

F. Antitrust

1. Exclusive supply agreements with gas stations:

On October 27, 1997 the Antitrust Commissioner and Delek Israel reached an agreement (in this subsection: "**the Agreement**"), which was filed for approval of the Antitrust Tribunal (in this section: "**the Tribunal**") under which the Commissioner narrowed the scope of his decision of June 28, 1993 ("**the Original Decision**"), under which the delivery arrangements between the fuel companies and the gas stations which are not owned or under primary lease from the ILA, are cartels, so that the original decision will only apply to gas stations where Delek Israel does not have an accepted lease agreement, (i.e. a lease agreement under which the lease fees paid exceed a certain amount, as defined in the agreement with the Commissioner).

The agreement also set terms for Delek Israel's future engagement with gas stations, providing that when engaging in exclusivity agreements it may request specific approvals for longer periods from the Tribunal. These conditions include, *inter alia*, an obligation for Delek Israel to file an application for approval of these agreements with the Tribunal. The Commissioner announced that he would recommend to the Tribunal that it approve exclusive supply agreements for limited periods of between one and 14 years, depending on the special circumstances of the station for which the approval of the agreement is requested.

Moreover, Delek Israel has undertaken that there will be no partnership or other arrangement between it and Paz and/or Sonol for rights in gas station land or in marketing agreements with the gas station operator.

Under the arrangement, Delek Israel agreed to the immediate release of 35 of its 65 stations with which it did not have an accepted lease agreement, while the Commissioner agreed to support the approval of Delek Israel's agreements with some of the other 30 stations for fixed and limited periods, based on the specific circumstances.

As of the reporting date, of the 35 stations that were released, 10 stations continue marketing Delek Israel's fuel. On July 1, 2002 Delek Israel reached agreement with the Commissioner concerning a consensual order under section 50B of the Restrictive Trade Practices law, 1988 ("**the Consensual Order**"), which was confirmed by the Tribunal. The key point of the Consensual Order is that Delek Israel's lease of gas stations for a period of longer than seven years, under the circumstances described in section 17 of the Restrictive Trade Practices Law, would be viewed as a merger. This means that in those cases, the transactions requires the consent of the Commissioner.

On January 21, 2007, Delek Israel received a written request for information from the Commissioner, requesting, *inter alia*, that Delek Israel submit information to the Authority concerning its rights in stations where other fuel companies also have rights. Delek Israel responded to the Authority's demand in two letters dated February 4, 2007 and February 8, 2007. Delek Israel was required by the Commissioner to separate sub-leasing rights shared by Delek Israel and another fuel company in one of these stations. On March 18, 2008, Delek Israel signed an agreement under which it acquired the sub-leasing rights of the other company, thereby complying with the Commissioner's requirement with regard to this station.

2. Commissioner's approval for the merger of Pi Gllot and Delek Israel - As part of the acquisition of the three storage and supply depots by Delek Israel, the Commissioner issued approval for this merger, with the following main points:
- A) Delek Israel and any person controlling it, corporation controlled by it and any corporation controlled by any of them (jointly referred to in this sub-section 1.8.19F.2) as "**Delek Israel**"), shall not unreasonably deny distillate supply services to anyone requiring them from the Ashdod and Jerusalem supply depots, under terms that were acceptable at Delek-Pi Gllot facilities prior to the merger, and shall not make provision of supply services contingent upon conditions which, by their nature or under acceptable trading terms, are unrelated to the subject of the arrangement. Delek Israel shall not set different terms of engagement for similar transactions for providing supply services, shall not discriminate among its customers, and shall not make the provision of supply services or grant any benefits contingent upon the purchase or receipt of other products or services.
 - B) Throughout operation of the Ashdod supply depot, Delek Israel will allocate storage tanks at the Ashdod depot to a third party for operating storage, as provided in the appendix to the privatization agreement, unless permitted otherwise in advance and in writing by the Commissioner. During the term of lease of tanks as stipulated in this section, Delek Israel will be responsible for their operation and proper maintenance so as to ensure continuous service and repair as provided by Pi Gllot prior to the merger.
 - C) Delek Israel shall not contract, directly or indirectly, with another person in an arrangement conferring upon it rights in infrastructure necessary for importing or refining operations or in land designated for the construction of infrastructure facilities, without the prior written consent of the Commissioner. The provisions of this section shall not apply to agreements in effect prior to this decision, between Pi Gllot and another person holding or operating storage or piping infrastructure for oil products or LPG, which are necessary for ensuring regular operation of the national pipeline network, or to the extension of such agreements.
 - D) Unless otherwise authorized by the Commissioner, any restriction applicable to any corporation by virtue of the Commissioner's approval applies also to any officer, agent or consultant of a corporation and to any agent or substitute of any of the foregoing, all by statute or agreement or in practice.
3. The rate of interchange fees – in August 2011, the Antitrust Court extended the validity of the temporary permit to determine cross-commission between clearance companies and Visa and Mastercard credit card issuing companies ("**the Credit Card Companies**") to end 2011. On March 7, 2012, the Antitrust Court issued a ruling allowing the compromise agreement which the credit card companies reached with the Antitrust Commissioner under which the interchange fees would be substantially reduced and the cross-clearing through 2018. Delek Israel estimates that approval of such compromise agreement may positively impact its profitability. This assessment is forward looking information as defined in the Securities Law, which may not materialize, *inter alia*, because of events contrary to Delek Israel's expectations and reasons beyond its control.

G. Recognized Ministry of Defense Supplier

Delek Israel participates in tenders published by the Ministry of Defense containing standards and preconditions, and complies with all of them. Delek Israel and Delek Oils are approved suppliers, recognized by the Ministerial Committee for the approval of suppliers to the Ministry of Defense.

H. Standardization

Israel has standards for the fuels that are marketed in Israel. Delek Israel markets only products that comply with these standards. Delek Israel and Delkol have permits from SII with respect to ISO 14001 (environmental), ISO 9001 (quality management) and Israeli Standard SI 18001 (safety management) standards. These permits were valid through May 31, 2013, March 31, 2013 and January 31, 2013, respectively.

Furthermore, in October 2006, the Fuel Administration published service standards designated as a normative code of conduct for the fuel infrastructure segment to improve service and bring it up to par with developed countries. If a particular subject is covered by an agreement between a service provider and a service recipient, the agreement supersedes these service

standards, provided it is not injurious to any third party, does not contravene the principle of service equality for all and is performed lawfully. Delek Israel complies with these service standards.

1.8.20 Material agreements

- A. Most of the fuel products sold by Delek Israel are purchased from ORL (for details, see section 1.8.13B above). Therefore, the agreements between Delek Israel and ORL are material for Delek Israel.
- B. Generally, the filling and commercial compounds segment has no single material agreement concerning rights in land and operating the gas stations, but the entire set of agreements in the segment is material for Delek Israel.
- C. In general, the fuel storage and supply segment has no single material agreement which is not in the course of Delek Israel's regular business.
- D. Pi Gllilot privatization agreements

On July 31, 2007, Delek Israel and Pi Gllilot entered into an agreement to acquire the terminals operation ("**the Terminal Acquisition Agreement**"), whereby Delek Israel acquired all rights in movable goods, land and other rights and obligations, including with regard to staff employed at the terminals, as set forth in the appendices to the agreement ("**the Property Being Sold**"), in return for NIS 806 million, after fulfilling provisions of the sale procedure and obtaining the approval of the Antitrust Commissioner (for a description of main points of the Commissioner's approval, see section 1.8.19F.2 of the report). Delek Israel acquired rights in the Property Being Sold as-is and undertook to comply with all conditions laid down by the Antitrust Commissioner. Delek Israel undertook to operate the Property Being Sold for periods defined by the State and within limits set by the State as follows: (1) Delek Israel undertook to operate the Ashdod terminal as a storage and supply depot for at least 10 years from the acquisition date. Delek Israel may, with consent of the Fuel Administration Director at the Ministry of Energy and Water, sell the terminal to a third party, provided the latter commits to comply with the same requirements. At any time after this 10-year period, depot operations may be cut back or discontinued, provided that the Fuel Administration is given at least two years' notice. The agreement further stipulates that throughout operation of the Ashdod terminal, five transit tanks would be leased to FPL, which is responsible for the fuel piping array in Israel, or to any successor thereof or to anyone designated by the Fuel Administration, in exchange for a price that would be set in an order. (2) Delek Israel undertook to continue operation of the Beer Sheva terminal and preserve its storage and supply capacity to ensure continued regular supply of fuel products to the Air Force base being supplied by pipeline from the depot, unless the Fuel Administration Director confirms that an alternative arrangement is in place. Notwithstanding the above, the buyer may discontinue operation of this terminal, provided that the Fuel Administration Director is given at least one year's notice. Delek Israel informed the Fuel Administration Director on November 17, 2007 of discontinuation of operation of the Beer Sheva terminal. Subsequent to negotiations with the Fuel Administration Director, it was agreed that Delek Israel will withdraw its foregoing discontinuation notice subject to the Fuel Administration Director's undertaking to store emergency supplies at the Beer Sheva depot. As of the reporting date, the Fuel Administration Director fulfilled its undertaking and Delek Israel withdrew its notice concerning the discontinuation of operations at said depot. (3) Delek Israel undertook to operate the Jerusalem terminal as a storage and supply depot for at least three years from the acquisition date. The buyer may, with the consent of the Fuel Administration Director, sell the depot to a third party, provided the latter undertakes to comply with the same requirements. At any time after this 3-year period, depot operations may be cut back or discontinued, provided that the Fuel Administration is given at least two years' notice. Delek Israel informed the Fuel Administration Manager in December 2007 of discontinuation of operation of this terminal at the end of the 3-year operation period.

Notwithstanding the above, the closing of any terminal by order of competent authorities would exempt the buyer from its undertakings, provided that the closure order was not given due to an act of commission or omission by the buyer.

Delek Israel made an irrevocable undertaking to Pi Gllilot and the State of Israel that it would not take any action in the Property Being Sold which is not in keeping with the foregoing, and that should it decide to transfer or pledge its rights in the Property Being Sold to any third party, the transferee would undertake to act in accordance with Delek Israel's undertaking.

Delek Israel and its interested parties have declared and undertaken that except for allegations against Pi Gllot in respect of breach of the Depot Acquisition Agreement, they waive any and all claims and demands of any kind against the State of Israel and/or the Joint Committee and/or any of its members and/or Pi Gllot and/or officers, managers and employees of Pi Gllot and/or anyone acting on behalf of any of the above in the sale which is the subject of the agreement. If despite the aforesaid such a claim or a claim whose cause pre-dates the agreement, in respect of which Delek Israel or its interested parties are compensated, Delek Israel shall be obliged to indemnify those entities in the amount of any compensatory amount charged to any of them.

1.8.21 Legal proceedings

For a description of legal proceedings (including motions for class action status) to which Delek Israel is party, see Note 32 to the financial statements.

1.8.22 Business Objectives and Strategy

Delek Israel reviews its strategic and business plans from time to time and updates them according to developments in the energy market, the gas station and retail roadway industry, the competitive environment and the economic situation.

Delek Israel's operations in the coming years are expected to focus on the following activities:

- A. Delek Israel will develop the retail roadways segment, while leveraging its wide geographical deployment and converting some of the gas stations into retail compounds including a variety of businesses.
- B. In recent years, Delek Israel will make material investments in the construction, acquisition and development of existing and new retail complexes, including leveraging its real estate infrastructure to set up dozens of various sized commercial centers at different scopes of investment. In this framework and as part of other operations, Delek Israel aspires to significantly increase the volume of sales from operations not originating from fuel. Delek Israel set a visionary target (updated) of five years to increase the volume of sales from trade operations (including franchises) that are not from fuel to NIS 0.7 billion in 2015-2016.
- C. Subject to obtaining the required approvals, Delek Israel strives to increase the number of convenience stores and Menta Market minimarkets in gas station and commercial compounds at strategic locations and expand their deployment. It also aspires to expand the range of solution is for its customers in the gas station and commercial compounds to meet most of their possible requirements, such as postal services, supplementary household shopping, coffee shops, etc.
- D. As part of its plans for 2012, and subject to obtaining various administrative approvals, Delek Israel intends establishing and completing establishment of 3-6 new gas station and commercial compounds as well as 10-15 new convenience stores (some in these new compounds). Delek Israel aspires in 2012 to increase its sales not from fuel by 10% to 15% compared to 2011. As of the report date, Delek Israel has 10 new Menta Market stores established in 2010 and early 2011. In 2012, Delek Israel also plans to integrate the Cup-O-Joe chain operations in 60 to 100 convenience stores and later on complete the deployment in all its compounds. In 2012, because of the economic slowdown in the market, Delek Israel intends focusing on reduced, focused development of its business with maximum control of the volume of investments and focusing on developing its existing properties.
- E. Marketing of LPG and natural gas – during the forthcoming year, Delek Israel plans to deploy automotive gas pumps in the chain's gas stations. It also intends deploying between 15 and 25 LPG refueling pumps. Delek Israel is also examining the development of an LPG marketing array for corporate customers and building infrastructures to market and transport natural gas. It will weight participating in State tenders to distribute natural gas in the Jerusalem and northern Israel regions.
- F. In the forthcoming years, Delek Israel intends implementing a plan to reduce the scope of its financial liabilities. The plan is based on sources which will be generated from the sale of properties and investments which are independent of its core business, repayment of the loans granted to Delek Group companies and reduction of the extent of the credit score provided mainly in direct marketing.
- G. Generally, Delek Israel acts to transfer public gas stations operated by operators and independent store owners to self-operation (operation by Delek Israel) of those facilities. However, it is quite possible that Delek Israel will examine the possibility of other operation,

including leaving some of the public gas stations in the hands of external operators, as long as this maximizes its profit margin in operating these facilities.

- H. Entering long-term rental contracts with gas station owners and reducing uneconomical rental contracts.
- I. Establishment of mini gas stations in strategic locations as long as licenses and approvals are granted by the authorities.
- J. Delek Israel intends to review developing the capacity to provide marine services in the open seas (including refueling) and refueling at other Israeli ports.
- K. Introduction of the private brand to new areas and categories and increasing the range of products offered in the chain's stores. Increasing the range of services offered at Menta stores, such as the postal service points offered in the chain's stores.
- L. Delek Israel intends to expand direct marketing to end users, *inter alia*, by increasing the number of internal gas stations. Delek Israel will also work to improve the marketing margins and collateral from its customers.
- M. Delek Israel to take steps to expand its share of the automatic devices for fleets segment.
- N. Development of a fuel product import array in cooperation with a leading international fuel trading entity, using the Pi Gllot terminals. This cooperation may also be carried out by introducing a partner at the Pi Gllot facility.
- O. Reviewing the establishment of additional storage tanks to maximize utilization of the storage facility land.
- P. Maximization of the storage and supply capacity at Delek-Pi Gllot facilities, including collaboration with international entities.
- Q. Reviewing of options of unloading distillates from ships anchored offshore directly to Ashdod port, which will save costs and reduce dependence on EAPC's facilities and FPL's pipelines.
- R. Examination of new opportunities in the oil industry and other chemical products and expanding the partnership with Sano to recycle solvents for industry.
- S. Enhancement of vacant property owned by Delek Israel.

Delek Israel's above estimations and intentions concerning the volume of investment in the retail compounds and its revenues therefrom, utilization of Delek Israel's real estate to establish commercial centers, increasing the number of Menta and Menta Market stores, and increasing Delek Israel's sales turnover is forward-looking information, as defined in the Securities Law, 1968, based on existing information at Delek Israel as of the date of this report. This estimation might not materialize, partially or fully. The factors which could affect it are, *inter alia*, changes in Delek Israel's work plan, market conditions, competitors entering the market and/or materialization of any of the risk factors described in this report.

1.8.23 Risk factors

It is noted that there are several risk factors on Delek Israel's operation as described below.

- A. Geopolitical situation – The geopolitical situation worldwide directly affect the economic situation, global oil prices, Delek Israel's general operations and its ability to import oil distillates. The security and political situation in Israel also materially affects the situation of economy. An economic slowdown in the Israel market may lead to a decline in demand for Delek Israel's products, resulting in a drop in the volume of sales of its fuel products and profitability. The security situation in southern and northern Israel could directly impact Delek Israel's infrastructure facilities and gas stations in these regions
- B. Exchange rate fluctuations – Fuel products are purchased by Delek Israel from its suppliers in or linked to the USD. Therefore, any fluctuation of the USD/NIS exchange rate could affect its stock value. Delek Israel's policy is to avoid currency exposure using various financial instruments and taking USD loans to finance inventory. It is noted that Delek Israel charges exchange rate differentials for the operating inventory immediately when they arise. In view of the above, exchange rate changes could impair its financial results.
- C. Interest rate changes – Interest rate changes may affect the bank loans granted to Delek Israel and debentures raised by it at variable interest rates. A rise in the interest rates will lead to increased financing expenses. Therefore, Delek Israel is exposed to interest rate changes.

- D. CPI fluctuations – Delek Israel has long-term CPI-linked loans arising mainly from the issue of CPI-linked debentures in August 2007 and June 2009. It also provided CPI-linked loans to the Delek Group, Delek Europe, and its customers. Thus, a substantial upswing in the CPI may lead to an increase in Delek Israel's financing expenses accordingly, and impair its profits
- E. Strikes and lockouts in the Israeli economy – Strikes and lockouts in the Israeli economy and especially lockouts at the ports and/or the fuel supply infrastructure companies could prevent the importation of raw materials and prompt supply of orders. This could impair Delek Israel's capacity to meet its commitments to its customers and impair its goodwill.
- F. Economic slowdown in Israel and worldwide – The global economic crisis, including in the Israeli market, may result in a decreased demand for Delek Israel's products, thus, *inter alia*, lowering the consumption of fuel and retail products purchased in Delek Israel's gas stations and impairing its business results.
- G. Difficulties in obtaining financing – Delek Israel finances its operations, *inter alia*, with banking and non-banking credit. Due to the grave global economic crisis which erupted towards the end of 2008, followed by the collapse of banks and investment houses worldwide and continuation of the European block crisis in 2011, the Israeli banks introduced more stringent requirements for granting bank financing. This is in addition to the regulatory requirements applicable to the banking system by reducing all the credit granted by them. The global economic crisis also affected the Israeli capital market there was less activity in the capital market in the second half of 2011. If the activity in the capital market drops, it will be difficult for Delek Israel to raise non-bank capital. In view of the above, if Delek Israel requires additional financing for its ongoing operations, it may encounter difficulties in obtaining bank and/or non-bank financing.
- H. Changes in oil and fuel product prices – The price Delek Israel pays for the fuel products purchases derives from their price on the free market in the Mediterranean region and is therefore exposed to fluctuations in the oil prices in these markets. An increase in fuel product prices worldwide leads to a rise in prices of the products sold by Delek Israel, which could cause a downturn in demand for these products and impair its business results. Among the factors affecting fuel prices are: changes in the global and domestic economy; the demand for fuel products in countries where Delek Israel operates; the global political situation in general and in the oil producing regions in particular (USA, the Middle East, former USSR countries, Western Africa and South America); the global production level of crude oil and distillates; development and marketing of fuel substitutes; disruptions in the supply lines; and domestic factors, including market and weather conditions.
- I. The competitive environment – The fuel market is characterized by fierce competition expressed in eroded margins and increased customer credit. Delek Israel's financial results are materially impaired by the competitive environment where it operates.
- J. Construction of additional gas stations – In recent years, there is a trend of constructing dozens of new gas stations annually. Continuation of this trend will strengthen competition in the fuel market. Approval of the proposed changed to the provisions of NOP 18 could aggravate this trend.
- K. Fuel taxation – The excise component in some of the oil product prices is significant. Since the credit terms which Delek Israel receives from the fuel suppliers to pay the price of fuel product (include the excise) is far shorter than that offered to its customers, its financial exposure will increase with any rise in excise rates (including on diesel fuel). This could impair its business results. An increase in excise taxes could also lead to a decline in demand for the products sold.
- L. Changes in maintenance of civilian inventory requirements – As stipulated in Section 1.8.19A.1 above, the High Court of Justice approved an interim arrangement requiring maintenance of emergency security inventory only. However, the State is permitted to change the existing situation by 60 days prior notice while reserving the rights of the parties to revert to the High Court of Justice. The significance of the requirement to maintain civilian inventory, at whatever volume, is on the one hand an increase in financing cost for Delek Israel and an increase in the volume of credit, and on the other hand could lead to a growth in demand for storage of inventory at its storage and supply facilities, affecting its business positively. Nevertheless, it is noted that such change could reduce its available storage for provision of storage services at economically viable prices for Delek Israel.
- M. Dependence on infrastructure facilities – The fuel industry is limited in infrastructure facilities (two refineries, a small number of storage and supply depots) and therefore, termination of

operation at an infrastructure facility could impair the proper operation of the refineries and fuel companies. Termination of operation could result from strikes, security events, accidents, natural disasters, etc. Additionally, damage of fuel pipelines to Delek Israel's storage and supply facilities may impair its operation in the fuel storage and supply segment. Delek Israel estimates that because of its fuel storage and supply operation, it is more exposed than other fuel companies which have no such infrastructure facilities.

- N. Regulatory intervention – As noted above, Delek Israel is affected by regulatory changes in the fuel economy, including control of gasoline and storage and supply prices, restrictions of the purchase price from refineries, and regulatory restrictions on contracts with respect to gas stations in the distillate segment. Regulatory changes in the fuel economy could affect the scope of investments required from Delek Israel in its area of operation, resulting in impairment of its financial results and profit margin. For information concerning control of the marketing margin of diesel oil for transportation, see section 1.8.19B(3) above.
- O. Marketing margin changes – Since the maximal profit margin on 95 octane gasoline is a fixed sum (due to governmental control), it is not materially affected by ORL ex-refinery fuel price fluctuations, excise tax value changes and infrastructure tariffs. Under circumstances where the global market price and the tax applicable to them increases, a situation arises where there is no built-in compensation for credit risk costs when customer credit increases. For information concerning the marketing margin changes, including the change in the updating method, see section 1.8.19B(2) above. Changes in the marketing margin calculation and updating method could materially impact Delek Israel's results, while the scope of the impact arises from change ultimately adopted.
- P. Infrastructure tariffs – The infrastructure services for fuel products in Israel include, *inter alia*, unloading and loading services at the fuel port, fuel product piping services, fuel product storage services, etc. The maximal price for the different infrastructure services are set out in the Commodity and Service Price Control (Infrastructure rates in the fuel economy) Order, 1995 (in this subsection: “**the Order**”). For information of the Committee for examination of the prices of infrastructure in the energy segment's draft report and Delek Israel's response in this matter, see section 1.8.19.B(4) above. Acceptance of the Committee's recommendations, mainly those concerning storage and leasing prices, may significantly affect Delek Israel's results, while the scope of the effect arises from the recommendations adopted, if any.
- Q. Environmental protection – The provisions of various laws, regulations and orders and the Ministry of Environmental Protection's environmental requirements concerning the gas stations, facilities and plants require Delek Israel to allocate financial resources in this matter. In recent years, the Ministry of Environmental Protection requirements have become more stringent and could expand and multiply, which may compel Delek Israel to allocate additional financial resources in this issue, including as stated in section 1.8.18 above. Delek Israel intends to continue working towards implementing the statutory provisions and the requirements of the Ministry of Environmental Protection and will also implement its soil identification and rehabilitation plan as described in section 1.8.18O above.
- R. Exposure to legal proceedings for environmental contamination – Delek Israel is exposed to civil and criminal legal proceedings for environmental contamination allegedly caused in the past and could be caused in the future as a result of its operations, and as part thereof, the enforcement authorities conduct inspections and investigations from time to time. There is risk of indictments against Delek Israel and its officers if soil and water contamination is discovered in other stations than those specified in section 1.8.18B above. As described above, rehabilitating the surroundings of a station where groundwater has been contamination may involve substantial expenses which cannot be estimated.
- S. Lack of insurance coverage – Delek Israel's third party liability insurance policy covers, *inter alia*, its liability for bodily harm or property damage from accidental environmental pollution up to a liability limit of USD 50 million per incident and per insurance period. Nevertheless, the third party liability limit for professional responsibility is USD 3.750 million. Delek Israel does not maintain an insurance policy for liability that could be imposed due to ongoing environmental contamination that is not accidental, such as the pollution described in section 1.8.18 above.
- T. Hazardous and toxic materials – Since Delek Israel deals in potentially explosive, flammable and poisonous hazardous and toxic materials, it is exposed to damages which may be caused by these materials, including health and environmental damage, and damage resulting from ignition of flammable substances, etc. Claims for these damages could impair its business

results and goodwill. Delek Israel purchases customary insurance policies accepted Israel to insure its assets and liabilities arising from dealing in these materials. It is uncertain whether the coverage and/or liability limits in the policies cover all the risks involved in Delek Israel's operations and whether it will be able to continue the policies in future under reasonable commercial terms or at all.

- U. Product liability – Delek Israel markets various distillates which are especially sensitive, because they are hazardous and because of how they are used. Many laws and regulation regulate the rights of victims or groups of victims to damage caused by a product manufactured, stored, marketed or sold by a supplier. If any damage is suffered by a consumer or group of consumers as a result of the products marketed by Delek Israel, it could be sued by them, including in class actions, which could be detrimental to its business and business results.
- V. Natural gas – Recently (February 2012), following a tender, the State granted a license to a third party to set up and operate a low pressure natural gas distribution network {“**the Distribution Network**”} in Southern Israel (Ashdod-Ashkelon-Kiryat Gat, where the connections are expected to be implemented within 24-58 months). Another license to establish and operate a distribution network relating to the Negev region was granted to a third party already in November 2009 (connections to customers are expected within 8 to 24 months). A further license was granted to a third party for the central region also in November 2009 (connection to customers is expected within 8-70 months). With respect to Northern Israel, the State recently (March 2012) published tenders to establish and operate a distribution network. The gas is used for burning and is an alternative to kerosene, fuel oil and LPG marketed by Delek Israel. Marketing natural gas expands the range of alternatives to Delek Israel's products and may result in a drop in its sales volumes. In this context it should be noted in early 2012, Delek Gas' operation was acquired by Delek Israel to reduce this exposure to competition.
- W. Development of alternative energy sources – Transition to using alternative energy sources such as natural gas, electric engines, etc. could affect the quantity of fuel products which Delek Israel sells and compel it to invest substantially in adapting its stations to new customer requirements and may also create competition beyond gas stations. Delek Israel estimates that this process will not materially affect its results in the forthcoming years, besides in the matter of natural gas as set out above.
- X. Automotive gas –The transition to automotive gas to replace gasoline will require Delek Israel to prepare in advance by setting up gas refueling points at a cost of hundreds of thousands of NIS per refueling point integrated into gas stations. It is emphasized that the extent of transition to refueling with automotive gas is still unclear, due *inter alia* to uncertainty regarding government intentions for taxing the gas (excise) and matching the tax levels to those levied on gasoline
- Y. Dependence on refineries – As stipulated in section 1.8.13B above, companies operating in the oil distillates segment are almost completely dependent on the refineries, which are the central suppliers of various distillates which they purchase. Due to the acquisition of the Pi Gllot storage and supply facilities in late July 2007, Delek Israel is slightly less dependent on the refineries.
- Z. Entry of ORL into the fuel marketing segment – Following its sale, ORL was given the opportunity to market fuels directly to consumers and to establish or acquire gas stations.
- AA. Economic slowdown in the domestic market – An economic slowdown brings about deterioration in payment ethics, including for objective reasons of impairment to the customers' ability to pay. The industry is characterized by offering extensive credit, some without or with partial collateral, and therefore, an economic slowdown exposes companies operating in the industry to the possibility that such credit might not be repaid. A slowdown in the global and Israeli economy may also decrease private consumption and commercial operations, causing a drop in sales of Delek Israel's products, revenues and profitability.
- BB. Transition to public transport – In recent years, there has been a steady increase in the use of trains, including the light rail which is planned to criss-cross the major cities and could reduce the use of private cars. The more this trend expands, so the quantity of gasoline and diesel oil sold to customers will decrease. This could impair Delek Israel's financial results
- CC. Antitrust Court ruling concerning exclusive supply agreements at stations where fuel companies have no proprietary rights – Under the Antitrust Court ruling of March 25, 2001, exclusive supply agreements may be entered into for a maximal period of three years in an

existing station and six years in a new station which fuel companies have constructed or invested in their construction where they have no ownership rights. This could increase competition and may lead to changes in the gas station deployment in Israel. Delek Israel has 20 such contracts

- DD. Food industry regulation – Food products sold in the Menta convenience store chain are subject to many diverse statutory provisions. In the event of non-compliance with these laws, Delek Israel may have to bear liability for harm from eating spoiled food and failure to meet the standards and legal provisions of the competent authorities
- EE. Universal Refueling Device Regulations - On October 23, 2011, the Universal Refueling Device Regulations were published coercing the fuel companies to install a universal refueling device system enabling the consumer to sign an agreement with various fuel companies and refuel at other fuel companies using the same device. Delek Israel estimates that the universal refueling device provisions may cause it to incur expenses (the extent of which cannot currently be determined) to convert existing Delkan devices to universal refueling devices. Moreover, converting the refueling devices to universal devices will increase the number of stations where customers may purchase fuel products and may lead to a reduction in the number of customers purchasing fuel products through its automatic refueling system. For further information, see section 1.8.19A(8) above.
- FF. Increase in the use value of company cars and decrease in the number of cars – On December 31, 2007, the Income Tax (Use value of a vehicle) (Amendment) Regulations, 2007 were published under which the use value of a company car will increase gradually over four years from January 1, 2008 through January 1, 2011. Simultaneous to approval of these regulations, income tax rates on middle level incomes were reduced, with the purpose of partially offsetting the additional tax that will be paid on the use of the company car. Following the "green tax" reforms, as of January 2010, the method of calculating the use value charge for a company car changed from the group price method to a linear method, whereby the use value is a fixed percentage of the vehicle price, thereby in effect canceling the group price with respect to cars registered as of January 1, 2010. The above regulations as well as increasing the number of lay-offs may in the long-term affect the number of company cars in used by employees, which may lead to a decline in fuel consumption.
- GG. In the fuel economy, a small number of companies other than Delek Israel operate in the distillate storage segment, the main companies being EAPC, Paz and ORL. An increase in their distillate storage capacity and/or expansion of their fuel supply capacity poses a real threat to Delek Israel's advantage of holding its own storage and supply facilities.
- HH. Failure to obtain required gas stations operation approvals and licenses – Operating a Delek Israel gas station requires approvals and licenses from many entities. At some of its stations Delek Israel does not have all the required approvals and licenses, while in other cases these have expired and require renewal. If Delek Israel does not succeed in obtaining these approvals and licenses, this could impair its operating results
- II. Credit risk – Most customer credit offered by Delek Israel not secured by any collateral or guarantees, thereby exposing it to credit risks. As of December 31, 2011 and December 31, 2010, Delek Israel had trade receivables amounting to NIS 1,704 million and NIS 1,515 million, respectively. As of December 31, 2011, over 96% of these debts are not secured with any collateral or guarantees. As of December 31, 2011, Delek Israel has nine customers with outstanding debt of between NIS 10-25 million and total debt of NIS 132 million; it also has two customers with outstanding debt ranging from NIS 25-50 million and total debt of NIS 63 million; and two customers with total debt of between NIS 50-95 million and an overall total of NIS 142 million.
- JJ. Default of customers loans – Delek Israel extended loans to customers who operate stations on its behalf or independent station operators in the normal course of business as described in section 1.8.5A above. As at December 31, 2011, these loan balances totaled NIS 158 million. Delek Israel has collateral for most development loans and commercial loans (which at December 31, 2011 amount to NIS 116 million), whereas for part of debt rescheduling loans, it has no collateral (which at December 31, 2011 amount to NIS 42 million). Therefore, it is exposed to credit risk for default of uncollateralized loans.
- KK. Non-renewal of Ionex's agreement with Haifa and Ashdod ports for marketing of fuel products to ships – The agreement with Ashdod Port Company Ltd. is effective through June 1, 2013. Under the agreement, Delek Israel has the concession to provide refueling services to ships and lease the Ashdod fuel oil supply facility, and Ashdod Port Company Ltd. is entitled to publish a new

tender for the supply of fueling services, and if Ionex does not win, it will be required to vacate the port on 60 days' notice. Early December 2010, Haifa Port Company Ltd. published a tender for the provision of fueling services there. Ionex submitted a proposal under this tender and on March 24, 2011 was notified that it was awarded the tender. As of the report date, the mandate to provide refueling services to vessels at Haifa Port is for three years, from June 1, 2011 through May 31, 2014, and includes the option to extend the validity for another two years and in total through May 31, 2016. If the leasing periods are not extended, this could have a materially impair Delek Israel's business. As of the report date, IP, owner of this distribution facility, published a tender to lease the facility for a period starting June 1, 2013. Ionex intends participating in the tender. This information is forward-looking information, which may not materialize, *inter alia*, due to the occurrence of events unforeseen by Delek Israel.

- LL. Ownership structure of gas stations – Due to the ownership structure of gas stations, some of which are rented by Delek Israel and some with which it only has a fuel supply contract, there is a risk that these stations will switch to marketing the products of other fuel companies at the end of the rental period /supply contracts. Additionally, at stations that it neither owns nor operates, Delek Israel is exposed to greater pressures from operators/owners, and therefore, the profitability of such stations is eroded.
- MM. Short-term direct marketing contracts – In direct marketing, the contracts are short-term and thus, there is a risk that customers will leave and move to competitors at short notice.
- NN. Lawsuits – There are material lawsuits against Delek Israel, including class actions in material amounts that could reach hundreds of millions or even billions of shekels, for some of which it is impossible at this stage to estimate the outcome (see Note 32 to the financial statements). Delek Israel is exposed to the consequences of these claims.
- OO. Dependence on brand name and goodwill – Delek Israel's goodwill has been earned over many years and has brand names that distinguish it and its subsidiaries and affiliates from its competitors. Harm to this goodwill or these brands through various publications or other means could impair Delek Israel's results even if such publications are incorrect.
- PP. Environment at Old Stations– Delek Israel has old public gas stations established before 1997, accounting for about 50% of all its stations. These stations were built to standards acceptable in the past and which according to current know-how do not guarantee that there will not be leakage from a tank or pipe.
- QQ. Delek Israel belonging to a Group and to its controlling shareholder, Mr. Yitzchak Teshuva – The fact that Delek Israel belongs to a group and its controlling shareholder, Mr. Yitzchak Teshuva, has implications on Delek Israel's capacity to raise credit, *inter alia*, due to the "single borrower" restrictions, which could result in its sources of bank credit being limited, and other regulatory regulations imposed on the banking system and institutional bodies by the Ministry of Finance and the Bank of Israel.

Below is a summary of the risk factors described above by type (macro risks, industry-wide risks and Delek Israel-specific risk), rated by extent of impact on Delek Israel's business (major, medium, minor):

	Impact of risk factors on Delek Israel's business		
	Minor Impact	Moderate Impact	Major Impact
Macro risks		• Security and political situation • Strikes and lockouts • Economic slowdown in Israel and worldwide • Foreign exchange rate fluctuations	• Interest rate fluctuations • CPI changes • Difficulties in obtaining finance
Industry-specific Risks	• Lack of insurance cover • Product liability • Automotive gas • Rise in company car utilization value • Transition to public transport	• Competition • Establishment of additional service station • Fuel taxation • Dependence upon infrastructure facilities • Exposure to lawsuits on environmental issues • Hazardous and toxic materials • Natural gas • Food segment regulations	• Oil and fuel product price changes • Civilian inventory requirement changes • Regulatory involvement • Marketing margin changes • Infrastructure rates • Environmental protection • Dependence upon refineries • Entry of ORL into the fuel marketing segment • Economic slowdown on local market • Antitrust Authority • Transition to automatic fueling facilities • Development of alternative energy sources • Substantial increase in competition's distillate storage capacity.
Delek Israel-specific risks		• Short term contracts in the direct marketing operations • Dependence on branding and goodwill • Default of loans extended to customers	• Failure to obtain permits and licenses for stations • Credit risks • Ownership structure of gas stations • Legal claims • Delek Israel belonging to the Delek Group and its controlling shareholder, Mr. Yitzhak Teshuva • Non-renewal of Ionex contracts with ports • Environmental issues at old stations

The impact of the risk factors on Delek Israel's business is based on estimates only and it is possible that in practice it could be different.

1.9 Fuel products in Europe

1.9.1 General

The Company's fuel product operations in Europe are carried out through Delek Europe Holdings Ltd., a subsidiary incorporated in Israel and owned by Delek Petroleum (80%) and Delek Israel (20%) ("Delek Europe").

The fuel products in Europe segment consists of fuel marketing operations in Belgium, the Netherlands and Luxembourg ("Benelux") and of fuel marketing operations in France.

A. Acquisition of fuel marketing operations in Benelux:

On August 8, 2007, Delek Benelux B.V. ("Delek Benelux"), an indirectly held foreign subsidiary of Delek Europe, incorporated in the Netherlands (together with its subsidiary incorporated in Luxembourg), acquired the marketing operations of Chevron Global Energy Inc. ("Chevron") in Benelux (Belgium, the Netherlands, and Luxembourg), which includes gas stations, convenience stores, food chain branches, carwash facilities, and holdings in two terminals ("Marketing Operations in Benelux"; for a quantitative account of assets, see Section 1.9.4(a) below; for information about the terminals, see Section 1.9.12 below). Marketing operations in Benelux are carried out by three separate companies in each of the aforesaid countries.

Consideration for the acquisition of the above operations totaled approximately EUR 404 million, after working capital adjustments. The acquisition was financed through foreign bank funding, raised by Delek Benelux and its subsidiaries, as well as an equity investment in Delek Benelux. Bank funding accounted for 63% of the total funding, while the equity investment accounted for the remaining 37%. The three acquired companies had previously included other operations, which Chevron withdrew from the companies prior to their acquisition.

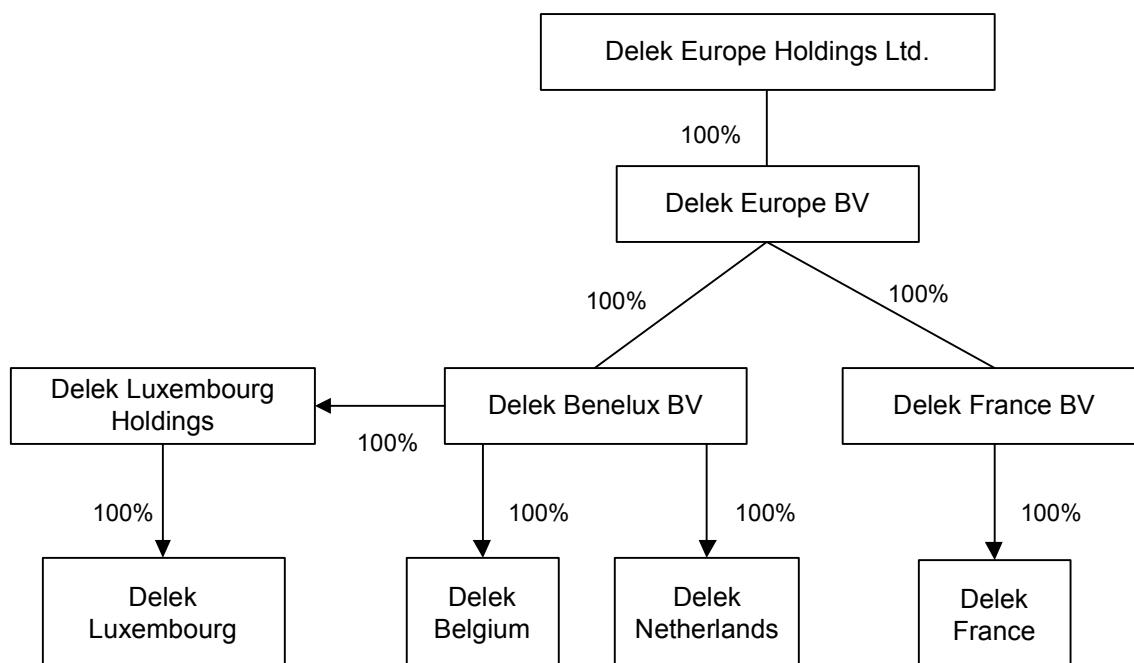
In the reporting period, an agreement was signed between Delek Benelux and Chevron for extending the use of the Texaco brand name through 2030.

B. Acquisition of fuel marketing operations in France:

On October 1, 2010, the subsidiary Delek Europe B.V. acquired BP France SA's "BP") fuel marketing and convenience store operations in France, which consist of gas stations, convenience stores, carwash facilities, and holdings in three terminals for the supply and storage of fuels used in the operations ("Marketing Operations in France"; for a quantitative account of assets, see Section 1.9.4(b) below). Acquisition of the marketing operations in France also included an exclusive usage license to the BP brand in the gas station chain in France, as well as long-term agreements concerning refueling cards. The marketing operations were acquired by Delek Europe through Delek France Finance SNC ("Delek France Finance"), a company incorporated in France which is a wholly-owned subsidiary of Delek Europe, indirectly held through Delek France B.V., a wholly-owned subsidiary of Delek Europe.

The consideration for acquiring the aforesaid operations amounted to EUR 209 million (after working capital adjustments but before transaction costs) and was financed through banks (70%) and shareholder loans extended by Delek Petroleum and Delek Israel (30%), pro rata to their holdings in Delek Europe. For more information concerning the financing for the acquisition of the marketing operations in France, see Section 1.9.23 below. The acquisition of the aforesaid operations was effected through the purchase of shares in the companies carrying out the said operations.

The following diagram illustrates Delek Europe's primary holding structure:



1.9.2 Financial information concerning the fuel products in Europe segment

A. Below are data for the operating segment in 2010 - 2011 (in EUR millions):

		2010 ⁴⁴	2011
Revenues	Revenues from externals	2.298	3.272
	Revenues from other segments	-	-
	Total	2.298	3.272
Total attributable costs	Costs constituting revenues for another segment	-	-
	Other costs	2.263	3.233
	Total	2.263	3.233
	Fixed costs attributable to segment	144	215
	Variable costs attributable to segment	2.119	3.018
Operating profit attributable to equity holders of the parent		35	39
Share in operating profit attributable to minority interests		-	-
Total assets attributable to segment		1.159	1.213
Total liabilities attributable to segment		1.033	1.080

⁴⁴ Includes the results of marketing operations in France starting October 1, 2010.

- B. Below are data regarding marketing operations in France in 2010 and 2011, presented by acquisition date (in EUR millions):

	Post-acquisition (Delek France's results)		Pre-acquisition (BP's results)
	2011	Q4/2010	Nine months ended Sept. 30, 2010
Revenues	992	218	602
Cost of revenues	860	184	526
Gross profit	132	34	13
Operating profit	11	3	602
Net profit ⁴⁵	2	0.4	
Assets ⁴⁶	385	350	
Liabilities ³	317	284	

1.9.3 Dividends and restrictions on the distribution thereof

Delek Europe has not distributed dividends in the past two years. For information concerning limitations on dividend distributions pursuant to financing agreements signed by Delek Europe, see Section 1.9.23 below.

1.9.4 Structure of the operating segment and changes therein

As aforesaid, fuel operations in Europe are comprised of marketing operations in Benelux and marketing operations in France.

A. Marketing Operations in Benelux

As of December 31, 2011, marketing operations in Benelux include 826 gas stations, of which 547 are in the Netherlands, 265 in Belgium, and 14 in Luxembourg. Furthermore, operations include 588 convenience stores, 231 bakeries, 181 carwash facilities, 7 motorway restaurants and a hotel. In 2012, two motorway restaurants will be added to the chain in Belgium.

B. Marketing Operations in France

As of December 31, 2011, marketing operations in France consist of 401 gas stations. Delek France's gas stations are located mainly in the north of France (including Paris - 224 stations) which account for 55% of Delek France's total fuel sales; and in southern France (from Lyon to the Mediterranean and Corsica - 122 stations), which account for 30% of all fuel sold by Delek France. 55 stations are located alongside motorways, and these stations account for 12% of all motorway gas stations in France. To the best of the Company's knowledge, Delek France is the second largest fuel supplier (19% market share) in northern France (including the Greater Paris Area), and holds the third largest market share (11%) in southern France.

Furthermore, marketing operations in France include 356 convenience stores, 235 carwash facilities and holdings of between 21.5%, 50%, and 100% in three terminals for the supply and storage of fuels used in the operations, which account for 40% of all fuel sold by Delek France.

For more information concerning Delek Europe's marketing products in Benelux and France as of December 31, 2010, see Section 1.9.12 below.

C. Marketing operations in Europe are carried out under several formats:

1. Gas stations owned or leased for the long term as well as operated by Delek Benelux or Delek France (Company-Owned-Company-Operated - COCO).
2. Gas stations owned or leased for the long by Delek Benelux or Delek France, and operated by third parties (Company-Owned Retailer-Operated - CORO. In France these stations were previously called - Company-Owned Dealer-Operated - CODO).

⁴⁵ Net profit includes finance expenses on shareholder loans amounting to EUR 30 million, provided for the transaction. Other finance expenses (EUR 65 million) are included under Delek Europe B.V.'s expenses.

⁴⁶ Asset and liability data are as of December 31, 2010, and 2011.

3. Gas stations owned or leased for the long term by Delek Benelux or Delek France, and operate by franchisees (Company-Owned Franchise-Operated - COFO; in Benelux, these stations were previously called - Company-Owned Retailer-Operated +, or CORO+).⁴⁷
4. Gas stations owned or leased and operated by third parties, who buy fuel exclusively from Delek Benelux or Delek France (Retailer-Owned Retailer-Operated - RORO; in France these stations were previously called - Dealer-Owned Dealer-Operated - DODO).
5. In the Netherlands only - holdings of 40% in a joint venture company operating independently in the marketing (to both the retail and wholesale markets) of fuels (Equity Distributors).
6. In Benelux only - Authorized Distributors - supply of fuel by Delek Benelux to 16 gas stations in Belgium and 29 gas stations in the Netherlands, who independently sell fuel to SMEs, households, and service stations.

1.9.5 Restrictions, legislation, standardization, and special constraints

Delek Benelux and Delek France's operations are subject to various regulatory restrictions and requirements, including environmental protection requirements, labor laws, regulations for the sale of alcohol and tobacco products, public access roads, and other legislation. For more information, see Sections 1.9.25 and 1.9.26 below.

1.9.6 Changes in the operating segment's scope and profitability

A. Economic conditions in Benelux and France

Belgium has one of the most developed economies in Europe. Its geographic location along the North Sea enables Belgium to rely mainly on international trade, with 70% of the country's GDP being generated through such trade. Antwerp is the second largest seaport in Europe, and is a key destination in the global fuel market. Belgium has a population of 11 million residents, and is ranked 16 in the world in GDP per capita. In 2011, the Belgian economy emerged from the global financial crisis and grew by 1.9%. According to forecasts by the Central European Bank, the Belgian economy is expected to remain stable in 2012 (0.8% growth).

The Netherlands is considered one of the strongest economies in Europe. Rotterdam is the largest seaport in Europe, and together with Amsterdam and Antwerp constitute Europe's gateway to the global fuel market (ARA - Amsterdam, Rotterdam, Antwerp). The Netherlands has a population of 16.7 million residents, and is ranked 9th in the world in GDP per capita. Unemployment in the Netherlands is among the lowest in the world, and in 2011, the Dutch economy grew by 1.4%. According to forecasts by the Central European Bank, the Netherlands' economy is expected to remain stable in 2012 (0.3% growth).

Luxembourg is one of the smallest countries in the world, with a population of just 0.5 million residents. However, Luxembourg is considered one of the best economies in the world, and is ranked first in GDP per capita. Fuel taxes in Luxembourg are low compared to other countries in Europe, and so the country is host to what has been termed "fuel tourism", with residents of neighboring countries and truck fleets crossing the continent passing through Luxembourg in order to benefit from the lower fuel prices. Considering the elevated fuel prices in the past year, this trend increased in 2011. In 2011, Luxembourg's economy grew by 1.1%, and according to forecasts by the Central European Bank is expected to remain stable in 2012 (0.3% growth).

Benelux is considered as having a high percentage of motor vehicles per capita.

France is the second largest economy in Europe, and accounts for 14% of the European Union's gross national product. Its population accounts for 13% of the European Union's population. Despite the economic crisis experienced by the European Union, France remained a healthy economy and is expected to continue growing in the coming years. France is one of the most important tourist destinations in the world, situated in a key geographic location in

⁴⁷ Under this method of station operation, Delek Europe provides full support for the supply, marketing and trade of fuel and convenience store products, so as to allow retailers and franchisers to focus on station operation and improving customer service and sales turnover.

Europe. Furthermore, France houses approximately 19% of Europe's roads, with 11,000 km of highways.

Annual gasoline and diesel consumption in France in 2011 was 50.7 billion liters, up 0.2% from 2010.

B. The gas station market in Benelux

1. The gas station and convenience store market in Benelux is relatively stable and centralized. Each of the Benelux countries has 5-6 key players, including Delek Benelux. To the best of Delek Benelux's management's knowledge, fuel consumption in Benelux went down 3% in 2009 compared to 2008, after a modest growth trend in recent years. This decrease is due mainly to the global economic crisis, which is primarily impacting the overland freight industry, which is an extremely significant component in fuel consumption in Benelux. In recent years, demand for diesel has gone up, while demand for gasoline has diminished, as the number of gasoline-powered vehicles is decreasing. This trend stopped in 2009, and in 2010 and 2011 demand for diesel leveled out. It is not possible for Delek Benelux to assess the duration and/or extent of this trend, but it may continue and adversely affect the results of Delek Benelux's operations, and may expand and affect convenience store operations as well.
2. The gross margin per liter of fuel sold in Benelux has remained relatively stable in recent years due to the structure of the market and the competition.
3. To the best of Delek Europe's knowledge, and based on research data from such companies as Wood Mackenzie and Nielsen, the convenience store market in Benelux has grown in recent years by an annual rate of between 4% and 5%. Among other reasons, this is due to changes made in the late nineties which eased restrictions on store opening hours, and due to liberal regulatory policies concerning the products allowed for sale. However, in 2010 and 2011, due to the global economic crisis, the market experienced a general slowdown.

C. The gas station market in France

The gas station and convenience store market in France is extremely competitive. In France, there are numerous competitors, notably the hypermarket chains which hold a market share of 57% - 59%, followed by the leading French company Total which holds a market share of 20%. The remaining portion of the market is mainly split among Esso; BP; the growing AVIA brand (which acquired Shell's off-motorway gas stations); and smaller, branded and non-branded companies. To the best of Delek France's knowledge, fuel consumption was down in 2008 as compared to previous years, mainly due to rising fuel prices since mid-2008 and the global economic crisis, which mainly affected the land transport industry which constitutes an extremely significant factor in fuel consumption in France. From 2009 and until the reporting date, no material changes have occurred in the annual fuel consumption in France, despite changes in the distribution of fuel consumption across customer categories. In 2011, elevated fuel prices and the general economic slowdown increased customer migration to gas stations offering discounted fuel prices, a development which primarily hurt motorway station operations. In recent years, there has been a continuing increase in diesel consumption, as compared to a decrease in gasoline consumption (in 2011, for example, diesel consumption grew by 1.5% while gasoline consumption decreased by 5.0%). This change is driven by a lack of substitute products, incentives promoting the use of diesel-powered cars over gasoline-powered cars (such as the incentive plan for cutting CO2 emissions), and regulation. In 2009, 2010, and 2011, fuel sales were distributed between diesel (76%, 77%, 78.5%, respectively) and gasoline (24%, 23%, and 21.5%, respectively).

D. Fuel prices and consumption and the effects thereof on Delek Europe's retail margin:

Fuel prices in Benelux and France are materially influenced by crude oil prices, which are subject to significant fluctuations on the global markets. Fuel consumption depends on various factors such as economic growth rates, population growth, taxation policies, growth in the number of vehicles, and the use made of those vehicles.

Retail margins in Europe have gradually increased since 2004. Retail margins are influenced by the following factors: (1) market competition - in Western European countries, where competition in the fuel market is high, retail margins have gone down compared to less competitive fuel markets in Europe; (2) changes in the number of self-service stations - an increase in the percentage of unmanned gas stations offering customers discounts of up to 12 euro-cents adversely affects retail margins on fuel sales; (3) the location of gas stations

alongside motorways enables higher retail margins and fuel sales turnover that is three times greater than that of non-motorway gas stations; (4) the competitiveness of the French market and the various competitors' reluctance to start a "price war" in recent years has led to an increase in retail margins. In competitive European countries, convenience store sales have become an important part of the fuel market. Furthermore, regulatory changes have accelerated the closing of less-profitable gas stations. Retail margins are extremely sensitive, in the short term, to changes in fuel prices.

1.9.7 Developments in the operating segment or changes in its customer profiles

- A. Netherlands: Following the global economic crisis which began in the second half of 2008, overall demand for fuel went down 3% in 2009 as compared to 2008, with the majority of this decrease being attributable to a decrease in diesel consumption. 2011 saw a continued stabilization in demand for fuel, a trend which began in 2010. Due to elevated fuel prices and the weak economy, consumers tended to refuel in unmanned stations and discount gas station chains.
- B. Belgium: Belgium serves as a passageway for goods to and from the ports of Rotterdam and Antwerp. Following the global economic crisis at the end of 2008, the growing demand for fuel, which characterized this market in earlier years, leveled off, and 2010 and 2011 saw a decrease in demand for fuel. Concurrently, higher fuel excises in Belgium drove fuel prices up above the prices in neighboring countries, which led consumers to refuel outside of Belgium and drove customers from more expensive motorway stations to discount gas station chains. In light of the aforesaid, the Belgian fuel market has seen a significant increase in the number of unmanned automatic self-service stations.
- C. Luxembourg: The fuel market in Luxembourg is characterized by high demand, mainly due to the low fuel tax as compared to neighboring countries (which leads to customers from other countries buying fuel in Luxembourg - "fuel tourism"), and due to Luxembourg's geographic location. Between the fourth quarter of 2008 and 2010, demand for fuels in general and for diesel in particular dropped significantly in Luxembourg, due to decreased motorway truck traffic. 2010 saw a recovery in demand, which drove diesel consumption up by 2.5%. This trend continued in 2011.
- D. France: Developments in the French market are affected mainly by three key trends:
 1. Entry of hypermarket chains into the fuel market - Between the 1980s and the early 2000s, the market share held by hypermarket chains grew consistently, and reached a record high of 55% of the entire fuel market in France in 2001. In recent years, the hypermarket chains' market share has stabilized at around 57%-59%. Hypermarkets offer fuels at significantly lower prices than those offered by the fuel companies, as they use fuel as a means of attracting customers to their stores (loss leader). The hypermarkets' share in the motorway segment is expected to decrease in the next few years in light of public statements made by the hypermarket chains that the significant capital and operating expenses involved in upgrading motorway gas stations do not coincide with the hypermarket chains' business model. These expenses are liable to damage their image as offering affordable prices. For example, as of the reporting date, two hypermarket chains operating in the motorway segment have not competed in tenders for new gas station franchises. Delek France estimates that the hypermarkets' share in the motorway segment may plummet to negligible percentages by 2020. This information concerning Delek France's expectations for a decrease in the hypermarkets' share in the motorway segment constitutes forward-looking information based on Delek France's assessments. However, such forward-looking information may fail to materialize, inter alia, due to decisions and changes in the hypermarket chains' policies, entry of new players into the market, changes in the operating results of fuel companies and hypermarket chains, consumer behavior, and more.
 2. Increase in non-branded and unmanned stations - Recent years have seen an increase in the number of unmanned stations, which allow fuel companies to offer more competitive, flexible and discounted prices. This trend was driven mainly by Esso's operation of more than 330 locations operating under the Esso Express brand in France, and by Total's initiative of offering discounted prices, rolled out in 600 gas stations. Furthermore, the trend of private entities opening non-branded stations has increased in France. These trends, which coincide with the increased consumption of discounted fuel, drives down demand in motorway stations and other manned gas stations.

3. Increase in motorway stations - As aforesaid, retail margins in motorway gas stations are higher than those in urban gas stations. Furthermore, fuel consumption in these stations is greater than that recorded in inner-city stations, and their convenience store and restaurant revenues are relatively higher. In 2011, the motorway gas station segment suffered from low vehicle throughput (both local and international), caused by the unfavorable economy and high fuel prices. However, massive investments, which dramatically improved station visibility and appeal along motorways, and a tax reform aimed to divert truck traffic to motorways which will come into effect in 2013, may facilitate growth in the motorway segment in coming years. This information, concerning Delek France's assessment for the motorway gas station market, constitutes forward-looking information base on Delek France's assessments. However, such forward-looking information may fail to materialize, inter alia, due to developments in consumer preferences and behavior, changes in tax policies, etc.

1.9.8 Critical success factors in the operating segment and changes therein

Delek Benelux and Delek France believe the critical success factors in the operating segment to be as follows:

- A. Widespread deployment and attractive location of gas stations - Transition of more profitable gas stations to ownership or long-term leasing and operation by Delek Benelux or Delek France (COCO), according to their location.
- B. Focusing solely on downstream operations (not involving refineries) enables the Company to optimize fuel prices from its various suppliers.
- C. Matching the gas station operation model to their potential and minimizing holdings in less profitable stations.
- D. Financial stability enabling, inter alia, investment in setting up new Company-owned stations and in renovating and expanding existing stations.
- E. Advanced retail strategy management, including investment in developing the convenience store chain so as to offer customers a value proposition (service/quality versus price).
- F. Advanced information technology and decision-support systems; establishing support for critical business processes.
- G. Ownership rights in the land on which the gas stations are built.
- H. Contracting terms with station operators.
- I. Development of fuel card programs.
- J. Availability of fuel and other products and storage capacity.
- K. Advanced marketing and logistics systems.
- L. Chains operating under international brands that are well-recognized in Benelux (Texaco) and France (BP).
- M. Economic conditions, which affect, inter alia, fuel consumption and convenience store turnover, as well as the price of the products on offer.
- N. Market penetration of premium fuel products, in order to increase retail margins.

1.9.9 Changes in suppliers and raw materials

A. Fuel product suppliers

In the Netherlands and Belgium, there is a relatively large number of refineries centered around Rotterdam and Antwerp that are able to supply fuel products, resulting in fuel supply exceeding local demand. Therefore, local refineries export to other countries in the European Union (mainly to Germany) and North America. Following a period of surplus production capacity, the market saw significant adjustment processes in 2011.

In the Netherlands, most fuel products are purchased by Delek Benelux from the large fuel companies (Shell, BP, Esso, Total, etc.), and from trading companies. Part of the annual volume is purchased through barter agreements and swap transactions. There are also storage and trading contracts with international companies such as Vitol, and North Sea Holdings. Most of the fuel in Belgium is supplied from the Total refinery and its distribution facilities. In Luxembourg, most fuel products are supplied from a terminal in Belgium, jointly

owned by Delek Benelux and Q8, which stores fuels from refineries in Antwerp and Flushing, and which also distributes fuels to eastern Belgium. Secondary supply, from the terminal or depot to the gas stations, is carried out mainly by road tankers operated by a third party transportation company.

In France, fuel products are bought from refineries centered in the north-west and south of France, as well as from imports. Delek France has signed an agreement for fuel supply and storage services with BP. Fuels are supplied via pipelines, barges and trucks, and stored in a number of terminals throughout France. Starting 2012, 65% of the fuel marketed by Delek France is stored in three terminals in which Delek France maintains ownership interest (for details concerning these terminals, see Section 1.9.18(d) below). The remaining fuel is stored in terminals owned by BP and third parties. Fuels are transported from the terminals via road tankers to the various gas stations according to agreements signed with three leading logistics service providers. As part of the agreement for acquiring the marketing operations in France, a supply agreement was signed by Delek Europe and BP, for the supply of fuels to Delek France-owned terminals, until the end of 2011, and another agreement was signed for the supply of fuels from various terminals not owned by Delek France, for a period running through the end of 2013. These agreements include an optional extension clause. In the reporting period, Delek France has contracted with Total for the supply of a significant portion of its fuel requirements in 2012. Furthermore, Delek France has contracted three leading companies for supplying road tanker transportation for fuels distributed by Delek France from the terminals to the gas stations.

As, fuel prices are stated in USD, the EUR-USD exchange rate may affect Delek Europe's buying prices. For more information concerning supply agreements, see Section 1.9.21 below.

B. Convenience store suppliers

In Benelux and France, there is a large selection of convenience store suppliers, and Delek Benelux and Delek France have contracted various suppliers for the supply of tobacco products, light beverages, and alcohol.

In France, convenience store operations are affected by two main factors: a) geographic location, which affects logistics and supply costs; b) ties with retail chains, which supply most of the products sold in the convenience stores.

In France, the 16-year long cooperation continues with French retail giant Carrefour (the second largest distributor in the world), which distributes a large portion of the products to gas stations throughout the country. This cooperation is based on a number of agreements, which include a global agreement, a store brand license agreement, a brand license, and a supply agreement. These agreements were signed for various periods (between 5 years and an indefinite period), and include various exclusivity clauses (in some of the agreements exclusivity is mutual; in others, exclusivity applies to Delek France only; and in others no exclusivity is applied to Delek France). Under these agreements, Delek France pays Carrefour various amounts.

1.9.10 Entry and exit barriers

The following material entry barriers are typical of the Benelux and French markets:

- A. Size of current market players and country size - Market characteristics in France and Benelux make it difficult for new competitors to enter the market other than through the acquisition of an existing player. This is due to the fact that the various Benelux markets have few companies, each with a market share in excess of 10%, while France is a vast country saturated with gas stations.
- B. Material investments requiring considerable capital - Investment in gas stations requires considerable capital, for various reasons, including the price of land (due, inter alia, to limited availability of suitable free land) and the cost of acquiring or constructing gas stations.
- C. Environmental protection and planning regulation - Strict standards set by environmental protection and planning authorities limit market entry, or increase entry costs.
- D. Limited availability of suitable free land for the operating segment (mainly along motorways) in Benelux and France - Leads to higher land prices and deters the entry of competitors interested in expanding gas station complexes into major commercial areas (retail chains).
- E. Furthermore, the Netherlands, Belgium and France require a tender process for operating gas stations on motorway sites, which increases prices at such locations to levels only affordable

to major players, and requiring complex planning capabilities and collaboration with restaurant chains.

The major exit barriers are the existence of rent/lease/operating contracts with land/station owners.

1.9.11 Structure of competition in the market

A. General

Recent years have been characterized by increased departure of the major international oil companies from the gas station segment. This is mainly due to the following factors: high oil prices lead to higher returns on investments; oil exploration and production have become more complicated, requiring the allocation of more resources; competition-increasing regulation is changing the traditional market shares and requiring CAPEX investments, which are needed in exploration and production operations; the gas station market has expanded to include convenience stores, fresh food, and retail products, which are “distant” for oil companies; oil is a commodity and no gas station holdings are required to sell it.

In light of this trend, Delek Benelux acquired Chevron's operations, which include gas stations operated under the Texaco brand, and Delek France acquired BP's operations.

Delek Europe aims to continue exploiting this trend in light of the following characteristics: its growth strategy; infrastructure supporting expansion of the gas station chain; financial resources supporting acquisitions; flexible and dynamic operating models; local management; ability to act on opportunities, and fast response times to changes in the market and in customer needs.

B. Structure of competition in Benelux

The fuel market in Benelux is relatively concentrated, with five or six major fuel companies holding 80% to 90% of the market.

According to Wood Mckenzie data, the six largest fuel marketing companies in the Netherlands comprise 80% of the market. The three companies with the largest market share are Shell, BP, and Delek Benelux (Texaco). The six largest fuel marketing companies in Belgium comprise 80% of the market. The three companies with the largest market share in Belgium are Total, Q8, and Shell. Delek Benelux (Texaco) holds the fifth largest market share in Belgium. The six largest fuel marketing companies in Luxembourg comprise 90% of the market. The company with the largest market share is BP, followed by Shell, Exxon and Total with similar market shares. Delek Benelux (Texaco) holds the sixth largest market share in Luxembourg.

Competition is focuses on gaining an advantage in the deployment of gas stations, gas station branding so as to attract customers, and expansion of additional on-site services (convenience stores, carwash services, restaurants, etc.), and fuel prices.

C. Structure of competition in France

Competition in the fuel market in France is extremely fierce, due to the presence of a large number of competitors and the large number of gas stations in the country. The market is primarily comprised of gas stations situated within retail chain complexes and operated by these chains. The retail chains hold between 57% and 59% of the fuel market in France. The market is further comprised of five major international fuel companies (Total; Esso; BP, whose operations were acquired by Delek France as aforesaid; Shell; and Agip), which together hold a share of approximately 32% of the French fuel market. Of the international fuel companies, Total holds the greatest market share (20%) and also holds the largest number of gas stations (approximately 2,300 Total-branded stations). Delek France's BP-branded gas stations have a market share of 3.3%. The stiff competition in the fuel market is reflected in price competition, in differentiation between the various companies (each as per its own strategy), in the deployment of gas stations, in the branding of gas stations so as to attract customers, and in the expansion of additional on-site services in gas stations (such as convenience stores and carwash services).

Delek France handles the competitiveness of the fuel market on four levels:

1. Focusing on high fuel consumption areas - Delek France seeks to establish and develop gas stations in the greater Paris area, characterized by greater population density, high levels of vehicle traffic by vacationers and commuters, and higher real estate prices which serve as barriers to entry. Delek France also focuses on establishing and

developing motorway gas stations throughout France, which are characterized by increased vehicle throughput, and lighter competition as compared to inner-city areas.

2. Differentiation and USP - Delek France markets both its fuel products and its convenience store products as premium products, which the Company believes offer a higher quality relative the market, and benefits from long-term commercial ties with well-known food chains (Autogrill and Elior), and with French retail giant Carrefour, and an extremely unique and attractive carwash offering;
3. Pricing - Prices on regular (non-premium) fuels in Delek France's gas stations are on par with local competition for the station. BP's premium products are competitively priced as compared to Total, the market leader in France.
4. Establishing a loyal customer base - Delek France has established a loyal base of commercial clients by marketing its "Go the easy way" fuel cards (which replaced previous cards), and by marketing its Carte Bienvenue loyalty cards to private customers, offering benefits based on customer loyalty.
5. Improvements to convenience stores, mainly by expanding food and baked goods offerings.

1.9.12 Products and services

A. Fuel and oil products

Diesel - Mainly for diesel-powered vehicles, as well as for heating and industrial use. Marketed both at gas stations and to industrial customers through joint ventures and independent distributors. Diesel sales accounted for 75% of Delek Benelux's total fuel sales, and 70% of Delek France's total fuel sales in 2011.

Various types of gasoline - For gasoline-powered vehicles and marketed mainly at gas stations. In 2011, gasoline sales accounted for 25% of Delek Benelux's total fuel sales, and 30% of Delek France's total fuel sales.

Premium fuels - The main objectives in marketing premium fuel products is to supply an innovative product which meets current customer expectations, and penetrate the premium fuel market which offers greater profitability. In 2007, Delek Benelux began marketing a premium fuel product under the XL brand in the Netherlands. In France, Delek France markets premium fuel products (diesel and gasoline) under the Ultimate brand.

B. Convenience store products

Convenience stores in Benelux - Delek Benelux sells various retail products in its convenience stores, including food products (sandwiches, baked goods, snacks, etc.), various beverages, cigarettes, car maintenance products, hygiene products, and other products. As of the reporting date, there are 588 branded convenience stores in the chain.

As part of its strategic plan, Delek Benelux decided to develop a new concept for the operation of its convenience stores, in order to increase its revenues and profit margin, enhancing their visual appeal, while emphasizing freshness and convenience on the road. In its stores, Delek Benelux offers a range of products suited to customer needs. The new concept has been given a private-label name - GO the fresh way. As of the end of 2011, this private label has been deployed in 200 convenience stores. In 2012, a similar roll-out began in France.

It is noted, that the transition to the own-label brand has resulted in increased profits and an expanded product offering, including Segafredo - Delek Benelux's coffee brand. As part of its current budget for the next few years, Delek Benelux plans to convert convenience stores to the house brand across all gas station operating formats, including distributors and franchisees. As of the date of this report, the various aspects of the convenience store chain are managed by Delek Benelux's in-house staff, who are working to refresh the customer experience and improve overall service.

Convenience stores in France - In its convenience stores, Delek France sells various retail products such as food products (sandwiches, baked goods, snacks, etc.), various beverages, cigarettes (only in motorway locations), car maintenance products, basic hygiene products, and other products. As of the second half of 2009, the sale of alcohol in gas stations is prohibited in France between 6pm and 8 am. It is noted that alcoholic beverage sales can

account for up to 50% of non-fuel sales in gas stations.⁴⁸ As of the reporting date, the chain includes 356 convenience stores, of which 54 are Proxi-branded stores (mainly in COCO and COFO motorway locations), and 47 are 8 a Huit-branded stores (mainly in COFO urban locations). A new brand, 8 a Huit Express, was launched in 2011 in two motorway stations, and will be expanded to additional motorway locations to be opened following Delek France's successful bids in the tendering process. The use of these two brands is the result of a 16-year strategic collaboration with French retail giant Carrefour. Delek France receives fixed rentals as well as part of the convenience store's revenues, and in return for using the brand name, Delek France buys the majority of the products from Carrefour and also pays usage fees for the brand.

C. Rental of commercial space and carwash facilities

As of the reporting date, Delek France provides carwash services in its gas stations, through a chain of 235 carwash facilities. Delek Benelux's gas stations include 181 carwash facilities. Delek France intends to continue expanding and developing these operations.

D. Bakeries

Marketing operations in Benelux include a chain of in-store bakeries operating under the "store within a store" concept. As of the reporting date, the chain includes 231 bakeries. As of the last quarter of 2009, bakeries operate under a format developed for the new house-brand convenience store concept - "GO the fresh way". The chain sells fresh fast food such as baked goods and salads, which are often prepared on-site.

In Delek France - food services are provided in several inter-city and express stations, in collaboration with the Columbo's Cafe franchisee or other restaurant companies, or in a non-branded format.

E. Restaurants and hotel

As of 2010, Delek Benelux operates seven restaurants and a hotel in motorway service areas in Belgium.

F. Terminals

Delek France maintains holdings in three terminals storing 45% of all fuel marketed by Delek France. For more information concerning these terminals, see Section 1.9.18(d) below.

Delek Benelux holds 50% of the Wandre terminal in Belgium and the Holerich terminal in Luxembourg. In 2011, Delek Benelux looked into a terminal in Kampen, in the Netherlands, which has been operating since October 2011.

⁴⁸ In practice, sales of alcoholic beverages account for 1% of non-fuel sales in motorway service areas, between 15% and 20% in 8aHuit, and 30% to 35% in COFO locations.

G. The following table details Delek Europe's products and services by country and site type:

Country	Site type	Gas stations	Convenience stores	Carwash facilities	Terminals ⁴⁹	Bakeries	Restaurants	Hotels
Belgium	COCO	37	37	4	1	31	7	1
	CORO/RORO	228	195	26		58	-	-
Netherlands	COCO	250	117	45	1	97	-	-
	COFO/RORO	179	144	66		48	-	-
	Partnerships and dealers	118	76	41		4	-	-
Luxembourg	COCO	12	12	1	1	12	-	-
	CORO/RORO	2	2	-		1	-	-
France	COCO	32	32	3	3	25	2	-
	COFO	77	77	49		-	-	-
	CORO	183	173	154		-	-	-
	RORO	109	74	29		-	-	-
Total		1,227	939	418	6	276	9	1

In COCO sites, Delek Benelux and Delek France bear the full costs of operating the gas stations and receive all profits therefrom. In CORO sites, gas stations are operated by third parties, and Delek Benelux and Delek France are entitled to payment in accordance with a rental agreement signed with these third parties for use of the site's facilities. Such payment is based on a fixed component and a variable component deriving in some cases from the sales turnover on the premises, excluding convenience store sales. In COFO sites, gas stations are operated by a franchise and Delek Benelux and Delek France are entitled to payment according to a rental agreement signed with the third party for use of the site's facilities. Such payment is based on a fixed component and a variable component deriving in some cases from the sales turnover on the premises, with Delek Benelux and Delek France additionally being entitled to payment deriving from the convenience store turnover. In RORO sites, gas stations are operated by third parties, and Delek Benelux and Delek France receive revenues from the sale of fuel to these stations. Furthermore, marketing operations in France also includes revenues on the retail sale of carwash cards.

⁴⁹ Various holdings by Delek Benelux and Delek France, and separate from gas station operations.

1.9.13 Segmentation of revenues and profitability from products and services

Below are the amounts and percentage of revenues from the sale of products and services in the operating segment in 2010 and 2011:

		2010			2011		
		EUR millions	% of segment revenues	% of Group revenues	EUR millions	% of segment revenues	% of Group revenues
Benelux	Fuel	1,807	78.7%	15.8%	1,970	60.2%	11.9%
	Convenience store and other operations ⁵⁰	272	11.9%	2.4%	310	9.5%	1.9%
	Other	-	-	-	2	0.1%	0%
	Total Benelux	2,080	90.5%	28.2%	2,280	69.7%	13.8%
France	Fuel	203	8.8%	1.8%	931	28.5%	5.6%
	Convenience store and other operations ⁵¹	14	0.6%	0.1%	61	1.9%	0.4%
	Other	0.4	0.0%	0.0%	-	-	-
	Total France	218	9.5%	1.9%	992	30.3%	6.0%
Segment total		2,298	100%	30.1%	3,272	100%	19.8%

Below are the amounts and gross margins from the sale of products and services in the operating segment in 2010 and 2011:

		2010			2011		
		EUR millions	% of revenues	% of Group revenues	EUR millions	% of revenues	% of Group revenues
Benelux	Fuel	170.8	7.4%	1.5%	170.4	5.2%	1%
	Convenience store and other operations ⁵⁰	75.6	3.3%	0.7%	85.6	2.6%	0.5%
	Other	-	-10.7%	0%	-	-	-
	Total Benelux	246.4	11.8%	2.2%	256.0	7.8%	1.5%
France	Fuel	21.8	10.7%	0.2%	84.1	2.6%	0.5%
	Convenience store and other operations ⁵¹	12.0	83.6%	0.1%	47.6	1.5%	0.3%
	Other	-	-	-	-	-	-
	Total France	33.8	15.5%	0.3%	131.7	4.1%	0.8%
Segment total		280.2	12.2%	21%	387.7	11.9%	2.3%

In 2011, Delek Benelux recorded an increase in gross profits, mainly due to improved retail margins, which offset the quantitative decrease in sales, and an increase in convenience store turnover in COCO gas stations. The latter was due to the implementation of the company-operation strategy, particularly in motorway locations, upgrades made to convenience stores, and implementation of the own-label brand.

It is noted that there are considerable differences in sales across gas stations, influenced by the stations' location, and operating format. It is further noted that the Capellen station in Luxembourg, one of Delek Benelux's COCO stations, boasts one of the largest sales volumes in Europe and is responsible for the majority of fuels sold by Delek Benelux in Luxembourg.

⁵⁰ Including carwash facilities, bakeries, restaurants, and hotels.

⁵¹ Including carwash facilities and terminals.

1.9.14 Customers

Customers in the fuel products in Europe segment are divided into several major groups:

Private customers: Private customers who buy fuel in Delek Benelux and Delek France COCO stations pay the stated price for fuel products at each station. In addition, private customers also purchase complementary products, food, or other products in the convenience stores, as well as food in the Go Bakery outlets in Benelux. Customers also use the carwash facilities offered in some of the gas station complexes. Payment is usually made in cash or by credit card. In Delek Europe-operated gas stations, prices on the sale of fuel products to end customers are determined by Delek Europe.

Customers who are station operators: CORO, COFO, and RORO station operators, whose contractual terms are anchored in separate agreements signed with each operator, and where payment is made by bank transfer to Delek Benelux or Delek France's account with an average of 7 days' credit.

Fuel card customers: Delek Benelux and Delek France work with commercial customers through two models;

1. Agreements with specialist companies that issue fuel cards and market them to international transportation companies and vehicle fleets.
2. Issuing fuel cards directly to commercial customers: vehicle and truck fleets. In January 2012, Delek Benelux launched a fuel card program targeting companies operating D-fleets, which consume large amounts of fuel and enjoy a significant discount. Furthermore, Delek France launched another fuel card program which is also usable in Benelux. This card is issued to companies and businesses who sign agreements with Delek France for purchasing fuel using this card. Fuel card sales account for 40% of all retail sales in gas stations in Benelux, and 20% of all sales in gas stations in France.

Additional customers in Benelux:

- Joint venture: The joint venture in which Delek Benelux holds 40% is another type of customer, that purchases fuel from Delek Benelux. This customer enjoys an average of 8 days' credit.
- Industrial and commercial customers / authorized dealers: Delek Benelux provides fuel to customers from industrial and commercial sectors, not through the gas stations, subject to contracts signed with these customers. These customers are granted an average credit of 40 days.

1.9.15 Marketing and distribution

Marketing channels employed in Europe are as follows:

- A. Marketing in gas stations - Delek Europe promotes its products and services by various means: sales in operating regions, local sales in specific stations, and use of promotions. Furthermore, advertising campaigns are occasionally conducted using various media.
- B. Agreements to purchase brand fuels - Fuel products sold in gas stations are marketed under the Texaco brand in Benelux and under the BP brand in France. Premium fuel products are marketed under the XL brand in Benelux and under the Ultimate BP brand in France. For more information, see Section 1.9.19 below. In Q4/2011, collaboration agreements were signed with another gas station chain with a strong presence in the truck refueling market. The Company seeks additional collaborations in Delek Benelux and Delek France's geographies.
- C. Additional marketing and distribution channels in France
 1. Loyalty cards - Delek France operates a loyalty card program called Carte Bienvenue. The card rewards customer loyalty by accumulating points, which can then be used to buy discounted products in the gas stations (mainly in convenience stores). The card has been issued to approximately 2 million customers, who carry out approximately 30 million transactions each year using the card. As of the reporting date, there are approximately 1.2 million active cards (i.e. - used in the last three months). The loyalty card also serves as a platform for promoting special sales.
 2. Convenience store branding agreements - Delek France has a long-standing collaboration with French retail giant Carrefour, whereby Delek France uses the Proxi and 8 a Huit brands in some of its convenience stores. All other convenience stores operate under the BP brand.

3. Collaboration agreement for the issue of international fuel cards - Delek Franc has signed a collaboration agreement with Routex, whereby customers using Routex cards can buy fuel in Delek France gas stations.
4. In November 2011, Delek France launched a new fuel card entitled "Go the easy way", and migrated Routex and BP plus card customers to this new card. Delek France also signed an agreement with AGIP whereby the "Go the easy way" card is also accepted in the AGIP chain.
5. Agreements for distributing fuels to gas stations - Delek France enters fuel distribution and branding agreements with RORO station owners. These agreements are valid for up to 5 years.
6. Consignment inventory in fuel sales - All Company-owned stations, and a third of distributor-owned stations, operate under this inventory model which enables greater control of operations, including end-customer pricing.

1.9.16 Backlog

Not applicable. Orders in the gas station segment are placed mainly by passing customers. Similarly, backlog does not apply to Delek Europe's terminal operations.

1.9.17 Seasonality

In general, the fuel products in Europe segment is not affected by any significant seasonality, although adverse winter weather and shorter daylight hours are liable to affect turnover in winter. Furthermore, the first and final quarters of the year are usually characterized by slower sales of fuel and convenience store products.

In France, motorway service areas are significantly affected by seasonality, with sales peaking in the summer months, on holidays, and on vacations. Most activity is seen by motorway stations, and not inner-city stations. Carwash operations are likewise affected by seasonality, with peak activity between April and September.

1.9.18 Property, plant and equipment and facilities

A. The following table details the breakdown of gas stations by type and Delek Benelux ownership rights as of December 31, 2011:

Country	Stations owned or leased and operated by Delek Benelux or Delek France (COCO)		Stations owned or leased by Delek Benelux or Delek France, operated by third parties or franchisees (COFO/CORO) ⁵²		Stations owned or leased by third parties, for which Delek Benelux or Delek France are an exclusive fuel supplier (RORO) ⁵³		Joint venture stations (ED)	Authorized distributor stations (AD)	Total stations
Netherlands	250		52		127		90	28	547
Belgium	37		123		82		--	23	265
Luxembourg	12		1		1		--	--	14
Total Benelux	299		176		210		90	51	826
France	32		260		109		-	-	401
Segment total	331		436		319		90	51	1,227
Holding status	Benelux	France	Benelux	France	Benelux	France	Benelux	Benelux	Benelux
Stations under ownership	49	-	57	99	--	--	--	--	--
Stations with remaining rental period of less than 3 years	63	12	9	107		--	--	--	--
Stations with remaining rental period of 3 to 10 years	145	16	90	48	--	--	--	--	--
Stations with remaining rental period of more than 10 years	42	4	11	15	--	--	--	--	--
Stations without ownership rights to which Delek Benelux and Delek France supply fuel	--	--	--	--	210	109	--	--	--

⁵² This group includes Delek Benelux's CORO+ stations, which are now termed COFO stations, and Delek France's CODO stations, which are now termed CORO stations.

⁵³ This group includes Delek France's DODO stations, which are now termed RORO stations.

COCO stations are owned or leased for the long term, and operated, by Delek Benelux or Delek France. The long-term leases of these stations average between 5 and 20 years, and their renewal dates are spread relatively evenly over the years. In these stations, Delek Benelux and Delek France own the inventory and equipment, and have direct control over pricing, supply, management, and maintenance. Therefore, Delek Benelux and Delek France receive all profits from these stations, as they serve as both owner and operator.

COFO stations (including former CORO+ stations) are owned or leased for the long term by Delek Benelux and Delek France, respectively, and operated by franchisees. The long-term leases on these stations average between 5 and 25 years, with renewal dates spread relatively evenly over the years. In these stations, Delek Benelux and Delek France own the equipment and in some cases the fuel inventory, and rent the stations to franchisees, who are responsible for the stations' operation. Delek Benelux and Delek France provide full support as regards sales, buying power, training, supply, marketing and merchandising, in return for franchise fees, and also receive the net profit from fuel sales less of the franchisee's commission, as well as a percentage of the on-site convenience store revenues. This method allows franchisees to focus on station operation and on improving service to customers, and on maximizing turnover.

CORO stations (including former CODO stations) are owned or leased for the long term by Delek Benelux and Delek France, respectively, and operated by third parties. The long term leases on these stations average between 5 and 25 years and are spread relatively evenly over the years. In these stations, Delek Benelux and Delek France own the equipment and in some cases the fuel inventory. Furthermore, in these stations, all fuel product marketing, retail and other operations are carried out by the third party operator. The operator signs a rental agreement with Delek Benelux or Delek France, as relevant, for its use of the site, and pays for the supply of products and for use of brand names. Delek Benelux and Delek France receive a percentage of the sales in the stores and facilities.

RORO stations (including former DODO stations) are owned or leased, as well as operated by third parties. In these stations, all fuel product marketing, retail, and other operations are carried out by the third party. Delek Benelux or Delek France, respectively, sign exclusive agreements with the stations for the supply of fuel, and are not entitled to rent or profits. Therefore, RORO stations are less profitable for Delek Benelux and Delek France. The aforesaid exclusive agreements are limited to a maximum term of five years, due to applicable antitrust laws. Therefore, a bidding process is generally held at the end of the period with potential suppliers (competitors). This process entails a possible loss of some of the stations or damage to profitability due to competition. On the other hand, there is a chance to win new stations from competitors. It is noted that re-branding costs upon transferring from one supplier to another constitute a significant exit barrier.

The joint venture in Benelux, in which Delek Benelux holds a 40% interest, is a company that operates independently in the fuel segment. Joint venture operations are not consolidated in the financial statements.

Authorized distributors in Benelux are mainly for supplying Delek Benelux fuel to 16 stations in Belgium and for the independent sale of fuel to SMEs, residential customers, and service stations. In the Netherlands, Van der Sluijs operates as a network of 25 complexes under the Texaco brand, for which it pays Delek Benelux licensing fees to use the brand in each complex.

- B. Delek Europe owns structures and equipment in most stations in which it has ownership rights. These structures and equipment form a part of Delek Europe's property, plant and equipment. In addition, Delek Europe owns equipment in all stations in which it has no ownership rights or in which it has short-term rental agreements. In some of these stations, Delek Benelux and Delek France have property, plant and equipment in station structures that were constructed many years ago, when the seller had ownership rights (including long-term lease/rental contracts) in those stations. This equipment includes tanks, pipes, pumps, computer and communications systems, office equipment, power supply systems and power generators if required, fire extinguishing systems and public restrooms.

It is noted, that in 2011 Delek Benelux made material investments of EUR 15 million in property, plant and equipment, primarily a planned investment in Delek Europe's new store concept, and another investment in a fuel card project. Other material investments include the acquisition of rights to operate stations along motorways in the Netherlands and Belgium, and the upgrading of on-site convenience stores. In 2011, Delek France invested EUR 6 million in

an enterprise resource planning (ERP) package, after acquisition of marketing operations in France, and made additional investments in motorway gas stations. In 2012, Delek Europe is expected to invest in regular maintenance of its gas stations, and in the upgrading of on-site facilities and convenience stores. Concurrently, material investments were made in motorway service areas in Belgium (EUR 20 million) and France (EUR 60 million). Delek Benelux invested EUR 9 million in the Kampen Depot in the Netherlands, and EUR 20 million in gas stations in Belgium.

- C. As of the reporting date, Delek Netherlands holds a 40% interest in a company (joint venture) operating independently in the retail and wholesale marketing of fuel (equity distributors), whose operations include 95 gas stations. The results of this joint venture's operations were not consolidated in Delek Netherlands's statements, and the contribution of its fuel sales is immaterial for the operating segment. However, Delek Benelux regards this venture as important, inter alia, as it expands Delek Benelux's Texaco brand presence, and provides an additional customer base for the fuel card program. It is noted, that until October 1, 2010, Delek Benelux maintained holdings in two additional joint ventures. At that date, Delek Benelux acquired the remaining interest in one of these joint ventures (POST), which then became a subsidiary of Delek Benelux, and sold its holdings in the other joint venture. In light of the above, starting October 1, 2010, POST's results are consolidated in Delek Benelux's financial statements.

D. Holdings in terminals -

Delek France maintains holdings in three terminals as detailed below:

1. The Vitry terminal in Paris, which is wholly-owned by Delek France. This terminal is located on an area of 37,000 square meters, owned/leased by Delek France, and operated by Delek France. The fuel stored in this terminal is supplied via a pipeline supplying fuel to the Paris region and northern France (Trapil pipeline), which is jointly owned by several companies, including BP. The Vitry terminal has a maximum capacity of 70 million liters.
2. The Lyon DPL terminal, located in Lyon and held by Delek France (50%) jointly with Carrefour (50%) through a private company incorporated in France ("DPL"). This terminal is operated by Delek France, and is located on an area of 26,700 square meters, leased by DPL from the Lyon port authorities (Compagnie Nationale du Rhone) until January 1, 2023. The fuel stored in this terminal is supplied via the pipeline supplying the southwest region of France (SPMR pipeline), which is jointly owned by several companies (including BP). The Lyon DPL terminal has a maximum capacity of 70 million liters.
3. The Bastia terminal includes two sites, located on Corsica, and is held by Delek France (21.5%) jointly with a number of other companies through a private company incorporated in France ("DPLC"). This terminal is located on land leased by DPLC from private entities. The terminal is operated by a local operating company specializing in terminal operation. The fuel stored in this terminal is supplied via ships by refineries in the FOS region. The terminal has a total maximum capacity of 33 million liters.

Delek Benelux maintains holdings in two terminals, as detailed below:

- A) The Wandre terminal - Delek Benelux and Q8 are joint holders (in equal parts) of a terminal located in Wandre, Belgium. This terminal almost exclusively serves the needs of Delek Benelux and Q8 in the Wandre port area. The terminal is located on an area of 13,500 square meters and has a maximum capacity of 18 million liters. The terminal is virtually the exclusive supplier of fuel in southern Belgium and Luxembourg.
- B) The Hollerich terminal - A terminal in Luxembourg, under full ownership of Delek Benelux. The terminal mostly serves to store Delek Benelux's compulsory obligation, as detailed in Section 1.9.26(a) below. The terminal has a maximum capacity of 17 million liters and is located on an area of 11,500 square meters.
- C) In 2011, Delek Benelux built a new terminal in Kempen, the Netherlands, which came online in October 2011. This terminal has a maximum capacity of 20 million liters, is located on an area of 2,500 square meters, and will serve Delek Benelux's operations.

1.9.19 Intangible assets

- A. The Texaco trademark - On August 8, 2007, Delek Benelux entered into a contract with companies of the Chevron Group (in this sub-section - "the License Holders") for obtaining a license to use the Texaco trademark and additional trademarks (primarily Start Market and Star Mart) in Benelux. The Texaco trademark with the star ("Texaco Star") is one of the best-known trademarks in the fuel industry, and has been in use in Benelux for many years. Pursuant to the contract, Delek Benelux was granted a non-exclusive license to use the trademarks in Benelux, with no royalty payments, for seven years commencing August 8, 2007. The contract includes guidelines on how to use the trademark, terms to ensure proper use of the trademarks, as well as control and supervision mechanisms for the license holders. Delek Benelux has the right to sub-license during the first six years of the license term. On October 13, 2011, Delek Benelux signed an agreement with the Chevron Group, extending its usage license in the Texaco trademark until 2030. This agreement comes into effect at the end of the previous agreement term. Consideration under this agreement included payment of one-time royalties for the entire extension period, to the amount of EUR 9.4 million. Delek Benelux has committed to rebrand all stations no later than three months prior to the end of the license term. If it fails to do so, it will be liable for such penalties as prescribed in the contract. As of the reporting date, Delek Benelux is in compliance with its obligations as aforesaid. The contract includes provisions whereby the license holders may terminate the contract at short notice due to a material breach which Delek Benelux fails to remedy. As of the reporting date, Delek Benelux is in compliance with the terms of the license.
- B. The BP trademark - On October 1, 2010, Delek Europe entered an agreement with BP for obtaining an exclusive usage license to the "BP" trademark and additional trademarks (primarily "Proxi" and "8 a Huit", deriving from BP's collaboration with French retail giant Carrefour) in all its gas stations in France. The agreement is valid for 5 years, with an option to extend the agreement for another 5 years (an additional extension was also specifically provided for motorway stations, so as to allow for the transfer of the franchise agreement). Under the agreement, Delek France may grant sub-licenses. According to the agreement, Delek France is obligated to use the brand in accordance with the rules set forth in the agreement, as was generally accepted prior to the acquisition of the aforesaid operations and as customary in BP operations worldwide. Delek France is obligated to market fuels conforming to BP's quality specifications. In the extension period, Delek France is obligated to purchase half the quantity of fuel sold in the stations from BP. In consideration for the license, Delek France pays a fixed amount and a variable amount, depending on the quantity of fuel sold in the BP-branded stations.

1.9.20 Human capital

A. General

Delek Europe's operations are managed from its central headquarters in Breda, the Netherlands, and from the headquarters in Cergy, near Paris. Delek Europe is managed through seven major divisions. The managers of these divisions are members of Delek Europe's management and report directly to the CEO of Delek Europe. The divisions are: retail operations in Benelux; retail operations in France; sales support; commercial operations; logistics operations; finance; human resources; and information technology (IT). There are also departments reporting directly to the CEO.

In 2009, changes were made in Delek Benelux's workforce, due to the merger of Delek Benelux's Rotterdam and Brussels offices into one central headquarters in Breda. As of the reporting date, Delek Europe is integrating marketing operations with France, acquired on October 1, 2010, with marketing operations in Benelux. This integration is designed to leverage the manpower, knowhow, systems, and resources developed through marketing operations in Benelux, towards marketing operations in France. This process is expected to be completed by the end of 2012, after which all units of Delek Europe will serve both marketing operations in France and in Benelux, except for the retail units, which will remain separate due to need for proximity to the gas station locations.

The following table details Delek Europe's workforce as of December 31, 2010 and 2011:

Department	Employees	
	2011	2010
Delek Luxembourg	6	8
Delek Belgium	43	47
Delek Netherlands	188	151
Delek France	134	-
Total Company headquarters	371	206
DGV	38	35
Salland	57	53
Schreurs	78	25
Post	22	-
Total subsidiaries	195	113
COCO stations in Belgium	378	261
COCO stations in Luxembourg	127	92
COCO stations in the Netherlands ⁵⁴	740	701
COCO stations in France	416	-
Gesmin management	14	-
Total COCO gas stations	1,661	1054
Segment total	2,241	1,373

Most of the growth in the Company's workforce in 2011 is attributable to the acquisition of marketing operations in France and the growth of COCO stations in Benelux.

B. Benefits and employment terms:

In Benelux and France, labor relations are governed by extensive legislation, with which Delek Europe complies. Most employees are covered by collective agreements, are represented by unions, and benefit from medical insurance, including work disability insurance, seniority and retirement bonuses.

Officers and senior managers in Delek Benelux and Delek France:

Country	Position	Employees	
		2011	2010
Europe	CEO	1	1
	VP Commercial Operations	-	1
	CFO	1	1
	CIO	1	1
	VP HR	1	1
	VP Logistics Operations	1	1
	VP Sales Support	1	-
Benelux	VP Retail	1	-
France	VP Retail	1	-
	VP Operations in France	1	-

Benefits and employment terms: please change A-E, the layout is not right.. thanks

- A. Senior officers in Delek Benelux and Delek France are employed under standard individual employment agreements, which include provisions concerning salaries, contributions to pension plans, personal days, sick days, and additional benefits as required by law.
- B. Delek Benelux granted Mr. Zion Ginat, former CEO of Delek Benelux, free of charge, 45,000 warrants exercisable into Delek Benelux shares, which at the date of their issue constituted

⁵⁴ Including DGV, Schreurs, Salland and Post's COCO stations.

2.5% of the issued and paid-up share capital of Delek Benelux. The shares' exercise price was based on a Delek Benelux value of EUR 129 million, with the exercise price of each portion from the second portion onwards accruing an additional 5% annual interest until the relevant grant date.

At the end of April 2011, Mr. Ginat ended his term as CEO of Delek Benelux, and Delek Benelux bought his unexercised but exercisable warrants (2.5% of Delek Benelux's issued capital), in consideration for EUR 5.4 million, based on a third party valuation.

- C. Mr. Hod Gibso, former CEO of Delek Europe, was granted, free of charge, warrants exercisable to shares in Delek Europe, which as of the grant date constituted 2.5% of Delek Europe's issued and paid-up share capital. These warrants are exercisable in six portions over an exercise period as set forth in the allocation agreement, beginning on the grant date (June 1, 2008) and ending in 2012. The exercise price is based on Delek Europe's equity. The exercise price of each portion from the second portion onwards will be the price of the first portion plus 5% annual interest which will accrue until the relevant purchase date.

On December 15, 2011, Mr. Gibso ended his term as CEO of Delek Europe, and notified the Company of his intention to sell to it his unexercised but exercisable warrants (5 of the 6 portions granted to him). As of the reporting date, the parties are following the provisions set forth in the agreement for determining the consideration, if any, to be paid for these warrants.

- D. On March 14, 2011, Mr. Boaz Chechik assumed the position of CEO of Delek Europe B.V. Under the terms of the management agreement which was signed with a management company owned by Mr. Chechik, the management company will be entitled, inter alia, to monthly management fees of EUR 30,000 (linked to the Dutch CPI), to an annual bonus to be determined by Delek Europe BV's board of directors, a company car (including maintenance and use expenses), a mobile phone, and reimbursement for expenses. Delek Europe will also cover monthly rental payments for Mr. Chechik's apartment in Europe. Mr. Chechik will further be entitled to an options package of 2.5% of Delek Europe BV's issued capital as at the agreement execution date. These options will vest in four installments over a five-year period (with individual installments of 0.5%, except for the first installment of 1% which will vest two years after the grant date). The exercise price (base price) is to be calculated according to Delek Europe's "Normalized EBITDA" value for 2010 (including Delek France's operations) multiplied by a factor of 8.25, less of external debt plus shareholder loans and imputed interest, divided by the number of shares issued at the time of signing the agreement. The exercise price will increase by 5% starting from the second installment, and will be subject to various adjustments as set forth in the agreement.
- E. Subsequent to the reporting period, and as of the date of signing this report, Mr. Ilan Shapir was appointed chairman of Delek Europe and Delek Europe BV (as of the reporting date, the Company and Mr. Shapir have yet to sign his employment agreement).

1.9.21 Raw materials and suppliers

For details regarding raw materials and suppliers in Delek Europe's operations, see Section 1.9.9 above.

1.9.22 Working capital

A. Finished goods inventory policy

Average inventory days for Delek Benelux is 5 days for fuel products. The carrying amount of inventories in Delek Benelux as of December 31, 2011 is EUR 73.5 million.

Average inventory days for Delek France is 10 days. The carrying amount of inventories in Delek France as of December 31, 2011 is EUR 45.2 million.

B. Credit terms

Customer credit: see Section 1.9.14 above.

Supplier credit: The average credit period in Benelux, including credit period pursuant to the supplier agreement with Nerefco, Vitol, Total Trafigura, and Shell, ranges from 5 to 25 days. In France, the average credit period, including the credit period pursuant to the supply agreement with BP for 2011, is 12 days. In 2012, the bulk of fuels in France will be purchased from Total under similar credit terms.

C. Investments

For details of Delek Benelux's holdings in joint ventures, see Section 1.9.18(c) above; for details of Delek France and Delek Benelux's holdings in fuel storage terminals, see Section 1.9.18(d) above.

1.9.23 **Financing**

In the acquisition of marketing operations in Benelux and France, Delek Europe employed both external funding and funding provided by its controlling shareholders - Delek Petroleum and Delek Israel.

A. Financing for the acquisition of marketing operations in Benelux:

On August 8, 2007, the transaction for the acquisition of marketing operations in Benelux was completed. The consideration for the acquisition totaled EUR 404 million. Approximately EUR 240 million of this amount was financed by a bank loan taken by Delek Benelux, while the remainder was financed by an equity investment in Delek Benelux and shareholder loans provided by Delek Petroleum and Delek Israel (in this sub-section - "Shareholder Loans") to a total amount of EUR 144 million (of which EUR 15 millions were received as shareholder loans). The shareholder loans carry an annual, CPI-linked interest of 5% plus VAT on CPI linkage differences. It was further determined that, subject to any surplus for payment in Delek Europe, interest, CPI-linkage differences and VAT will be paid in annual installments starting August 6, 2008. Lacking any surplus in Delek Europe, payment of the linkage differences and interest will be postponed, and they will be payable upon repayment of the loans. In October 2010, Delek Petroleum and Delek Israel, after obtaining such approvals as required by law, extended the loan repayment date to December 31, 2012, with the shareholder loans bearing an annual interest of 5.5% starting August 7, 2010, and until the loan repayment date. The principal of these loans is linked to the CPI (the base index being the known CPI at the original repayment date (i.e. - August 6, 2010)). The principal and interest payments will be subject to VAT as required by law. It was further agreed, that in the event that Delek Europe raises capital and/or loans during the loan period, these moneys will serve to repay the loans, unless Delek Petroleum and Delek Israel provide written notice that they waive such early repayment. The aforesaid notwithstanding, transfer of control in Delek Europe to a legal entity outside the Company's control, is subject to early repayment of the loans. The outstanding balance of the shareholder loans as of December 31, 2011, totals EUR 15 million. For details concerning the bank loans and their terms, see sub-sections (c) and (d) below.

It is noted, that in 2008, Delek Benelux received an additional bank loan of EUR 45 million for acquiring the other partners' interests in 3 joint ventures.

B. Financing for the acquisition of marketing operations in France:

On June 23, 2010, Delek Europe BV signed an agreement for the acquisition of marketing operations in France. The consideration for acquiring the marketing operations in France amounted to EUR 209 million (after working capital adjustments), and was financed by bank loans and shareholder loans provided, pro rata, by Delek Petroleum and Delek Israel, as detailed below:

1. A total of EUR 80 million was financed through a loan from a bank in Israel to Delek France B.V. ("the Borrower"). The loan is for a period of 7 years at variable interest equivalent to the three-month LIBOR rate, plus an additional margin. As of December 31, 2011, the outstanding balance of this loan is EUR 80 million.
2. A total of EUR 40 million was financed by a short-term loan from another bank in Israel, with an interest of LIBOR plus a margin, secured by Delek Petroleum. After completion of the required paperwork, the bank undertook to provide the loan for a period of 8 years. The said loan was repaid at the end of November 2010, and was replaced by a loan extended to Delek Europe by Delek Petroleum. This loan carries an interest of 5.5% and is linked to the CPI.
3. The balance of the consideration was financed through shareholder loans extended by Delek Petroleum (EUR 44 million) and Delek Israel (EUR 11 million). The shareholder loans are repayable on December 31, 2012, will be linked to the CPI, and will bear 5.5% annual interest. As of December 31, 2011, the outstanding balance of the said loans amounts to EUR 44 million for Delek Petroleum's loan and EUR 11 million for Delek Israel.

4. The balance of the consideration was financed through cash flows from working capital in the acquired business.
 5. Moreover, the Delek Group (with cross-guarantees by Delek Petroleum and Delek Israel) extended further guarantees to third parties, to the amount of EUR 97 million, towards the acquired operations, for financing working capital for the benefit of the VAT and excise authorities and for purchasing fuel from BP. As of December 31, 2011, the guarantees have been reduced to a total of EUR 55 million.
 6. Delek Petroleum and Delek Israel will be entitled to annual management fees amounting to EUR 1.2 million, pro rata to their share in Delek Europe. Delek Europe is entitled to annual management fees of EUR 0.2 million.
- C. The following table details the average interest rate on bank loans and off-bank loans in effect during 2010 and 2011, which are not designated for specific use by Delek Benelux or Delek France. The table distinguishes between short-term and long-term loans, as well as bank and off-bank loans:

		Average interest rate in 2011		Average interest rate in 2010	
		Short term borrowing	Long term borrowing	Short term borrowing	Long term borrowing
Benelux	Banks	3.06%	4.27%	2.53%	3.77%
	Off-bank	-	3.59%	-	3.06%
France	Banks	2.44%	5.59%	2.91%	5.08%
	Off-bank	-	5.50%	-	5.50%

Subsequent to the reporting period, in March 2012, Delek France signed a financing agreement with a consortium of 4 banks. The financing agreement includes working capital credit facilities of EUR 30 million (which replaces credit facilities in effect during the reporting period), NIS 35 million in credit for new investments in France, and facilities of EUR 20 million for the provision of bank guarantees.

D. CAPEX credit facilities:

In order to finance CAPEX investments in Benelux, Delek Benelux signed a loan agreement with Depot Kampen BV ("the Lender"). The lender provided Delek Benelux a 10-year loan of EUR 8.5 million with a variable interest rate equal to the 3-month EURIBOR rate plus a margin. The loan will be utilized for construction of the new terminal in Kampen, the Netherlands (for more information, see Section 1.9.18(d) above). Another credit facility of EUR 13 million is available for financing construction of the gas station in Hevelee, Belgium, following the Company's winning bid on this station, comprised of a gas station, convenience store, and restaurant.

E. Limitations on credit facilities:

1. Limitations for acquisition of marketing operations in Benelux - As part of the financing agreement for receiving the bank loan as aforesaid in Section 1.9.23(a), credit facilities for the future, financial covenants, and other conditions were set forth, and they bind Delek Benelux under the financing agreement.

The loan agreements require compliance with financial covenants relating primarily to the ratio of debt to EBITDA (as defined in the agreement), variable ratios depending on the different periods throughout the lifetime of the loan, ratios of EBITDA to financing expenses throughout the loan periods, and compliance with a maximum threshold of CAPEX investments. As of December 31, 2011 and the reporting date, Delek Benelux is in compliance with all these financial covenants.

2. Limitations for acquisition of marketing operations in France - In order to secure repayment of the loan extended by an Israeli bank as detailed in Section 1.9.23(b)(1) above, shares in the borrowing company and in Delek France were encumbered, and various financial covenants were set forth (based primarily on the ratio of debt to EBITDA and coverage ratios). In addition, as part of the said guarantees, Delek Petroleum and Delek Israel provided separate guarantees, pro rata to their respective interests.

As of December 31, 2011 and the reporting date, Delek France is in compliance with all these financial covenants.

F. Credit facilities:

Delek France has credit facilities for working capital purposes, extended by ING Bank and secured by the Delek Group, to the amount of EUR 30 million (of the total amount of EUR 55 million) for a period of one year at an interest rate of LIBOR plus a margin. Subsequent to the reporting period, these facilities were replaced by new facilities as detailed above.

G. Variable interest credit:

The following table details credit facilities bearing variable interest in Delek Benelux and Delek France, as of December 31, 2011:

Country	Type of loan	Variance mechanism Eurobor+	Principal repayment date / facility term	Interest payment	Interest rate at completion date	Loan / facility amount (EUR millions)
Benelux	First Lien Facilities ⁵⁵	2.25%-3.25%	In one installment at the end of 8-9 year terms (until 2015-2016)	Monthly (from Sept. 28, 2009)	5.7%-6.7%	245
	Facility B1 ⁵⁶	1.75%	In one installment after 2.6 years (until 2014)	Monthly, starting Dec. 26, 2011	3.11%	11.375
	Second Lien Facilities	5.125%	In one installment after 9.5 years (by 2017)	Monthly (from 2009)	8.875%	40
	Revolver Credit Facility ⁵⁷	1.75%	7 years (by 2015)	Monthly (From 2009)	5.03%	50
France	Bank Loan	4.25%	EUR 40 million in one lump sum after 7 years (2017), EUR 2 million over 5 years from 2012 through 2017	Quarterly (from 2010)	5.45%	80
	Revolver Credit Facility	1.85%	One year (until Q4/2011)	Daily-weekly	2.95%	28
Delek Europe Finance	Bank Loan Kampen	2.65%	EUR 8.5 million in 36 equal quarterly installments over two years from 2012 through 2015	Quarterly (from 2011)	5.45%	8.5
	Bank loan Heverlee	1.50%	EUR 16.7 million, 4.5 in one lump sum after one year, EUR 12.2 million in 59 fixed quarterly installments from 2012 through 2027	Quarterly (from 2011)	2.97%	16.7

⁵⁵ Loan with preferred repayment over second lien facilities.

⁵⁶ Loan with preferred repayment over second lien facilities.

⁵⁷ Credit facilities for current working capital, from which Delek Benelux may withdraw amounts as per its needs and discretion.

1.9.24 Taxation

- A. Tax laws applicable to Delek Benelux - The tax reports of Delek Benelux (a Dutch company) are consolidated for tax purposes with those of its Dutch subsidiaries in which it holds 95% or more. The future tax liability will be determined based on the value of Delek Benelux's assets, volume of operations and equity. In general, the Dutch corporate tax rate in 2011 is 25.0%. Companies operating in Belgium and Luxembourg are taxed at the applicable rates in those countries. In 2011, the tax rate in Belgium was 33.99% and in Luxembourg - 29.63%. Taxes on capital gains, interest and dividends are affected by the tax treaty between Israel and the Netherlands. Under this treaty for prevention of double taxation, a dividend distributed by a Dutch company to an Israeli company holding at least 25% of its share capital is subject to a 5% withholding tax in the Netherlands.
- B. Tax laws applicable to Delek France - In general, the corporate tax rate in France as of 2011 is 34%.

For more information pertaining to taxation, including business losses carried forward, see Note 42 to the financial statements.

1.9.25 Environmental risk and management thereof

Delek Europe is subject to various regulations relating to environmental protection, including fuel handling, prevention of soil and water pollution, and waste treatment. In the 1990s, environmental protection requirements for gas stations in Benelux were made more stringent. This raised the level of environmental protection at existing stations, and also created an entry barrier to the establishment of new gas stations.

Environmental protection requirements vary from country to country:

In the Netherlands, fuel station operators require a license under the Dutch Environmental Control Act, and must comply with the terms of this license. Furthermore, station operators must comply with requirements laid down in numerous orders, including a duty to analyze soil quality at specified intervals, to remedy any pollution caused in the period when the station operated under license, and to obtain a special license if any activity other than fuel sales takes place at the gas station and which has environmental protection implications (such as above-ground fuel tank storage). The Dutch Provincial Executive is authorized to order soil pollution tests and to take action. Obligations can be imposed on owners as well as on the lease-holders of the complex, and may apply to Delek Benelux, primarily with regard to COCO or CORO stations.

In Belgium, environmental protection requirements vary according to the exact location of each station, since the country is divided into three regions with different regulatory requirements. Each region has a separate authority for issues relating to environmental protection, including licensing and pollution. The state remains responsible for certain matters involving health and safety. Gas station operators must obtain an environmental protection license which includes operating conditions, quality-related conditions, and conditions related to the upgrading of station equipment. In addition, various requirements are imposed on the operator for matters of cleanliness and testing for soil pollution, which apply both to the operator and to whoever holds rights in the station.

In Luxembourg, gas station operation requires a license from the Ministry of Labor and Ministry of Environmental Protection. Licenses are granted to operators for a limited term (usually 15 years). In general, a station operator is not required to deal with any defects unless the license expires or is revoked, or if any environmental damage is caused during the term of the license.

In France, operations are subject to various environmental provisions covering, inter alia, the handling of fuels, preventing damage to soil and water, handling of waste, etc. In recent years, and as part of the global efforts towards environmental protection, environmental protection requirements in France have become more strict in general, and particularly as regards gas station operations. Furthermore, the government set a mandatory minimum quota for bio fuel out of the total fuel consumption for fuel-marketing companies, calculated as a percentage of total fuel sales, which as of the reporting date stands at 7%. In France, government encouragement to increase use of biofuels is more aggressive than in other European Union countries, and consequently the quotas in France are higher than those set by the European Union. Furthermore, fines were prescribed in the event of failure to comply with these quotas. To the best of Delek France's knowledge, no changes are expected in the bio fuel quotas until 2015. Furthermore, two of Delek France's terminals (Vitry and Lyon DPL) have equipment and capacity for producing bio fuel mixtures.

To the best of Delek France's knowledge, new legislature is expected in France concerning air pollution and conditions for operating gas stations, the safety of pumps and fixed minimum distances between pumps and motorways. As of the reporting date, Delek Europe cannot estimate the effects of this new legislation, if enacted.

The Company's total provisions for Delek Europe's environmental protection investments, as of the end of 2011, amounted to EUR 23 million.

This information concerning Delek Benelux and Delek France's assessment of the need for additional investments in environment-related items constitutes forward-looking information. It is possible that such forward-looking information will fail to materialize, inter alia in the event that material deviations are found in Delek Benelux and Delek France's operations, or that new environmental requirements come into force, requiring additional material expenses.

It is noted that Delek France and Delek Benelux regularly allocate 10%-15% of all CAPEX investments to regulatory and environmental adjustments.

1.9.26 Restrictions and supervision of Company operations

Delek Europe operations are subject to laws and regulations including, inter alia, labor laws, regulations for the sale of alcohol and tobacco products, minimum wage, work conditions, public access roads, and additional laws, including:

- A. Storage obligation - Benelux countries and France are obligated to comply with a Compulsory Storage Obligation (CSO) for fuel, based on annual sales volumes.

The annual storage obligation in Belgium, the Netherlands, Luxembourg and France is 90 days' storage.

The Dutch, Belgian and French governments established separate agencies for managing compulsory storage obligation quotas. Companies can hold their quotas as actual inventory, or by paying these agencies (tickets). About 95% of the quota in Belgium, 90% in France, and 83% in the Netherlands. Payment to the government agency is per liter, and is almost completely refunded through the retail margin, i.e. - passed on the end-customers at the fuel pump. The remainder of the statutory quota in these countries is covered by the companies themselves through various means. In these countries, Delek supplements its compulsory storage obligation by buying 'tickets' from other entities in the fuel industry, who have surplus inventory balances, and by using its operating inventory in the various terminals, which are used in the ordinary course of business.

In Luxembourg, the fuel companies are responsible for managing their 90 days' compulsory storage quota. In 2011, Delek Luxembourg covered its compulsory storage obligation by holding inventory in BP's Nerefco terminal in Rotterdam, and by holding inventory in the Company-owned terminal in Luxembourg, with remaining quota requirements covered through the purchase of 'tickets'. In 2012, the Company aims to streamline operations by transferring its physical inventory in the Nerefco terminal in Rotterdam to the Company-owned Vitry terminal in France, thereby discontinuing storage payments to BP Nerefco.

- B. Provisions to promote competition -

1. In Benelux: In June 2006, a law was enacted in the Netherlands which requires a tender process for obtaining fuel station franchises along Dutch motorways. The law aims to increase the number of players in the market. This trend is also evident in agreements (unrelated to this law) signed between the Dutch government and the four largest fuel industry companies (including Texaco) in 2001, whereby the number of motorway stations belonging to these companies would be reduced by 50. Each of the companies is required to sell a number of motorway gas stations in a tender process. The number of stations for sale is based on market share in the Netherlands, and stations are tendered once every 15 years. The process has led to the publication of a list of all the sites held by all the companies and the date on which they were tendered. The list is for fifteen years from the date of its publication, so that in each year there is a tender for stations whose identity is known ahead of time. The tender mechanism contains a concession when a station is being tendered for the first time - if the station owner wins the tender, then he pays the state the lesser of either 30% of the bidding price or the difference between his bid and the next-lowest bid. If the station owner loses the tender, he will receive its value based on the price in the winning bid. As noted below, a similar mechanism is employed in Belgium, but without the concession component, and a list of the sites of all the companies and the dates on which they will be tendered is also

published in this country. In Belgium, BOT (Build, Operate, Transfer) tenders are customary for the construction of motorway gas stations, and there is legislation regulating full and fair disclosure prior to entering into contracts.

2. In France: A tender process is mandatory in France for obtaining franchises to gas stations, restaurants, and hotels along motorways in the country. This requirement aims to increase the number of players in the market. As part of the tendering process, bidders must meet various planning requirements and propose attractive solutions in terms of customer service and offering, design and innovation. In addition, bidders must offer payment for use of the franchise. Sites are offered for periods of 10 to 15 years. Delek France believes this law to present both risks and opportunities, whereby during the next three years 10 of its motorway stations will be up for tender, while 267 of Delek France's competitors' sites (gas stations, restaurants, and hotels) will also be tendered in the same period, and will be open to bids by Delek France. Despite BP's history of winning 38% of the tenders in which it bid, Delek France's base estimate is that in 2011-2014, the number of tenders that Delek France will win will be greater or at least equal to the number of tenders that it will lose.

This information pertaining to Delek France's estimates concerning the ratio of Delek France's tender wins and losses constitutes forward-looking information, which is based on Delek France's estimates concerning its operations in Benelux and its familiarity with the French market, including BP's historic operations in this market. Nonetheless, it is possible that this forward-looking information may fail to materialize, inter alia, if Delek France changes its bidding strategy, if there will be regulatory changes which will affect the said ratio, etc. There is no restriction or obligation concerning the number of stations that may be offered in these tenders.

3. In addition, Benelux and France are subject to the 1999 European Regulation of Vertical Restraints, which limits the term of exclusive contracts (such as with suppliers and agents) to a maximum of 5 years, unless the supplier owns or rents the site.
- C. Gas station licensing and fuel sale operations - Delek Benelux and Delek France are required to comply with a range of municipal, regional and national regulations, including periodic testing of soil quality, licensing of station buildings and fire safety directives. Detailed directives also apply to the construction and operation of motorway gas stations.
 - D. Environmental protection requirements - see Section 1.9.25 above.
 - E. Convenience store licensing - Convenience stores are subject to regulation by the authorities in the various countries, as regards health and sanitation, safety, fire, and planning and construction. Among other factors, in 2009, France imposed a prohibition on the sale of alcohol between 6 pm and 8 am, and the sale of refrigerated alcoholic beverages is prohibited. It is noted that alcoholic beverage sales can account for up to 50% of non-fuel sales in gas stations in France. Therefore, enforcement of this law may lead to the closing of gas stations, and affect the economic viability of additional stations. As of the end of 2010, the ban on selling alcoholic beverages has mainly impacted convenience store operations in CORO and COFO stations, with an estimated decrease of EUR 1 to 1.5 million in Delek Europe's profits. In 2011, the prohibition did not significantly damage operations, and its effects leveled off.
 - F. Fuel taxation - Tax rates on fuel sales in the Netherlands, Belgium and France are currently among the highest in Europe. Tax rates in Luxembourg are lower than in neighboring countries.
 - G. Labor laws - Delek Benelux and Delek France are subject to legislation regarding wage protection, overtime, and work conditions. In addition, labor laws in Benelux and France restrict layoffs, and require various actions to be taken for premature termination of employment (such as applying for prior approval from a government agency, or a relatively long notice period prior to actual termination of employment). It is noted that trade unions in Benelux and France are relatively powerful, and have the right to obtain information on significant issues, to be consulted on various processes (such as the sale of an operation, or liens), and are even able to prevent certain Delek Benelux and Delek France initiatives by applying to the courts. As of the reporting date, labor relations in Delek Benelux and Delek France are proper.
 - H. Price control - In the Netherlands, there are no regulations prescribing maximum prices for fuel. In Belgium, legislation provides for maximum prices, and there is a price control arrangement based on this legislation, between the Belgian Ministry of Economics and the

country's fuel companies. In Luxembourg, there is a mechanism for setting maximum prices similar to the Belgian mechanism, although it is based on other laws. Furthermore, Benelux countries have restrictions on price fixing between fuel companies, by virtue of antitrust laws. In France, there are no price controls, though there are restrictions on price fixing between fuel companies by virtue of antitrust laws.

1.9.27 Material agreements

Delek Benelux considers the franchise agreement with Chevron to be a material agreement. Delek France considers the franchise agreements with BP and Carrefour, and the fuel supply agreement with BP to be material agreements. For more information, see Sections 1.9.9 and 1.9.19 below.

1.9.28 Legal proceedings

As of the reporting date, Delek Europe is not party to any material legal proceedings.

1.9.29 Strategy and objectives

Delek Europe periodically reviews its strategic plans and goals, and revises them according to developments in the fuel market, market competition, and macro-economic effects. Delek Europe's operations in the coming years are expected to focus on the following activities:

- A. Increased presence in the European gas station market through targeted acquisitions - Identification of opportunities for acquiring gas stations stemming, inter alia, from the international fuel companies' trend towards selling their gas station holdings so as to increase Delek Europe's presence in the European gas station market and improve the gas station chain.
- B. Strengthening Delek Europe's position in the European fuel market - Delek Europe believes that by seizing opportunities, increasing Delek Europe's fuel offering, strengthening ties with Delek Europe's customers, advertising activities, increasing fuel product marketing efforts, brand awareness, and convenience store sales, Delek Europe will be able to improve and establish its position as a leading player in the European fuel market.
- C. Optimization of operating methods - Optimizing gas station operating methods by minimizing low-profitability models (such as CORO and CODO), and expanding more profitable operations (such as COCO, RORO, and COFO); closing low-revenue sites; achieving operating excellence through process and administrative automation; developing the sales mechanism for fuel cards targeting the commercial segment; identification of additional RORO or DODO retailers while retaining existing distributors; operational improvements and cost savings, inter alia by sourcing maintenance systems and electronic invoice management.
- D. Increasing non-fuel operations - Profits from convenience store sales, and from the sale of additional non-fuel products sold in the gas stations, are greater than those on fuel sales. Delek Europe is renovating and re-designing its convenience store chain. These efforts include the offering of new products (focusing mainly on fresh products), intelligent in-store product arrangement, and efficient inventory management aimed at reducing costs. Furthermore, Delek Europe seeks to increase the number of convenience stores in its gas station complexes and offer additional products in these stores, so as to further increase its products. These additional products include food products, baked goods, restaurants, own-brand products, and carwash facilities.
- E. IT investments - Investing in Delek Benelux and Delek France's IT systems, including ERP and CRM systems, and the ENVOY store management system, so as to merge Delek Benelux and Delek France's price and workflow management systems. Delek Europe expects this investment to amount to EUR 7-8 million in the period 2012-2013.
- F. Synergy - Generating synergies in Delek France, based on experience gained in Benelux, by improving growth and operational streamlining, and utilizing the geographic proximity between France and Benelux for expanding Delek France's market (and similarly, the operations in Benelux).

1.9.30 Risks

Delek Europe estimates the following to be the major risks associated with its operations in Europe:

- A. Competition - The fuel market in Benelux and France includes numerous competitors, which are constantly striving to increase their market share. Competition is manifested in the acquisition of gas stations, sales promotions, price reduction, etc. Increased competition, including the entry of retail chains, may affect segment margins and the operating results of

Delek Benelux and Delek France. Furthermore, existing and future regulatory restrictions aimed at limiting the power of major market players and increasing market competitiveness could affect the ability of Delek Benelux and Delek France to expand their operations or might restrict them in contracting with other parties.

- B. Exposure to fluctuation in global fuel prices - The price paid by Delek Benelux and Delek France for fuel product purchases is derived from global oil prices, and therefore Delek Benelux and Delek France are exposed to fluctuations in oil prices in these markets. The factors influencing fuel prices include changes in the state of the global and local economies; demand for fuel products in and outside Benelux and France; geopolitical conditions in general and in oil producing regions in particular (USA, the Middle East, former Soviet Union countries, West Africa, and South America); production levels of crude oil and petroleum distillates around the world; development and marketing of fuel substitutes; disruption in supply lines; and local factors including market and weather conditions. The global rise in fuel markets increases the price of products sold by Delek Benelux and Delek France, which can lead to a decrease in demand for these products, while impairing their profits on every product sold. At the same time, since fuel prices are stated in USD, and despite Delek Benelux and Delek France's strategy of hedging their open foreign currency positions, the EUR-USD exchange rate is also likely to affect Delek Benelux and Delek France's purchase prices.
- C. Environmental protection requirements - Although the statutory provisions for environmental protection in Benelux and France are relatively stringent, future regulations and orders due to increasing awareness of the dangers associated with uncontrolled operations by fuel companies in general and by Delek Benelux and Delek France in particular, could increase the monetary expenditure by Delek Benelux and Delek France. In addition, failure to comply with these regulations could lead to sanctions, expose Delek Benelux and Delek France to lawsuits, and impair the results of operations.
- D. Credit limits and financing needs - Delek Benelux and Delek France operate under financing and current credit agreements. As of December 31, 2011, and the reporting date, Delek Benelux has loans and guarantees as detailed in Section 1.9.23. Delek France is party to the financing agreement detailed in Section 1.9.23, whereby it has undertaken to comply with various financial covenants. These liabilities may increase Delek Benelux and Delek France's vulnerability to economic downturns, compel them to allocate a substantial part of their cash flows for debt repayment, limit their ability to plan, make changes and react quickly to changes in their operations, and curtail their ability to borrow additional funds.
- E. *Alternative energy sources* - Transition to the use of alternative energy sources, such as natural gas and electric-powered engines, could have an adverse effect on the volume of fuel sold by Delek Benelux and Delek France, or, alternatively, might require them to adapt gas stations to new customer requirements which would involve significant investments.
- F. Biofuels - Government encouragement to increase the use of biofuels may lead to additional investments to allow for the blending and distribution of these products.
- G. Food product regulation - Food products and beverages sold in Delek Benelux and Delek France's convenience stores are subject to various regulatory requirements. Failure to comply with these requirements and incurring consequent damages, or more stringent regulatory requirements, could affect the results of Delek Benelux and Delek France's operations.
- H. Fuel taxation - An increase in the current fuel tax rates in Benelux and France may affect fuel consumption in these countries, and may also have an adverse effect on Delek Benelux and Delek France's operations.
- I. Economic slow-down in the local markets (Benelux and France) - A continuation of the global economic crisis may lead to a prolonged decline in fuel consumption and retail product purchases in Delek Benelux and Delek France's complexes, and adversely affect the results of their operations.
- J. Economic crisis in the Eurozone - The Eurozone is currently in the midst of an economic crisis, reflected as a debt crisis in several European Union countries, and general economic instability throughout the Eurozone. In light of this crisis, international rating agencies downgraded the rating of several key countries in the Eurozone in 2011, including France, Spain, Italy, Ireland, Greece, Portugal, Belgium, Cyprus, and Slovenia. Severe budgetary cutbacks which will lead to a general economic slowdown and even a recession in some European Union countries, lower demand for fuel by transportation companies and by commercial entities downsizing their workforce and vehicle fleets, and by private consumers

affected by the above economic crisis, may damage Delek Europe's operations and profitability, and reduce the volume of its operations. Furthermore, pressure on the banking system, possible writeoff of equity, and increased capital adequacy requirements may increase pressures in the financial system, which would manifest in a reduction of credit facilities, difficulty in raising or extending funds, and more stringent compliance tests for borrowers in general, including Delek Europe.

- K. Regulatory developments - Delek Benelux and Delek France are subject to a range of regulatory provisions on matters such as gas station licensing, labor law, environmental protection, price control and restrictive trade practices. Violation of regulatory requirements, or more stringent regulatory requirements applicable to Delek Benelux and Delek France may lead to increased expenditure, prohibit the expansion of operations or affect existing operations, and may have an adverse effect on Delek Benelux and Delek France's operations.
- L. Changes in consumer preferences - Changes in consumer preferences could adversely affect Delek Europe's profits on two levels: **a)** Environmental awareness could reduce vehicle usage, and consequently lead to a decrease in fuel consumption; **b)** changes in dietary preferences, such as the preference of healthier food, could reduce consumption of various food types, such as fast food, and reduce Delek Europe's convenience store revenues.
- M. Discontinued operations in relatively high-turnover gas stations - Turnover varies from station to station, so that some gas stations account for larger operating volumes than others. Discontinuing operations in COCO gas stations, or in motorway gas stations with relatively high turnover, or a reduction in their turnover, for any reason whatsoever, would adversely affect Delek Europe's operations.
- N. Franchises use by Delek Benelux and Delek France in their operations - Delek Benelux and Delek France use several franchises for fuel and store branding. Discontinuing the use of these franchises for any reason whatsoever could affect the results of Delek Benelux and Delek France's operations.
- O. Risks related to the integration of new / acquired operations - Possible transactions involving various new operations entail certain risks such as difficulties in integrating the acquired operations with existing Delek Europe operations, the results of the acquired operations failing to meet expectations, the need to obtain financing, and additional regulatory requirements pursuant to such acquisition. Completion of the acquisition of operations in France entails such risks as aforesaid, and also entails difficulties in integrating the marketing operations in France with existing operations in Benelux and an increase in Delek Europe's debt.
- P. Negative press and damage to goodwill - Marketing operations in France are carried out exclusively under the BP brand. BP's involvement in the Gulf of Mexico oil spill drew criticism in the press and even boycotting of BP by consumers around the world. Recurrence of similar incidents and increased consumer awareness of these incidents may draw negative press and damage BP's goodwill, thus adversely affecting Delek Europe's revenues. It is noted, that the above incident did not actually affect Delek France's operations.
- Q. Risks related to the migration of BP's IT systems to Delek Europe's IT systems - In the coming year, Delek France plans to migrate BP's information systems to Delek Europe's information systems. As detailed above, this is a lengthy and complicated process. Failures during this process could adversely affect proper operation of Delek France's gas stations and convenience stores.

The following table summarizes the aforesaid risks by type (macro risks, industry-wide risks, and company-specific risks), rated according to Delek Europe's management's estimates of their effect on operations: major, moderate or minor:

	Degree of risks effect on Delek France's operations		
	Major effect	Moderate effect	Minor effect
Macro risks	• Economic slowdown in the local markets (Benelux and France). • Eurozone economic crisis		
Industry-specific risks	• Exposure to global fuel price fluctuations • Changes in consumer preferences	• Competition • Fuel taxation • Regulation	• Environmental requirements • Alternative energy sources • Biofuels • Food product regulation
Company-specific risks	• Negative press and damage to goodwill	• Discontinuing operations in high-turnover stations • Franchises used by Delek Benelux and Delek France • Risks related to the integration of new / acquired operations	• Credit restrictions and financing nee • Migration of BP IT systems to Delek Europe IT systems

The effect of these risks on Delek Europe's operations are based solely on Delek Europe's assessments, and actual effects may differ.

1.10 **Motorway Service Areas in the UK**

1.10.1 **General**

- A. On January 25, 2011, Delek Petroleum completed a transaction with Delek Belron International Ltd. ("**Delek Belron**") and Delek Real Estate, companies controlled by the Company's controlling shareholder, for the acquisition of 75% of the issued and paid up share capital of Delek Motorway Services Ltd. ("**DMS**") and of the shareholders loans granted to Delek Motorway Services UK Ltd. ("**DMS UK**"), a company that holds 100% of the share capital of MSA Acquisitions Co. Limited ("**MSA**"), whose sole activity is the holding of all the issued and paid up capital of Roadchef Limited ("**Roadchef**"). Subsequent to this transaction, Delek Petroleum, that from July 2007 until the date of the transaction, held 25% of the issued and paid up capital of DMS, holds 100% of the issued and paid up capital of DMS at the reporting date. Consideration of the transaction is an amount in New Israel Shekels, equal to GBP 86.25 million, reflecting a value of GBP 115 million for Roadchef, which was paid as follows: Delek Real Estate's debt in respect of various loans it received from the Company was offset and a direct payment was made to a bank in respect of Delek Real Estate's debt towards it. In addition, as part of the transaction, the Company acquired another of Delek Real Estate's debts towards it from the bank.

The terms of the agreement signed in connection with the said transaction prescribe that Delek Real Estate and Delek Belron (together: "the Seller") will, in addition to the DMS shares, also transfer to the Company all their rights and obligations by virtue of the owners' loans to **DMS UK** (by way of assignment). Furthermore, the agreement stipulates that the Seller shall indemnify the Company in respect of parts of the tax payments made by DMS originating in the period prior to the completion of the transaction, subject to conditions prescribed in the agreement, and that the Seller shall indemnify the Buyer in respect of 75% of any amount that the Company is required to pay should a claim or request be submitted to DMS to pay the management company under the management agreement that was signed with County Estates Management (Services) Ltd., and all subject to the conditions of the

agreement. For further details of the aforementioned transaction and its conditions, see the Company's Immediate Report from January 5, 2011 (ref. 2011-01-006393), in which the relevant information is presented here by way of referral. The transaction was approved by AGMs of the Company and Delek Real Estate on January 10, 2011.

The holdings in DMS, that were acquired as part of the transaction described above, were transferred to Delek Petroleum, so that subsequent to the completion of the transaction, Delek Petroleum holds all the share capital of DMS, whereas Delek Real Estate's debt arising from the acquisition of Delek Real Estate's debts from the banking corporation is towards the Company. The proceeds of this transfer of holdings was grossed up as a loan from the Company to Delek Petroleum in an amount that is the shekel equivalent of GBP 86.25 million.

Whereas the sole activity of DMS is the holdings of the shares in MSA and the sole activity of MSA is the holding of Roadchef's shares, the following description relates principally to Roadchef.

Roadchef was established in 1973 and since then its operations have centered on motorway service areas in the UK. For details about operations in neighboring service stations - see section B, below. Through wholly owned subsidiaries and second-tier subsidiaries, Roadchef operates 27 service sites at 20 different locations in England, Scotland and Wales (eight service stations are located on both sides of the motorway). The service stations are located on main highways including the M25, M5, M1, M6 and M4.

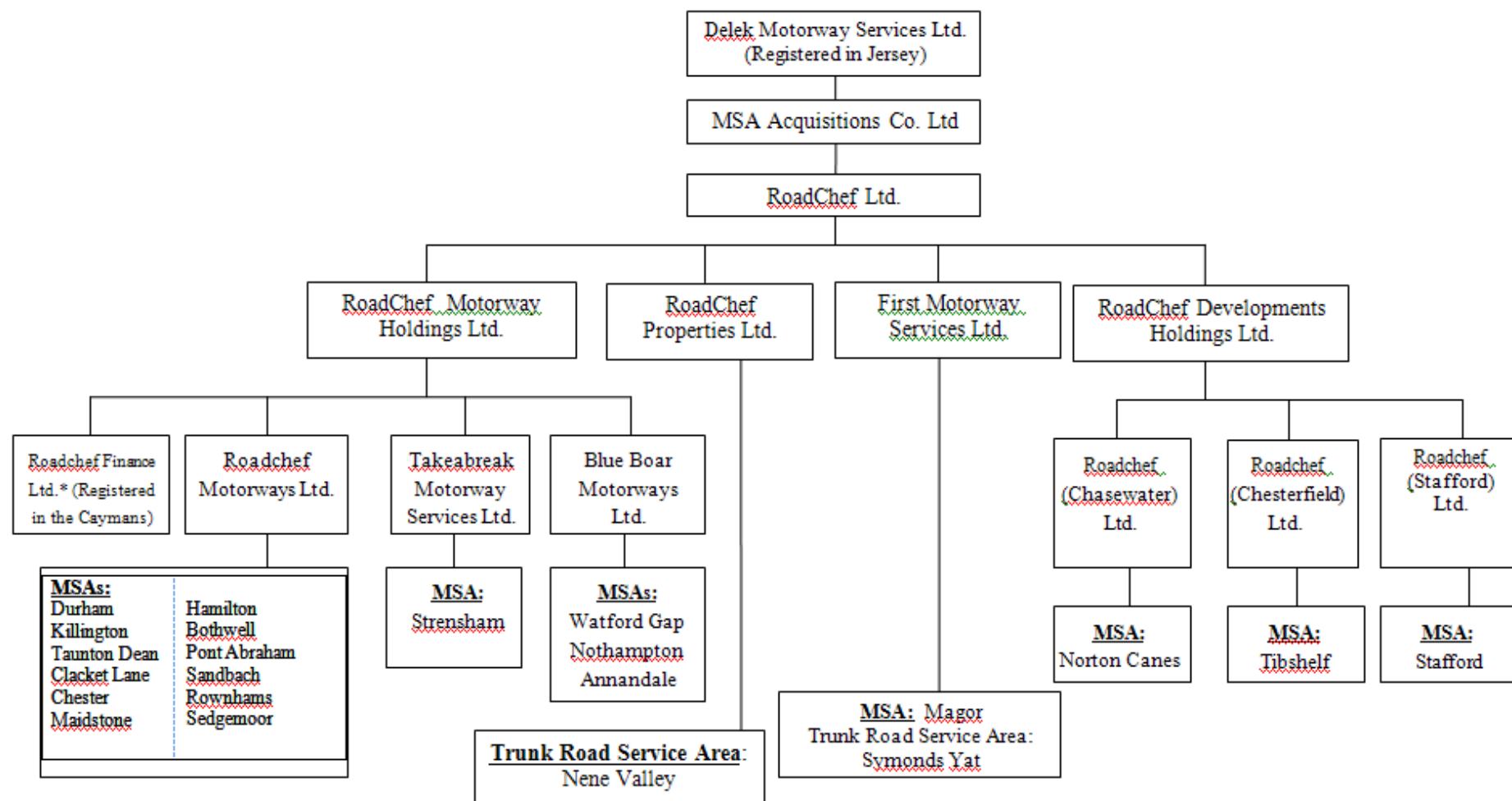
During the 1980s, Roadchef operated eight service stations. In 1998, Nikko Principal Investments Ltd acquired the controlling interest in Roadchef. That same year Roadchef acquired two companies (Blue Boar and Take a Break) which themselves operated service stations, thus increasing the number of service areas that it operates. Moreover, that same year, Roadchef (through a subsidiary) completed a securitization process, in which context it raised GBP 210 million on the Luxembourg Stock Exchange that it used to invest in developing and enlarging the volume of Roadchef's operations.⁵⁸ Thus, in 2000 and 2001 Roadchef opened three new motorway service areas and in the ensuing years it renovated and significantly expanded its existing stations.

On 10 August 2011, the Group acquired 100% of the voting equity shares of First Motorways Services Limited ("Magor"), a private company that owns a service station along the M4 motorway in Britain. The value of the transaction was GBP 10 million. After the acquisition, Roadchef began developing the station, which included replacing some of the services provided and adapting it to the network.

Over the last few years, Roadchef has concentrated on entering into franchise agreements with prominent chains such as Costa Coffee, WHSmith, Premier Inn (this agreement terminated in 2010), and more recently also with Days Inn (replacing the terminated agreement with Premier Inn), and McDonald's.

The following is a diagram of the holding structure:

² For further details, see Section 1.10.14 below.



Note 1: All companies are 100% wholly owned by their holding companies.

Note 2: All companies are registered in England, except for Delek Petroleum, which is registered in Israel and Delek Motorway Services Ltd., which is registered in Jersey.

* SPV established to raise debt. For details see Section 1.10.14 (C) (2) below

- B. The motorway services activity consists of the sale of retail products, including a variety of products for motorway travelers (food, newspapers and magazines, tobacco products, gifts and car accessories), catering services, including restaurants under Roadchef's private brand, fast food restaurants and coffee shops under franchise agreements, and the sale of fuel at the filling stations that are part of the service stations, some of which are operated by Roadchef itself and some of which are operated through rental and/or other operating agreements with the petroleum companies (BP, Esso and Texaco). At some of the motorway service areas, Roadchef operates hotels in the services area, under the Days Inn brand. Likewise, during the course of its business activity, Roadchef enters into agreement with commercial companies and various service providers for the sale of services and/or products on service station sites, as specified in Section 1.10.4 (E) below ("Other Services").

C. Distribution of dividends and restrictions on their distribution

During the two years preceding the reporting date, DMS and/or MSA and/or Roadchef did not distribute dividends. At December 31, 2011, DMS has no distributable surpluses.

As part of a debt raised by a subsidiary of Roadchef in 1998 through the issuance of bonds (for details see Section 1.10.14 (C)(2) below), Roadchef and/or its subsidiaries made a commitment to preserve certain financial criteria that may in future prevent the distribution of a dividend. Likewise, a commitment was made to refrain from distributing a dividend in certain instances. For details, see Section 1.10.14 (E)(D) below.

1.10.2 Financial information about motorway services activity:

Following are figures (in GBP thousands) about this operating segment in 2010-2011.

		2010	2011
Revenue from externals (in GBP 000)		203,792	202,277
Total costs attributed (in GBP 000)	Other costs	4,246	11,466
	Fixed costs attributed to the operating segment*	987	1,166
	Variable costs attributed to the operating segment**	195,257	194,342
	Total costs	200,490	206,974
Operating profit / (loss)	Total	3,302	(4,697)

* Fixed costs are costs that are usually not dependent on the turnover of operations, e.g. maintenance charges, licensing fees, rental agreements, and fixed payments consistent with the contract for operating the hotels.

** Variable costs are costs that vary in line with operating turnover.

1.10.3 Structure of the operating segment and the applicable changes

A. United Kingdom (UK)

The UK comprises four countries – England, Wales, Scotland and Northern Ireland – together governed by a constitutional monarchy. The UK is a member of the European Union (EU), although it has not joined the monetary union (Eurozone) and it retains its own domestic currency – the pound sterling (GBP).

The UK has a population of more than 60 million and its economy is one of the largest in the world in terms of GDP (fifth largest in the world, and second largest in Europe). The UK was seriously affected by the global financial crisis that began in 2008, during which the British economy shrank sharply, the unemployment rate rose, property prices plummeted and the rate of inflation declined, despite a devaluation of the pound. The UK authorities adopted an aggressive economic policy to contain the economic crisis, which proved to be effective in bringing the crisis to a halt, and there are now positive signs that confidence in the markets is returning. Interest rates have remained low although inflation has increased partly due to an increase in the VAT rate to 20% in January 2011. Nevertheless, despite the improved economic atmosphere and expectations that the slowdown will be reversed, Britain's macroeconomic data continue to present a negative picture, mainly due to the high level of debt in the public sector and in the households sector.

UK GDP continued to improve through 2011 with the first quarter growing by 0.5%, the second by 0.1% and the third by 0.5% before the final quarter of the year declined by 0.2%. The full year saw GDP growth of 0.8%. The final quarter of the year was reportedly impacted by lower business investment levels across the UK. GDP growth forecasts for 2012 vary between 0.6% and 1% so essentially the same as 2011.

B. Structure of the motorway service stations market in the UK

As noted above, Roadchef holds 28 motorway service areas at 20 different locations in England, Scotland and Wales. Motorway service areas (including Roadchef's service stations) currently operate at 91 different locations throughout the UK. 88% of the market is divided among three key operators: Roadchef, Moto and Welcome Break. The other service areas (13 in all) are run by small operators. Roadchef accounts for 21% of the market (according to the number of locations that have service stations). As noted in Section 1.10.3 (C) below, the government closely supervises the erection and operation of service stations, and various restrictions apply. In view of these restrictions, the chance of another significant competing entity entering the service station market is small. Most of the competition between the different operators relates to obtaining franchise agreements with recognized brands that will attract potential customers on the roads to enter the service areas.

Overall, the retail and dining operations are the most profitable services offered by the service stations. Fuel products usually generate the highest revenues however gross profit rates from petroleum and diesel fuel are significantly lower than in the retail and catering sectors.

C. Legislative restrictions, standardization, and special constraints that affect this area of activity

The UK motorway service areas' market is controlled by the Highways Agency in Britain's Ministry of Transport. The erection and operation of a new motorway service area is approved subject to significant legislative requirements, and even after construction, restrictions apply to permitted operations, as well as supervision of signage and traffic directions from the motorway to the service station. These restrictions are designed mainly to ensure that the service areas do not become an attraction in their own right, thus increasing the number of cars using the motorways. Control of the motorway service areas market is reflected principally in two areas: 1) requirements for the erection of a service station (such as the number of parking spaces or the number of lavatories); and 2) restrictions on the activity permitted in the service areas.

The process of erecting service stations is long and costly and includes compliance with the requirements of government entities and local authority development plans in whose jurisdiction the motorway service areas are located. The main restrictions pertain to the distance between motorway service areas, and determine a distance of at least 28 miles or 30 minutes of travel time between the location proposed for erection of a new service area and the nearest existing service area.

The restrictions concerning the operation of motorway service areas include, inter alia, restrictions on the types of services provided (catering services, accommodation services, retail services, fuel, entertainment and amusement, as well as long-term parking are permitted), as well as restrictions on the products that may be sold – the sale of alcohol is prohibited, including in restaurants and hotels. In addition, the service stations must be open 365 days a year and provide round-the-clock forecourt services, catering services and short-term parking. In 2011 the Highways Agency advised that the current restrictions on the sale of alcohol may be reviewed with regard to hotels and grocery outlets at the sites but as yet the restrictions remain.

Restrictions also apply to the size of the areas that can be used for different types of services. Thus for example, the size of the area in each service area that can be used for retail trade is limited to 500 sq.m., the size of the areas used for slot machines is limited to 100 sq.m., and business lounges are limited to a maximum of 15 people. Restrictions also apply to the size and content of the signs positioned along the motorways directing drivers to the motorway service areas. In 2011, the Highways Agency advised that there may be changes to the restrictions on the size of areas. The Highways Agency also initiated new signage along the motorways in response to operator demands that signs provide details of available regarding the brands available at the station.

It is worth noting that as part of their operations, and like other businesses in the UK, all service areas must be licensed by the UK authorities to run the various services and facilities

at the service areas, such as: license to operate a petrol station, license to operate slot machines, etc.

D. Changes in the volume of activity and profit in this segment

As noted above, the process of erecting service stations is long and costly and extensive regulatory restrictions apply that impede their construction. As far as Roadchef is aware, only three additional motorway service areas are slated for construction over the next ten years. There are therefore few changes in number of operational service areas. Moreover, the variety of products that can be sold at the motorway service areas is also limited. As noted above, the Highways Agency has advised that there may be some relaxation of certain restrictions which will be to the advantage of the operators.

The volume of activity in the motorway service areas' segment is influenced by the total number of drivers on the motorways on which the service areas are located, the number that turn into the service area and by the volume of their purchases. According to estimates prepared by the different companies in the industry, about 300 million people pass through the UK's motorway service areas every year. About 60 million people pass through Roadchef's sites every year, and it is estimated that 37% of them purchase catering services, and 27% make a retail purchase. An economic crisis and/or change in the price of fuel that may affect the number of cars on the roads, may also affect the volume of activity and profitability of the service stations.

E. Principal success factors in the motorway service areas market and the applicable changes

Roadchef's principal success factors are:

- 1) the type and mix of the retail chains and food chains whose products and services are available at the service stations (known brands such as McDonald's, Costa Coffee, and WHSmith attract more customers);
- 2) effective signage, within the framework of the legal restrictions, that attract customers to the motorway service areas;
- 3) a broad range of available products and services, combined with new shops at the service stations;
- 4) constant improvement of the management and operation of the service areas so as to increase profits;
- 5) financial robustness that is required for investing in improving the products on offer at the existing stations and in the erection of the service areas;
- 6) finding suitable locations for the erection of motorway service areas that comply with the existing legislative restrictions;
- 7) conditions of the agreements with concessionaires and suppliers.

F. Principal barriers to entering the motorway service areas market

The UK's motorway service areas' market has high entry barriers, principally for the following reasons:

- 1) the need to find suitable locations for the erection of service areas, particularly taking in to account the existing legislative restrictions as noted in Section (C) above;
- 2) prolonged, costly planning procedures for the erection of each service area;
- 3) considerable investment in the actual construction of each service area.

The barriers to leaving the service station market are the high investment in entering the market and existing commitments towards third parties.

G. Effect of external factors on Roadchef's activity

The economic situation in the UK – may affect the number of vehicles on the roads, in part depending on the severity and duration of the period in which it continues.

Changes in public transport arrangements – changes and improvements in public transportation arrangements that may lead to the supply of means of transport that replace private cars may reduce the number of drivers on the motorways and adversely Roadchef's revenues.

Legislative restrictions and changes – the existing legislative restrictions regarding the operation of motorway service stations in the UK may affect Roadchef at two levels: a) the abolition of legislative restrictions regarding the required distance between service areas may lead to the erection of more service areas, which will affect the revenues generated by Roadchef's existing service areas, but could also provide an opportunity for an expansion of Roadchef's activity; b) the failure to grant relief in existing legislative amendments with respect to the positioning of signs along the motorways and the sale of products at the service areas may make it difficult to increase revenues.

The extent to which Roadchef is affected by these events, if at all, depends on their intensity, scope and duration, and on Roadchef's ability to address them in future.

1.10.4 Products and services

The products and services marketed by Roadchef in this operating segment mostly include the following:

- A. Retail products – according to existing regulatory restrictions, the variety of retail products that can be sold at motorway service areas is restricted to products that drivers require when on the road. These include food products (snacks, sandwiches, etc.), books, newspapers and magazines, tobacco products, gifts, and in the convenience stores at the refueling stations, car accessories and cleaning products. Over the last thirty years, the variety of products that can be sold has changed very slightly nevertheless, the volume of sales has grown substantially.

It is worth noting that Roadchef's competitors have begun to operate branded grocery stores such as Marks & Spencer, Simply Food, and Waitrose at their motorway service areas. Roadchef believes that these stores, together with other categories of retail products (such as pharmacies, mobile phones, and clothing stores) contain considerable potential for increasing retail revenues, insofar as the sale of these products is possible.

- B. Catering – Roadchef operates a variety of self-service restaurants at its service stations, offering a range of hot and cold meals, fast food (hamburgers and chicken products), salads, snacks, hot and cold drinks, sandwiches, cakes and desserts. The catering services consist of restaurants under an external brand, or under Roadchef's own brand names (i.e. The Burger Company, RestBite, and Hot Food Company). In recent years, Roadchef has expanded the catering services it offers under leading, well-known brands such as McDonald's, Pizza Hut, Costa Coffee, and SOHO Coffee, through franchise agreements.

It is worth noting that the prices of products sold at the service areas through the retail and dining activity are, with the exception of McDonald's, generally higher than the prices of these products in the cities.

- C. Fuel products - 28 petrol stations operate at the service stations, and in accordance with regulatory provisions, petrol stations must be open 24 hours a day, 365 days a year. Convenience stores are located next to the petrol stations.

The petrol stations operate in several forms:

1. Independently operated – the petrol stations that Roadchef operates according to agreements for the supply of fuel with external petroleum companies (Texaco, Esso, BP, and Shell). At the reporting date, there are six petrol stations that operate in this form.
2. Agency agreements – petrol stations in which the petroleum companies hold proprietary rights, and Roadchef serves as an agent and sells fuel and other products as per an agreement with the relevant petroleum company. At the reporting date, six petrol stations operate in this manner.
3. Licensing agreement⁵⁹ – Roadchef receives a license to operate a petrol station where the proprietary right in the station is that of the petroleum company. At the reporting date, there are two petrol stations that operate in this manner.
4. Rental – Roadchef operates some stations in accordance with rental agreements with the petroleum companies. At the reporting date, there are two petrol stations that operate in this manner.

⁵⁹ It should be noted that the operation of petrol stations through agency agreements and licensing agreements are essentially similar – the actual agreement is determined by the petroleum companies.

5. Leasing to outside operators – in agreements of this kind, Roadchef holds the proprietary right to the petrol station, and gives one of the fuel supply companies exclusive rights to operate the station in return for a fixed rent, and the rent is derived from the quantity of petrol sold. At the reporting date, six stations are leased to BP Oil UK Ltd.
6. Petrol stations operated by the petroleum companies that also hold the proprietary rights in the stations. These petrol stations do not generate any income for Roadchef. At the reporting date, there are six petrol stations that operate in this manner, two of which are run by BP.

It is worth noting that in May 2009, Roadchef entered into an agreement with BP, whereby BP gradually began to rent from Roadchef the leasing rights, management and operating rights to 14 petrol station forecourts and adjacent convenience stores in the service areas (including two forecourts that it had already leased by virtue of agreements that were signed by the parties in the past). For further details about this agreement, see Section 1.10.17 (B) below.

- D. Accommodation – Roadchef operates 15 hotels located in the motorway service areas. Until 2010, the hotels were run under the Premier Inn brand. During the course of 2010, Roadchef entered into 15 separate agreements with Days Inn (Wyndham Worldwide) to operate the hotels on Roadchef's motorway service areas that hold 632 rooms in all, for a period of 20 years from September 2010, where Roadchef may end each of the agreements after 10 years. Roadchef runs and manages the hotels on an on-going daily basis. The hotel rooms are reasonably equipped, and provide various services of the type generally accepted at budget hotels. It should be noted that during 2009, 2010 and 2011, the average occupancy rate was 46%, 54% and 41% respectively.
- E. Other services – as part of the agreements that Roadchef reached with commercial companies and various service providers that render services and/or provide different products at the service areas, such as: parking areas, cash points [ATMs], the sale of advertising space at the stations, slot machines, passport photo machines, massaging recliners, public telephones, and mobile phone accessories. These agreements create additional revenue for Roadchef in respect of rent, and amounts that are a certain percentage of the operator/service provider's profit, all as prescribed in the agreements.

1.10.5 Breakdown of revenues from products and services

The following shows the distribution of Roadchef's revenues by category of product and service in 2009-2011 (in GBP thousands, as a % of the Group's net revenues, and % of revenues from motorway services): ⁶⁰

	2011			2010		
	GBP 000	As % of Group's revenues	As % of revenues from sector	GBP 000	As % of Group's revenues	As % of revenues from sector
Retail products	42,293	0.4%	20.8%	46,273	0.6%	22.9%
Catering	64,191	0.6%	31.5%	58,095	0.8%	28.7%
Fuel products **	83,115	0.8%	40.8%	81,624	1.1%	40.3%
Accommodation	3,355	--	1.6%	4,832	0.1%	2.4%
Other Services	10,838	0.1%	5.3%	11,453	0.1%	5.7%
Total	203,792	1.9%	100%	202,277	2.6%	100%

* The figures reflect revenues in respect of the holding of 25% of the issued and paid-up capital of DMS by Delek Petroleum for those years.

** After signing the BP agreement in May 2009, whereby petrol stations will be leased to BP (for details see Section 1.1.17 (B) below) and given that the leasing of the stations also includes the convenience stores, revenues from the convenience stores at the petrol stations run by BP do not belong to Roadchef thus reducing the revenues received from retail products and fuel products.

⁶⁰ It should be noted that from May 2009, Roadchef presents the rent from the leasing of petrol stations to BP as part of the reduction of variable costs for each site, and they therefore do not appear in the table.

1.10.6 Marketing and distribution

Following is a concise description of Roadchef's marketing methods:

- A. General – motorway service area marketing activity, aimed at attracting customers to the service stations and helping to market all Roadchef's activity, is divided into two stages: marketing activity aimed at encouraging customers to stop at Roadchef's motorway service areas, and marketing activity to motivate travelers who have stopped at the service areas to make purchases while they are on site.

Regarding the first stage – most of the effort focuses on signage directing travelers to the service areas. Strict regulatory restrictions apply to signage positioned along the motorways with respect to the service areas limiting the ability of the chains or companies that provide services at the service stations to advertise. Within the context of the existing restrictions, Roadchef (and the other companies that operate motorway service areas) lists the names of the most popular brands available at each service area on the way finding signs. As noted above, recent changes announced by the Highways Agency will improve brand signage from the roadside. For the second stage – most of the effort is invested in dominant brands to increase the amount of shopping that takes place at the service stations.

In addition, Roadchef regularly conducts sales promotion campaigns in order to encourage repeat visits to the service areas, and it also works to cooperate with different companies in an effort to promote Roadchef among their employees and/or customers.

- B. Marketing of retail products – the branded retail shops are usually located in a central building on the service area. The convenience stores are located adjacent to the forecourts and set apart from the service area's main building.

Retail products are sold mostly in two ways:

1. By shops run by Roadchef under the brand name WHSmith ("WHS"). These shops are managed and operated as part of a franchise agreement signed between Roadchef and WHS, that also stipulates the manner in which the WHS brand and its related trade names can be used, and the consideration that Roadchef pays for the franchise, through supply agreements between Roadchef and WHS regarding the supply of some of the products sold in the shops, and in agreements with additional product suppliers whose products are sold in these shops. It should be noted that under the signed agreement with WHS, WHS may enter into similar agreements with other companies that operate motorway services areas. (In practice, WHS has pre-existing agreements with two of Roadchef's competitors.)
2. Through convenience stores – convenience stores operate in the forecourts that are set apart from the main service station building and which sell various products, such as: car products and accessories, hot and cold drinks, fast food (pastries, sandwiches, etc.). The operation and management of the convenience stores is usually prescribed in the agreements for the sale of petrol that Roadchef enters into with the different petroleum companies. These agreements also determine the composition of the products to be sold in the convenience stores, display arrangements in the convenience stores and their pricing method. Each agreement contains standard grounds for early termination of the agreement by the parties (including, inter alia, the operation of the petrol stations contrary to the agreement, the failure to pay the amounts stipulated in the agreement, fundamental violation of any of the conditions of the agreement, etc.).

- C. Marketing of catering products – Roadchef operates catering services under the Roadchef brand name (45 fast food outlets or restaurants) and where the dining services are operated under franchise brand names (e.g. McDonald's, Costa Ltd. and SOHO Coffee Shops Ltd. – 35 restaurants in all), the operations are dictated by the conditions of the franchise and the license prescribed with the franchise owner in the franchise agreement. It should be noted that there are several restaurants at each service area, operating under different brands, all of which are run by Roadchef.

In 2011 Roadchef closed the last of its Wimpy franchised restaurants replacing the offer with either its in-house offer The Burger Company or its franchised McDonald's offer. Roadchef settled the early termination agreement with Wimpy and has no ongoing relationship with the brand.

- D. Marketing of the accommodation activity – in addition to the branding support that Roadchef receives from Days Inn, Roadchef uses a special consultant and manager to promote its

accommodation activity and to increase occupancy through travel agents and direct marketing initiatives.

1.10.7 Order backlog

In view of the nature of Roadchef's activity and the fact that most of its sales are made to random customers, Roadchef has no order backlog.

1.10.8 Customers

Roadchef's target customers are all motorway travelers. Nevertheless, vehicles can be divided into several categories, such as private cars, buses/coaches, trucks (light and heavy load) and motorbikes. Some of the motorway service areas can be characterized by the class of vehicles that pass through them.

Other categories of customer are families with children, business travelers, holidaymakers, groups and organized tours, who are more likely to visit the service stations and spend money at them. It should be noted that Roadchef maps its customers based on the reason for their journey – business or pleasure.

Roadchef is not dependent on any single customer.

1.10.9 Seasonality

Roadchef's activity is characterized by seasonality, with most activity taking place in the summer months (July to September) and the school holidays. There are differences between the various sites depending on their characteristics, so that at sites located on routes to leisure spots, levels of activity are higher during the holidays, and at sites located along routes leading to business centers, there is more activity during the week than at weekends.

The following details Roadchef's revenues (in GBP thousands), by quarter in 2011 and 2010:

Year	Q1	Q2	Q3	Q4	Total
2011	42,411	55,117	62,457	43,807	203,792
2010	42,375	54,128	59,721	45,553	202,277

1.10.10 Fixed assets and plant

The following details the motorway service areas and real-estate assets on which the service stations operate:

- A. The service areas are at 20 different locations along the motorways in England, Scotland and Wales (eight service areas are located on both sides of the motorway, so that in all Roadchef operates 28 service stations). The motorway service areas occupy a land area of 2,459 dunam (245 hectares). The service areas house petrol stations, hotels, restaurants, retail shops and coffee stands, with total floor space of 61,300 sq.m. The land area on which each service area is built is usually quite large, to accommodate the range of services offered. The area varies for each station depending on the design features, date on which it was constructed, and the volume of traffic on the adjacent motorway.
- B. Each service area has an area on which the main building is located which contains the retail shops, restaurant services, slot machine halls and restrooms. There is a parking lot and a hotel (at some stations) next to the main building. The petrol station forecourt and adjacent convenient store are set several hundred meters away from the main building.
- C. The most prominent service areas operated by Roadchef are Strensham, located on the M5, Watford Gap on the M1, Clacket Lane on the M25, and Norton Canes on the M6 Toll. The difference in revenues generated by the service stations is generally the result of the volume of traffic on the adjacent roads, as well as the characteristics of the drivers who use those roads (for example, drivers who use the roads for traveling to work and back usually stop less than holiday travelers).
- D. Roadchef operates systems that provide information about the number of people visiting the service stations and how many people make purchases at the service stores, the types of products they buy and changes in this information at different times of day. Roadchef uses this information to increase the number of purchases made at the stations.
- E. The real estate assets on which the service stations operate are partly wholly owned by Roadchef (seven assets), partly leased for long periods of more than 70 years (four assets),

and the rest are on medium-term leases (less than 70 years).⁶¹ All the assets are located in England, with the exception of two in Scotland and one in Wales. The offices of MSA and Roadchef's management are located at Roadchef House at the Norton Canes service station in Cannock. Roadchef holds this asset in accordance with a rental agreement that is in force until 2029.

The following details the proprietary rights at the service stations operated by Roadchef.

Name of station	Built in:	Description of proprietary rights
Annandale Water	1995	Leasehold - 2093
Hamilton & Bothwell	1984	Leasehold– 2034
Chester	1998	Leasehold– 2148
Clacket Lane*	1993	Leasehold - 2043
Durham	1994	Owned
Killington Lake	1972	Owned
Magor**	1992	Leasehold - 2042
Maidstone	1997	Leasehold - 2122
Northampton	1982	Leasehold - 2032
Norton Canes	2004	Leasehold - 2029
Pont Abraham	1982	Owned
Rownhams	1976	Owned
Sandbach	1976	Leasehold - 2031
Sedgemoor	1986	Owned
Stafford	1999	Leasehold - 2124
Strensham (North)*	2002	Leasehold - -2042
Strensham (South)*	1992	Leasehold - 2032
Taunton Deane	1977	Owned
Tibshef	1999	Owned
Watford Gap	1959	Leasehold - 2032

* The site's EBITDA earnings account for more than 10% of Roadchef's total EBITDA profit.

** Purchased in August, 2011.

- F. In addition to the foregoing, Roadchef has fixed assets that include equipment located at the service stations, including equipment required for operating the petrol stations, retail shops and restaurants, furniture and computers.
- G. H. The revenues from each of the service areas Strensham (north and south combined), Clacket Lane, Taunton Deane, Hamilton and Bothwell account for more than 10% of Roadchef's total revenues; discounting the fuel activity, the revenues from each of the service areas Strensham (north and south combined) and Clacket Lane, account for more than 10% of Roadchef's total revenues.

1.10.11 Intangible assets

Roadchef holds the following intellectual property rights:

- Registered trademarks – Roadchef owns the registered trademark "Roadchef" and its logo. Roadchef and the companies it owns also hold several trademarks that are registered with the UK Registrar of Trademarks;
- trademarks that are not registered – Roadchef owns the rights to the Takeabreak trademark, which is not registered. Likewise, Roadchef is entitled to trade under other trademarks, although it does not use them;

⁶¹ Norton Canes that is leased until 2029, is owned by one of the owners of one of the service station chains in competition with the Company.

- c) domain names – Roadchef owns the domain names: roadchef.co.uk, roadchef.com and roadchef.net;
- d) copyright – Roadchef is the owner of all the copyright and intellectual property on its website content;
- e) permits to use trademarks – Roadchef has permits to use trademarks consistent with the franchise agreements signed with branded companies, such as: McDonald's, Costa Coffee, WHSmith, etc. It should be noted that the rights to use these trademarks do not confer proprietary rights on Roadchef;
- e) third-party permits – from time to time Roadchef's trademarks are used by third parties and suppliers for marketing and advertising purposes by obtaining unofficial permits from Roadchef.

1.10.12 Human capital

- A. At the reporting date, Roadchef (including its subsidiaries) has 2,287 employees, as detailed below, most of whom work at the motorway service areas that it operates:

Department	No. of employees & service providers at December 31, 2011	No. of employees & service providers at December 31, 2010
Senior management	4	5
Management	49	49
Service station employees	2,234	1,946
Total	2,287*	2,000

*Including Magor, purchased August, 2011.

In 2011, the total number of service area employees consists of 1,439 workers employed in catering activity, 391 employed in retail activity and the petrol station forecourts, and 404 administrative and management employees.

During the course of 2011 and 2010, there has been an increase in the number of Roadchef employees in catering activity. The increase in the number of Roadchef employees in 2011 compared with 2010 can be attributed to the opening of eight additional McDonald's restaurants pursuant to the agreement with McDonalds.

- B. Benefits and the quality of employment agreements

Roadchef's employees are divided into three categories, consistent with their employment agreements:

Hourly paid employees – most workers at the service areas are paid on an hourly basis and are employed according to Roadchef's fixed employment agreements. Workers at the service areas work in shifts, sometimes including overtime, and most of them receive the minimum wage set in the UK, plus a wage for overtime and/or work on public holidays (where necessary), as prescribed in UK labor laws. As part of their employment agreements, all workers are entitled to annual vacation as well as a pension plan after a certain period of work. It should be noted that under UK labor regulations, hourly paid employees who are temporary, are entitled to the same rights as permanent employees.

Service area and salaried management – management employees at all service stations, as well as Roadchef's management employees, who work at Roadchef's offices, are entitled to a global salary and their employment is regulated by standard managerial agreements. It should be noted that the management structure is based on a set of principles for managing a service area based on the size of the operation and sides of the road although there may be local differences based on historical agreement. Under the management agreements, management employees are entitled to annual vacation, a pension plan (the payments into the pension plan are made by the employee and Roadchef), life assurance, medical insurance (for Site Directors), reimbursement of expenses (in certain conditions), an annual bonus, and senior management employees are also entitled to use of a company car if they need to travel long distances for work. In addition, the management agreements include provisions concerning the severance of employment, confidentiality, and a non-competition clause.

Senior management and the chief managers of the service areas – Roadchef's senior management and the chief managers of the service stations are entitled to a global salary and

they are employed on personal employment contracts. As part of their employment agreements, these employees are also entitled to pension arrangements, medical insurance, annual vacation, a company car or the right to use a car, refund of expenses and an annual bonus.

Roadchef has two pension plans and at the end of 2011 they have a deficit of GBP 3.9 million. Nevertheless, Roadchef has long-term payment arrangements that will wipe out the deficit and create a surplus in these plans.

C. Employee compensation plans

Hourly paid employees enjoy several bonus plans commensurate with their performance and with meeting sales targets.

The management staff of the motorway service areas, Roadchef's managerial employees, chief managers of the service stations and Roadchef's senior management are entitled to an annual bonus, as follows: The service station management employees and the chief managers of the service stations are entitled to an annual bonus, fixed as a certain percentage of their wage based on the annual operating profit of the relevant service station before interest, tax and depreciation (EBITDA) as noted in their employment agreements. It should be noted that the service area managers are entitled to a higher bonus; Roadchef's management employees and senior management are entitled to an annual bonus fixed as a certain percent of their wage and based on Roadchef's annual operating profit before interest, tax, and depreciation (EBITDA) as noted in their employment agreements. It is worth noting that senior management employees are entitled to a higher bonus.

D. The company's senior officers and senior executives

1. The following details the number of employees and service providers that form the company's senior officers and senior executives:

	No. of employees
Acting Chairman	1
CEO	1
Business Development Director	1
CFO	1
Chief Operating Officer	1
Total	5

2. **Benefits and quality of the employment agreements**

Roadchef's senior officers and senior executives are employed according to personal employment agreements that include pension arrangements on a variety of tracks, a bonus plan, and related benefits (such as a company car and insurance arrangements). The acting chairman is also entitled to share based payments.

Roadchef is not dependent on any particular employee.

1.10.13 Raw materials and suppliers

Roadchef has agreements with several suppliers, consistent with its various operations. The main suppliers that Roadchef has agreements with as part of its retail activity are Palmer & Harvey and WHSmith; as part of its catering operations, Roadchef has franchise agreements with fast-food and coffee-shop chains such as McDonald's, SOHO Coffee, Costa Coffee, etc. (together in this section: "the Chains"), from which Roadchef is committed to purchase most of the raw materials it requires and/or from suppliers the chains have approved in advance. The raw materials for the restaurants that operate under Roadchef's independent brands are supplied mainly by the Brakes Group; for fuel sales, the petroleum companies that operate and/or lease the forecourts are also the suppliers of the fuel. Regarding the service areas that Roadchef operates independently, Roadchef has supplier agreements with the large petroleum companies.

Roadchef is not dependent on any particular supplier.

- A. **Service station operating inventory** – inventory is held so as to allow on-going sales without creating a shortage of products, at the same time maintaining reasonable levels of inventory.

Inventories are monitored at all service stations, according to the type of inventory and amount of stock that can be held at any given time.

- B. Accounts receivable – customer credit that is usually created as a result of the use of credit cards at the service stations, accounting for about 50% of Roadchef's total sales. This credit is usually paid within 3 or 4 days.
- C. Suppliers' credit – is usually 30 – 45 days. The following details the average volume of credit and average number of credit days to suppliers (calculated on an annual basis) in 2009 – 2011.

Year	Average volume of credit (in GBP 000)	Average credit days (in days)
2011	12,737	39
2010	13,035	42

- D. Deficit in working capital – is due to short-term bank credit, taken by Roadchef. At December 31, 2011, DMS had a deficit in working capital of GBP 52 million (about NIS 308 million), including a balance of GBP 40.1 million (about NIS 237.5 million) of credit from banks. The credit limit of GBP 14.5 million (about NIS 85.9 million) have been replaced with a long term loan of 5 years on January 2012 and the other credit was renewed on February 2012. The balance of the deficit in working capital in the amount of GBP 11.9 million (about NIS 70.1 million) can be largely attributed to suppliers' credit given during the normal course of Roadchef's activity and it is expected that the availability of the credit will be preserved continuously in the foreseeable future.

1.10.14 Financing

A. General

Roadchef finances its on-going operations from the following sources:

- 1) current revenues from motorway service areas;
- 2) short-term bank credit;
- 3) suppliers' credit;
- 4) advances received from suppliers and/or franchise companies with which Roadchef has franchise agreements;
- 5) owners' loans.

Roadchef's long-term investments were financed by raising debt during the course of 1998, in a securitization process, and through a loan of GBP 23.5 million received from Barclays Bank in 1999, which was fully repaid on October 2011.

B. Short-term credit

1. Bank loans

At 31 December, 2011, Roadchef had short-term loans that it received from Barclays Bank in the amount of GBP 21.2 million and an overdraft facility of GBP 2.0 million. Following the renewal of the facilities with Barclays in February 2012 the Group now has short-term loans of GBP 12.735 million, an overdraft facility of GBP 2.0 million and a long-term loan of GBP 14.5 million (see 1.1.14 (C)(3) below).

During 2011, Roadchef received a loan of GBP 10.0 million from Bank Leumi (UK) to fund the acquisition of First Motorway Services and to fund the development of its existing sites. The loan and overdraft bear interest of LIBOR + 1.75% and is repayable on demand. The loan from Bank Leumi (UK) is secured by Delek Group guarantee.

Long-term loans

2. Owners' loans

From 2007, MSA via DMS UK received loans from companies owned by its then controlling shareholders, Delek Belron and Delek Petroleum, with an overall value of GBP 162.1 million. One loan of GBP 150 million bore interest of 6.5% (linked to the CPI), and the balance of GBP 12.1 million bore interest of LIBOR + 2.65%. It should be noted that

MSA received a commitment from the lending companies that repayment of the loans and the interest they accrue will not be requested before January 1, 2013. At December 31, 2011, the outstanding balance of the loans is GBP 231.6 million. Following the transfer of ownership to Delek Petroleum Limited on 19 January, 2011, the loan, which was denominated in Israeli shekels, was denominated in GBP and was converted to non-interest bearing.

3. Capital raised in a securitization process

In December 1998, Roadchef completed a securitization process in which context RoadChef Finance Ltd., a special purpose subsidiary ("the SPV") raised GBP 210 million on the Luxembourg stock exchange. The consideration received by the SPV was extended as loans to some of the companies in the Roadchef Group ("the Borrowers") for purposes prescribed in the issuance. The following bonds were issued in the securitization process:

1) Bonds (Series A1) in the amount of GBP 35 million bearing variable interest that were repaid in 2008;

2) bonds (series A2) in the amount of GBP 133 million bearing interest at a rate of 7.418 (paid once a year on October 31), to be repaid in pre-determined installments from 2009 through 2023;

3) bonds (Series B) in the amount of GBP 42 million, bearing interest at a rate of 8.015% (paid once a year on October 31), to be repaid in pre-arranged installments from 2023 until 2026.

It should be noted that if the issuing company does not have enough capital to pay the interest and the principal in respect of the bonds (Series B), these payments shall be postponed to the payment date on which the issuing company has adequate capital for payment and they shall bear interest until that time. Payment of the principal and the interest in respect of the Series A2 bonds shall take preference over payment of the principal and interest in respect of the Series B bonds. At the reporting date, the Series A2 bonds and Series B bonds have a rating from Fitch Ratings Ltd. of B+ and B- respectively, and are rated B- and CCC+ respectively by Standard & Poor's. The balance of the bond principal (excluding accrued interest and surplus cost attributed at the time of the MSA acquisition in 2007) at December 31, 2010 and December 31, 2011, was GBP 164 million and GBP 158 million, respectively.

4. Loans from Barclays Bank

Following the renewal of the Development Group facilities in February 2012, the company has a long-term loan with Barclays of GBP 14.5 million, which replaced a short-term loan.

5. Money received from Lloyds Bank

The Group received a loan from Lloyds Bank plc in August 2011 to fund the acquisition of First Motorway Services Limited. The loan of GBP 8.145 million bears interest of LIBOR + 1.75% and is repayable in equal annual instalments from 2103 until 2016. The Group hedged GBP £6 million of the loan to fixed interest of 1.795%.

6. Money received as part of the franchise agreements

As part of some of the franchise agreements signed with the brand owners, Roadchef received Partner funding from the brand owners to support the catering development and improving the shops and services rendered under the franchise agreements.

7. Advance from BP on account of rentAs part of the BP agreement, described in Section 1.10.17 (B) below, during the course of 2009 and at the beginning of 2010, Roadchef received a total sum of GBP 10 million as a down payment for rent that BP will pay during the agreement period.

C. Average interest

The following shows the average interest rate on loans from banks and non-banking sources of credit, that are in force on the reporting date and that are not for the exclusive use of Roadchef:⁶²

⁶² The interest rates refer to actual interest payments, excluding accounting adjustments.

	Average interest rate during 2010		Effective interest rate during 2010	
	Short-term loans	Long-term loans	Short-term loans	Long-term loans
From banks	6.34%	-	6.34%	-
From non-banking sources	-	7.69%	-	7.69%

	Average interest rate during 2011		Effective interest rate during 2011	
	Short-term loans	Long-term loans	Short-term loans	Long-term loans
From banks	4.72%	3.70%	4.72%	3.70%
From non-banking sources	-	7.64%	-	7.64%

D. Restrictions that apply to Roadchef in accepting credit

1. Financial criteria determined for the issuance of bonds by Roadchef:

In addition to placing a lien on assets, as noted in Section (K) below, the bond issuance agreement prescribes several financial criteria and covenants that the borrowers must comply with. The main points of these covenants are detailed below:

- A) The EBITDA ratio on the annual payment to the bond holders plus interest expenses ("Profit Ratio") shall not be less than 1:1.25. Compliance with this ratio is examined quarterly, in accordance with Roadchef's consolidated and unaudited financial statements for that quarter, to be submitted within 45 days of the end of the quarter. At the end of a quarter that ends the financial year, compliance with this ratio is examined in accordance with Roadchef's annual audited consolidated financial statements, to be submitted within 120 days of the end of the quarter.

It should be noted that under the conditions of the bond issuance agreement, a failure to comply with the aforesaid ratio can be remedied within 120 days of reviewing the ratio ("the Grace Period"), inter alia, by the owners or another entity providing the borrowers with additional equity.

It should be noted that since the date on which Delek Belron acquired the controlling interest in Roadchef, there were instances in which DMS supplemented the necessary capital during the Grace Period (so that Roadchef was not in violation of the agreement) by injecting capital into the SPV, originating in DMS' activity and/or by injecting owners loans from DMS' shareholders. In 2007, to comply with the financial criteria, additional equity of GBP 1.5 million was extended for this purpose, and in 2008 and 2009, a total of GBP 6.5 million and GBP 5.9 million, respectively, was provided.

At December 31, 2011 and close to the reporting date, the profit ratio was 1.25 and 1.48 respectively.

- B) An undertaking not to engage in any other activity besides the operation of the motorway service areas (including providing catering services, retail, leisure, and accommodation services, and the sale of fuel) and only to perform transactions that are the normal course of business of the Roadchef Group's companies.
- C) All the companies in the Roadchef Group (excluding MSA) may transfer their assets, areas of activity and property to the other companies in the Roadchef Group (including MSA) without the need to obtain prior permission from the bond trustee and provided that another asset with similar features is pledged in favor of the trustee.
- D) Restrictions on carrying out the following activities without obtaining the bond trustee's approval: exercising an unpledged asset with a value of more than GBP 5 million; entering into a leasehold contract or license for a period of more than 25 years; entering into a leasehold contract or license for a period of less than 25 years that is not during the normal course of business; granting loans to companies that are not part of the Roadchef Group or to any other third party, unless, when the loan is granted, Roadchef

has profit ratio of 1:1.5 during the 4 quarters preceding the loan, and that the EBITDA in the quarter before the loan is at least 90%, or that the loan was given during the normal course of business and the amount that has yet to be repaid is at less than GBP 1 million at any time; distribution of a dividend, capital repayments, capital distribution and any other distribution, unless at the time of the distribution Roadchef has a profit ratio of more than 1:1.5 for the 4 quarters preceding the distribution and that the EBITDA in the quarter before the distribution is at least 90%, or that one of the rating companies has announced that the distribution will not affect the rating of the bonds, or that the bonds are rated, the profit ratio is 1:1.5 and the total value of the Roadchef Group's assets is more than 200% at least of the balance of the debts that have not been repaid under the bond agreement; granting loans to employees of any of the Roadchef Group's companies, unless the outstanding debt that has not yet been repaid is less than GBP 1 million at any time.

Moreover, the bond agreement prescribes several alleviating conditions whereby the borrowers will be able to exercise pledged assets when certain conditions are met (some of which must be approved by the trustee), and they will also be able to acquire additional business activity, provided that the bond trustee give his approval that one of the conditions prescribed in the bond agreement, and pertaining to the manner of financing the acquisition, is met. In addition, pursuant to the provisions of the bond agreement, the borrowers are entitled to take action to develop the pledged assets, as they are defined in Section 1.10.18 below, without obtaining the bond trustee's prior approval under the conditions of the bonds, and including even to take loans of up to GBP 20 million.

The trust deed in respect of the issued bonds prescribes various undertakings and restrictions on the SPV, such as negative lien, prohibition on other activities, prohibition on paying a dividend and other activities that may not be performed without first obtaining the bond trustee's approval.

At the reporting date, Roadchef is in compliance with all the foregoing conditions.

E. Credit received between the date of the financial statements and close to the date of the report.

During the period between the reporting date and immediately prior to the date of the report, additional credit was of GBP 3.5 million was received from Barclays following renewal of the facilities of the Security and Development Groups.

F. Credit limits

At December 31, 2011, Roadchef's total credit limits were GBP 43.38 million, of which GBP 10.0 million was repayable on demand, GBP 22.235 million was in the process of being renewed, GBP 3.0 million was in force until October 2012 and GBP 8.145 million was in force until February 2016.

At the reporting date following the renewal of the facilities in January and February 2012, Roadchef's total credit limits were GBP 47.38 million of which GBP 10.0 million was repayable on demand, GBP 14.735 million is in force until December 2012, GBP 8.145 million is in force until February 2016 and GBP 14.5 million is in force until February 2017. Of these credit limits, at December 31, 2011 and close to the date of the report, GBP 41.276 million and GBP 43.876 million respectively have been utilized.

G. Credit at variable interest

The following details credit at variable interest:

Change mechanism	Range of interest 2010 (in %)	Range of interest 2011 (in %)	Amt. of credit (in GBP 000) at 31.12.2010	Amt. of credit (in GBP 000) at 31.12.2011	Interest rate at 31.12.2011 (in %)
LIBOR +	4.0	4.0	7,000	7,000	5.02
Base interest +	3.5-4.0	4.0	2,771	4,000	4.50
LIBOR +	2.1	2.1	11,235	11,235	2.73
LIBOR +	-	2.75	-	12,145	3.77
LIBOR +	4.0-9.0	4.0-9.0	3,000	3,000	5.47

Following renewal of the facilities the following credit is at variable interest:

Change mechanism	Range of interest 2011 (in %)	Range of interest at reporting date (in %)	Amt. of credit (in GBP 000) at 31.12.2011	Amt. of credit (in GBP 000) at reporting date	Interest rate close to the date of the report (in %)
LIBOR +	4.0	4.0	7,000	-	-
Base interest +	4.0	2.0	4,000	3,000	2.50
LIBOR +	2.1	1.75	11,235	11,735	2.89
LIBOR +	-	2.0	-	5,800	3.08
LIBOR +	2.75	2.75	12,145	12,145	3.83
LIBOR +	4.0-9.0	4.0-9.0	3,000	-	-

H. Credit at fixed rates

The following details credit at fixed interest:

Change mechanism	Range of interest 2011 (in %)	Range of interest at reporting date (in %)	Amt. of credit (in GBP 000) at 31.12.2011	Amt. of credit (in GBP 000) at reporting date	Interest rate close to the date of the report (in %)
Fixed 1.795% +	2.75	2.75	6,000	6,000	4.55
Fixed 1.57% +	2.50	2.50	-	8,700	4.07

- As of February, 2012

I. The company hedged GBP 6 million of the GBP 8.145 million loan received from Lloyds Bank PLC at a fixed rate of 1.795% against LIBOR and post balance sheet date, hedged GBP 8.7 million of GBP 14.5 million loan from Barclays at a fixed rate of 1.57% against LIBOR.

J. Other sources

Roadchef estimates that, following the renewal of the facilities of the Development and Security groups in January and February respectively, it will only need other sources of finance to accelerate the site development programme, but will not need other sources of finance for its on-going operations in the coming year.

K. The liens that apply to Roadchef's assets

1. The debt in respect of the securitization process was guaranteed by liens that, inter alia, include a fixed senior lien on 16 of the service stations that Roadchef operates ("the Pledged Service Stations"),⁶³ as well as several fixed liens on the borrowers' current and future rights in the pledged stations, on all their property and assets in England, Scotland and Wales, on the issued capital of all the subsidiaries owned by the borrowers, and on the intellectual property rights, rights by virtue of agreements and contracts, and licenses and permits owned by the borrowers. Likewise, a floating charge was placed on all the assets of the borrowers that were not pledged in a senior lien ("the Pledged Assets").
2. The short-term loans and credit limits, as specified in sections 1.10.14 (B) and (G) above, were guaranteed by pledging three service stations that are not included in the pledged service stations defined above. A total of GBP 11.235 million was also guaranteed by placing a lien on the pledged assets to the bond owners. Furthermore, assets belonging to subsidiaries of Roadchef that hold the three aforementioned service areas, as well as Roadchef's holdings in these companies, were pledged to Barclays Bank.

⁶³ It should be noted that the pledged stations also serve as collateral for part of the loan received from Barclays Banks, described in Section 1.1.14 (K) (1) above, as per the bond owners agreement that should the loan from Barclays Bank and the bonds be made available for repayment at the same time and there is a need to exercise the lien on the pledged stations, the repayment of the loan from Barclays Bank shall take precedence over repayment of the bonds.

1.10.15 Taxation

A. The applicable tax laws

DMS, which holds Roadchef shares, is domiciled in the Jersey Islands. When Roadchef's shares are sold and when certain conditions are met, DMS will not be liable for capital gains tax.

MSA and Roadchef are both incorporated in the UK. The following provides a brief description of the tax laws applicable in the UK:

Corporate tax: At the reporting date, corporate tax in the UK is 26% for companies with profits of more GBP 1.5 million (for a limited group of companies, profits are divided among the number of companies in the group). Profits below this amount are liable for tax at lower rates. A company that is not domiciled in the UK for tax purposes, that generates revenues in the UK not by way of a Permanent Establishment, may be liable for corporate tax at a rate of 20%.

The following changes in the tax rates made in the Budget in March 2011 will affect Roadchef: a) change in the rate of corporate tax from 26% to 23% over a three-year period from April 1, 2011; b) ordinary and special depreciation rates on assets will be lowered to 18% and 8% respectively, from the accounting periods ending after April 1 2012. As of the reporting date only the decrease of the tax rate to 25% was enacted and will start from April 2012.

Capital gains tax: The ordinary corporate tax rates apply.

Tax on dividends: Income from dividend received from a company domiciled in the UK is tax exempt. Dividend received from a company not domiciled in the UK is liable for tax in the UK, although a credit will be given if tax was withheld when the dividend was distributed. Under internal provisions of law, distribution of a dividend by a UK domiciled company is not subject to tax withholding at source.

B. Final tax assessments

DMS has not issued final tax assessments since it was established. Roadchef and most of its subsidiaries that operate in the UK have final tax computations submitted up to 2010.

C. Losses carried over for tax purposes

DMS and Roadchef have business losses and capital losses for tax purposes that are carried over to the following years, which at December 31, 2011, amount to GBP 78 million (about NIS 462 million), in respect of which DMS created deferred tax assets in the amount of GBP 20 million (about NIS 119 million).

1.10.16 Environmental protection

During the course of its activity, Roadchef is subject to the same environmental regulations as other companies and businesses that are involved in activity similar to Roadchef's. Roadchef's activity exposes it to several environmental hazards, such as: carbon emissions and effluent from the petrol stations and parking areas, that may contaminate water sources, and the gas emitted from the air conditioning systems above the quantity permitted according to the regulations. The following details the significant regulations and special permits pertaining to environmental protection that particularly affect Roadchef:

Fuel permits for operating petrol stations by companies that are not petroleum companies – to obtain a license, regulatory provisions and regulations must be complied with concerning safety on the forecourts, the method of storing the fuel at the station, fire prevention, operation of measures for detecting and treating leaks and malfunctions. At the reporting date, Roadchef is in compliance with all the provisions and regulations. It should be noted that Roadchef has several old petrol stations that will require considerable investment in coming years for renovation purposes and to bring them up to standard with the regulations. At the date of the report, Roadchef's management has yet to prepare estimates concerning the required financial investment.

Waste supervision – in recent years, regulations have been introduced aimed at reducing the area occupied by landfill and encouraging the recycling of waste. At the date of the report, Roadchef is working to improve its waste recycling capacity, which is expected to reach 75% of all the waste to be recycled in the coming months.

Food hygiene – extensive regulations apply to the manufacture and holding of food. The regulations are enforced by local environmental bureaus acting on behalf of local government in each area. Roadchef employs a health and safety manager who is responsible for compliance with all the food-related regulations. In addition, Roadchef cooperates fully with the Ministry of the Environment to advance and improve its compliance with the regulations.

Reducing carbon emissions – over the last year, a plan to reduce carbon gas emissions has been introduced in the UK. Roadchef is a part of this plan according to which every year, as of 2012, each company will deposit a certain sum of money to be determined in line with the quantity of carbon gas emissions emitted from its sources (in Roadchef's case – from its petrol stations). Although no precise mechanism has yet been determined regarding the amount of the deposit, Roadchef is of the opinion that it will be required to deposit about GBP 300,000. The part of this deposit that will be refunded at the end of the year will also be determined in line with the rates of carbon gases emitted.

It should be noted that at the date of this report, Roadchef is not party to any significant legal or administrative procedure in connection with the environment, no amounts have been ruled against it in proceedings pertaining to environmental quality, and it did not make any provision recognized in its financial statements in respect of such procedures.

Protection of the environment by Roadchef – in addition to the foregoing regulations, Roadchef takes action at various levels to maintain a clean environment: Roadchef works to promote energy-conservation measures. To this end, in 2010, Roadchef spent GBP 100,000 and intends to expend amounts of between GBP 200-300,000 over the next two years.

In addition, Roadchef has developed a program for the protection and enforcement of environmental regulations at its plants, that includes: details of all the obligations applicable to Roadchef within the context of the regulatory provisions; quarterly follow-up of compliance with all the regulatory provisions pertaining to environmental quality, and a review of compliance with these conditions; identifying all the processes required to uphold the environmental provisions, including: reducing carbon dioxide emissions, the efficient use of water, monitoring waste output, operation of the petrol stations, as well as other general instructions; annual follow-up by management, supported by an external audit to ensure compliance with the program and procedures defined in the program, and more. In addition, all Roadchef employees are committed to protecting the environment and complying with the environmental regulations that apply to Roadchef.

1.10.17 Material agreements

Roadchef is party to material agreements that are not part of the normal course of business:

- A. Concerning an agreement with the bond holders as part of the securitization process in 1998 (see Section 1.10.14 (C) (2) above).
- B. **BP agreement** – in May 2009, Roadchef entered into an agreement with the petroleum company, BP, whereby BP will rent from Roadchef the leasehold rights, management and operating rights to 14 petrol stations and adjacent convenience stores in the motorway service areas (including two service areas that it had already leased by virtue of agreements that were signed by the parties in the past). In consideration of the management and operation of the service areas, BP paid Roadchef an initial amount and will make further payments to be collected during the agreement period and to be calculated in line with the sale of fuel (an amount to be set in advance for every liter of fuel sold multiplied by the quantity of fuel sold in a year) and sales in the convenience stores (a fixed percentage of all sales during the year). This agreement period is until 2032. Nevertheless, in those service areas for which the leasehold ends at an earlier date (for details of the leases on Roadchef's assets, see Section 1.1.10 above), the agreement period will end when the lease ends (it should be noted that the closest date for termination of a lease is 2029).

Management and operation of forecourts at 14 service areas (including two areas that were already being run by BP when the agreement was signed) is to be transferred to BP as follows: The management of two service areas that were already operated by BP was transferred to BP immediately after the agreement was signed; by the end of 2009 six more service areas were transferred to BP; the management of four service areas, two of which at the reporting date were operated through licensing agreements and two through agency agreements, will be transferred to BP during the course of 2013, and the management of the last two service areas, that at the reporting date are operated through agency agreements, will be transferred to BP in 2017, after the existing operating and supply agreements between Roadchef and the different petroleum companies that currently operate them, for these areas have ended.

The aforesaid agreement enabled Roadchef to transfer responsibility for environmental protection and the resulting monetary expenses at 14 petrol stations to BP, and to reduce its workforce, as the employees at the petrol stations and adjacent convenience stores will be employed by BP and not by Roadchef.

- C. **Agreement with McDonald's** – during 2010, Roadchef signed a franchise agreement with McDonald's for use of the McDonald's brand and to run restaurants under the McDonald's brand (in this section: "the Agreement"). The agreement is in force for 20 years from January 1, 2010 (with an option for early termination after 10 years), and includes, inter alia, a development plan whereby Roadchef opened 3 restaurants at various motorway service areas in 2010, and further 5 restaurants by December 2011. On 2012 Roadchef is planning to open 3 additional restaurants (of which one was opened at the beginning of 2012).⁶⁴

Due to the outstanding success of the development program Roadchef agreed with McDonald's to accelerate the opening program which resulted in eight restaurants being opened by the end of August 2011 with a further three to be opened by the end of June 2012.

In September 2012, the business performance of the restaurants will be reviewed again, and accordingly a decision will be made whether to open more restaurants. The agreement stipulates that money will be invested in development of the restaurants according to McDonald's conditions and that Roadchef will give McDonald's guarantees to ensure that it meets its obligations under the agreement. Roadchef will pay McDonald's a fixed amount for opening each restaurant under the brand name, as well as additional amounts to be derived from sales.

According to other conditions in the agreement, Roadchef will not enter into agreements with McDonald's competitors in the fast-food sector, excluding agreements that are in force when the agreement with McDonald's was signed.

The agreement also stipulates that should there be a change in the control of Roadchef and/or in its management ("the Change"), as a result of which there is concern that the operation of the restaurants will be affected, McDonald's may appoint a development manager of its own to oversee operation of the restaurants for 6 months from the date of the change. Furthermore, McDonald's shall be entitled to appoint a development manager of its own in the event that it announces the early termination of the agreement or should force majeure prevent Roadchef from meeting its obligations under the agreement.

It should be noted that McDonald's did not take any of the aforementioned action subsequent to the acquisition of the DMS shares that were held by Delek Belron.

- D. **Franchise agreements for the operation of the restaurant services** - in addition to the foregoing agreement with McDonald's, Roadchef has agreements with other brand owners in the restaurant sector (e.g. Costa Coffee and SOHO Coffee). These agreements usually include provisions that regulate the use of the brands, method of managing the restaurants, design and operation of the restaurants, compliance with the franchise policy and standards, employee training, use of equipment, customer service, pricing of the products sold to customers, permitted raw materials, the supply of products and payment for them, as well as looking after the brand and its quality. In addition, each franchise agreement contains provisions concerning the protection of the brand owner's intellectual property, non-competition clauses and details of those instances in which either party may terminate the franchise agreement early by giving written notification. These instances are mainly cases of a failure to pay under the provisions of the franchise agreement, infringement of the concessionaire's trademarks and/or goodwill and/or intellectual property, situations of insolvency or liquidation or the appointment of a receiver or implementation of debt arrangements, the closing of branches by Roadchef without the franchise owner's prior approval, engaging in competing business, fundamental violation of one of the conditions of the franchise agreement that was not remedied within a certain number of days as specified in the franchise agreement. As soon as the franchise agreement ends, Roadchef must stop using the franchise owner's trademarks, must stop selling its products and the parties will pay one another the amounts specified in the franchise agreement in respect of the early termination of the agreement. Some of the agreements also include an undertaking for the parties to invest money to adapt the service areas to the criteria defined by the franchise brands.

1.10.18 Legal Proceedings

At the reporting date, Roadchef is not party to any significant litigation. The following details the proceedings that have yet to be formulated as a legal proceeding, but may affect Roadchef:

- A. **Agreement with CEM** – in January 2008, a management agreement from June 29, 2007 (and revised on May 15, 2008, and March 5, 2009) took effect between MSA and a third party,

⁶⁴ At the date of the report, Roadchef and McDonald's are negotiating to open 3 more restaurants that were not included in the agreement, by the end of December 2012.

Country Estate Management (Services) Ltd. ("CEM" and "the Management Agreement" respectively).⁶⁵

Under the management agreement, CEM undertook to perform, in the name of MSA's Board of Directors, the duties and activities involved in exercising control over the operation and decision making in Roadchef and its subsidiaries for MSA. Likewise, CEM made an undertaking to maintain a minimum annual EBITDA for Roadchef and its subsidiaries of an amount that varies each year (where the annual average for five years is GBP 30 million). Under the management agreement, if and insofar as in a particular year the actual EBITDA is less than the EBITDA to which CEM is committed for that year, MSA shall be entitled to receive the difference. Pursuant to an appendix from March 5, 2009, it was determined that this difference, should it exist, will be paid at the end of the period of the management agreement (in lieu of an annual calculation mechanism that was included in the original agreement).

In consideration of its services, CEM shall be entitled to GBP 400,000 a year (representing a refund of the expected amount of CEM's expenses and costs) as well as additional payments pertaining to the increase in Roadchef's EBITDA or value (should there be such). In practice, Roadchef's results were lower than guaranteed in the management agreement.

In April 2010, the Board of Directors of MSA decided to terminate the agreement with CEM and from that date CEM ceased to manage and operate the group's assets. At the date of the report MSA it continues to review its options for collecting CEM's debt towards it. Initial meetings have been held and additional legal advice sought but at this stage it is impossible to estimate the chances of collecting the debt and the outcome of the negotiations.

It should be noted that in September 2009, the Board of Directors of MSA decided to make provision for the entire outstanding debt in the amount of GBP 14 million, created on account of the agreement with CEM in view of examining the possibility of terminating the agreement with CEM.

- B. **Investigation by the Israel Securities Authority (ISA)** – on December 3, 2009, the ISA initiated an open investigation into matters relating to reports that had been published in Israel by Delek Real Estate, which at that time was the controlling shareholder (through Delek Belron) in DMS. As far as DMS is aware, the ISA's investigation included, inter alia, an examination of the agreement between MSA and CEM. On August 31, 2010, the ISA announced that it had completed the investigation and submitted the file to the State Prosecutor's Office so that it can decide how to proceed with the case. Subsequent to the balance sheet date, the State Attorney notified Delek Real Estate that it has been decided, subject to a hearing, to charge Delek Real Estate and previous officers with offenses against the Securities Law. Based on Delek Real Estate's estimations, the Company estimates that this will not affect the financial statements. Nevertheless, the Company is unable to predict what the State Attorney may decide in the hearing and what the implications of this decision will be (if any).

1.10.19 Business goals and strategy

The following includes business forecasts and forward-looking information: For a variety of reasons, Roadchef's business goals and strategy may not materialize and/or may be changed depending on the decisions made by Roadchef's Board of Directors.

- A. Improved profitability and supply of products – over the next few years, Roadchef's management intends to work to improving profitability by streamlining its operations. At the date of this report, about 34% of visitors to the motorway service areas do not make any purchases, this number has improved from 40% not purchasing in 2010. Roadchef's management intends to introduce further marketing measures in an effort to increase the percentage of visitors who make purchases. Likewise, Roadchef's management intends to expand supply in the branded chains, whose products are available in the service stations, and it is also looking into expanding the range of products on offer at the services areas (for example, by way of adding groceries). The following details the measures planned to help achieve the aforementioned goals:

1. Brands and services – Roadchef's management believes that the use of known brands and providing quality service will generate higher sales at the service areas, particularly in

⁶⁵ As far as the company is aware, CEM is a special purpose vehicle established in connection with the management agreement, and as far as the company is aware it is owned by a third party that has knowledge and experience in managing and operating real estate assets and operating assets in England.

the catering category. Roadchef works continuously to improve the branding of its products (thus, for example, Roadchef replaced Wimpy with McDonald's and a brand of its own) and the quality of the service it provides for its customers. Roadchef also works to renovate its restaurant and dining areas so as to attract and serve the public, based on the assumption that this will help increase its sales.

2. Speed of service – the success of the retail and restaurant activity relies on open areas, served by staff who are available and ready to serve customers, on the constant availability of products, and on sufficient check-out counters to help reduce waiting time. To meet its customers' needs, Roadchef's management tries to improve accessibility by increasing the number of check-out counters in the service areas, through employee training to improve their service capability and by extending opening hours at the retail and restaurant areas.
 3. Increasing the number of products offered – with 60 million visitors a year, the range of products available at the service stations must be expanded. Thus for example, Roadchef's competitors have begun operating branches of Marks & Spencer and Waitrose at their service areas. In an effort to increase sales and meet the competition, Roadchef is working to increase the number of products on offer at the service stations and to introduce familiar retail products in different sectors.
 4. Competitive pricing – as noted, the UK's motorway service area market has three principal competitors. To meet existing competition in the motorway service area market, Roadchef sets prices that are competitive with those offered by its competitors and are closer to the prices at which these products are sold in the ordinary markets.
 5. Additional revenues – Roadchef's management also intends to examine improvements to revenues from slot machines, parking and revenues from long-term parking at the service areas.
- B. Acquisition of other sites – despite the low probability that more motorway service areas will be opened in the coming years due to strict regulations, several motorway service areas are run by small companies and if they are put up for sale Roadchef's management would consider acquiring them as they did with the First Motorways business in 2011.

1.10.20 Expectations for development in the coming year

During the course of 2010, Roadchef announced a two-year investment of GBP 12 million to develop restaurant activity at its 10 most profitable motorway service areas, including the opening of a branch of McDonald's, Costa Coffee upgrades, Hot Food Company, and the renovation of existing restaurants. By the end of 2011 eight service areas had been completed and a further six are planned for 2012. Roadchef is of the opinion that this investment will be financed from the credit facilities provided by Barclays Bank, and by partners, as well as from Roadchef's cash flow as noted above in Section 1.10.14 (B).

It should be clarified that the information in this section is forward-looking information and that changes may be made in this plan pursuant to decisions made by Roadchef's management, as they may be from time to time, in part taking into account the availability of sources of capital to implement the investments.

1.10.21 Risk factors

Several risk factors can be mentioned that MSA and Roadchef have to address during the course of their operations:

- A. **Price of energy** – Roadchef has considerable costs in respect of the consumption of energy (electricity and petrol). An increase in the prices of electricity and petrol may lead to higher operating expenses for Roadchef and reduce its profits. Likewise, an increase in the price of petrol may lead to fewer travelers on the motorways, thus reducing Roadchef's profits.
- B. **Increase in the minimum wage** – Roadchef employs a large number of workers at a salary based on the minimum wage applicable in the UK. An increase in the minimum wage in the UK would increase Roadchef's expenses and reduce profits.
- C. **Changes in interest rates** – some of MSA's loan agreements are at variable interest, so that MSA is exposed to changes in the interest rate. Likewise, changes in the interest rates may affect the business performance of MSA and its investees.
- D. **Outsourcing** – during 2005, Roadchef transferred its back-office operations and operation of its information system to IBM. During this transfer, several difficulties emerged relating to the transfer,

most of which were dealt with. Nevertheless, at the reporting date, a number of outstanding issues remain pertaining to the services rendered by IBM that have yet to be resolved. Management are planning to bring its finance and IT functions back in-house and this work will commence in 2012.

- E. **Roadworks on the M1 and M6** – roadworks taking place as part of the government's program to widen the M1 and M6 motorways, may adversely affect activity at Roadchef's service stations on those roads. During the second half of 2010, the British Minister of Transport announced that the work would continue.
- F. **Improvements in public transport** – public transport services in the UK force many people to use their private cars and consequently the motorways. An improvement in public transport that could lead to an increase in the number of people who use public transportation would reduce the number of drivers on the roads thus affecting Roadchef's revenues.
- G. **Legislative restrictions and the applicable changes** – existing legislative restrictions pertaining to the operation of motorway service areas in the UK could affect Roadchef, so that an abolition of the restrictions pertaining to the requisite distance between service stations could result in the opening of more stations and this would affect revenues at Roadchef's existing service areas.
- H. **Inability to obtain franchise agreements** – at the date of the report, Roadchef has franchise agreements with different brands in connection with its retail activity, restaurant activity and the sale of fuel at its service stations. Thus for example, Roadchef's franchise agreements with Costa and McDonald's are for 10 and 20 years respectively. An inability to reach new franchise agreements, as well as the failure to extend existing franchise agreements may affect Roadchef's revenues and its ability to compete with other service station operators.
- I. **Increase in the rate of VAT** – an increase in the VAT rate by the authorities may affect Roadchef's activity due to the fact that prices on some of the products that it sells cannot be raised by the rate of the VAT increase. The current VAT rate is 20%.
- J. **Weakness of the UK economy** – the UK's economy suffered considerably as a result of the global economic crisis in 2008 and forecasts show that the economy will continue to be weak. Roadchef's activity relies mainly on the UK's economic environment. The growth of GDP leads to an increase in the number of travelers on the motorways and increases Roadchef's profit potential. Nevertheless, in view of the state of the UK economy, a slowdown in the growth of GDP in the UK and a reduction in the number of travelers on the roads could affect Roadchef's revenues and profit.

The following table presents the aforementioned risk factors by quality – macro risks, Sectoral risks and risks that are special to MSA and Roadchef. The risks are rated according to estimates of Roadchef's management by the extent to which they affect Roadchef's business:

	Extent to which the risk factor influences Roadchef's business		
	Strong influence	Moderate influence	Small influence
Macro risks	• Increase in minimum wage • Weakness of the UK economy		• Changes in interest rates • Increase in the VAT rate
Sectoral risks	• Abolition of legislative restrictions • Improvements in public transport	• Price of energy • Roadworks on the M1 and M6	
Risks special to the company		• Inability to obtain franchise agreements	• Outsourcing

The extent to which the risk factors affect MSA and Roadchef's activity is based on estimates only, and in practice the impact may differ.

1.11 Energy⁶⁶

1.11.1 General

- A. The Company's energy segment operates under Delek Energy Systems Ltd., a public company whose shares have been listed on the Tel Aviv Stock Exchange Ltd. ("the TASE") since 1982 ("Delek Energy"), and as from December 2010, under Cohen Development and Industrial Buildings Ltd. ("Cohen Development"), a public company whose shares have been listed on the TASE since 1982.
- B. On December 28, 2011, the Company acquired all the holdings of the Tadmor and Cohen families in Cohen Development, representing 51.76% of the issued and paid up share capital of Cohen Development, for a total consideration of NIS 274 million. The payment dates are set out below. The sellers also have a call option to acquire participation units in Delek Drilling and Avner Partnership from the Company (according to a mix to be decided by the Company) in a quantity reflecting a total value of NIS 150 million. The option is granted in two lots: the first lot (reflecting a value of NIS 75 million) is for up to 6 months from the date of completion, and the second lot (reflecting a value of NIS 75 million) is for up to 12 months from the date of completion. The payment dates of the consideration for the shares of Cohen Development are as follows: NIS 200 million was paid on the date of completion, NIS 37.5 million will be paid when exercising the first lot the option, and the balance of NIS 37.5 million will be paid when exercising the second lot (subject to a mechanism for offsetting and interest). As collateral for the second and third payments, participation units held by the Company with a value of NIS 112.5 million were pledged in favor of the sellers (subject to adjustment of the pledged units, such that a ratio of 150% will be retained between the value of the pledged participation units and the balance of the unpaid consideration). Following the transaction, the Company became a controlling shareholder in Avner Oil and Gas Ltd., the general partner in the limited partnership - Avner Oil Exploration Ltd. (by virtue of the Company's holdings in Delek Energy and the holdings of Cohen Development in Avner as set out below), and as a result, in Avner Partnership. See Note 4 to the financial statements for further information about the effect of the transaction on the Company's results and the presentation method of the holding in Cohen Development in its financial statements. Cohen Development manages oil and gas exploration and production as well as real estate. See section 1.11.1(D) for further information about the operations of Cohen Development.
- C. Delek Energy operations
1. Delek Energy's core business is exploration, development and production of oil and natural gas in Israel and exploration in the territorial waters of Cyprus.⁶⁷ The Company also owns 29.3% of the shares in Matra Petroleum Plc ("Matra"), a public company registered in the UK, which has rights in an exploration and production project in Russia, 2.77% of the shares in Nexus Energy Ltd. ("Nexus"), an Australian oil and natural gas exploration and production company and the full share capital of Delek Energy Systems (Gibraltar) Limited ("Delek Gibraltar"), a wholly owned subsidiary of Delek Energy, registered in Gibraltar, which has rights in an exploration project in the North Sea. It is clarified that Delek Energy's holdings in Matra, Nexus and Delek Gibraltar are not a significant part of Delek Energy's operations.
 2. From 2006 to 2011, Delek Energy, through a subsidiary registered in the United States ("the subsidiary"), engaged in oil and natural gas exploration and production, mainly in the Southern USA (Texas, Louisiana, Colorado, Kansas, Oklahoma, New Mexico and Utah).
 3. In 2011, Delek Energy disposed of its oil and gas assets in the United States, as part of its plans to focus on its core businesses in Israel, following the significant gas discoveries at Tamar, Dalit and Leviathan. Accordingly, in 2011, all the oil assets held by Delek Energy in the United States were sold for a total consideration of USD 165 million. See section 1.11.11 below for further information about the sale of the assets.

⁶⁶ For more explicit definitions of part of the professional terminology included in this section, see the definitions appendix at the end of the section.

⁶⁷ On September 15, 2011, temporary provisions of the TASE came into effect, expanding the definition of an oil and gas exploration "project", to include oil or gas exploration and production in the area in the territorial waters of the country whose territorial waters border the territorial waters of the State of Israel.

4. At the date of this report, the Yam Tethys project produces most of the Company's revenue. This project includes the Mari-B gas reservoir, which was discovered in February 2000 in the I/10 Ashkelon lease and which produces natural gas that is sold to customers. Other key projects are the development of the Tamar gas reservoir, discovered in 2009 in the area covered by the I/12 Tamar lease; development of the Noa gas reservoir, discovered in 1999 in the area covered by the I/7 Noa lease; appraisal operations in the Leviathan reservoir, discovered in December 2010 in the area covered by the 349/Rachel license; the Block 12 project, which includes the Aphrodite gas reservoir, discovered in December 2011; the Dolphin project, which includes the Dolphin gas reservoir, discovered in December 2011 in the area covered by the 351/Hannah reservoir; and the Tanin project, which includes the Tanin gas reservoir, discovered in February 2012 in the area covered by the 364/Alon A license. Delek Energy is also involved in other offshore oil exploration projects off the coast of Israel.
5. Delek Energy operates in Israel and Cyprus through its holdings in Delek Drilling Limited Partnership ("Delek Drilling Partnership") and Avner Oil Exploration Limited Partnership ("Avner Partnership"). Delek Drilling and Avner Partnership are referred to collectively in this section 1.11 as "the partnerships" or "the limited partnerships". The general partner in Delek Drilling Partnership, Delek Drilling Management (1993) Ltd. is a wholly owned subsidiary (100%) of Delek Energy. The general partner in Avner Partnership, Avner Oil and Gas Ltd., is a subsidiary (50%) of Delek Energy and the balance of its the shares are owned by Cohen Development. As from December 28, 2011, Cohen Development is controlled by the Company as described above.
6. In addition to management of the partnerships, at the publication date of the Periodic Report, Delek Energy owns participation units in the partnerships, issued by the limited partners as follows:
7. Direct and indirect holding of 62.63% of participation units issued by the limited partner in Delek Drilling Partnership ("the Delek units").⁶⁸ The limited partnership and trustee of this partnership is Delek Trustees Drilling Ltd., wholly owned (100%) by Delek Energy. These holdings in the limited partner do not confer on Delek Energy any management rights or rights to profits.
8. Direct and indirect holding of 47.48% of the participation units issued by the limited partner in Avner Partnership ("the Avner units").⁶⁹ The limited partnership and trustee of this partnership is Avner Trustees Ltd., owned 50% by Delek Energy. The remaining shares are owned by Cohen Development. These holdings in the limited partner do not confer on Delek Energy and/or Cohen Development any management rights or rights to profits.

At the publication date of the Periodic Report, the Company owns 6.53% of Delek Drilling Partnership units and 9.11% of Avner Partnership units.

D. Operations of Cohen Development

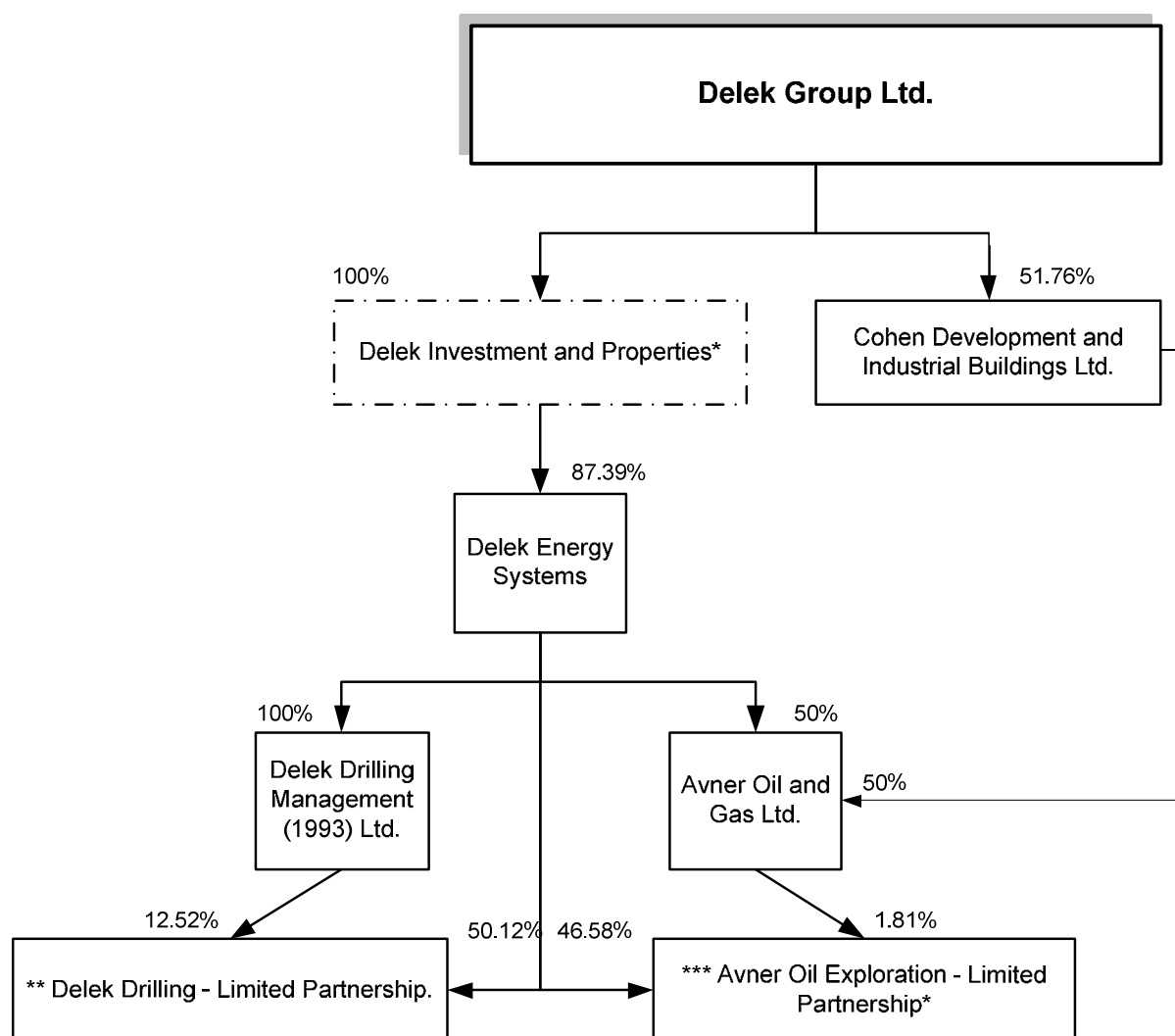
The oil and gas exploration and development operations of Cohen Development are carried out through Avner Oil and Gas Ltd., which is the general partner in the Avner Oil Exploration limited partnership. Cohen Development holds half of the share capital of Avner Oil and Gas Ltd. and the balance is held by Delek Energy. At the publication date of the report, Avner Oil and Gas Ltd. holds 1.81% of Avner units. In addition, Cohen Development holds half of the share capital of Avner Trusts Ltd., the limited partner in Avner Partnership. Cohen Development is also entitled to royalties from Avner Partnership at the rates set out below, from each share of Avner Partnership in the oil, gas or any materials of value produced and used from the oil assets in which the partnership has or will have an interest: 2.75% of the Ashkelon and Noa leases; and 2.875% of the other leases and licenses held by Avner Partnership and other oil assets in which Avner Partnership will have rights in the future.

⁶⁸ At February 29, 2012, the participation units issued by the limited partner in Delek Drilling Partnership are held, inter alia, by Delek Energy (50.11%), Delek Drilling Management (1993) Ltd. (12.52%) and the Company (6.53%).

⁶⁹ At February 29, 2012, the participation units issued by the limited partner in Avner Partnership are held, inter alia, by Delek Energy (46.58%), the Company (9.11%), Avner Oil and Gas Ltd. (1.81%) and Gideon Tadmor 0.17%).

E. The chart below describes the holdings structure of the main companies in this field of operations:⁷⁰

The rates of holdings in the limited partnerships are of the participation units in the limited partner.



* Delek Investments and Properties are in the process of merging with Delek Group such that all the assets, rights, liabilities and debts of Delek Investments (the target company) will be transferred to and bought by the Company (the acquiring company). On completion of the merger, Delek Investments will be dissolved without liquidation.

** Delek Group has a direct holding of 6.53% in Delek Drilling – Limited Partnership.

*** Delek Group has a direct holding of 9.11% in Avner Oil Exploration – Limited Partnership.

⁷⁰ The chart does not include Delek Drilling Trusts Ltd. and Avner Trusts Ltd., nor does it include the subsidiaries of Elk, Vogil or Matra.

F. Summary of information about Delek Energy's operations⁷¹

1. Rights in oil assets in Israel

Project	Name of oil asset	Type of right	Delek Drilling Partnership's rights in the oil assets	Avner Partnership's rights in the oil assets
Yam Tethys project	I/7 Noa I/10 Ashkelon	Lease	25.50%	23%
Tamar project	I/12 Tamar I/13 Dalit	Lease	15.625%	15.625%
Ratio Yam project	349/Rachel 350/Amit 351/Hannah 352/David 353/Eran	License	22.67%	22.67%
Ruth licenses	358/Ruth A 359/Ruth B 360/Ruth C72	License	27.835%	25.106%
Alon licenses	364/Alon A 365/Alon B 366/Alon C 367/Alon D 369/Alon F	License	26.4705%	26.4705%

2. Rights in oil assets in Cyprus

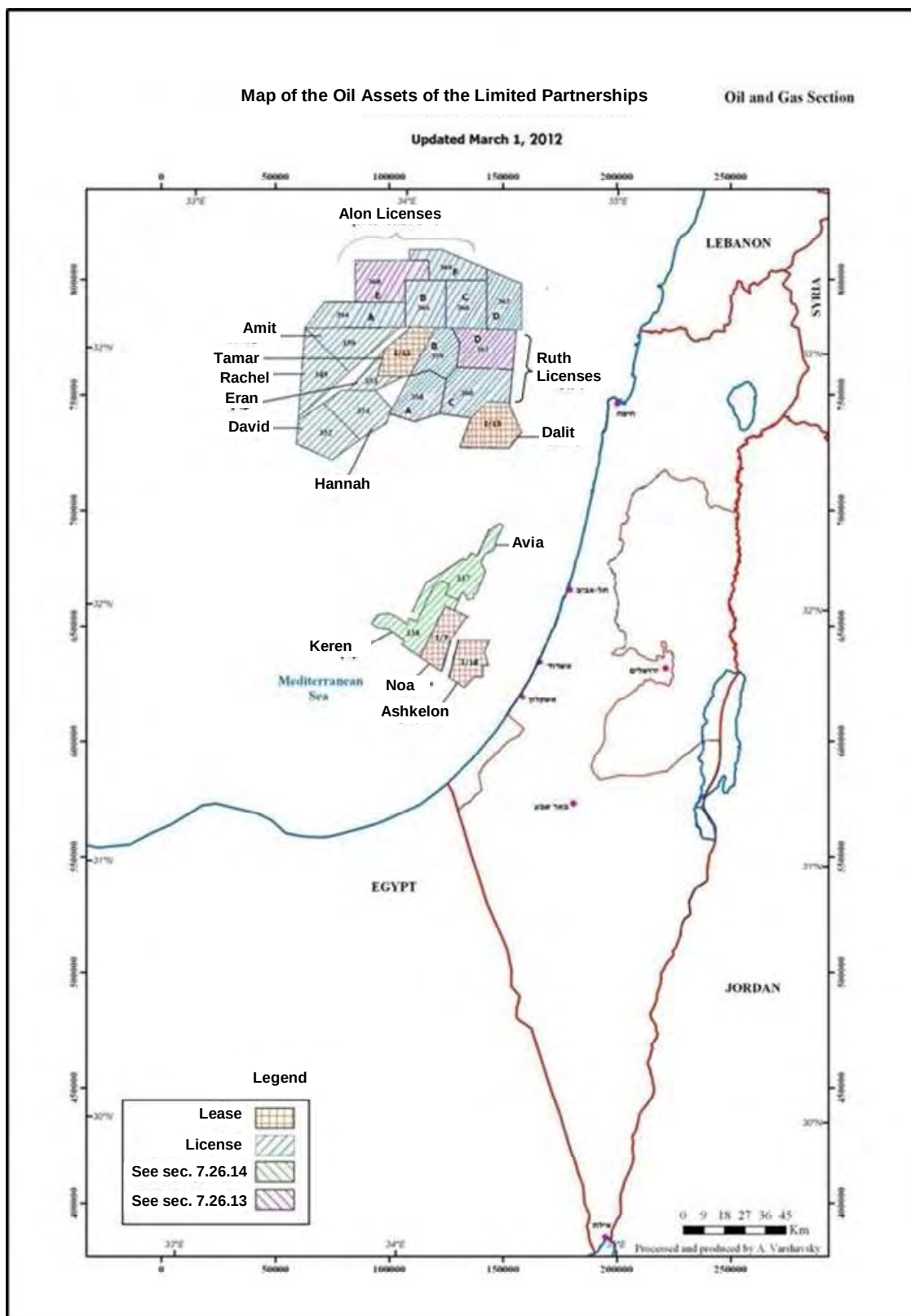
Project	Name of oil asset	Type of right	Delek Drilling Partnership's rights in the oil assets	Avner Partnership's rights in the oil assets
Block 12	Aphrodite	License ⁷³	15%	15%

⁷¹ Up to the publication date of the report, the following licenses expired: 361/Ruth D, 368/Alon E and 337/Avia. The 338/Keren license will expire on March 3, 2012. For further information, see section 1.11.11 below.

⁷² An application submitted to the Commissioner for approval of the continuation of the lease in the Ruth C license in addition to the 12 licenses. Licenses covering an area of more than 400,000 hectares, see section 1.11.11 below.

⁷³ For further information, see section 1.11.10 below.

G. Map of all oil assets of the limited partnerships:



1.11.2 Investments in capital and transactions in Delek Energy securities:

To the best of the Company's knowledge, in the past two years there have been no material investments in Delek Energy's capital and/or off-floor transactions in Delek Energy by interested parties, with the exception of the following:

- A. On February 6, 2011, the Company acquired ⁷⁴ 3,800 ordinary shares in Delek Energy, in an off-floor transaction, at an average price per share of NIS1,332.666.
- B. On February 9, 2011, the Company acquired 1,060 ordinary shares in Delek Energy, in an off-floor transaction, at an average price per share of NIS 1,407.26.
- C. On April 13, 2011, the Company acquired 3,910 ordinary shares in Delek Energy, in an off-floor transaction, at an average price per share of NIS 1,356.
- D. On August 2, 2011, the Company and the partnerships issued a shelf offer by way of full exchange tender offer and specifications for a tender offer for the acquisition of 1,009,910 ordinary shares of Delek Energy for participation units of Delek Drilling Partnership and Avner Partnership held by the Company, under shelf prospectuses issued by the partnerships on July 22, 2011 and amended on August 2, 2011 ("the tender offer").

As part of the tender offer, on September 11, 2011, the Company acquired 353,988 shares of Delek Energy for 12,743,570 participation units conferring participation rights in the rights of the general partner in Delek Drilling Partnership and 167,082,364 participation units conferring participation rights in the limited partner's rights in Avner Partnership.

- E. On October 25, 2011, the Company acquired 23,275 ordinary shares in Delek Energy, in an off-floor transaction, at an average price per share of NIS 1,340.
- F. On November 11, 2011, Delek Energy acquired from the former CEO of Delek Energy 55,343 options exercisable for ordinary shares of Delek Energy for NIS 53.528 million. The options that were acquired were canceled by Delek Energy. See section 22 of Part D for further information.

1.11.3 General information about the area of operations

A. Operating segment structure and changes

Oil and gas exploration in Israel is regulated by the Petroleum Law, 1952 (the Petroleum Law), which stipulates, inter alia, that exploration in Israel may only be in geographical areas where the exploration company holds oil and gas rights under the Petroleum Law. In addition, the Natural Gas Sector Law, 2002 ("the Natural Gas Sector Law") regulates the transmission, distribution and marketing of natural gas in Israel. The economic feasibility of natural gas production from reservoirs discovered by the limited partnerships and the reservoirs that may be discovered in the future is heavily dependent on the demand for natural gas in domestic and international markets and on the export potential of natural gas (through pipelines, compressed or liquefied), which also requires significant gas reserves and long-term agreements for the sale of large quantities of natural gas, which would justify the heavy investment required to establish suitable infrastructure. Conversely, if oil is discovered, it may be sold to consumers in Israel and other countries at the global price of oil at that time.

Israel - Development of Israel's natural gas sector started in 2004, with gas supply from the Mari reservoir to the Eshkol power station in Ashdod, belonging to the Israel Electric Corporation Ltd. Total consumption of natural gas in Israel has increased alongside the progress of the pipeline installed by Israel Natural Gas Lines Ltd. ("INGL") and the connection of other consumers and power stations to the pipeline. Within a few years, natural gas has become the main source of fuel for electricity production and a material source of energy for large industries. According to the Ministry of Energy and Water ("the Ministry of Energy") natural gas consumption in Israel in 2011 amounted to 4.95 BCM. According to the assessment of the Ministry of Energy, the growth in the use of natural gas in Israel is expected to continue in the coming years, reaching 13.4 BCM by 2020 and 19.5 BCM by 2030, of which 85% will be for electricity generation and industry. According to the assessment of the Ministry of Energy, the total forecast demand for 2011-2040 is 493 BCM (or 455 BCM, if transportation and methanol are excluded). The forecast demand for natural gas is based on a continued increase in electricity consumption at a multi-annual average of 3.1%; minimum use of heavy

⁷⁴ As from February 11, 2011, the holdings of the Company and Delek Investments are consolidated under the Company.

fuel oil; reliance on coal power stations to the same extent as at the present time; gradual adoption of renewable energy sources to reach a level of 10% in 2030; and a transition to natural gas as the primary fuel for electricity generation as of 2014, reaching 60% in 2027 and 68% in 2040 of all fuels used to generate energy.⁷⁵

Cyprus - The remainder of Delek Energy's operations are in Cyprus, Russia and the North Sea and are subject to the relevant regulations and restrictions set out below.

Oil and natural gas exploration and production operations are complex, involving considerable costs and extremely high uncertainty as to exploration cost, schedule, availability of oil or natural gas and the ability to produce it while maintaining economic viability. As a result, despite considerable investments, often drillings do not achieve positive results and do not produce any revenues, resulting in loss of all or part of the investment. Exploration and production of oil and natural gas are usually undertaken by joint ventures involving multiple partners, who sign a joint operation agreement (JOA) whereby one of the partners is appointed to operate the joint venture (for a description of the JOA, see the Yam Tethys operating agreement in section 1.13.2F below).

Oil and natural gas exploration and production in any concession involves several stages, including the following:

1. Preliminary analysis of geological and geophysical data for the selection of areas showing potential for oil and gas exploration
2. Consolidation of a lead for drilling
3. Seismic surveys, which assist in locating geological formations that may contain hydrocarbons (oil and/or gas) and data processing and analysis.
4. Examination of the geological formations and preparation of viable prospects for exploration
5. Decision to conduct exploration drilling and preparation for drilling
6. Entering into agreements with contractors for drilling and accompanying services
7. Exploration drilling including logs and other tests
8. Production tests (in certain cases)
9. Final analysis of drilling results, and in the event of a discovery, based on a preliminary evaluation of reservoir properties and quantities of oil and/or natural gas reserves, economic data is analyzed (including a market valuation) and physical data, preliminary evaluation of the development format and cost are prepared Additional seismic surveys, confirmation drillings and appraisal wells may be required in order to form a better evaluation of the reservoir properties and oil and/or natural gas quantities
10. Consolidation of a development plan and preparation of a detailed economic plan for the project
11. Final analysis of the data and decision whether the discovery is commercial
12. Development and production work for the commercial discovery
13. Production from the commercial discovery. It is noted that in period, additional development works are often carried out to maintain and/or increase production capacity.

These stages do not exhaust all the stages of the exploration and production process for a specific project, which due to its quality and nature could include only some of these stages and/or additional stages and/or stages in a different order.

Sometimes no formations are found that are suitable for drilling, therefore preparation of a prospect for drilling is not feasible and the process is terminated at an earlier stage. Similarly, sometimes an oil and/or natural gas discovery turn out to be commercially unviable and therefore are not suitable for development and production. Moreover, the period for each stage varies according to the nature of the project and it is difficult to demonstrate an exploration, development and production process in which all the above

⁷⁵ The information is taken from the website of the Ministry of Energy:
<http://energy.gov.il/Subjects/NG/Pages/GxmsMniNGEconomy.aspx>

stages are conducted consecutively in the order described above and without changes being made or unexpected events occurring.

The commercial viability of an oil and/or gas discovery is complex and depends on many different factors. In this context, there is a significant difference between an offshore discovery, which requires immense development costs, and an onshore discovery, and between an oil discovery and a gas discovery, whose viability depends on the ability to sell the gas to an attractive target market, as gas, unlike oil, is not a commodity sold at similar prices worldwide. Furthermore, the commercial nature of the oil discovery is greatly affected by global oil prices. For example, a discovery that is not commercial when a barrel costs USD 20 could become commercial when the price of a barrel increases to USD 100 and vice versa. In view of the above, an oil and/or gas discovery that is commercially unviable under certain market conditions may become commercial if significant changes occur in market conditions, and vice versa.

B. Restrictions of legislation, standardization and special constraints

Oil and fuel exploration and production are subject to extensive regulation of the relevant countries. For details of regulations applicable to Delek Energy's operations, see section 1.11.26 below.

C. Significant technological changes

In the past decades, there have been technological changes in oil and natural gas exploration and production, relating to testing as well as drilling and production methods. These changes have improved the quality of data available to oil and gas exploration companies and allow more advanced identification of potential oil and gas reservoirs, which might also reduce the risks involved in drilling. These developments will also improve drilling operations. Technological improvements allow operation under far more difficult conditions than in the past, further offshore and at a greater water depth. Accordingly, oil exploration companies are able to invest exploration efforts in areas where drilling used to be impossible, or was only possible at a very high cost and much greater risk.

D. Critical success factors in the area of operations

1. Locating and obtaining exploration rights (purchase or participation) in areas where there is potential for commercial discoveries;
2. The ability to raise considerable financial resources;
3. The use of advanced technologies (such as 3D seismic surveys and advanced data processing technologies) to locate and prepare drilling prospects and to formulate an offshore development plan;
4. Partnering with international entities operating in the sector, to carry out complex drilling, using their professional knowledge and participation in the cost of the investment;
5. Successful exploration and development work;
6. If natural gas is found, signing agreements for the sale of the gas in satisfactory quantities and at good prices.

E. Changes in raw materials and suppliers

In recent years, there has been a significant rise in the prices of metals, which are a vital component in exploration and development costs. In addition, the increase in oil prices in recent years led to a sharp increase in demand for service providers in the oil sector, leading to a significant increase in operating costs in the sector and to reduced availability of contractors and required equipment.

F. Entry and exit barriers

The major entry barriers in the exploration sector are the permits and licenses required for exploration and production of oil and natural gas, compliance with guidelines and criteria set by the Commissioner of Petroleum Affairs in the Ministry of Energy and Water ("the Commissioner" or "the Commissioner of Petroleum Affairs" and "the Ministry of Energy") (and in Cyprus - guidelines and criteria set out in legislation and arrangements under the PSC for the transfer/acquisition of participation rights in oil assets, including proof of financial robustness to obtain them and the heavy investments and relatively high risk level involved in these activities).

There are no significant exit barriers in the segment, other than the partnerships' long-term gas supply agreements as well as the duty to dismantle production facilities prior to abandoning lease areas, and in Cyprus, other than the conditions set out in the production sharing contract (PSC) for transfer of rights to third parties. Exit barriers also include TASE bylaws and the limited partnership agreements, which limits the partnerships to oil and gas exploration only.

G. Substitutes for products of the operating sector

Natural gas and oil are used as fuels for combustion and are sold to both industrial and private customers. The partnerships sell natural gas in Israel mainly to Israel Electric Corporation, electricity producers and other industrial customers as set out in section 1.11.13 below. Natural gas and oil substitutes include diesel fuel, fuel oil, coal, hydro-electric energy, solar energy, wind energy and biofuel. Each of the above substitutes has advantages and disadvantages and is subject to price fluctuations. The transition from use of one energy source to another usually requires considerable investment. The major advantages of natural gas over coal and liquid fuels are high efficiency and relatively low pollution.

H. Structure of competition in the segment: see section 1.11.15 below

Description of the partnerships' oil assets

1.11.4 Yam Tethys project

A. General

Ashkelon Lease	
General information about the oil asset	
Name of the oil asset:	I/10 Ashkelon ⁷⁶
Location:	Approximately 25 km west of the Ashkelon coast
Area:	Approximately 250 sq. m
Type of oil asset and description of permitted operations according to that type:	Lease Operations permitted under the Petroleum Law - exploration and production
Original grant date of the oil asset:	June 11, 2002
Original expiry date of the oil asset:	June 10, 2032
Dates of decision to extend the term of the oil asset:	-
Current expiry date of the oil asset:	June 10, 2032
Note whether there is an additional option of extending the period of the oil asset: if there is such an option – note the period of the possible extension:	Subject to the Petroleum law for an additional 20 years
Note name of operator:	Noble Energy Mediterranean Ltd. ("Noble")
Note the names of the direct partners in the oil asset and their direct shares in the oil asset, and also, to the best of the Company's knowledge, the names of the controlling interests in the partners	(1) ("Noble") (47.059%) To the best of the Company's knowledge, Noble is a wholly owned subsidiary of Noble Energy Inc. ("Noble"), a public company traded on the NYSE"). According to Noble's reports, there is no shareholder holding more than 10% of its issued share capital (2) Delek Drilling Partnership (25.5%) (3) Avner Partnership (23%) (4) Delek Investments and Properties Ltd. ("Delek Investments") (4.441%)

Ashkelon lease	
General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	-
Description of the Company's holding in the oil asset	Direct holding and holdings in participating units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset attributable to equity holders of the Company	<u>In revenue:</u> After return on investment - 31.725% <u>In the right to participate in revenue</u> After return on investment - 28.65% <u>In right to receive royalties:</u> After return on investment - 3.075%
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 96,852 thousand

⁷⁶

The Mari-B gas reservoir was discovered in the area of the Ashkelon lease in February 2000

Noa lease	
General information about the oil asset	
Name of oil asset	I/7 Noa ⁷⁷
Location	Approximately 25 km west of the Ashkelon coast
Area	Approximately 250 sq. m
Type of oil asset and description of permitted operations according to that type	Lease Operations permitted under the Petroleum Law - exploration and production
Original grant date of the oil asset	February 1, 2000
Original expiry date of the oil asset	January 31, 2030
Dates of decision to extend the term of the oil asset	-
Current expiry date of the oil asset	January 31, 2020
Note whether there is an additional option of extending the period of the oil asset: if there is such an option, note the period of the possible extension	Subject to the Petroleum Law
Note name of operator	Noble
Names of the direct partners in the oil asset and their direct share in the oil asset and, to the best of the Company's knowledge, the names of the controlling owners in the partners	(1) Noble ⁷⁸ (47.059%); (2) Delek Drilling Partnership (25.5%) (3) Avner Partnership (23.00%) (4) Delek Investments ⁷⁹ (4.441%)

Noa lease	
General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	-
Description of the Company's holding in the oil asset	Direct holding and holdings in participating units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset attributable to equity holders of the Company	In revenue: Before return on investment - 30.2671% After return on investment - 31.607% <u>In the right to participate in revenue</u> After return on investment - 29.82% After return on investment - 30.15% <u>In right to receive royalties:</u> Before return on investment - 0.4471% After return on investment - 1.457%
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 27,950 thousand

⁷⁷ The Noa gas reservoir was discovered in the area of the Noa lease in June 2000

⁷⁸ For further information about Noble, see the description of the Ashkelon lease above.

⁷⁹ For further information about Delek Investments, see the description of the Ashkelon lease above.

B. Main terms of the Yam Tethys lease

The main terms of the leases in the Yam Tethys project are as follows:

1. Noa lease:

The 1/7 Noa lease (the Noa lease) received on February 10, 2000, stipulates, inter alia, the following special terms:

- A) Appropriate effort will be invested to develop the discovery and produce gas
- B) After the first six years of the lease, and every three years thereafter, the lease holder will submit an updated work plan to the Petroleum Commissioner.
- C) The terms of the Noa lease include additional provisions relating to breaches, environmental insurance, an abandonment plan, compliance with international treaties and Israeli law, coordination with the security forces and announcement of the operator's identity.

2. Ashkelon lease:

The 1/10 Ashkelon lease ("the Ashkelon lease) received on June 11, 2002, stipulates, inter alia, the following special terms:

- A) The lease is granted for production of natural gas only. No other use will be made of the lease area, seabed and subterranean in the lease area.
- B) Natural gas will be delivered from the platform/reservoir in accordance with the Natural Gas Sector Law.
- C) The terms of the Ashkelon lease include additional provisions relating to preparation of reservoir reports at the end of each production year, breaches, environmental insurance, abandonment plan, compliance with international treaties and Israeli law, coordination with the security forces and announcement of the identity of the operator.

C. Compliance with the terms of the work plan in the Yam Tethys project

Description of work plan items not yet completed in the period	Description of work plan items completed in the period	Description of the work plan defined for the period	Period
---	---	As set out above, the Ashkelon lease was granted in June 2002 and the Noa lease was granted in February 2000. At the date of the report, there is no binding work plan for this period.	2009-2011

D. Future binding work plan according to the terms of the oil asset in the Yam Tethys project

The Company's effective share of the total budget (USD thousands) (divided into the main items)	Estimated work plan budget (USD thousands) (divided into the main items)	Description of the updated work plan defined for the period	Period
---	---	As set out above, the Ashkelon lease was granted in June 2002 and the Noa lease was granted in February 2000. At the date of the report, there is no binding work plan for these leases in the period.	2012-2014

E. Actual and planned work plan for the Yam Tethys project

1. The table below includes a summary of the main operations actually performed in the Noa and Ashkelon leases since January 1, 2009 through to the date of this report and a summary of the planned operations:

Ashkelon lease			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ⁸⁰	The Company's effective share in the cost/budget (USD thousands)
2009	Continuation of preparations to install the compression system at Mari B	34,668	10,681
2010	Two production drillings: Mari-B 9 and Mari-B 10 and continued installation of the compression system	108,936	33,563
2011	Completion of installation of the compression system, serviceability test and operation Feasibility test of exploration drilling at the satellite reservoirs of the Mari B reservoir ("Pinnacles")	17,139 ⁸¹	6,575
	Planning of the Pinnacles 1 drilling and assessing options for development	3,721	
2012 onwards	Pinnacles 1 exploration drilling to assess the presence of natural gas in the Pliocene target layers. The drilling is 3.5 km from the Mari B reservoir. Drilling started in March 2012 and is expected to continue for five weeks. The water depth at the drilling site is 375 m and the final planned depth for the well is 1,859 m.	26,279	8,394
	If natural gas is found in the target layers of the Pinnacles 1 well, in a quantity that is sufficient for development, the Pinnacles 1 drilling will be completed as a production drilling and will be connected to the production facilities of the Yam Tethys project.	70,000	22,358

Noa lease			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands)	The Company's effective share in the cost/budget (USD thousands)
2009	Appraisal of the development feasibility of the Noa reservoir	216	67
2010	No significant operations were performed in this period	-	-

⁸⁰ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

⁸¹ The amount does not include USD 10,464 thousand (the Company's share is USD 2,814 thousand) for a provision for future dismantling costs of production infrastructure.

Noa lease			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands)	The Company's effective share in the cost/budget (USD thousands)
2011	As part of the development of the Noa North reservoir (as defined below), two production wells were drilled, Noa 2 and Noa 3.	75,173 ⁸²	23,695
2012 onwards	- Continuation of development works at the Noa North reservoir, including completion of wells, installation of pipelines and connection to the Yam Tethys project, and start of natural gas production - See section 1.11.4(e)(2) below for further information about the development plan in the Noa lease.	136,877	43,719

Forward-looking information: The above estimate of the partnerships regarding costs and schedules of the planned operations in the Yam Tethys project is forward-looking information, as defined in the Securities Law, based on assessments made by the general partner in the partnerships regarding the cost components of the project, which are based on assessments that the general partners in the partnerships received from the operator. Actual schedules and costs may differ from the above estimate, and are contingent, inter alia, on completion of detailed planning of the project components, applicable regulation, bids from contractors, changes to global suppliers and raw material markets, and the implementation of these operations.

2. Development plan for the Noa lease

On June 12, 2011, the Petroleum Commissioner informed the project operator that he approves the development of the northern part of the Noa field ("Noa North"). The Commissioner also accepted the operator's assessment (according to the information presented to him) that there is a low probability that significant quantities of gas will migrate to the Noa North reservoir from other parts of the reservoir extending further to the south and southwest. In addition, the Commissioner instructed the Company to limit the total quantity of gas produced to the quantity in the Noa North reservoir, which the operator estimates at 1.2 BCM, to prevent allegations of gas production from other parts of the reservoir extending beyond the lease area.

On July 31, 2011, the partnerships approved the budget and development plan for the Noa North reservoir in the Noa Lease, according to the outline presented by Noble ("the development plan").

Development of the Noa North reservoir will provide additional supply of natural gas to the Israeli market, mainly to customers that have signed agreements with the partnership for the supply of natural gas, until gas supply from the Tamar project commences.

The development plan includes mainly drilling of two diagonal production wells with subsea completions, Noa 2 and Noa 3, to a vertical depth of 1,880 m (including a water depth of 800 m). The drillings will be completed subsea, which the operator believes will allow production of 100 MMcf/d of natural gas from both wells. The natural gas will flow through a pipeline to the Mari-B production platform for processing, and then through the existing 30-in pipeline to the Yam Tethys reception terminal at Ashdod.

According to Noble, development of the Noa North reservoir should be completed in the third quarter of 2012 at a total development cost (for 100% of the rights) of USD 212 million (the partnerships' share is estimated at USD 102.82 million).

⁸² The amount does not include USD 12,967 thousand (the Company's share is USD 3,486 thousand) for a provision for future dismantling costs developing drilling in the lease.

Forward looking information: The estimates and information, including for the development plan, timetables, scope, manner of production and estimated costs of the plan are forward-looking information as defined in the Securities Law. The estimates and information are based on information received from Noble, which is as yet uncertain. The estimates and information are expected to be adjusted as additional information becomes available and/or as the result of a range of factors related to natural gas exploration and production projects.

F. Disclosure of the effective participation rate in the expenses and revenues in the Yam Tethys project

Ashkelon lease				
Participation rate	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of the oil asset attributable to the Company	31.63%	100%	100%	The Company's holdings in the oil asset are direct and indirect holdings through holdings in the participation units of the partnerships.
Effective share of the oil asset revenues attributable to the Company	28.60%	90.43%	90.43%	See the calculation in section 1.11.401.11.4G(H) below.
Effective share of expenses for development or production of the oil asset, attributable to the Company	31.90%-31.94%	100.85%	101.00%	See the calculation in section 1.11.4(H) below.
Effective share of expenses for exploration and development of the oil asset, attributable to the Company	31.94%-32.89%	101.00%	104.00%	See the calculation in section 1.11.4(H) below.

Noa lease					
Participation rate	Percentage before return on investment	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of the oil asset attributable to the partnership	31.63%	31.63%	100%	100%	The Company's holdings in the oil asset are direct and indirect holdings through holdings in the participation units of the partnerships.
Effective share of the oil asset revenues attributable to the partnership	29.82%	30.15%	94.29%	95.33%	See the calculation in section 1.11.4(H)1.11.4G below.
Effective share of expenses for development or production of the oil asset, attributable to the partnership	31.90%	31.94%	100.85%	101.00%	See the calculation in section 1.11.4(H) below.

G. Calculation of the effective share of revenues in the Tamar project attributable to equity holders of the Company

Ashkelon lease		
Description	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (reference to the agreement)
Theoretical annual revenues of the oil asset	100%	
The State	(11.34%)	Calculated at the wellhead price according to the 2011 calculation (meaning, of 12.5%, expenses are deducted for gas development, transmission and treatment systems up to the delivery point of the gas at Ashdod).
Total	(11.34%)	
Adjusted revenues on the level of the oil asset	88.66%	
The share of the adjusted oil asset revenues attributable to the equity holders of the Company (concatenation)	31.63%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	28.04%	
Royalties or payments (derived from revenues after discovery) in respect of the oil asset at the level of the Company		
Share of the equity holders of the Company in the payment to related parties and third parties that collect payment at the level of the Company	2.4669%	In the Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In the Avner Partnership – overriding royalties at a rate of 6%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	
Total	25.5731%	
Share of holders of the Company's equity rights in revenues due to additional royalties from the asset	3.075%	Overriding royalties at a rate of 3% up to ROI and 13% after ROI, and overriding royalties at a rate of 6% calculated at the wellhead price according to the calculation in 2011 in the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	28.65%	

Noa lease			
Description	Before return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (reference to the agreement)
Theoretical annual revenues of the oil asset	100%	100%	
Royalties or payment (derived from revenues after the discovery) related to the oil asset:			
The State	(5.5%)	(5.5%)	Calculated at the wellhead price according to the calculation in 2011 for the Yam Tethys project
Total	(5.5%)	(5.5%)	
Adjusted revenues on the level of the oil asset	94.50%	94.50%	
The share of the adjusted oil asset revenues attributable to the equity holders of the Company (concatenation)	31.63%	31.63%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	29.89%	29.89%	
Royalties or payments (derived from revenues after discovery) in respect of the oil asset at the level of the Company			
Share of the equity holders of the Company in the payment to related parties and third parties that collect payment at the level of the Company	0.5129%	1.1956%	In the Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In the Avner Partnership – overriding royalties at a rate of 13%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	=====	
Total	29.3771%	28.6944%	
Share of holders of the Company's equity rights in revenues due to additional royalties from the asset	0.4471%	1.457%	Overriding royalties at a rate of 3% up to ROI and 13% after ROI, and overriding royalties at a rate of 6% calculated at the wellhead price according to the calculation in 2011 in the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	29.82%	30.15%	

H. Calculation of the effective participation rate of the Company's equity holders in exploration, development and production expenses in the Yam Tethys project

Ashkelon lease – exploration operations		
Description	%	Summary of the calculation method for royalties or payments (reference to the agreement)
Theoretical expenses in the work plan for the oil asset (without royalties)	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	1%-4%	These amounts are for indirect expenses and are in addition to reimbursement of direct expenses paid to the operator. The rate of payment to the operator decreases as exploration expenses increase.
Total effective rate of expenses at the level of the oil asset	101% -104%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	31.63%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	31.94%-32.89%	
On the level of the Company		
Payments (derived from expenses) in respect of the oil asset and on the level of the Company		
General partner in Avner Partnership		In accordance with the partnership agreement in the Avner Partnership, the general partner is entitled to the higher of 7.5% of the Avner Partnership's exploration expenses or USD 40 thousand a month on a quarterly calculation.
Effective share of expenses for exploration and development of the oil asset, attributable to the Company	31.94%-32.89%	

Ashkelon lease - development or production operations		
Description	%	Summary of the calculation method for royalties or payments (reference to the agreement)
Theoretical expenses in the work plan for the oil asset (without royalties)	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	1%-0.85%	These amounts are for indirect expenses and are in addition to reimbursement of direct expenses paid to the operator. The rate of payment to the operator decreases as development or production expenses increase.
Total effective rate of expenses at the level of the oil asset	100.85% - 101%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	31.63%	

Ashkelon lease - development or production operations		
Description	%	Summary of the calculation method for royalties or payments (reference to the agreement)
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	31.90%- 31.94%	
<u>On the level of the Company</u>		
Payments (derived from expenses) in respect of the oil asset and on the level of the Company		
General partner in Avner Partnership	-	
Effective share of expenses for exploration and development of the oil asset, attributable to the Company	31.90%- 31.94%	

Noa lease - development or production operations		
Description	%	Summary of the calculation method for royalties or payments (reference to the agreement)
Theoretical expenses in the work plan for the oil asset (without royalties)	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	1%-0.85%	These amounts are for indirect expenses and are in addition to reimbursement of direct expenses paid to the operator. The rate of payment to the operator decreases as development or production expenses increase.
Total effective rate of expenses at the level of the oil asset	100.85% - 101%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	31.63%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	31.90%- 31.94%	
<u>On the level of the Company</u>		
Payments (derived from expenses) in respect of the oil asset and on the level of the Company		
General partner in Avner Partnership	-	
Effective share of expenses for exploration and development of the oil asset, attributable to the Company	31.90%- 31.94%	

I. Royalties and payments paid during exploration, development and production operations for the oil asset (USD thousands)

Ashkelon lease			
Description	Total share of equity holders of the Company in investment in the oil asset in this period ⁸³	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator (beyond the direct return of expenses)
Budget actually invested in 2009 (including the payments)	15,736	28	198
Budget actually invested in 2010 (including the payments)	39,506	28	378
Budget actually invested in 2011 (including the payments)	13,909	28	180

Noa lease			
Description	Total share of equity holders of the Company in investment in the oil asset in this period	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator (beyond the direct return of expenses)
Budget actually invested in 2009 (including the payments)	67	0	0
Budget actually invested in 2010 (including the payments)	0	0	0
Budget actually invested in 2011 (including the payments)	23,694	0	113

J. Contingent reserves and resources from the Yam Tethys project

1. Reserves in the Ashkelon lease

A) Quantitative data

According to a report received by the Company from NSAI, prepared in accordance with the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), the natural gas reserves in the Mari-B field, are classified as on production reserves and as of December 31, 2011, they are as follows:

Reserve category	Total in the oil asset (gross) BCF	Company's share (net) BCF
P1 proved reserves	206.3	59.1
Probable reserves	22	6.3
P2 proved + probable reserves	228.2	65.4
Possible reserves	22	6.3
Total P3 reserves (proved + probable + possible reserves)	250.3	71.7

⁸³ Including costs for which payments are not made to the operator.

Forward-looking information: Possible reserves are the additional reserves that are not expected to be produced to the same extent as probable reserves. There is a 10% chance that actual quantities produced will be equivalent to or higher than the proved reserves, with the addition of the quantity of the probable and possible reserves.

The NSAI report noted a number of assumptions and qualifications, including: (1) The appraisals do not reflect the risk;⁸⁴ (2) NSAI did not visit the drilling site or check the mechanical operational state of the facilities and the wells; (3) NSAI did not examine the possible exposure arising from environmental matters. However, according to NSAI, at the date of the reserves report, it is unaware of any possible environmental liability that could have a material effect on the amount of reserves estimated in the reserves report, or on whether they are commercial, therefore the reserves report does not include the costs that could arise from such liability.

Forward-looking information: The estimates of NSAI in respect of the natural gas reserves in the Mari B field are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling and from the lease operator, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas consumed may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production projects, including due to production from the reservoir and due to operational and/or market and/or regulatory conditions.

B) The Company declares that all of the above information has been prepared in compliance with SPE- PRMS.

C) Discounted cash flows

In relation to calculation of the discounted cash flows described below, NSAI also noted that (1) The estimates were not adjusted to reflect risk.⁸⁵ (2) The operating costs taken into account are costs provided to NSAI by the partnerships and appear reasonable, based on NSAI's experience in similar projects. These costs include only direct costs on the project level and the partnerships' estimate of their share in the overheads, general and administrative expenses which can be directly attributed to the project. As required by the partnerships, these costs remain fixed during the life of the project. (3) The capital expenditure taken into account includes capital expenditure provided to NSAI by the partnerships and are expenses for investments approved by the partnerships and actual expenses for recent operations, including for upgrading the production platform, and appear reasonable, based, inter alia, on the development plan in the Mari B field and NSAI's experience in similar projects. As required by the partnerships, these costs remain fixed until actually expended. (4) The abandonment costs taken into account are costs provided to NSAI by the partnerships according to its assessments of the cost of abandoning wells, platforms and production facilities. These costs do not take into account the salvage value of the Mari B lease and facilities in the Mari B field. As required by the partnerships, abandonment costs remain fixed until actually expended. (5) The tax calculations take into account corporate tax rates provided to NSAI by the partnerships, which are the expected tax rates for each of the years included in the discounted cash flows. (6) Actual production capacity for each of the reserve categories described above could be lower or higher than the production capacity used to estimate the

⁸⁴ The estimates in the report, as is standard in estimating reserves based on the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), are not adjusted to reflect external risks that are not directly related to the scope of the reservoir and its production capacity (such as security and commercial risks).

⁸⁵ The estimates in the report, as is standard in estimating reserves based on the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), are not adjusted to reflect external risks that are not directly related to the scope of the reservoir and its production capacity (such as security and commercial risks).

discounted cash flows. NSAI did not prepare a sensitivity analysis for the production capacity of the wells. A sensitivity analysis could lead to a conclusion that the reserves are not feasible for production.

It is further noted that the discounted cash flow is based on the gas price of USD 4.404 per MMBtu, which is fixed up to December 31, 2012. In 2013, the gas price is expected to be USD 3.15 per MMBtu. As from January 1, 2014 and through to the end of the project life, the discounted cash flow is based on the gas price of USD 2.5 per MMBtu.

It is further noted that the discounted cash flow includes royalties as described in section 1.11.4G above, as well as taxes applicable to the partnerships in accordance with the Taxation of Petroleum Profits Law, 2011 ("the Law"). It is emphasized that calculation of the levy was based on the definitions, formulas and mechanisms set out in the law as understood and interpreted by the partnerships, however, since the law is new and the calculation formulas and mechanisms set out in the law are complex, it is not certain whether this interpretation of the calculation method for the levy will be the same as that adopted by the tax authorities and/or the same as the interpretations of the law by the court, insofar as a ruling is required on these issues. At the date of the report, these issues have not been brought before the courts in Israel. The levy was calculated according to the transitional provisions in the law for a project that started commercial production before the law came into effect, based on the following assumptions: The developer will report in US dollars according to section 13(B) of the law, the rate of inflation in the United States in the coming years will be 2%, all of the developer's payments (production costs and investments) will be recognized by the tax authorities for calculation of the levy and calculation of the developers revenues will take into account actual selling prices of the gas.

It is emphasized that the discounted cash flow is based on the updated assessment of the operation for actual production capacity, which could change in the future, and which does not allow production of the full quantity of the reserves until gas supply starts from the Tamar project.

In recent months, there has been a significant decrease in the production capacity of natural gas from the Mari B reservoir, which led to reduced supply of natural gas from the reservoir to customers in the Yam Tethys project. From information provided to the partnerships by the operator, based on an assessment and analysis carried out by the operator by itself and through third parties, production of natural gas from the Mari B reservoir, which resulted in a steady decline in the pressure in the reservoir, caused large-scale sinking of the layers above the reservoir and below the production platform. Sinking of the soil layers also resulted in damage and loss of production capacity in some of the production wells, so that today, natural gas is only produced from Mari B 5, 9, and 10 wells (in one of these wells, increased penetration of water into the production wells was detected, in a way that impairs production capacity). It is noted that the production platform at the Yam Tethys project is planned from an engineering and technical aspect to allow for sinking, mainly due to sinking of the soil layers above the reservoir and below the production platform, and at this stage, sinking of the production platform is within permitted levels according to the engineering plan.

The operator intends to produce natural gas from the reservoir at the production rate, which will retain steady production capacity from the reservoir and will not cause damage to the platform.

In addition, the project partners are taking steps to develop the Noa reservoir, drill the satellite reservoirs of the Mari B reservoir (Pinnacles) and develop them (if natural gas is discovered), with the aim of timely production, thereby reducing the steady decline in supply capacity and moderating its implications, while maintaining the serviceability of the production system of the Yam Tethys project.

According to the reserves report, attached as Appendix A to this report, there is no change in the estimate of the reserves in the reservoirs (other than a decrease in amounts actually produced), therefore this development is mainly reflected in a significant decrease in the production capacity of the Mari B reservoir and production facilities.

The discounted cash flow in the reserves report is based on the operator's estimate of the expected reduction in production capacity from the Mari B reservoir.

The project operator informed the partnerships that the estimated average daily amount of gas that the Yam Tethys project will supply in the period up to the expected date of gas supply from the Tamar project is expected as set out in the discounted cash flow of the Mari B reservoir (for further information see section 1.11.4(I)(1)(c) above). If the Noa reservoir is developed and connected to the Yam Tethys production system, an average daily amount of gas will be added as set out in the discounted cash flow of the Noa reservoir (see section 1.11.4(I)(2)(c) above). If and when Pinnacles is developed and connected to this production system, an average amount of gas of MMcfd 60 will be added.

The decline in production capacity of natural gas is expected to have an adverse effect on the financial results of the partnerships, however, at this stage, the partnerships are unable to estimate at high level of certainty the full commercial implications and the extent of the effect, partly due to the frequent developments in the project.

The partnerships are holding discussions with their customers regarding the decrease in supply and its legal implications. The partnerships' position is that the decrease in supply capacity is a force majeure incident as defined in the gas supply contracts. If the partnerships' position is not accepted, the partnerships may be exposed to payment of fines in accordance with mechanisms and restrictions set out in the gas supply contracts. However, in the reporting year, the Company recognized a provision of USD 5 million for losses due to these events (net, less royalties).

Forward-looking information: The estimates of the partnerships regarding the amounts of gas that will be produced as set out above are forward-looking information as defined in the Securities Law. These estimates are based on various assumptions, including the rate and duration of natural gas sales from the reservoirs, which may not be realized, and the quantity of natural gas actually produced, which may be different from these estimates, inter alia, due to operational and technical conditions and/or changes in regulations and/or supply and demand in the natural gas market and/or actual performance of the reservoirs.

According to the aforesaid, including the operator's estimates submitted to the partnerships of the expected production capacity from the Mari B reservoir in 2012 and the partnership's estimates of the commercial implications of the decline in production capacity of natural gas to its customers, below the Company's estimate of the discounted cash flow in USD thousands (after the levy and income tax) attributable to the partnership's share in the reserves in the Mari B field, for each of the reserve categories set out above.

Total discounted cash flow from proved reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
		-	-	-	-	-	-	-	-	Total discounted cash flow after tax					
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
	100%	-	-	-	-	-	-	-	-	-					
Dec. 31, 2012	1.70	84,746	(16,221)	8,176	(5,231)	-	-	71,470	16,271	8,465	46,734	45,608	44,559	43,580	42,662
Dec. 31, 2013	0.50	17,828	(3,412)	1,701	(735)	(1,581)	-	13,800	3,450	24	10,325	9,597	8,950	8,372	7,855
Dec. 31, 2014	0.12	3,396	(650)	323	(63)	-	-	3,006	751	-	2,254	1,996	1,776	1,590	1,429
Dec. 31, 2015	0.12	3,396	(650)	323	(63)	-	-	3,006	751	-	2,254	1,901	1,615	1,382	1,191
Dec. 31, 2016	0.12	3,396	(650)	323	(63)	-	-	3,006	1,368	-	1,638	1,315	1,066	873	721
Dec. 31, 2017	0.12	3,396	(650)	323	(63)	-	-	3,006	1,368	-	1,638	1,252	970	759	601
Dec. 31, 2018	0.12	3,396	(650)	323	(63)	-	-	3,006	1,368	-	1,638	1,193	881	660	501
Dec. 31, 2019	0.12	3,396	(650)	323	(63)	-	-	3,006	1,368	-	1,638	1,136	801	574	417
Dec. 31, 2020	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	-	3,647	2,409	1,622	1,112	774
Dec. 31, 2021	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	-	3,647	2,294	1,475	967	645
Dec. 31, 2022	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	-	3,647	2,185	1,341	841	538
Dec. 31, 2023	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	-	3,647	2,081	1,219	731	448
Dec. 31, 2024	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	-	3,647	1,982	1,108	636	373
Dec. 31, 2025	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	-	3,647	1,887	1,007	553	311
Dec. 31, 2026	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	753	2,894	1,426	727	381	206
Dec. 31, 2027	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	912	2,735	1,284	624	313	162
Dec. 31, 2028	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	912	2,735	1,223	568	273	135
Dec. 31, 2029	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	912	2,735	1,165	516	237	113
Dec. 31, 2030	0.27	7,563	(1,448)	719	(141)	-	-	6,694	3,047	912	2,735	1,109	469	206	94
Dec. 31, 2038	0.00	-	-	-	-	-	(16,170)	(16,170)	-	-	(16,170)	(4,438)	(1,294)	(398)	(129)
Total	5.86	206,148	(39,458)	19,719	(7,892)	(1,581)	(16,170)	160,765	60,213	12,889	87,663	78,602	69,999	63,641	59,046

Total discounted cash flow from probable reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
		-	-	-	-	-	-	-	-	Total discounted cash flow after tax					
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
	100%	-	-	-	-	-	-	-	-	-					
Dec. 31, 2012	0.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2013	0.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2014	0.05	1,443	(276)	137	-	-	-	1,304	326	-	978	866	771	690	620
Dec. 31, 2015	0.05	1,443	(276)	137	-	-	-	1,304	326	-	978	825	701	600	517
Dec. 31, 2016	0.05	1,443	(276)	137	-	-	-	1,304	594	-	710	570	463	379	313
Dec. 31, 2017	0.05	1,443	(276)	137	-	-	-	1,304	594	-	710	543	421	329	261
Dec. 31, 2018	0.05	1,443	(276)	137	-	-	-	1,304	594	-	710	517	382	286	217
Dec. 31, 2019	0.05	1,443	(276)	137	-	-	-	1,304	594	-	710	493	348	249	181
Dec. 31, 2020	0.03	756	(145)	72	-	-	-	683	311	-	372	246	166	114	79
Dec. 31, 2021	0.03	756	(145)	72	-	-	-	683	311	-	372	234	151	99	66
Dec. 31, 2022	0.03	756	(145)	72	-	-	-	683	311	-	372	223	137	86	55
Dec. 31, 2023	0.03	756	(145)	72	-	-	-	683	311	-	372	212	124	75	46
Dec. 31, 2024	0.03	756	(145)	72	-	-	-	683	311	595	(222)	(121)	(68)	(39)	(23)
Dec. 31, 2025	0.03	756	(145)	72	-	-	-	683	311	1,005	(632)	(327)	(175)	(96)	(54)
Dec. 31, 2026	0.03	756	(145)	72	-	-	-	683	311	252	120	59	30	16	9
Dec. 31, 2027	0.03	756	(145)	72	-	-	-	683	311	93	279	131	64	32	17
Dec. 31, 2028	0.03	756	(145)	72	-	-	-	683	311	93	279	125	58	28	14
Dec. 31, 2029	0.03	756	(145)	72	-	-	-	683	311	93	279	119	53	24	11
Dec. 31, 2030	0.03	756	(145)	72	-	-	-	683	311	93	279	113	48	21	10
Dec. 31, 2038	0.00	-	-	-	-	-	-	-	-	-	-	(1,807)	(1,227)	(661)	(333)
Total	0.60	16,979	(3,250)	1,614	-	-	-	15,343	6,449	2,223	6,670	3,023	2,445	2,231	2,004

Total discounted cash flow from possible reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
		-	-	-	-	-	-	-	-	Total discounted cash flow after tax					
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
	100%	-	-	-	-	-	-	-	-	-					
Dec. 31, 2012	0.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec.31, 2013	0.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2014	0.05	1,472	(282)	140	-	-	-	1,330	332	-	997	883	786	703	632
Dec.31, 2015	0.05	1,472	(282)	140	-	-	-	1,330	332	-	997	841	714	611	527
Dec.31, 2016	0.05	1,472	(282)	140	-	-	-	1,330	605	-	724	582	472	386	319
Dec.31, 2017	0.05	1,472	(282)	140	-	-	-	1,330	605	-	724	554	429	336	266
Dec. 31, 2018	0.05	1,472	(282)	140	-	-	-	1,330	605	-	724	528	390	292	221
Dec.31, 2019	0.05	1,472	(282)	140	-	-	-	1,330	605	-	724	502	354	254	185
Dec.31, 2020	0.03	818	(157)	78	-	-	-	739	337	-	403	266	179	123	86
Dec.31, 2021	0.03	818	(157)	78	-	-	-	739	337	-	403	253	163	107	71
Dec. 31, 2022	0.03	818	(157)	78	-	-	-	739	337	110	293	175	108	67	43
Dec.31, 2023	0.03	818	(157)	78	-	-	-	739	337	1,105	(703)	(401)	(235)	(141)	(86)
Dec. 31, 2024	0.03	818	(157)	78	-	-	-	739	337	511	(108)	(59)	(33)	(19)	(11)
Dec.31, 2025	0.03	818	(157)	78	-	-	-	739	337	101	302	156	83	46	26
Dec.31, 2026	0.03	818	(157)	78	-	-	-	739	337	101	302	149	76	40	21
Dec. 31, 2027	0.03	818	(157)	78	-	-	-	739	337	101	302	142	69	35	18
Dec. 31, 2028	0.03	818	(157)	78	-	-	-	739	337	101	302	135	63	30	15
Dec.31, 2029	0.03	818	(157)	78	-	-	-	739	337	101	302	129	57	26	12
Dec.31, 2030	0.03	818	(157)	78	-	-	-	739	337	101	302	122	52	23	10
Dec.31, 2038	0.00	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total	0.63	17,828	(3,412)	1,694	-	-	-	16,110	6,788	2,331	6,992	4,957	3,727	2,919	2,355

Sensitivity analysis for the main parameters of the discounted cash flow (gas price and quantity of gas sold) at December 31, 2011

Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%	Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%
10% increase in the quantity/price of gas					10% decrease in sales/price of gas				
P1	96,747	76,430	69,455	64,437	P1	78,552	63,345	57,592	53,424
Proved reserves					Proved reserves				
Probable reserves	7,338	2,772	2,487	2,213	Probable reserves	6,003	2,132	1,984	1,801
Total P2 reserves	104,084	79,202	71,942	66,650	Total P2 reserves	84,555	65,477	59,576	55,225
Proved + probable reserves					Proved + probable reserves				
Possible reserves	7,691	4,057	3,174	2,560	Possible reserves	6,293	3,407	2,673	2,155
Total P3 reserves	111,775	83,259	75,116	69,210	Total P3 reserves	90,848	68,884	62,248	57,380
Proved + probable + possible reserves					Proved + probable + possible reserves				
15% increase in the quantity/price of gas					15% decrease in sales/price of gas				
P1	101,298	79,650	72,368	67,139	P1	74,013	60,011	54,563	50,612
Proved reserves					Proved reserves				
Probable reserves	7,671	2,933	2,612	2,315	Probable reserves	5,670	1,973	1,859	1,697
Total P2 reserves	108,969	82,583	74,980	69,453	Total P2 reserves	79,683	61,985	56,422	52,310
Proved + probable reserves					Proved + probable reserves				
Possible reserves	8,041	4,215	3,294	2,656	Possible reserves	5,943	3,244	2,546	2,051
Total P3 reserves	117,009	86,798	78,274	72,110	Total P3 reserves	85,626	65,229	58,967	54,361
Proved + probable + possible reserves					Proved + probable + possible reserves				
20% increase in the quantity/price of gas					20% decrease in sales/price of gas				
P1	105,858	82,870	75,282	69,844	P1	69,461	56,653	51,514	47,783
Proved reserves					Proved reserves				
Probable reserves	8,005	3,103	2,745	2,422	Probable reserves	5,336	1,815	1,732	1,592
Total P2 reserves	113,863	85,972	78,027	72,266	Total P2 reserves	74,797	58,468	53,245	49,375

Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%	Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%
Proved + probable reserves					Proved + probable reserves				
Possible reserves	8,390	4,373	3,413	2,752	Possible reserves	5,593	3,082	2,419	1,947
Total P3 reserves	122,253	90,345	81,440	75,018	Total P3 reserves	80,391	61,550	55,664	51,322
Proved + probable + possible reserves					Proved + probable + possible reserves				

Note: It is clarified that the discounted cash flow figures, whether they have been calculated at a specific discount rate or without a discount rate, represent the present value but not necessarily the fair value

Forward-looking information: The discounted cash flows set out above are forward-looking information as defined in the Securities Law. The information above is based on various assumptions, including the rate and duration of natural gas sales from the reservoir, which may not materialize, and the quantity of natural gas actually produced could be different from these estimates and assumptions, inter alia, due to operational and technical conditions and/or changes in regulation and/or the supply and demand in the natural gas market and/or actual performance of the reservoir.

D) **Production data**

The following table presents production data for the Mary-B field, attributable to the Company:⁸⁶

		2011	2010	2009
Total output (attributable to the Company's share) in the period (MMcf)		48,330	35,386	30,520
Average price per production unit (attributable to the Company) (USD thousands per MMCF)		4.71	4.03	3.48
Average royalties (every payment derived from the output of the producing asset, including from the gross income from the oil asset) paid per production unit (attributable to the Company's share) (USD thousands per MMCF)	The State	0.53	0.45	0.39
	Third parties	0.05	0.05	0.04
	Interested parties	0.32	0.26	0.23
Average intake for royalties (derived from the output of the producing asset, including from the gross income from the oil asset) received per production unit (attributable to the Company's share) (USD thousands per MMCF)		0.41	0.34	0.30
Average production costs per production unit (attributable to the Company's share) (USD thousands per MMCF)		0.22	0.25	0.23
Average production costs per production unit (attributable to the Company's share) (USD thousands per MMCF)		4.00	3.36	2.89
Oil and gas profits tax		0.29	0	0
Average net intake per production unit after oil and gas profits tax (attributable to the Company's share) (in USD thousands for MMcf)		3.71	3.36	2.89
Depletion rate in the reporting period in relation to the overall quantity of gas in the reservoir (%) ⁸⁷		42.8%	24.3%	20.0%

E) **Opinion of the appraiser**

The reserves report prepared by NSAI at December 31, 2011 is attached to this report as Appendix A and includes the consent of NSAI to attach them to this report.

F) **Management declaration**

Declaration date: March 30, 2012

Name of reporting corporation: Delek Group Ltd.

Name of officer for assessment of the resources: Gabi Last

We hereby confirm that the assessor received all the relevant information required to perform the work.

We hereby confirm that nothing came to our attention that indicates any dependence between the assessor and the partnership.

We hereby confirm that the preparation of the resource assessment and the disclosure therein are our responsibility.

We hereby confirm that to the best of our knowledge, the resources assessed by the assessor are the most relevant, accurate and updated estimates available to us.

We hereby confirm that no change has been made to the identity of the assessor preparing the reserves report or the most recent contingent resources report issued by the partnership.

We agree to include this statement in this report.

Gabi Last, director

⁸⁶ Without depreciation and amortization and administrative and general expenses

⁸⁷ The depletion rate is the rate of gas produced in a year from the proved and expected reserves at the beginning of the year.

2. Reserves in the Noa lease

A) Quantitative data

According to a report that the Company received from NSAI, which was prepared in accordance with the guidelines set out in the SPE-PRMS, the natural gas reserves in the Noa field as of December 31, 2011 are as follows:

Reserve category	Total in the oil asset (gross) BCF	Company's share (net) ⁸⁸ BCF
P1 proved reserves	35.3	10.6

It is noted that the amount of reserves set out above is based on the decision of the Yam Tethys partnership to produce BCM 1 from the reservoir.

The NSAI reserves report noted a number of assumptions and qualifications, including: a) The appraisals do not reflect the risk;⁸⁹ b) NSAI did not visit the oil field or check the mechanical operational state of the facilities and the wells; c) NSAI did not examine the possible exposure arising from environmental matters. However, according to NSAI, at the date of the reserves report, it is unaware of any possible environmental liability that could have a material effect on the amount of reserves estimated in the reserves report, or on whether they are commercial, therefore the reserves report does not include the costs that could arise from such liability. (4) The resources are in undeveloped areas and accordingly they are based on assessments in respect of the size of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological properties.

Forward-looking information: The estimates of NSAI in respect of the natural gas reserves in the Noa field are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling and from the lease operator, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas consumed may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production, including due to the continued production from the reservoir and the operational conditions.

B) The Company declares that all of the above information has been prepared in compliance with SPE-PRMS.

C) Discounted cash flows

In relation to calculation of the discounted cash flows, NSAI also noted that (1) The estimates of the discounted cash flow do not reflect risk.⁹⁰ (2) The discounted cash flow is based on the gas price of USD 5.91 for Mcf, which is fixed until December 31, 2012. As from January 1, 2013 and through to the end of the project life, the discounted cash flow is based on a fixed gas price of USD 5.63 per Mcf. The

⁸⁸ In view of the attribution of some of the production infrastructure costs of the Mari B reservoir to the Noa reservoir, it is possible that there will be no return on investment (as defined in the royalties agreement set out in section 1.11.29(I) below). Accordingly, the Company's share is calculated after royalties are paid at the rate applicable before the return on investment.

⁸⁹ The estimates in the report, as is standard in estimating reserves based on the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), are not adjusted to reflect external risks that are not directly related to the scope of the reservoir and its production capacity (such as security and commercial risks).

⁹⁰ The estimates in the report, as is standard in estimating reserves based on the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), are not adjusted to reflect external risks that are not directly related to the scope of the reservoir and its production capacity (such as security and commercial risks).

partnership provided the information for the gas price to NSAI. (3) The operating costs taken into account are costs provided by the partnerships and appear reasonable, based on NSAI's experience in similar projects. These costs include only direct costs on the project level and the partnership's estimate of their share in the overheads, general and administrative expenses which can be directly attributed to the project. As required by the partnerships, these costs remain fixed during the life of the project. (3) The capital expenditure taken into account includes capital expenditure provided to NSAI by the partnerships and appears reasonable, based, inter alia, on the development plan in the Noa field and NSAI's experience in similar projects. The capital expenditure taken into account is the capital expenditures required to develop and complete wells and production equipment. As required by the partnerships, this capital expenditure remains fixed until actually expended. (5) The abandonment costs taken into account are costs provided to NSAI by the partnerships according to its assessments of the cost of abandoning wells, platforms and production facilities. These costs do not take into account the salvage value of the Noa lease and facilities in the Noa field. As required by the partnerships, abandonment costs remain fixed until actually expended. (6) The tax calculations take into account corporate tax rates provided to NSAI by the partnerships, which are the expected tax rates for each of the years included in the discounted cash flows. (7) Actual production capacity could be lower or higher than the production capacity used to estimate the discounted cash flows. NSAI did not prepare a sensitivity analysis for the production capacity of the wells. A sensitivity analysis could lead to a conclusion that the reserves are not feasible for production.

It is further noted that the discounted cash flow includes royalties as described above, as well as taxes applicable to holders of participating units in accordance with the Taxation of Petroleum Profits Law ("the Law"). It is emphasized that calculation of the levy was based on the definitions, formulas and mechanisms set out in the law as understood and interpreted by the partnerships, however, since the law is new and the calculation formulas and mechanisms set out in the law are complex, it is not certain whether this interpretation of the calculation method for the levy will be the same as that adopted by the tax authorities and/or the same as the interpretations of the law by the court, insofar as a ruling is required on these issues. To date, these issues have not been brought before the courts in Israel. The levy was calculated according to the transitional provisions in the law for a project that started commercial production before the law came into effect, based on the following assumptions: The developer will report in US dollars according to section 13(B) of the law, the rate of inflation in the United States in the coming years will be 2%, all of the developer's payments (production costs and investments) will be recognized by the tax authorities for calculation of the levy and calculation of the developers revenues will take into account actual selling prices of the gas.

Following is the discounted cash flows in thousands of USD (after the levy and income tax) of the Company from the reserves in the Noa field (the cash flow is based on assumptions, which are described above).

Total discounted cash flow from proved reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
											Total discounted cash flow after tax				
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
Dec. 31, 2012	0.42	28,242	2,011	400	1,261	47,407	-	(22,037)	-	-	(22,037)	(21,506)	(21,012)	(20,550)	(20,117)
Dec. 31, 2013	0.58	36,944	2,631	523	846	-	(4,428)	29,563	-	-	29,563	27,476	25,624	23,972	22,489
Dec. 31, 2014	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2015	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2016	-	-	-	-	-	-	(1,518)	(1,518)	-	-	(1,518)	(1,219)	(989)	(809)	(668)
	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total	1.00	65,187	4,642	923	2,107	47,407	(5,946)	6,007	-	-	6,007	4,751	3,624	2,612	1,704

Note: It is clarified that the discounted cash flow figures, whether they have been calculated at a specific discount rate or without a discount rate, represent the present value but not necessarily the fair value

Forward-looking information: The discounted cash flows set out above are forward-looking information as defined in the Securities Law. The discounted cash flow information above is based on various assumptions, including in respect of construction and operating costs and the rate and duration of natural gas sales, which may not materialize, and the quantity of natural gas actually produced, if produced, and/or actual construction and operating costs and/or cash flow information may be different from these estimates and assumptions, inter alia, due to technical and operational conditions and/or regulatory changes and/or supply and demand conditions in the natural gas market and/or from implementation of the Petroleum Profits Tax Law and/or changes in the construction budget for the production and transmission facilities that have yet to be completed and/or actual performance of the reservoir.

Sensitivity analysis for the main parameters of the discounted cash flow (gas price and quantity of gas sold) at December 31, 2011⁹¹

Future net income (USD thousands)					Future net income (USD thousands)				
Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%	Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%
10% increase in the price/quantity of gas sales					10% decrease in the price/quantity of gas sales				
P1 proved reserves	12,154	9,183	7,920	6,785	P1 proved reserves	(139)	(1,934)	(2,696)	(3,377)
15% increase in the price/quantity of gas sales					15% decrease in the price/quantity of gas sales				
P1 proved reserves	15,227	11,962	10,574	9,325	P1 proved reserves	(3,212)	(4,714)	(5,350)	(5,918)
20% increase in the price/quantity of gas sales					20% decrease in the price/quantity of gas sales				
P1 proved reserves	18,301	14,741	13,228	11,866	P1 proved reserves	(6,286)	(7,493)	(8,004)	(8,458)

⁹¹ It is clarified that the sensitivity analyses described below for this period were carried out by the Company.

3. Contingent resources in the Noa field

A) Quantitative data

According to a report that the partnership received from NSAI, which was prepared in accordance with the guidelines set out in the Petroleum Resources Management System approved by the SPE-PRMS, the contingent resources in the Noa lease as of December 31, 2011 are as follows:

Contingent resources	Total in the oil asset (gross) BCF	Company's share (net) ⁹² BCF
Low estimate (1C)	21.5	6.4
Best estimate (2C)	42.6	12.8
High estimate (3C)	68.9	20.7

The contingent resources described above are classified as development pending, and they are subject to removal of the restriction set by the Commissioner regarding the total amount of gas to be produced from the Noa North reservoir (as set out above) and additional development drillings. As there is no approved development plan for all the resources in the Noa lease at this stage, the resources in the Noa lease, other than the reserves in the Noa North field, are classified according to the principles of SPE-PRMS as contingent and not as reserves (as classified in the reserves report prepared on February 28, 2001). According to the contingent resources report, if these conditions are fulfilled, some of the contingent resources could be classified as reserves. The potential market for the Noa reservoir is the domestic market. For further information about the domestic gas market, see section 1.11.3(A) above.

Forward-looking information: There is no certainty that it will be commercially possible to produce any percentage of the contingent resources.

The contingent resources report prepared by NSAI includes a number of assumptions and qualifications: (1) The appraisals do not reflect development risks. (2) NSAI did not visit the oil field nor check the mechanical operation of the well or its state. (3) NSAI did not examine the possible exposure arising from environmental matters. However, according to NSAI, at the date of the contingent resources report, it is unaware of any possible environmental liability that could have a material effect on the amount of contingent resources estimated in the report, or on whether they are commercial, therefore the report does not include the costs in respect of this exposure. (4) The contingent resources are in undeveloped areas and accordingly they are based on assessments in respect of the size of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological properties.

Forward-looking information: The estimates of NSAI in respect of the contingent resources of natural gas in the Noa field are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling and from the lease operator, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas consumed may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production projects, including due to any development of the field and due to operational and/or market and/or regulatory conditions.

⁹² In view of the attribution of some of the production infrastructure costs of the Yam Tethys project to the Noa reservoir, it is possible that there will be no return on investment (as defined in the royalties agreement set out in section 1.11.29(I) below). Accordingly, the Company's share is calculated after royalties are paid to the State and to related parties at the rate applicable before the return on investment.

B) The Company declares that all of the above information has been prepared in compliance with the SPE-PRMS.

C) Opinion of the appraiser

The reserves report and contingent resources report prepared by NSAI at December 31, 2011 are attached to this report and include the consent of NSAI to attach them to this report.

D) Management declaration

1. Declaration date: March 30, 2012
2. Name of reporting corporation: Delek Group Ltd.
3. Name of officer for assessment of the resources: Gabi Last
4. We hereby confirm that the assessor received all the relevant information required to perform the work.
5. We hereby confirm that nothing came to our attention that indicates any dependence between the assessor and the Company.
6. We hereby confirm that the preparation of the resource assessment and the disclosure therein are our responsibility.
7. We hereby confirm that to the best of our knowledge, the resources assessed by the assessor are the most relevant, accurate and updated estimates available to us.
8. We hereby confirm that no change has been made to the identity of the assessor preparing the reserves report or the most recent contingent resources report issued by the Company.
9. We agree to include this statement in this report.

Gabi Last

4. Prospective resources in the Ashkelon lease - Pinnacles

On March 1, 2012, the Yam Tethys project partners decided to implement a drilling and development plan, contingent on discovery of natural gas in a quantity sufficient for development, in small satellite reservoirs (Pinnacles) adjacent to the Mari B reservoir, which may contain natural gas.

A) Quantitative data

According to a report that the partnerships received from NSAI, prepared in accordance with the guidelines set out in the Petroleum Resources Management System approved by the SPE-PRMS, at December 31, 2011, the prospective resources in the target layers of the satellite reservoirs adjacent to the Mari B reservoir (Pinnacles), as set out above are as follows:

Probability	Total in the oil asset (gross) BCF	Total Company share (gross)⁹³ BCF
Prospective resources - low estimate	25.7	7.3
Prospective resources - best estimate	47.6	13.6
Prospective resources - high estimate	78.2	22.4

B) The report was prepared on the basis of the results of adjacent drillings, geological maps and a 3-D seismic survey carried out and processed in 2000 and 2001 ("the seismic survey").

C) Basic parameters used to calculate the different scenarios:

⁹³ Before calculation of royalties

Parameter	Low	High
Gross rock volume (acre*feet)	42,432	87,616
Gross thickness (feet)	264	427
Area (acres)	161	205
Net to gross (decimal)	0.40	0.90
Porosity (decimal)	0.26	0.30
Gas saturation (decimal)	0.60	0.75
Gas formation volume factor (SCF/RCF)	214	214
Gas recovery factor (decimal)	0.65	0.80

- D) Material risks (referring to pre-drilling data) in continuing the process: The significant risks involved in drilling are mainly technical-operating risks, including risks of malfunctions in drilling activities and when running electric logs. If the technological-operational activities are completed without malfunctions, the risks later in the process that is required to achieve a commercial discovery include that the porosity and conductivity of the reservoir rock will not be high enough to allow a commercially-significant flow, penetration of water into the well, which will prevent economically feasible production, and development costs of the discovery. See section 1.11.3(I) below for a discussion of the risk factors involved in exploration.
- E) The estimated probability of success of each of the risk factors in the drilling and statistical estimate of the geological probability of finding natural gas in the well (pre-drilling data) are as follows:

Trap integrity (%)	Reservoir quality (%)	Source evaluation (%)	Migration / timing (%)	Total (%)
90	75	95	90	58

- F) Estimated probability of development for commercial production: At the date of the report, if a quantity of natural gas sufficient for development of the satellite reservoirs (Pinnacles) is discovered in the well, the well will be completed subsea as a production well and developed as part of the development plan for the Noa reservoir, with connection to the Yam Tethys production platform for treatment and flow to the receiving terminal in Ashdod, to allow commercial production in the second half of 2012. Drilling and development is possible due to the proximity of the well to the Yam Tethys production facilities, the projected size of the satellite reservoirs (Pinnacles), possible timetable for their development, and their being vital for supplying the requirements of the natural gas market in Israel until natural gas starts to flow from the Tamar reservoir. In view of the aforesaid, the immediate potential market for these resources is the Israeli market. For further information about the Israeli market, see section 1.11.3(A) above.
- G) The partnership's explanations of the basic parameters used to calculate the different scenarios: The parameters used to calculate the estimates are based, inter alia, in the results of the seismic survey, information obtained from drillings in the adjacent Mari B reservoir and from similar reservoirs in the region and in other countries.

There is no certainty that any part of these potential resources will indeed be discovered, and if discovered, there is no certainty that it will be commercially possible to produce any part of the resources. The prospective information does not constitute an evaluation in respect of the contingent reserves and resources, which can only be evaluated after exploration drilling, if at all.

Forward looking information: The drilling timetable, quantity of prospective resources, development plan and timetable for implementation, the technical possibility of connecting the satellite reservoirs to the Yam Tethys project facilities, production capacity from the satellite reservoirs, assuming hydrocarbons are found in the well, and additional data in respect of the drilling, are based on evaluations and assumptions received from the operator and/or NSAI, which is forward-looking information as defined in the Securities Law. These estimates are professional estimates and assumptions only. There can be no certainty in respect of them and they are expected to be adjusted.

These estimates are partially based on geological, geophysical and other information received from a seismic survey carried out in the lease area, drillings in adjacent areas, and technical-engineering information. Actual quantities of natural gas discovered (if discovered) and produced (if produced) may be different from these estimates and assumptions, partly due to geological conditions and/or technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of satellite reservoirs. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production projects, including due to drilling and its results and due to operational and/or market and/or regulatory conditions.

H) The Company declares that all of the above information has been prepared in compliance with the SPE-PRMS.

I) Opinion of the appraiser

A reserves report prepared by NSAI as of December 31, 2011 is attached to this report as a reference to the reserves report attached as Appendix C to the Periodic Report for 2011 of Delek Drilling Partnership, which was published on March 29, 2012 (ref. 2012-01-084516).

K. Joint operating agreement for the Yam Tethys project

Exploration and production operations in the Yam Tethys leases are carried out under a joint operating agreement (JOA) signed on February 24, 1999. The parties to the JOA are the Company, the limited partnerships and other partners in the Yam Tethys project. On July 1, 2011, the agreement was divided into two separate agreements for each of the I/7 Ashkelon and I/10 Noa leases. According to the JOA, Noble was appointed operator of the Yam Tethys project. Noble is an indirect subsidiary of Noble Energy Inc., a US oil and natural gas exploration and production company. Noble Energy Inc. is a public company traded on the NYSE under the symbol NBL.

The JOA includes the following provisions:

1. Noble will be the operator under the JOA and will bear sole responsibility for management of the joint operations. In managing the joint operations, Noble is subject to obligations concerning, inter alia, compliance with directives of the operating committee, agreements, licenses and legislation.
2. The operator will determine the number and identity of the workers, their work hours and the salary that will be paid to them regarding the joint operations.
3. Provisions were determined for indemnification and limit of liability for the operator, its officers and related parties in respect of the fulfillment of its duties as an operator, according to which the operator is entitled to indemnification for any damage, expense or liability pertaining to its duties as an operator (except in exceptional cases of gross negligence by its senior employees, in which case indemnification will apply for damages, expenses or liability exceeding one million dollars), as set out in the JOA.
4. The operator is entitled to reimbursement for all direct expenses arising from the fulfillment of its duties as an operator and reimbursement of its indirect expenses arising from the share of the joint venture expenses, ranging from 1% of the project expenses when the annual project expenses exceed USD 12 million, to 4% of project expenses when these are less than USD 4 million annually. For expenses associated with development and production operations for the Yam Tethys project, the parties agreed that for development and production expenses from January 1, 2004 the operator will be paid the equivalent of 1% of the indirect expenses up to a limit of USD 20 million in expenses, and 0.85% of expenses exceeding that amount.
5. The parties to the JOA have undertaken a duty of protection and indemnification for the operator, according to the rate of their participation in the Yam Tethys licenses. The operator's liability is limited to certain cases, such as gross negligence.
6. According to the JOA, Avner Oil and Gas Ltd. was appointed as the Israeli operator to carry out duties, functions, roles and services in Israel for the benefit of the joint operations, subject to coordination with Noble. The proceeds from these services are immaterial.

7. Operations committee: Under the agreement, the parties established an operations committee with the authority to approve and supervise the joint operations required to fulfill the terms of licenses to which the joint operating agreement applies. The operations committee is comprised of representatives of the parties, with each representative having voting rights in accordance with the rights of the party that they represent. Unless otherwise determined in the JOA, all decisions, approvals and other activities of the operating committee in respect of any proposal that is present to it, will be decided by an affirmative vote of two or more parties (which are not related or associated parties) which jointly hold at the time of the vote at least 51% of total participating rights in the area covered by the license to which the decision applies.

1.11.5 **Tamar project**

A. **General**

Tamar lease	
General information about the oil asset	
Name of oil asset	I/12 Tamar ⁹⁴
Location	Offshore asset about 100 kilometers west of Haifa
Area	Approximately 250 sq. m
Type of oil asset and description of permitted operations according to that types	Lease Operations permitted under the Petroleum Law - exploration and production
Original grant date of the oil asset	December 2, 2009
Original expiry date of the oil asset	December 1, 2038
Dates of decision to extend the term of the oil asset	-
Current expiry date of the oil asset	December 1, 2038
Note whether there is an additional option of extending the period of the oil asset: if there is such an option, note the period of the possible extension	Subject to the Petroleum law for an additional 20 years
Note name of operator	Noble
Names of the direct partners in the oil asset and their direct share in the oil asset and, to the best of the Company's knowledge, the names of the controlling owners in the partners	A. ("Noble") (36%)⁹⁵ B. Isramco Negev 2 Limited Partnership ("Isramco") (28.75%). To the best of the Company's knowledge, the general partner in Isramco, Isramco Oil and Gas Ltd., is a private company that is directly controlled by Haim Tsuff.⁹⁶ C. Delek Drilling Partnership (15.625%) D. Avner Partnership (15.625%) E. Dor Gas Exploration Limited Partnership ("Dor") (4%) To the best of the Company's knowledge, the general partner in Dor Gas Exploration, Alon Gas Exploration Management Ltd. is a private company controlled by Alon Israel Oil Company Ltd. Alon Israel Oil Company Ltd. is controlled by Bielsol Investments (1987) Ltd. (50.38%), a private company.

⁹⁴ The Tamar gas reservoir was discovered in the area covered by the Tamar lease in 2009.

⁹⁵ For further information about Noble, see section 1.11.3(A) above.

⁹⁶ As of February 29, 2012, the entities controlled by Haim Tsuff hold 32.25% of the participating units issued by Isramco Management (1998) Ltd. (the limited partner in Isramco). Moreover, Haim Tsuff has a direct holding of 0.43% of the participating units issued by the limited partner in Isramco.

Tamar lease	
General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	⁹⁷
Description of the Company's holding in the oil asset	Through its holdings in the Delek Drilling and Avner partnerships
Effective share of oil asset revenues attributable to equity holders of the Company	In revenue: Before return on investment - 15.89% After return on investment - 17.59% <u>In the right to participate in revenue</u> Before return on investment - 15.30% After return on investment - 15.72% In right to receive royalties: Before return on investment - 0.5940% After return on investment - 1.8706%
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 302,512

Dalit lease	
General information about the oil asset	
Name of oil asset	I/13 Dalit ⁹⁸
Location	Offshore asset about 50 kilometers west of Haifa
Area	Approximately 250 sq. m
Type of oil asset and description of permitted operations according to that types	Lease Operations permitted under the Petroleum Law - exploration and production
Original grant date of the oil asset	December 2, 2009
Original expiry date of the oil asset	December 1, 2038
Dates of decision to extend the term of the oil asset	-
Current expiry date of the oil asset	December 1, 2038
Note whether there is an additional option of extending the period of the oil asset: if there is such an option, note the period of the possible extension	Subject to the Petroleum law for an additional 20 years
Note name of operator	Noble
Names of the direct partners in the oil asset and their direct share in the oil asset and, to the best of the Company's knowledge, the names of the controlling owners in the partners	(1) Noble (36%) ⁹⁹ (2) Isramco (28.75%) ¹⁰⁰ (3) Avner partnership (15.625%) (4) Delek Drilling Partnership (15.625%) (5) Dor (4%) ¹⁰¹

⁹⁷ The leases were granted to the Partnership on December 2, 2009 following the Tamar and Dalit natural gas fields that were discovered in 2009 in the 309/Matan and 308/Michal licenses. The partnerships acquired most of the licenses in 2006 from third parties for no consideration.

⁹⁸ The Dalit gas reservoir was discovered in 2009 in the area covered by the Dalit lease.

⁹⁹ For further information about Noble, see section 1.11.3(A) above.

¹⁰⁰ See the details that appear above in respect of the Tamar lease for the names of the controlling owners.

¹⁰¹ For further information about Dor, see section 1.11.4(A) above.

Dalit lease	
General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	¹⁰²
Description of the Company's holding in the oil asset	Through its holdings in the Delek Drilling and Avner partnerships
Effective share of oil asset revenues attributable to equity holders of the Company	In revenue: Before return on investment - 15.89% After return on investment - 17.59% <u>In the right to participate in revenue</u> After return on investment - 15.30% After return on investment - 15.72% <u>In right to receive royalties:</u> Before return on investment - 0.5940% After return on investment - 1.8706%
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 9,726 thousand

- B. The terms that were set in the Tamar and Dalit leases are almost identical, and they include, inter alia, provisions on the following main subjects: The holders of the leases and their holding rates in each of the leases, as detailed above; a determination that the holders of the leases are not to replace the operator except by a company that has been approved by the Commissioner, in advance and in writing; the area of each of the leases is 250 square kilometers, which has been selected out of the areas covered by the licenses in which the leases have been given; the extent of the lease and the duties of the lease holder; the period of the lease is from December 2, 2009 through to December 1, 2038, and is divided into the development period, during the course of which the lease holder will carry out all of the activities that are required for the purpose of reaching the commercial production stage, and the commercial production stage, which is the period from the end of the development and until the end of the period of the lease, during the course of which the lease holder will carry out commercial production from the area covered by the lease subject to the provisions of the lease documentation; sale to consumers in Israel; duties on the part of the lease holder in respect of construction of the production system and the transportation system, in a manner that will enable an overall commercial production capacity from the area covered by both of the leases, which is not to fall below 7 billion cubic meters of natural gas a year from the beginning of the commercial production period and subject to the provisions of the lease documentation; a duty on the part of the lease holder to operate in accordance with timetables in respect of the achievement of the development plan for the production system, construction of the transportation system and reception facility, and in respect of the commencement of the construction of all of the aforesaid; a commitment with a supervision company to supervise planning and construction of the production system; conditions relating to commercial production' the storage of natural gas; provisions in respect of the cancellation or the restriction of the lease' provisions in respect of the abandonment of the production system facilities; the presentation of bank guarantees as collateral for the compliance with the lease documents, which is to be in force for the length of the entire period of the lease and for a period of two years after the time at which the period of the lease ends for any reason whatsoever, and terms for their exercise.

¹⁰² The leases were granted to the partnerships on December 2, 2009, following the natural gas discoveries at the Tamar and Dalit fields in 2009 in the area covered by the 309/Matan and 308/Michal licenses. The partnerships acquired the rights in the licenses in 2006 from third parties for no consideration.

C. Compliance with the terms of the work plan in the Tamar project¹⁰³

Period	Description of the work plan defined for the period	Description of work plan items completed in the period ¹⁰⁴	Description of work plan items not yet completed in the period
2009	--- ¹⁰⁵	---	---
2010	Submission of a development plan for the production system, including drilling - 12 months after receiving the lease; the plan will be updated from time to time, based on progress of implementation.	For further information, see the actual work plan and intended work plan for the Tamar and Dalit lease.	---
2011	- Submission of a plan to install the lease holder's pipeline - 15 months after receiving the lease - Submission of a plan to construct the receiving terminal - 15 months after receiving the lease - Start of construction of the production system - 18 months after receiving the lease - Start of installation of the lease holder's pipeline - 18 months after receiving the lease	For further information, see the actual work plan and intended work plan for the Tamar and Dalit lease.	---

D. Binding work plan according to the terms of the oil asset¹⁰⁶

Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012-2013	Continued construction of the production system and pipeline	-	-

¹⁰³ The work plan described in this table sets out the milestones in the Tamar and Dalit leases. At the date of the report, a detailed development plan for the Tamar lease only has been submitted.

¹⁰⁴ The description of the components of the work plan in the period are for the period up to the report date.

¹⁰⁵ As stated above, the lease was granted in December 2009.

¹⁰⁶ The work plan described in this table sets out the milestones in the Tamar and Dalit leases.

E. Actual and planned work plan for the Tamar project

1. The table below includes a summary of the main operations actually performed in the Tamar project from January 1, 2009 through to the date of this report and a summary of the planned operations:

Tamar lease			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹⁰⁷	The Company's effective share in the cost/budget (USD thousands)
2009	- On January 12, 2012, drilling of the Tamar 1 well, which started on November 18, 2008, reached a final depth of 4,900 meters and ended in the Tamar reservoir discovery. On April 27, 2009, work at the Tamar 2 well began 5.5 kilometers north of the Tamar 1 well down-dip of the Tamar formation, to verify data of the reservoir quality and continuation of the formation. On July 1, 2009, the well reached a final depth of 5,145 meters. - Planning and development works at the Tamar reservoir and initial acquisition of equipment	175,724	29,769
2010	- Implementation of planning and development works at the Tamar reservoir and initial acquisition of equipment - In December 2010, a development plan for the Tamar and Dalit fields was submitted to the Commissioner ("the Tamar reservoir development plan"). The development plan includes reference to the transmission system and flow of natural gas through the new production platform to the Yam Tethys receiving terminal at Ashdod. For further information see section 1.11.5(E)(2) below.	434,221	73,560
2011	- Implementation of the development plan in the Tamar reservoir, including - Implementation of an engineering plan, purchase of equipment and preparation before development drilling - Four development drillings, Tamar 3, Tamar 4, Tamar 5 and Tamar 6, two of which were completed in the first quarter of 2012. - Supply and installation of most of the transmission system from the Tamar field to the area where the production platform will be constructed - Construction of the command and control pipeline system connecting the production platform to the drillings, allowing control and command - Construction of the production platform and supply of most of the equipment	1,073,910	186,465

¹⁰⁷ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

Tamar lease			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹⁰⁷	The Company's effective share in the cost/budget (USD thousands)
	- Construction of the tower bearing the production platform - Supply and production of all the subsea equipment that will be installed in the Tamar field - Implementation of the changes required at the onshore receiving terminal in Ashdod and the Mari B production platform		
2012	- Continuation of the development plan in the Tamar reservoir, including - Completion of production drillings - Completion of connection of the pipeline - Transportation and construction of the production platform - Continuation of connection of the subsea equipment in the Tamar field - Completion of changes required in the Mari B production platform - Continuation of changes required in the onshore receiving terminal at Ashdod	1,328,328	231,607
	- Completion of the development plan in the Tamar reservoir, including - completion of changes required in the onshore receiving terminal at Ashdod - Running in and operation of the Tamar project - Start of natural gas flow to the pipeline	110,000 ¹⁰⁸	19,180

Dalit lease			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹⁰⁹	The Company's effective share in the cost/budget (USD thousands)
2009	On March 6, 2009, drilling at the Dalit 1 well began On March 25, 2009 the well reached a final depth of 3,660 meters and ended in the Dalit reservoir discovery.	57,208	9,691
2010	-	-	-
2011	-	-	-
2012 onwards	A work plan has yet to be set for this period.		

¹⁰⁸ The investments taken into account include only development costs approved by the partnerships for development of the Tamar lease, and do not include future costs after production begins for use of part of the development facilities of the Yam Tethys project and expansion of output at the receiving terminal in Ashdod.

¹⁰⁹ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

2. Development plan for the Tamar project

On August 10, 2010, the Ministry of Energy announced that the Minister of Energy granted the partners in the Tamar project approval to develop the Tamar gas field as a dual pipeline for the delivery of natural gas from the field to a platform that will be constructed north of and nearby the Yam Tethys platform and from there, through the existing pipeline to the Yam Tethys receiving terminal in Ashdod, which will be expanded to receive the gas.

On August 18, 2010, the Commissioner informed Noble that he was approving its application for the development of the Tamar reservoir in accordance with the above outline. The Petroleum Commissioner also asked Noble for a reservoir development plan, including the arrangements between the partners in the Tamar lease and the holders of rights in the Ashkelon lease regarding use of the pipeline and receiving terminals as well as the onshore handling facilities, including storage arrangements.

In December 2010, a development plan for the Tamar field was submitted to the Commissioner. The development plan, which was updated several times in 2011, is for the Tamar and Dalit reservoirs, however, the partners decided, in the first stage, to advance the development of the Tamar field only ("the development plan").

The development plan includes mainly five wells, each with a planned production capacity of 200-250 MMcf/d. The gas will flow from the Tamar field through two 16" pipelines to the new handling platform which will be constructed opposite the coastline at Ashkelon, adjacent to the existing platform for the Mari-B reservoir. The Tamar platform will connect to the existing 30" pipeline that delivers natural gas to the Yam Tethys onshore receiving terminal in Ashdod, which will be rehauled to allow preliminary processing capacity of up to 1 billion cubic feet of gas per day. The development plan could include penetration and storage of natural gas from the Tamar reservoir in the Mari B reservoir and expansion of gas supply capacity, if required and according to the needs of the country.

The development plan is carried out in three stages: In the first stage, four development wells were drilled (Tamar 6, Tamar 5, Tamar 4 and Tamar 3) to an initial depth of 2,500 m (including water depth). In the second stage, these wells were drilled to a final depth of 5,200 m, and in the final stage, these wells and the Tamar 2 well (which was drilled in 2009 as an appraisal drilling) are completed for production. At the publication date of the report, the first and second development stages have been completed. The running in of the project systems is expected to start in the fourth quarter of 2012, with the objective of starting commercial supply of gas in the first half of 2013. After completing the development plan, the maximum possible production rate from the project is planned at 1 BCF a day.

The development plan for the Tamar project, approved by the lease partners, is USD 3.06 billion, including:

- A) Planning works
- B) Drilling and completion of five production wells
- C) Development of the subsea systems in the gas field
- D) Equipment and pipes for the subsea production system
- E) Contractor services for construction of the subsea systems
- F) Pipes to connect the gas field to the platform:
- G) 16" pipes
- H) service pipes
- I) control and command pipes
- J) Service pipes to connect the platform to the Ashdod receiving terminal
- K) Contractor to install the pipeline
- L) Planning and construction of the offshore production platform and the equipment to be installed on the platform
- M) Transportation services for the platform and construction of the platform

N) Expansion of the Ashdod onshore receiving terminal

Forward-looking information: The above estimate of the Company regarding costs and schedules of the planned operations in the Tamar project, including development drilling, is forward-looking information, as defined in the Securities Law, based on initial assessments made by the general partner in the partnerships regarding the cost components and timetables of the project, which are based on assessments that the general partners received from the operator. Actual schedules and costs may be materially different from the above estimate, and are contingent, inter alia, on the completion of detailed planning of the project components, bids from contractors, changes to global suppliers and raw material markets, such as metals, and the actual implementation of this complex project.

Further to this section, at the date of the report, the partners in the Tamar project in the advance stages of negotiations with the partners in the Yam Tethys project for commercial arrangements regarding connection of the Tamar project to the Yam Tethys pipeline and reception terminal in Ashdod and regarding storage of natural gas from the Tamar project at the Mari-B reservoir, to the extent that storage is possible from a technical and regulatory aspect. At the date of the report, the commercial terms have yet to be agreed.

F. Disclosure of the effective participation rate in the expenses and revenues in the Tamar project

Tamar lease					
Participation rate	Percentage before return on investment	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of oil asset attributable to equity holders of the Company	17.436%	17.436%	100%	100%	Through its direct holding and holdings in participation units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset revenues attributable to equity holders of the Company	15.30%	15.72%	87.77%	90.15%	See the calculation in section 1.11.5(H) below.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	17.436%	17.436%	100%	100%	See the calculation in section 1.11.5(H) below.

Dalit lease					
Participation rate	Percentage before return on investment	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of oil asset attributable to equity holders of the Company	17.436%	17.436%	100%	100%	Through its direct holding and holdings in participation units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset revenues attributable to equity holders of the Company	15.30%	15.72%	87.77%	90.15%	See the calculation in section 1.11.5(H) below.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	17.436%	17.436%	100%	100%	See the calculation in section 1.11.5(H) below.

G. Calculation of the effective share of revenues in the Tamar project attributable to equity holders of the Company

Tamar Lease			
Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical annual revenues of the oil asset after the discovery	100%	100%	
Royalties or payment (derived from revenues after the discovery) related to the oil asset *:			
The State	(11.34%)	(11.34%)	Calculated at the wellhead price according to the calculation in 2011 for the Yam Tethys project
	=====	=====	
Adjusted revenues on the level of the oil asset	88.66%	88.66%	
The share of the adjusted oil asset revenues attributable to the equity holders of the Company	17.436%	17.436%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	15.46%	15.46%	

Tamar Lease			
Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Royalties or payments (derived from revenues after discovery) in respect of the oil asset at the level of the Company			
<u>On the level of the Company</u>			
Share of the equity holders of the Company in the payment to a third party that collects payment at the level of the Company	0.0576%	0.0576%	Overriding royalties at a rate of 6% for 1.25% of the rights in the Tamar lease are paid to the owner of the royalty after deducting the royalty to the state in accordance with the Petroleum Law and less the amount of oil used for production and wellhead expenses based on the rate used in calculation of royalties for the state. The royalties for each partnership is at a rate of 0.06%.
Share of the equity holders of the Company in the payment to related parties and third parties that collect payment at the level of the Company	0.6906%	1.5533%	In the Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In the Avner Partnership – overriding royalties at a rate of 6%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	=====	
Total	14.7118%	13.8491%	
Share of holders of the Company's equity rights in revenues due to additional royalties from the asset	0.5940%	1.8706%	Overriding royalties at a rate of 3% up to ROI and 13% after ROI, and overriding royalties at a rate of 6% calculated at the wellhead price according to the calculation in 2011 in the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	15.30%	15.72%	

Dalit Lease			
Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical annual revenues of the oil asset after the discovery	100%	100%	
Royalties or payment (derived from revenues after the discovery) related to the oil asset *:			
The State	(11.34%)	(11.34%)	Calculated at the wellhead price according to the calculation in 2011 for the Yam Tethys project
	=====	=====	
Adjusted revenues on the level of the oil asset	88.66%	88.66%	

Dalit Lease			
Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
The share of the adjusted oil asset revenues attributable to the equity holders of the Company	17.436%	17.436%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	15.46%	15.46%	
Royalties or payments (derived from revenues after discovery) in respect of the oil asset at the level of the Company			
On the level of the Company			
Share of the equity holders of the Company in the payment to a third party that collects payment at the level of the Company	0.0576%	0.0576%	Overriding royalties at a rate of 6% for 1.25% of the rights in the Tamar lease are paid to the owner of the royalty after deducting the royalty to the state in accordance with the Petroleum Law, less the amount of oil used for production and less wellhead expenses based on the rate used in calculation of royalties for the state. The royalties for each partnership is at a rate of 0.06%.
Share of the equity holders of the Company in the payment to related parties and third parties that collect payment at the level of the Company	0.6906%	1.5533%	In the Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In the Avner Partnership – overriding royalties at a rate of 6%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	=====	
Total	0.7482%	1.6109%	
Share of holders of the Company's equity rights in revenues due to additional royalties from the asset	0.5940%	1.8706%	Overriding royalties at a rate of 3% up to ROI and 13% after ROI, and overriding royalties at a rate of 6% calculated at the wellhead price according to the calculation in 2011 in the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	15.30%	15.72%	

H. Calculation of the effective share of expenses in the Tamar project attributable to equity holders of the Company

Tamar Lease		
Description	%	Summary of the calculation method for royalties or payments (with reference to the agreement)
Theoretical expenses in the work plan for the oil asset (without royalties)	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	(0%)	The operator is entitled to reimbursement of direct expenses for its duties as operator. The partners are jointly reviewing the option of setting operator's fees that will be paid for indirect expenses.
Total effective rate of expenses at the level of the oil asset	100%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	17.436%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	17.436%	
Payments (derived from expenses) in respect of the oil asset and on the level of the Company		
General partner in Avner Partnership		In accordance with the partnership agreement, the general partner is entitled to the higher of 7.5% of the Avner Partnership's exploration expenses or USD 40,000 a month on a quarterly calculation.
Effective share of expenses for exploration and development of the oil asset, attributable to equity holders of the Company	17.436%	

Dalit Lease		
Description	%	Summary of the calculation method for royalties or payments (with reference to the agreement)
Theoretical expenses in the work plan for the oil asset (without royalties)	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	(0%)	The operator is entitled to reimbursement of direct expenses for its duties as operator. The partners are jointly reviewing the option of setting operator's fees that will be paid for indirect expenses.
Total effective rate of expenses at the level of the oil asset	100%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	17.436%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	17.436%	

Dalit Lease		
Description	%	Summary of the calculation method for royalties or payments (with reference to the agreement)
Details of payments (derived from the expenses) in respect of the oil asset and at the level of the Company (the following percentages will be calculated in accordance with the Company's share in the oil asset)		
General partner in Avner Partnership		In accordance with the partnership agreement, the general partner is entitled to the higher of 7.5% of the Avner Partnership's exploration expenses or USD 40 thousand a month on a quarterly calculation.
Effective share of expenses for exploration and development of the oil asset, attributable to equity holders of the Company	17.436%	

I. Royalties and payments paid during exploration, development and production operations for the oil asset (USD thousands)

Tamar Lease			
Description	Total share of equity holders of the Company in investment in the oil asset in this period ¹¹⁰	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator
Budget actually invested in 2009 (including the payments)	29,805	850	0
Budget actually invested in 2010 (including the payments)	73,577	0	0
Budget actually invested in 2011 (including the payments)	186,470	0	0

Dalit Lease			
Description	Total share of equity holders of the Company in investment in the oil asset in this period ¹¹¹	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator
Budget actually invested in 2009 (including the payments)	9,691	343	0
Budget actually invested in 2010 (including the payments)	0	0	0
Budget actually invested in 2011 (including the payments)	0	0	0

¹¹⁰ Including costs for which payments are not made to the operator.

¹¹¹ Including costs for which payments are not made to the operator.

J. Reserves, contingent and prospective resources in the Tamar lease¹¹²

1. Quantitative data

A) Reserves in the Tamar lease

According to a report that the partnerships received from NSAI, which was prepared in accordance with the guidelines set out in the Petroleum Resources Management System approved by the SPE-PRMS, the natural gas reserves in the Tamar field, classified as reserves approved for development as of December 31, 2011 are as follows:

Reserve category	Total in the oil asset (gross) BCF	Company's share (net) ¹¹³ BCF
P1 proved reserves	6,892.6	1,083.5
Probable reserves	2,817.9	442.9
P2 proved + probable reserves	9,710.5	1,526.4
Possible reserves	1,562.4	245.6
Total P3 reserves (proved + probable + possible reserves)	11,272.9	1,772.0

Forward-looking information: Possible reserves are the additional reserves that are not expected to be produced to the same extent as probable reserves. There is a 10% chance that actual quantities produced will be equivalent to or higher than the proved reserves, with the addition of the quantity of the probable and possible reserves.

The NSAI report noted a number of assumptions and qualifications, including: 1) The appraisals do not reflect the risk;¹¹⁴ (2) NSAI did not visit the oil field or check the mechanical operational state of the facilities and the wells; (3) NSAI did not examine the possible exposure arising from environmental matters. However, according to NSAI, at the date of the reserves report, it is unaware of any possible environmental liability that could have a material effect on the amount of reserves estimated in the reserves report, or on whether they are commercial, therefore the reserves report does not include the costs that could arise from such liability. (4) The resources are in undeveloped areas and accordingly they are based on assessments in respect of the size of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological properties.

Forward-looking information: The estimates of NSAI in respect of the quantities of natural gas reserves in the Tamar field are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling and from the lease operator, and are the estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas consumed may be different from these estimates and assumptions, partly due to technical and operational conditions and/or

¹¹² The quantities included in the reserves report are higher than the quantities in the reserves report of the Tamar lease attached to the Delek Drilling's prospectus of July 22, 2011 (ref. 2011-01-219678) and amended on August 2, 2011, mainly due to additional information about the reservoir following the production drillings between that date and the date of this report, which provides a more complete picture of the reservoir formation.

¹¹³ The calculation is after royalties (at the rate after ROI), assuming the investment is after the total quantity is sold (for 100% of the rights in the oil asset) of 932 BCF. Since the ROI date is affected by the price of gas sales, production capacity, production costs and percentage of royalties, and since the production system has not yet been completed, and since additional agreements for the sale of natural gas are expected to be signed, the ROI date could be materially different from the aforesaid date.

¹¹⁴ The estimates in the report, as is standard in estimating reserves based on the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), are not adjusted to reflect external risks that are not directly related to the scope of the reservoir and its production capacity (such as security and commercial risks).

regulatory changes and/or the supply and demand conditions in the natural gas market and/or as a result of actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production.

Discounted cash flows

In relation to calculation of the discounted cash flows described below, NSAI also noted that (1) The estimated discounted cash flow does not reflect risk.¹¹⁵ (2) The discounted cash flow is based on the weighted average gas prices in the gas sales contracts, which are based on different price formulas that include linkage to the CPI or the electricity generation price as set from time to time by the Public Services Authority - Electricity. The partnership provided the information for the gas price to NSAI. (3) The operating costs taken into account are costs provided by the partnerships to NSAI and appear reasonable, based on NSAI's experience in similar projects. These costs include only direct costs on the project level and the partnerships' estimate of their share in the overheads, general and administrative expenses which can be directly attributed to the project. (4) The capital expenditure provided to NSAI by the partnerships, which appear reasonable, is based, inter alia, on the development plan in the Tamar project and on NSAI's experience in similar projects. The capital expenditures taken into account are the capital expenditures required to develop and complete wells, develop new wells and for production equipment. As required by the partnerships, these costs remain fixed until actually expended.¹¹⁶ (5) The abandonment costs taken into account are costs provided to NSAI by the partnerships according to its assessments of the cost of abandoning wells, platforms and production facilities. These costs do not take into account the salvage value of the Tamar lease and facilities in the Tamar field. As required by the partnerships, abandonment costs remain fixed until actually expended. (6) The tax calculations take into account corporate tax rates provided to NSAI by the partnerships, which are the expected tax rates for each of the years included in the discounted cash flows. (7) Actual production capacity for each of the reserve categories described above could be lower or higher than the production capacity used to estimate the discounted cash flows. In addition, NSAI did not prepare a sensitivity analysis for the production capacity of the wells. A sensitivity analysis could lead to a conclusion that the reserves are not feasible for production.

It is noted that the discounted cash flow does not take into account revenue and/or expenses relating to the offshore project for liquefaction of gas for export as set out in section 1.11.29(K) below.

It is further noted that the discounted cash flow includes royalties as described in section 1.11.5(G) above, as well as taxes applicable to holders of participating units in accordance with the Taxation of Petroleum Profits Law ("the Law"). It is emphasized that calculation of the levy was based on the definitions, formulas and mechanisms set out in the law as understood and interpreted by the partnerships, however, since the law is new and the calculation formulas and mechanisms set out in the law are complex, it is not certain whether this interpretation of the calculation method for the levy will be the same as that adopted by the tax authorities and/or the same as the interpretations of the law by the court, insofar as a ruling is required on these issues. At the publication date of the report, these issues have not been brought before the courts in Israel. The levy was calculated according to the transitional provisions in the law for a project that started commercial production before the law came into effect, based on the following assumptions: The developer will report in US dollars according to section 13(B) of the law, the rate of inflation in

¹¹⁵ The estimates in the report, as is standard in estimating reserves based on the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), are not adjusted to reflect external risks that are not directly related to the scope of the reservoir and its production capacity (such as security and commercial risks).

¹¹⁶ The capital investments taken into account when preparing the discounted cash flow exceed the development costs approved by the partnership for development of the Tamar lease, and it also includes estimated costs of future investments after production starts for use of part of the development facilities of the Yam Tethys project and expansion of output at the receiving terminal in Ashdod. These investments have not yet been approved by the project partners.

the United States in the coming years will be 2%, all of the developer's payments (production costs and investments) will be recognized by the tax authorities for calculation of the levy and calculation of the developers revenues will take into account actual selling prices of the gas.

Following is the estimated discounted cash flows at December 31, 2011, in thousands of USD (after the levy and income tax) attributable to the Company's share in the reserves in the Tamar field for each of the reserve categories set out above (the cash flow is based on assumptions, which are described above). It is noted that there is a significant change in the discounted cash flow compared to that published on March 31, 2011, for the following reasons: (1) change in the forecasted quantities of sales in each of the project years, due to signing gas supply contracts and estimates for the scope of market demand; (2) change in estimated selling prices, in view of prices in gas supply agreements signed recently; (3) the scope of the partnerships' actual investments in the project as from June 2011 until the end of 2011; (4) the effect of the passage of time on the discounted cash flow; (5) change in estimated ongoing investments and capital investments in view of the updated estimates; (6) elimination of the tax reduction that was expected in the past, which also resulted in a change in the expected maximum levy in accordance with the Petroleum Profits Tax Law.

Total discounted cash flow from proved reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
									Total discounted cash flow after tax						
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
	100%														
Dec. 31, 2012	0.00	-	-	-	2,005	236,589	-	(238,594)	-	-	(238,594)	(232,844)	(227,490)	(222,490)	(217,805)
Dec. 31, 2013	5.32	191,634	30,069	6,528	15,354	55,897	-	96,843	-	21,224	75,619	70,283	65,545	61,318	57,525
Dec. 31, 2014	7.50	283,195	44,436	9,648	16,912	38,864	-	192,631	-	40,677	151,954	134,505	119,737	107,144	96,329
Dec. 31, 2015	10.77	421,087	66,072	14,345	17,071	29,448	-	322,841	-	70,876	251,965	212,411	180,495	154,489	133,109
Dec. 31, 2016	11.11	440,935	85,479	39,131	18,050	-	-	376,536	-	76,938	299,599	240,540	195,107	159,735	131,894
Dec. 31, 2017	11.46	463,128	95,585	49,687	26,007	-	-	391,224	-	80,610	310,614	237,509	183,892	144,007	113,953
Dec. 31, 2018	11.84	493,189	101,789	52,912	18,280	20,924	-	405,109	123,100	53,306	228,703	166,549	123,089	92,201	69,919
Dec.31, 2019	11.84	508,360	104,920	54,540	17,408	20,924	-	419,648	191,261	44,664	183,723	127,422	89,892	64,407	46,806
Dec.31, 2020	11.84	523,999	108,148	56,218	18,280	-	-	453,789	206,565	58,899	188,325	124,394	83,766	57,408	39,982
Dec. 31, 2021	11.84	531,879	109,774	57,063	17,408	-	-	461,760	210,193	59,985	191,582	120,519	77,468	50,784	33,895
Dec. 31, 2022	11.84	539,508	111,349	57,882	26,998	-	-	459,043	208,956	59,615	190,472	114,115	70,018	43,904	28,082
Dec. 31, 2023	11.84	547,319	112,961	58,720	17,408	-	-	475,670	216,525	63,723	195,422	111,506	65,307	39,170	24,010
Dec. 31, 2024	11.84	555,494	114,648	59,597	18,280	-	-	482,162	219,480	64,842	197,840	107,510	60,104	34,482	20,256
Dec. 31, 2025	11.84	564,229	116,451	60,534	17,408	-	-	490,903	223,459	66,033	201,411	104,239	55,627	30,526	17,185
Dec. 31, 2026	11.84	573,077	118,277	61,483	18,280	-	-	498,003	226,691	67,000	204,312	100,705	51,298	26,926	14,527
Dec.31, 2027	11.84	581,950	120,109	62,435	26,126	-	-	498,150	226,758	67,020	204,372	95,937	46,648	23,421	12,109
Dec.31, 2028	11.84	591,723	122,126	63,484	18,280	-	-	514,801	234,337	69,288	211,176	94,411	43,819	21,044	10,427
Dec. 31, 2029	8.49	433,041	89,375	46,459	16,354	-	-	373,771	170,140	50,079	153,551	65,379	28,965	13,306	6,318
Dec. 31, 2030	5.66	294,468	60,775	31,592	16,334	-	-	248,951	113,323	33,079	102,550	41,585	17,586	7,727	3,516
Dec. 31, 2031	2.83	150,179	30,995	16,112	14,569	-	-	120,726	54,954	15,615	50,157	19,370	7,819	3,286	1,433
Dec. 31, 2032	1.78	96,557	19,928	10,359	23,829	-	-	63,158	28,750	7,774	26,635	9,796	3,775	1,518	634
Dec. 31, 2033	-	-	-	-	-	-	26,154	(26,154)	-	-	(26,154)	(9,162)	(3,370)	(1,296)	(519)
Dec. 31, 2034	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec.31, 2035	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Total discounted cash flow from proved reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
									Total discounted cash flow after tax						
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
Dec. 31, 2036	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2037	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2038	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2039	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2040	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2041	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2042	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2043	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2044	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2045	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total	195.17	8,784,950	1,763,269	868,730	380,642	402,644	26,154	7,080,971	2,654,493	1,071,245	3,355,234	2,056,679	1,339,099	913,016	643,584

Total discounted cash flow from probable reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
									Total discounted cash flow after tax						
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
Dec. 31, 2012	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2013	-	-	-	-	-	-	-	-	-	237	(237)	(220)	(205)	(192)	(180)
Dec. 31, 2014	-	-	-	-	-	-	-	-	-	237	(237)	(209)	(186)	(167)	(150)
Dec. 31, 2015	-	-	-	-	-	-	-	-	-	237	(237)	(199)	(170)	(145)	(125)
Dec. 31, 2016	-	-	-	-	-	-	-	-	-	237	(237)	(190)	(154)	(126)	(104)
Dec. 31, 2017	-	-	-	-	-	-	-	-	-	237	(237)	(181)	(140)	(110)	(87)
Dec. 31, 2018	-	-	-	-	-	-	-	-	-	237	(237)	(172)	(127)	(95)	(72)
Dec. 31, 2019	-	-	-	-	-	-	-	-	-	237	(237)	(164)	(116)	(83)	(60)
Dec. 31, 2020	-	-	-	-	-	-	-	-	-	237	(237)	(156)	(105)	(72)	(50)
Dec. 31, 2021	-	-	-	-	-	-	-	-	-	237	(237)	(149)	(96)	(63)	(42)
Dec. 31, 2022	-	-	-	-	-	-	-	-	-	237	(237)	(142)	(87)	(55)	(35)
Dec. 31, 2023	-	-	-	-	-	-	-	-	-	237	(237)	(135)	(79)	(47)	(29)
Dec. 31, 2024	-	-	-	-	-	-	-	-	-	237	(237)	(129)	(72)	(41)	(24)
Dec. 31, 2025	-	-	-	-	-	-	-	-	-	237	(237)	(122)	(65)	(36)	(20)
Dec. 31, 2026	-	-	-	-	-	-	-	-	-	237	(237)	(117)	(59)	(31)	(17)
Dec. 31, 2027	-	-	-	-	-	-	-	-	-	237	(237)	(111)	(54)	(27)	(14)
Dec. 31, 2028	-	-	-	-	-	-	-	-	-	237	(237)	(106)	(49)	(24)	(12)
Dec. 31, 2029	3.34	170,329	35,154	18,274	1,053	-	-	152,396	69,371	20,993	62,032	26,412	11,702	5,375	2,552
Dec. 31, 2030	6.17	320,970	66,245	34,436	1,945	-	-	287,215	130,740	39,355	117,119	47,493	20,085	8,825	4,016
Dec. 31, 2031	9.00	477,568	98,565	51,236	2,838	-	-	427,401	194,553	58,449	174,400	67,353	27,189	11,427	4,983
Dec. 31, 2032	10.05	543,744	112,223	58,336	3,168	-	-	486,690	221,541	66,524	198,625	73,055	28,150	11,317	4,730
Dec. 31, 2033	11.84	653,107	134,795	70,069	17,407	-	(26,154)	597,129	259,908	77,175	260,046	91,092	33,505	12,884	5,160
Dec. 31, 2034	11.84	666,169	137,491	71,471	18,279	-	-	581,871	264,867	78,659	238,344	79,514	27,917	10,268	3,941
Dec. 31, 2035	11.84	679,493	140,240	72,900	17,407	-	-	594,745	270,728	80,413	243,605	77,399	25,939	9,126	3,357
Dec. 31, 2036	6.07	355,656	73,404	38,157	16,463	-	-	303,947	138,357	40,806	124,784	37,759	12,079	4,065	1,433

Total discounted cash flow from probable reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
									Total discounted cash flow after tax						
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
Dec. 31, 2037	3.87	231,142	47,705	24,798	23,615	-	-	184,620	84,039	24,554	76,027	21,910	6,690	2,154	728
Dec. 31, 2038	2.82	171,798	35,457	18,432	15,438	-	-	139,334	63,425	18,386	57,524	15,788	4,602	1,417	459
Dec. 31, 2039	1.86	115,580	23,854	12,400	14,263	-	-	89,862	40,905	11,648	37,309	9,752	2,713	799	248
Dec. 31, 2040	1.09	69,087	14,259	7,412	14,892	-	-	47,348	21,553	5,857	19,938	4,963	1,318	371	110
Dec. 31, 2041	-	-	-	-	-	-	26,154	(26,154)	-	-	(26,154)	(6,201)	(1,572)	(424)	(121)
Dec. 31, 2042	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2043	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2044	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2045	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total	79.79	4,454,643	919,393	477,922	146,767	26,154	-	3,866,404	1,759,987	526,604	1,579,813	543,788	198,552	76,292	30,574

Total discounted cash flow from probable reserves at December 31, 2011 (in USD thousands for the Company's share)															
Cash flow items															
									Total discounted cash flow after tax						
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
	100%														
Dec. 31, 2012	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dec. 31, 2013	-	-	-	-	-	-	-	-	-	57	(57)	(53)	(50)	(46)	(44)
Dec. 31, 2014	-	-	-	-	-	-	-	-	-	57	(57)	(51)	(45)	(40)	(36)
Dec. 31, 2015	-	-	-	-	-	-	-	-	-	57	(57)	(48)	(41)	(35)	(30)
Dec. 31, 2016	-	-	-	-	-	-	-	-	-	57	(57)	(46)	(37)	(31)	(25)
Dec. 31, 2017	-	-	-	-	-	-	-	-	-	57	(57)	(44)	(34)	(27)	(21)
Dec. 31, 2018	-	-	-	-	-	-	-	-	-	57	(57)	(42)	(31)	(23)	(18)
Dec. 31, 2019	-	-	-	-	-	-	-	-	-	57	(57)	(40)	(28)	(20)	(15)
Dec. 31, 2020	-	-	-	-	-	-	-	-	-	57	(57)	(38)	(25)	(17)	(12)
Dec. 31, 2021	-	-	-	-	-	-	-	-	-	57	(57)	(36)	(23)	(15)	(10)
Dec. 31, 2022	-	-	-	-	-	-	-	-	-	57	(57)	(34)	(21)	(13)	(8)
Dec. 31, 2023	-	-	-	-	-	-	-	-	-	57	(57)	(33)	(19)	(11)	(7)
Dec. 31, 2024	-	-	-	-	-	-	-	-	-	57	(57)	(31)	(17)	(10)	(6)
Dec. 31, 2025	-	-	-	-	-	-	-	-	-	57	(57)	(30)	(16)	(9)	(5)
Dec. 31, 2026	-	-	-	-	-	-	-	-	-	57	(57)	(28)	(14)	(8)	(4)
Dec. 31, 2027	-	-	-	-	-	-	-	-	-	57	(57)	(27)	(13)	(7)	(3)
Dec. 31, 2028	-	-	-	-	-	-	-	-	-	57	(57)	(26)	(12)	(6)	(3)
Dec. 31, 2029	0.00	187	39	20	1	-	-	167	76	80	11	5	2	1	0
Dec. 31, 2030	0.00	191	39	20	1	-	-	171	78	81	13	5	2	1	0
Dec. 31, 2031	0.00	195	40	21	1	-	-	174	79	81	14	5	2	1	0
Dec. 31, 2032	0.00	199	41	21	1	-	-	178	81	81	15	6	2	1	0
Dec. 31, 2033	0.00	202	42	22	1	-	-	181	83	82	17	6	2	1	0
Dec. 31, 2034	0.00	207	43	22	1	-	-	185	84	82	18	6	2	1	0
Dec. 31, 2035	0.00	211	43	23	1	-	-	189	86	83	20	6	2	1	0

Total discounted cash flow from probable reserves at December 31, 2011 (in USD thousands for the Company's share)

Cash flow items															
											Total discounted cash flow after tax				
	Sales quantity (BCM)	Revenues	Royalties payable	Royalties received	Operating costs	Development costs	Abandonment and restoration costs	Total cash flow before levy and income tax (discounted at 0%)	Levy	Income tax	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
Dec. 31, 2036	5.77	337,641	69,686	36,224	1,817	-	-	302,362	137,635	41,239	123,488	37,367	11,954	4,023	1,418
Dec. 31, 2037	7.63	455,714	94,055	48,892	2,404	-	-	408,147	185,788	55,647	166,712	48,044	14,671	4,722	1,595
Dec. 31, 2038	8.68	528,584	109,094	56,710	2,734	-	-	473,465	215,521	64,543	193,401	53,081	15,472	4,764	1,542
Dec. 31, 2039	6.92	429,890	88,725	46,121	2,180	-	-	385,106	175,300	52,509	157,297	41,116	11,440	3,369	1,045
Dec. 31, 2040	6.27	397,554	82,051	42,652	1,977	-	-	356,178	162,132	48,569	145,477	36,216	9,618	2,710	806
Dec. 31, 2041	4.68	302,755	62,486	32,481	15,153	-	(26,154)	283,753	117,259	34,551	131,943	31,283	7,931	2,137	609
Dec. 31, 2042	3.03	199,807	41,238	21,437	24,222	-	-	155,784	70,913	20,683	64,188	14,494	3,507	904	247
Dec. 31, 2043	1.24	83,405	17,214	8,948	14,068	-	-	61,071	27,800	7,784	25,488	5,481	1,266	312	82
Dec. 31, 2044	-	-	-	-	-	-	26,154	(26,154)	-	-	(26,154)	(5,357)	(1,181)	(279)	(70)
Dec. 31, 2045	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total	44.24	2,736,742	564,836	293,615	64,563	-	-	2,400,958	1,092,916	327,010	981,031	261,159	74,266	22,351	7,029

Note: It is clarified that the discounted cash flow figures, whether they have been calculated at a specific discount rate or without a discount rate, represent the present value but not necessarily the fair value

Forward-looking information: The information about discounted cash flow is forward-looking information as defined in the Securities Law. The discounted cash flow is based on various assumptions, including in respect of future sales of natural gas from the reservoir, the selling price of natural gas (including price indexation) and construction and operating costs which may not be realized, and the quantities of natural gas actually produced, if produced and/or construction and operating costs and/or selling prices of natural gas, including indexation of selling prices and/or annual quantities sold may differ from these estimates and assumptions, including due to operational and technical conditions and/or changes in regulation and/or supply and demand conditions in the natural gas market and/or terms of natural gas sales contracts from the reservoir that have been signed and/or will be signed and/or implementation of the provisions of the Petroleum Profits Tax Law and/or future prices and quantities and/or changes in actual costs of the project, which has not been completed and/or actual performances of the reservoir.

Sensitivity analysis for the main parameters of the discounted cash flow (gas price and quantity of gas sold) at December 31, 2011

Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%	Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%
10% increase in the price/quantity of gas sales					10% decrease in the price/quantity of gas sales				
P1 proved reserves	3,676,231	1,473,517	1,010,325	718,044	P1 Proved reserves	3,044,907	1,208,223	817,580	569,972
Probable reserves	1,743,791	218,971	84,164	33,768	Probable reserves	1,415,834	178,133	68,419	27,380
Total P2 proved + probable reserves	5,420,022	1,692,488	1,094,489	751,812	Total P2 Proved + probable reserves	4,460,741	1,386,356	885,999	597,353
Possible reserves	1,081,772	81,852	24,646	7,765	Possible reserves	880,290	66,680	20,055	6,294
Total P3 proved + probable + possible reserves	6,501,795	1,774,340	1,119,135	759,577	Total P3 Proved + probable + possible reserves	5,341,031	1,453,036	906,055	603,647
15% increase in the price/quantity of gas sales					15% decrease in the price/quantity of gas sales				
P1 proved reserves	3,835,642	1,539,682	1,058,035	754,438	P1 Proved reserves	2,882,896	1,137,891	765,760	529,729
Probable reserves	1,825,780	229,181	88,100	35,365	Probable reserves	1,333,845	167,924	64,483	25,784
Total P2 proved + probable reserves	5,661,421	1,768,863	1,146,135	789,802	Total P2 Proved + probable reserves	4,216,742	1,305,815	830,243	555,512
Possible reserves	1,132,143	85,645	25,794	8,133	Possible reserves	829,919	62,887	18,907	5,926
Total P3 proved + probable + possible reserves	6,793,564	1,854,508	1,171,929	797,935	Total P3 Proved + probable + possible reserves	5,046,661	1,368,702	849,151	561,439
20% increase in the price/quantity of gas sales					20% decrease in the price/quantity of gas sales				
P1 proved reserves	3,993,425	1,604,778	1,104,871	790,113	P1 Proved reserves	2,723,480	1,068,980	715,078	490,433
Probable reserves	1,907,769	239,390	92,036	36,962	Probable reserves	1,251,856	157,715	60,547	24,187
Total P2 proved + probable reserves	5,901,194	1,844,168	1,196,907	827,075	Total P2 Proved + probable reserves	3,975,336	1,226,694	775,625	514,619
Possible reserves	1,182,514	89,438	26,942	8,500	Possible reserves	779,549	59,094	17,760	5,559
Total P3 proved + probable + possible reserves	7,083,707	1,933,606	1,223,849	835,575	Total P3 Proved + probable + possible reserves	4,754,885	1,285,788	793,385	520,178

Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%	Sensitivity/category	Total	Present value discounted at 10%	Present value discounted at 15%	Present value discounted at 20%
10% increase in the price/quantity of gas sales					10% decrease in the price/quantity of gas sales				
P1 proved reserves	3,673,538	1,472,301	1,009,421	717,338	P1 Proved reserves	3,047,573	1,209,448	818,500	570,696
Probable reserves	1,742,763	218,842	84,114	33,747	Probable reserves	1,416,862	178,263	68,469	27,401
Total P2 proved + probable reserves	5,416,302	1,691,143	1,093,534	751,086	Total P2 Proved + probable reserves	4,464,435	1,387,711	886,969	598,097
Possible reserves	1,081,203	81,809	24,633	7,761	Possible reserves	880,860	66,723	20,068	6,298
Total P3 proved + probable + possible reserves	6,497,505	1,772,952	1,118,168	758,847	Total P3 Proved + probable + possible reserves	5,345,295	1,454,434	907,038	604,395
15% increase in the price/quantity of gas sales					15% decrease in the price/quantity of gas sales				
P1 proved reserves	3,831,634	1,537,880	1,056,696	753,393	P1 Proved reserves	2,883,237	1,137,712	765,614	529,646
Probable reserves	1,824,239	228,987	88,025	35,334	Probable reserves	1,335,387	168,118	64,558	25,814
Total P2 proved + probable reserves	5,655,872	1,766,867	1,144,720	788,727	Total P2 Proved + probable reserves	4,218,624	1,305,830	830,172	555,461
Possible reserves	1,131,288	85,580	25,775	8,126	Possible reserves	830,774	62,952	18,927	5,933
Total P3 proved + probable + possible reserves	6,787,161	1,852,447	1,170,495	796,853	Total P3 Proved + probable + possible reserves	5,049,398	1,368,782	849,099	561,393
20% increase in the price/quantity of gas sales					20% decrease in the price/quantity of gas sales				
P1 proved reserves	3,988,123	1,602,404	1,103,109	788,741	P1 Proved reserves	2,728,868	1,071,490	716,971	491,926
Probable reserves	1,905,714	239,131	91,936	36,921	Probable reserves	1,253,911	157,973	60,647	24,228
Total P2 proved + probable reserves	5,893,837	1,841,536	1,195,045	825,661	Total P2 Proved + probable reserves	3,982,779	1,229,464	777,618	516,153
Possible reserves	1,181,374	89,351	26,916	8,492	Possible reserves	780,688	59,180	17,786	5,567
Total P3 proved + probable + possible reserves	7,075,212	1,930,887	1,221,961	834,153	Total P3 Proved + probable + possible reserves	4,763,467	1,288,644	795,404	521,720

The Company declares that all of the above information has been prepared in compliance with the SPE-PRMS.

Opinion of the appraiser

A reserves report prepared by NSAI as of December 31, 2011 is attached to this report as a reference to the reserves report attached as Appendix D to the Periodic Report for 2011 of Delek Drilling Partnership, which was published on March 29, 2012 (ref. 2012-01-084516) and the assessor's consent to include the report in this report is attached.

K. Contingent and prospective resources in the Dalit lease

After completion of the Dalit 1 drilling in the Dalit lease, the project operator announced that it estimates that the gross mean resources in the natural gas reserves prospect in the Dalit formation is 500 BCF (14.2 BCM). According to a report prepared by NSAI, at December 31, 2011, set out below, there was no change or development that could have a material effect on the quantity or probability of these resources as set out in the resources report prior to December 31, 2010. NSAI also believes that the Dalit formation is separated into a number of fault blocks and that it is possible that the reserves in blocks that are not connected to the main block of the Dalit 1 drilling will not have the same quality as those discovered in the main block and that there is also a very small chance that no hydrocarbons whatsoever will be found in these blocks. In view of the above, NSAI has classified part of the gas resources in the Dalit lease as contingent resources, at the development pending stage, and they are contingent on approval of the project, which will include an approved development plan and a reasonable expectation for gas sales from the field, and part of the resources as prospective resources, as described below:

1. Contingent resources in the Dalit lease

Quantities

According to a report received by the partnerships from NSAI, which was prepared in accordance with the principles of the SPE-PRMS, the contingent resources in the Dalit lease at December 31, 2011 are classified as development pending, as described below:

Contingent resources	Total in the oil asset (gross) BCF	Company's share (net)¹¹⁷ BCF
Low estimate (1C)	216.9	34.0
Best estimate (2C)	270.7	42.5
High estimate (3C)	334.8	52.48

According to the report, after approval of the project, which will include a development plan and a reasonable forecast for gas sales from the field, some of the contingent resources could be classified as reserves.

At this stage, a schedule has not been defined for the preparation of a development plan for the Dalit reservoir. It is noted that the main potential market for these resources, which will be added to the resources in other discoveries in which the partnerships are involved, is the domestic market and the international market (export of LNG).

For further information about the domestic gas market, see section 1.11.3(A) above and for further information about possible export of gas, see section 1.11.29(K) below.

Forward-looking information: There is no certainty that it will be commercially possible to produce any percentage of the contingent resources.

The NSAI report noted a number of assumptions and qualifications, including: (1) The appraisals do not reflect the development risk; (2) NSAI did not visit the oil field or check the mechanical operation of the well or its state; (3) NSAI did not examine the possible

¹¹⁷ After receiving royalties (at the rate after ROI) and assuming ROI is after the total quantity is sold (for 100% of the rights in the oil asset (of 70.6 BCF) Since the ROI date is affected by the price of gas sales, production capacity, production costs and percentage of royalties, and since the production system has not yet been planned and constructed and agreements for the sale of natural gas have not yet been signed, the ROI date could be materially different from the aforesaid date.

exposure arising from environmental matters. However, it was noted that at the date of the resources report, NSAI is unaware of any possible environmental liability that could have a material effect on the amount of reserves estimated in the contingent resources report, or on whether they are commercial. (4) The resources are in undeveloped areas and accordingly they are based on assessments in respect of the size of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological properties.

Forward-looking information: The above estimates of NSAI in respect of the contingent resources in the Tamar lease are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling and from the lease operator, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas consumed may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production.

2. Prospective resources in the Dalit lease

A) Quantitative data

According to a report received by the partnerships from NSAI, prepared in accordance with the guidelines set out in the Petroleum Resources Management System approved by the SPE-PRMS, the prospective (undiscovered) resources in six blocks in the Dalit formation, adjacent to the fault block in which the Dalit discovery was made, as of December 31, 2011, are as follows:

Prospective resources category	Prospect	Total in the oil asset (gross) BCF	Total Company share (gross) ¹¹⁸ BCF
Low estimate	West 1	134.2	21.0
	West 2	64.0	10.0
	West 3	2.9	0.5
	East 1	3.4	0.5
	East 2	1.8	0.3
	East 3	5.9	0.9
Best estimate	West 1	169.1	26.4
	West 2	80.8	12.6
	West 3	3.7	0.6
	East 1	4.3	0.7
	East 2	2.3	0.4
	East 3	7.4	1.2
High estimate	West 1	210.2	32.8
	West 2	101.8	15.9
	West 3	4.6	0.7
	East 1	5.5	0.9
	East 2	2.9	0.5
	East 3	9.3	1.5

¹¹⁸ After receiving royalties (at their rate after ROI)

The report was based on the results of the Dalit 1 drilling and on a 3D seismic survey carried out and processed in 2001. The survey results were reprocessed in 2008 and 2010.

B) Basic parameters used to calculate the different scenarios:

Parameter	Gross rock volume (acre*feet)		Acres (feet)		Average gross thickness (feet)		Net-to-gross (decimal)	
	Low estimate	High estimate	Low estimate	High estimate	Low estimate	High estimate	Low estimate	High estimate
West 1	73,444	104,920	1,075	1,353	68	78	0.742	0.842
West 2	34,754	46,649	534	729	65	68	0.742	0.842
West 3	1,595	2,279	19	30	84	76	0.742	0.842
East 1	1,864	2,663	20	144	93	18	0.742	0.842
East 2	1,005	1,436	16	75	63	19	0.742	0.842
East 3	3,199	4,570	55	152	58	30	0.742	0.842

Parameter	Porosity (decimal)		Gas saturation (decimal)		Gas formation volume factor (SCF/RCF)		Gas recovery factor (decimal)	
	Low estimate	High estimate	Low estimate	High estimate	Low estimate	High estimate	Low estimate	High estimate
West 1	0.270	0.330	0.790	0.864	354	354	0.60	0.70
West 2	0.270	0.330	0.790	0.864	354	354	0.60	0.70
West 3	0.270	0.330	0.790	0.864	354	354	0.60	0.70
East 1	0.270	0.330	0.790	0.864	354	354	0.60	0.70
East 2	0.270	0.330	0.790	0.864	354	354	0.60	0.70
East 3	0.270	0.330	0.790	0.864	354	354	0.60	0.70

C) Material risks involved in continuation of the process

According to the report, the most significant risk from the commercial aspect of the reservoir is the reservoir quality, which determines the amount of gas that the reservoir layers may contain, and the trap integrity, which determines whether any gas remains in the reservoir layer.

D) The estimated probability of success of each of the risk factors in the oil exploration process and the total estimated probability of success are as follows:

Parameter	Probability of success (%)
Trap integrity	90
Reservoir quality	90
Source evaluation	100
Timing/migration	95
Total probability of success	77

E) Estimated probability of development for commercial production

According to the report, based on the development of similar fields, assuming a discovery, the prospective resources in the best estimate category have a reasonable chance of becoming commercial. The main potential market for these resources, which will join the resources in the discoveries in which the partnerships are involved, is the Israeli market and the international market. For further information about the domestic gas market, see section 1.11.3(A) above and for further information about possible export of gas, see section 1.11.29(K) below.

F) Partnerships' explanations of the basic parameters used to estimate the scenarios: The parameters used to calculate the estimates are based, inter alia, on the results

of the seismic survey, information obtained from drillings in the adjacent Mari B reservoir and from similar reservoirs in the region and in other countries.

There is no certainty that any part of these potential resources will indeed be discovered, and if they are discovered, there is no certainty that it will be possible from the commercial perspective to produce any part of the resources. The prospective information does not lie within the bounds of an evaluation in respect of the contingent reserves and resources, which can only be evaluated after exploration drilling, if at all.

Forward-looking information: The above estimates of NSAI in respect of the prospective resources in the Tamar lease are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling and from the lease operator, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas consumed may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and gas exploration and production.

G) The Company declares that all of the above information has been prepared in compliance with the SPE-PRMS.

H) Opinion of the appraiser

A contingent and prospective resources report prepared by NSAI as of December 31, 2011 is attached to this report as a reference to the reserves report attached as Appendix E to the Periodic Report for 2011 of Delek Drilling Partnership, which was published on March 29, 2012 (ref. 2012-01-084516) and the assessor's consent to include the report in this report is attached.

L. Joint operating agreement for the Tamar project

Exploration and production under the leases in the Tamar project are carried out through a joint operating agreement (JOA) dated November 16, 1999 (as amended from time to time). The parties to the JOA are the limited partnerships and the other Tamar project partners (as described below), which includes the following provisions:

1. All the rights and interests, and all the liabilities of the parties, in respect of the JOA, will be according to the percentage of the parties' participation in the oil assets
2. Noble is the operator according to the JOA and bears sole responsibility for the management of the joint operations, subject to the terms of the JOA and under the supervision and provisions of the joint operating committee, as defined below. As the operator, Noble is subject to obligations concerning compliance with the terms and provisions applicable to oil assets, the provisions of the JOA and the operations committee, agreements with third parties, insurances according to the JOA, access authorization for the parties to the JOA to supervise the joint operations and determining the number of workers and their wages.
3. The operator is entitled to reimbursement for all direct expenses arising from fulfillment of its duties as an operator and reimbursement for indirect expenses arising from the share of the joint venture expenses, according to the operator's accounting principles and practices.
4. The operator is not liable to any of the other parties to the JOA (except for its proportionate share) for any claim, liability, loss or damage arising from or in respect of joint operations, unless these are a result of the operator's willful misconduct or failure to obtain the required insurance and in any case shall not be responsible for consequential damages. The aforesaid does not exempt the operator from liability for its share according to the rate of participation in any damage, loss or liability.
5. Operations committee: The parties have set up an operations committee as part of the agreement, which has the authority to make decisions regarding operating policy, approval of plans and requests for budgets, determining schedules, making decisions regarding applications for licenses and leases, replacement of the operator and more.

The operations committee is comprised of representatives of the parties, with each representative having voting rights according to the rights of the party that they represent. The Committee's resolutions will be passed by a vote of two or more of the partners, holding together at least 68% of the rights in the lease (related parties as defined in the agreement will be considered as one party).¹¹⁹ To approve a decision related to the termination of the lease or waiver of any part of the lease area, a vote in favor is required by all parties.

6. The procedure for submitting and approving work plans, budgets and authorization for expenditure (AFE) for operations in the JOA areas applies to the partnerships, including exploration and development plans and budget.
7. Operations in which not all the parties participate (defined in the agreement as exclusive operations, and which are commonly known as sole risk operations in the oil exploration sector) will not be carried out if they contradict the joint operations of all the partners. The JOA establishes rules for these operations.
8. The operator may resign with 180-days written notice or shorter notice with the consent of the joint operating committee. In addition, subject to the provisions of the agreement, the operating committee may dismiss the operator if one of the events stipulated in the JOA occurs, including if the operator ceases to hold at least 10% of the participating rights in the leases or insolvency or liquidation of the operator.
9. Sanctions that apply to the partners and conditions for imposing the sanctions if one of the parties fails to pay its proportionate share in the joint expenses, including denying participation rights in the operations committee, denial of the right to receive information, and if the breach continues for more than six days, denial of the partner's proportional share of production. If the breach continues for more than 45 days, the other partners may demand the removal of the partner from the agreement and the oil asset.
10. The JOA includes provisions for withdrawal of a party from any license, and determines the cases in which withdrawal is possible, including the rights and obligations of the withdrawing party towards the other partners in the license.

1.11.6 Ratio Yam licenses

A. General

General information about the oil asset	
Name of oil asset	349/Rachel 350/Amit 351/Hannah 352/David 353/Eran
Location	Offshore assets 140-130 kilometers west of Haifa
Area	The area covered by all the licenses together is 1,800 square kilometers
Type of oil asset and description of permitted operations according to that types	License Operations permitted under the Petroleum Law - exploration and production
Original grant date of the oil asset	December 15, 2008
Original expiry date of the oil asset	December 14, 2011
Dates of decision to extend the term of the oil asset	-
Current expiry date of the oil asset	June 14, 2013
Note whether there is an additional option of extending the period of the oil asset: if there is such an option, note the period of the possible extension	Subject to the Petroleum Law, the period can be extended for up to seven years from the grant date, with an option for another two-year extension in the event of a discovery

¹¹⁹

The Delek Drilling and Avner partnerships hold together less than 68% of the license.

General information about the oil asset	
Note name of operator	Noble
Names of the direct partners in the oil asset and their direct share in the oil asset and, to the best of the Company's knowledge, the names of the controlling owners in the partners	(1) Noble (39.66%);¹²⁰ (2) Ratio Oil Exploration (1992) – Limited Partnership ("Ratio") (15%) To the best of the Company's knowledge, the general partner in Ratio, Ratio Oil Exploration Ltd., is jointly owned by D.L.I.N. Ltd. (40%), Hiram Landau Ltd. (40%), Eitan Eisenberg Ltd. (10%) and the estate of the late Zvi Tsafirri (10%). D.L.I.N. Ltd. is a private company owned by Yair Rotlevy (1/3) and Ligad Rotlevy (2/3). Hiram Landau Ltd. is a private company controlled by Yeshayahu Landau. Eitan Eisenberg Ltd. is a private company controlled by Eitan Eisenberg. There is a shareholders agreement between the shareholders in Ratio Oil Explorations Ltd.¹²¹. (3) Delek Drilling Partnership (22.67%)¹²² (4) Avner Partnership (22.67%)¹²³

General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	- ¹²⁴
Description of the Company's holding in the oil asset	Through its direct holding and holdings in participating units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset revenues attributable to equity holders of the Company	In revenue: Before return on investment - 23.152% After return on investment - 25.604% <u>In the right to participate in revenue</u> Before return on investment - 22.29% After return on investment - 22.89% <u>In right to receive royalties:</u> Before return on investment - 0.862% After return on investment - 2.714%
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 119,745 thousand

¹²⁰ For further information about Noble, see section 1.11.3(A) above.

¹²¹ At December 29, 2011, the interested parties in Ratio Yam held less than 27% (other than the holding in mutual funds and provident funds).

¹²² For further information about Delek Drilling Partnership, see section 1.11.1(D) above.

¹²³ For further information about Avner Partnership, see section 1.11.1(D) above.

¹²⁴ These licenses were granted to the license partnerships on December 15, 2008 instead of the 198/Ratio Yam preliminary permit, the rights in which the partnerships acquired from Ratio in 2007.

B. Compliance with the terms of the work plan in the Ratio Yam licenses

Period	Description of the work plan defined for the period	Description of work plan items completed in the period ¹²⁵	Description of work plan items not yet completed in the period
2009	- Mapping potential prospects based on a seismic survey, seismic facies analysis, and assessment of potential by September 15, 2009 - Financial analysis of prospects – within 12 months after the Ratio Ram licenses were granted, in other words, by December 15, 2009;	For further information, see the actual work plan and intended work plan for the Ratio Yam licenses.	The operations in the work plan were carried out.
2010	- Additional 2D and 3D seismic surveys, if required - within 24 months after the Ratio Yam licenses were granted, in other words, by December 15, 2010¹²⁶ - Signing an offshore drilling contract with a drilling contractor within 24 months after the Ratio Yam licenses were granted, meaning by December 15, 2010	For further information, see the actual work plan and intended work plan for the Ratio Yam licenses.	The operations in the work plan were carried out.
2011	A binding work plan has yet to be determined for this period.	For further information, see the actual work plan and intended work plan for the Ratio Yam licenses.	-

C. Binding work plan according to the terms of the oil asset

The following are the planned activities for each of the Ratio Yam licenses:

Rachel license			
Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012 up to June 14, 2013	- Continuation of the Leviathan 1 drilling to the deepest targets as submitted by the operator. The operator will determine the final depth according to engineering and safety limitations. - The summary report of the drilling findings will be submitted no later than three months after completion and the summary report of the operations in the Ratio Yam licenses will be submitted by June 14, 2013.	45,000	11,840

¹²⁵ The description of the components of the work plan in the period are for the period up to the report date.

¹²⁶ Completed in 2009

Amit license			
Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012 up to June 14, 2013	- Continuation of the Leviathan 3 drilling to the targets defined in the prospects by the operator - Abandonment of the Leviathan 2 drilling according to the plan submitted by the operator - The summary report of the drilling findings will be submitted no later than three months after completion and the summary report of the operations in the license will be submitted by June 14, 2013.	For further information, see footnote Error! Bookmark not defined..	For further information, see footnote Error! Bookmark not defined..

Hannah license			
Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012 up to June 14, 2013	- Continuation of the Dolphin 1 drilling to the targets defined in the prospects by the operator - The summary report of the drilling findings will be submitted no later than three months after completion and the summary report of the operations in the license will be submitted by June 14, 2013.	-	-

David license			
Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012 up to June 14, 2013	- Submission of quarterly reports, including exploration results, geological, geophysical and engineering data and details of expenses for works carried out in the license. - Submission of a drilling prospect at least three months before the planned date for drilling in the license area - Submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three months before drilling¹²⁷ and no later than March 14, 2013¹²⁷	50,000 – 70,000	13,155-18,417

¹²⁷ If the drilling is carried out by one of the rigs already operating in licenses in which Noble is partner (Sedco Express, Pride North America and Homer), this document is not required.

David license			
Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
	• Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. • A summary report of the drilling findings will be submitted no later than three months after completion. • A report summarizing the operations in the license will be submitted by June 14, 2013		

Eran license			
Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012 up to June 14, 2013	• Submission of quarterly reports, including exploration results, geological, geophysical and engineering data and details of expenses for works carried out in the license. • Submission of a drilling prospect at least three months before the planned date for drilling in the license area • Submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three months before drilling and no later than March 14, 2013¹²⁸ • Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. • A summary report of the drilling findings will be submitted no later than three months after completion. • A report summarizing the operations in the license will be submitted by June 14, 2013	50,000 – 70,000	13,155-18,417

¹²⁸ If the drilling is carried out by one of the rigs already operating in licenses in which Noble is partner (Sedco Express, Pride North America and Homer), this document is not required.

D. Actual and planned work plan in the Ratio Yam licenses

The table below includes a summary of the main operations actually performed in the Ratio Yam licenses since January 1, 2009 through to the date of the report and a summary of the planned operations in the project:

Rachel license			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹²⁹	Company's effective share in the cost/budget (USD thousands)
2009	- Mapping of potential prospects based on a 2D seismic survey conducted in 2008 3-D seismic surveys - Feasibility analysis of the prospects - Signing an agreement for drilling in the license area	3,471	853
2010	- Processing and interpretation of the seismic surveys, as described above - In October 2010, drilling started at the Leviathan 1 well in the area covered by the Rachel license. The drilling targets were defined as Oligo-Miocene (main) and lower Oligocene and lower Cretaceous (secondary) - On December 22, 2010, the drilling reached a depth of 5,170 m (including water depth), to the base of the main target. After various tests, including electrical tests (logs) and coring from the target layer, the Leviathan 1 drilling was declared a natural gas discovery.	1,124 87,468	276 21,499
2011	- Drilling at Leviathan 1 continued with the aim of reaching the secondary targets as set out above, at a total depth of 7,200 meters. - At the beginning of April 2011, drilling at Leviathan 1 was suspended for operational-technical reasons, which prevented continuation of drilling works. - Assessment of alternatives for development of the Leviathan gas field	109,579 7,132	27,604 1,797
2012 up to June 14, 2013	- At the beginning of January 2012, the Homer Ferrington drilling rig resumed drilling at Leviathan 1, with the aim of deepening the well to the secondary targets. Production tests are planned at Leviathan 1. - Continuation of interpretation of seismic surveys in the Ratio Yam licenses that have not been drilled - Assessment of alternatives for development of the Leviathan gas field - Submission of a summary report of the drilling findings no later than three months after completion. - Submission of a report summarizing the operations in the license area by June 14, 2013	45,000	11,840

¹²⁹ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

Amit license			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹³⁰	Company's effective share in the cost/budget (USD thousands)
	abandonment of the well and preparation of an emergency plan for immediate intervention in the well, as required.¹³³ • Drilling at the Leviathan 3 well was suspended a number of times due to technical problems in the subsea equipment of the Pride North America rig (the name of Pride North America was changed to Ensco 5006). Accordingly, the rig left the Leviathan 3 drilling site and in October 2011, the Transocean Sedco Express rig arrived to complete drilling. • On December 14, 2011, drilling at the Leviathan 3 well was completed, and natural gas was discovered, as set out above. • Assessment of alternatives for development of the Leviathan gas field	7,132	1,617
2012 up to June 14, 2013	• Continuation of interpretation of seismic surveys • Abandonment of the Leviathan 2 drilling according to the plan submitted by the operator • Assessment of alternatives for development of the Leviathan gas field • Submission of a summary report of the drilling findings no later than three months after completion. • Submission of a report summarizing the operations in the license area by June 14, 2013	For further information, see footnote Error! Bookmark not defined..	For further information, see footnote Error! Bookmark not defined..

¹³³ The Commissioner also defined activities for abandonment of the Leviathan 2 well, to be performed in 2011 according to the timetable set out below: Preparation of a detailed control and monitoring plan to assess the drilling site and its surroundings and submission to the Commissioner for approval by July 5, 2011; preparation of a full abandonment plan for the Leviathan 2 drilling site and submission to the Commissioner for approval by August 1, 2011; providing the commitment of all the license holders, without derogating from their obligations under the law to meet all the conditions listed in the Commissioner's approval, and to take all measures required for this purpose, by June 30, 2011; providing an unconditional bank guarantee approved by the Commissioner, up to USD 30 million and valid until June 30, 2012, by June 30, 2011. As of this date, the license holders have submitted a control and monitoring plan to the Commissioner, with a commitment to comply with the conditions listed in the Commissioner's approval, and provided an unconditional bank guarantee as set out above. On August 1, 2011, the operator submitted an abandonment plan to the Commissioner of Petroleum Affairs. The partnerships estimate that the cost of the different options will range from an insignificant amount to USD 50 million (for 100% of the project rights). The operator also submits a monthly report to the Commissioner, describing the activities performed during the month to advance the abandonment plan and the monitoring activities that were performed.

Forward looking information: The estimated abandonment costs of the Leviathan 2 well are the initial estimates of the partnerships, based on the initial estimates received from the operator. Actual costs may differ from the estimates above and are subject, inter alia, to selection of the preferred option for the abandonment plan and its approval by the Commissioner, receiving bids from and signing agreements with contractors to implement the abandonment plan, changes in the supplier and raw material market, and the method for actual implementation of the abandonment plan.

Hannah license			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹³⁴	The Company's effective share in the cost/budget (USD thousands)
2009	- Mapping of potential prospects based on a 2D seismic survey conducted in 2008 3-D seismic surveys - Feasibility analysis of the prospects - Drilling plan in the license area	3,471	853
2010	Processing and interpretation of the seismic surveys, as described above	1,124	276
2011	- Dolphin 1 exploration drilling - On December 18, 2011, the partnerships announced a natural gas discovery at the Dolphin 1 well.	56,632	14,266
2012 up to June 14, 2013	- Submission of a report summarizing the drilling findings - Submission of a report summarizing the operations in the license area by June 14, 2013	-	

David license			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹³⁵	The Company's effective share in the cost/budget (USD thousands)
2009	- Mapping of potential prospects based on a 2D seismic survey conducted in 2008 3-D seismic surveys - Feasibility analysis of the prospects - Signing an agreement for drilling in the license area	3,471	853
2010	Processing and interpretation of the seismic surveys, as described above	1,124	276
2011	Continuation of interpretation of seismic surveys	1,101	277
2012 up to June 14, 2013	- Continuation of interpretation of seismic surveys - Submission of quarterly reports, including exploration results, geological, geophysical and engineering data and details of expenses for works carried out in the license. - Submission of a drilling prospect at least three months before the planned date for drilling in the license area	50,000-70,000	13,155-18,417

¹³⁴ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

¹³⁵ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

David license			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹³⁵	The Company's effective share in the cost/budget (USD thousands)
	- Submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three months before drilling and no later than March 14, 2013¹³⁶ - Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. - Submission of a summary report of the drilling findings no later than three months after completion. - Submission of a report summarizing the operations in the license area by June 14, 2013		

Eran license			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹³⁷	The Company's effective share in the cost/budget (USD thousands)
2009	- Mapping of potential prospects based on a 2D seismic survey conducted in 2008 3-D seismic surveys - Feasibility analysis of the prospects	1,562	384
2010	Processing and interpretation of the seismic surveys, as described above	505	124
2011	Continuation of interpretation of seismic surveys	495	125
2012 up to June 14, 2013	- Continuation of interpretation of seismic surveys - Submission of quarterly reports, including exploration results, geological, geophysical and engineering data and details of expenses for works carried out in the license. - Submission of a drilling prospect at least three months before the planned date for drilling in the license area - Submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three	50,000-70,000	13,155-18,417

¹³⁶ If the drilling is carried out by one of the rigs already operating in licenses which Noble holds (Sedco Express, Pride North America and Homer), this document is not required.

¹³⁷ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

Eran license			
Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹³⁷	The Company's effective share in the cost/budget (USD thousands)
	months before drilling and no later than March 14, 2013¹³⁸ - Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. - Submission of a summary report of the drilling findings no later than three months after completion. - Submission of a report summarizing the operations in the license area by June 14, 2013		

E. Disclosure of the effective participation rate in the Company's expenses and revenues in the Ratio Yam licenses

Participation rate	Percentage before return on investment	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of oil asset attributable to equity holders of the Company	25.297%	25.297%	100%	100%	The Company's holdings are through its holdings of participation units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset revenues attributable to equity holders of the Company	22.29%	22.89%	88.10%	90.48%	See the calculation in section F below.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	25.55%	26.31%	101%	104%	See the calculation in section G below.

¹³⁸ If the drilling is carried out by one of the rigs already operating in licenses which Noble holds (Sedco Express, Pride North America and Homer), this document is not required.

F. Calculation of the effective share of revenues in the Ratio Yam licenses attributable to equity holders of the Company

Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical annual revenues of the oil asset after the discovery	100%	100%	
Royalties or payment (derived from revenues after the discovery) related to the oil asset *:			
The State	(11.34%)	(11.34%)	Calculated at the wellhead price according to the calculation in 2011 for the Yam Tethys project
Total	(11.34%)	(11.34%)	
Adjusted revenues on the level of the oil asset	88.66%	88.66%	
The share of the adjusted oil asset revenues attributable to the equity holders of the Company	25.297%	25.297%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	22.43%	22.43%	
Royalties or payments (derived from revenues after discovery) in respect of the oil asset at the level of the Company			
On the level of the Company			
The share of the equity holders of the Company in the payment to the general partner/another service provider that collects payment at the level of the Company	1.0019%	2.2537%	In the Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In the Avner Partnership – overriding royalties at a rate of 6%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	=====	
Total	1.0019%	2.2537%	
Share of holders of the Company's equity rights in revenues due to additional royalties from the asset	0.862%	2.714%	Overriding royalties at a rate of 3% up to ROI and 13% after ROI, and overriding royalties at a rate of 6% calculated at the wellhead price according to the calculation in 2011 in the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	22.29%	22.89%	

G. Calculation of the effective participation rate of the Company's equity holders in exploration, development and production expenses in the Ratio Yam licenses

Description	%	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (reference to the description of the agreement)
Theoretical expenses of the oil asset after the discovery	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	1%-4%	The rate in the table refers to exploration expenses. These amounts are for indirect expenses and are in addition to reimbursement of expenses paid to the operator. The rate of payment to the operator decreases as exploration expenses increase. The partners are jointly reviewing the option of setting operator's fees that will be paid for indirect development and production expenses.
Total effective rate of expense at the level of the oil asset	101%-104%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	25.297%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	25.55%-26.31%	
On the level of the Company		
Details of payments (derived from the expenses) in respect of the oil asset and at the level of the Company (the following percentages will be calculated in accordance with the Company's share in the oil asset)		
General partner in Avner Partnership	25.55%-26.31%	In accordance with the partnership agreement, the general partner is entitled to the higher of 7.5% of the associate partnership's exploration expenses or USD 40,000 a month on a quarterly calculation. Since exploration is taking place in the area covered by the license during this period, the operator's fees are at the level that was determined in the partnership agreement.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	139	

¹³⁹ When the share of Avner Partnership in the exploration expenses exceeds USD 1.6 million per quarter, the effective share will increase to 25.62-26.39%.

H. Royalties and payments paid during exploration, development and production operations for the oil asset (USD thousands)

Description	Total share of equity holders of the Company in investment in the oil asset in this period ¹⁴⁰	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator
Budget actually invested in 2009 (including the payments)	3,796	0	87
Budget actually invested in 2010 (including the payments)	22,728	804	169
Budget actually invested in 2011 (including the payments)	92,291	3,880	833

I. Contingent resources in the Leviathan discovery

1. Quantitative data

According to a report received by the partnerships from NSAI, which was prepared in accordance with the principles of the SPE-PRMS, the contingent resources of natural gas in the Leviathan discovery at December 31, 2011 are classified as development pending, as described below:

Target	Probability	Gas (BCF)	Company's net share (concatenation) (BCF) ¹⁴¹
A Sands	Low estimate	10,334.9	2,365.6
	Best estimate	13,300.4	3,044.4
	High estimate	16,726.4	3,828.6
	Mean *	13,441.7	3,076.8
B Sands	Low estimate	1,204.3	275.6
	Best estimate	1,870.8	428.2
	High estimate	2,618.2	599.3
	Mean *	1,896.9	434.2
C Sands	Low estimate	1,234.6	282.5
	Best estimate	1,516.0	347.0
	High estimate	1,838.2	420.7
	Mean *	1,529.2	350.0

At the partnerships' request, in addition to the disclosure requirements of the Securities Authority regarding oil and gas exploration ("the disclosure requirements") in the contingent resources report, NSAI included the mean distribution value. The partnerships believe that in this case, this is important information for investors, since Noble and the partnerships have published this information in the past and its publication provides continuity of the partnerships' reports and a full and comparative picture.

¹⁴⁰ Including costs for which payments are not made to the operator.

¹⁴¹ After receiving royalties (at the rate after ROI) and assuming ROI is after the total quantity is sold (for 100% of the rights in the oil asset (of 882.5 BCF) Since the ROI date is affected by the price of gas sales, production capacity, production costs and percentage of royalties, and since the production system has not yet been planned and constructed and agreements for the sale of natural gas have not yet been signed, the ROI date could be materially different from the aforesaid date.

2. The following is noted:

The estimates in the contingent resources report, prepared by NSAI according to PRMS methodology, are based on the following statistical model:

- A) NSAI's technical team defines a range for each parameter in the above table, according to the information available to the team ("the parameters")
- B) A statistical program randomly chooses a value for each parameter and multiplies the values with each other according to a standard equation ("the random choice and multiplication stage").
- C) The statistical program performs the random choice and multiplication stage repeatedly (in this report, multiplication was performed approximately 30,000 times, producing 30,000 values).
- D) Of the 30,000 values produced, PRMS requires that the following values are stated:
 - 1. Low estimate: 90% of the values exceed this value.
 - 2. Best estimate: 50% of the values exceed this value
 - 3. High estimate: 10% of the values exceed this value.
- E) The mean, which is not required by PRMS, is defined simply as the sum total of the 30,000 values, divided by 30,000. It is important to note that generally, the mean is different to the best estimate, and may be higher or lower.

Forward-looking information: This mean was not prepared according to PRMS methodology and may take into account, more significantly in reference to the best estimate, extreme scenarios with low probability. It is noteworthy that actual results could be significantly different than the mean.

It is emphasized that the geological and engineering database used to calculate the mean is identical to the database used to calculate the parameters required by PRMS, such that the mean figure is another product of the same statistical method used to calculate the other estimates. According to the contingent resources report, given the discovery and its development, the probability that the quantity of resources will be equal to or higher than the mean is: 48% for A Sands; 48% for B Sands; and 48% for C Sands.

- 3. The report was based on the results of a 3D seismic survey carried out by Petroleum Geo-Services in 2009 and processed in 2010 and on information collected from the Leviathan 1 and Leviathan 3 drillings.
- 4. The resources are contingent on approval of the development plan for the Leviathan project, which includes a reasonable forecast for natural gas sales. In addition, according to the report, based on development of similar reservoirs, there is a reasonable probability that the contingent resources in the best estimate category will be economically viable.
- 5. The contingent resources report prepared by NSAI includes a number of assumptions and qualifications:
 - A) The estimates were not adjusted to reflect commercial risk.
 - B) The assessor did not visit the drilling site, and did not assess the mechanical activity at the well or its state.
 - C) The assessor did not assess possible exposure from environmental events. However, the assessor noted that at the date of the report, it is unaware of any possible liability for environmental events that could have a material effect on the amount of contingent resources in the assessor's report.
 - D) The contingent resources are in an undeveloped location, therefore the appraisal is based on the estimated volume of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological characteristics and properties.
- 6. In view of the considerable estimated resources in the Leviathan discovery, the main potential market for these resources is the international market. Therefore, the partnership is examining various alternatives for the gas shortage, including the option of exporting gas and selling it on the international market. For a description of the potential market for the resources and a number of possible alternatives, see section 1.11.31(E)

below. At this stage, it is not possible to determine an estimated timetable for preparing or implementing a development plan for the Leviathan reservoir, until completion of the milestones set out below and preparation of a development plan and commercialization of the reservoir. It is emphasized that each option has a different timetable and different establishment and operational costs, and until the option for commercialization of gas is selected and the development plan for the field is approved, it is not possible to reasonably estimate the timetables and development budget of the field.

7. Central milestones for preparing a natural gas export project include: Analysis of the target markets; feasibility studies of various technologies and sites at which facilities will be built; partial preliminary engineering planning, including definition of the underlying assumptions of the project and its components, the scope and an initial estimate of timetables and budget (Pre-FEED); formulation of long-term agreements for the sale of natural gas (in LNG form and/or through pipes) with potential consumers; formulation of a financial and financing program; full preliminary engineering planning of the project, including definition of the project, timetables and budget (FEED); obtaining the regulatory approvals required in accordance with the law; approval of a development program by the partners and adoption of a final investment decision (FID); signing of performance agreements for the project. It is noted that state-level agreements between Israel and other countries that may be involved in the project could require renewal.

Forward-looking information: There is no certainty that commercial production of any part of the contingent resources is possible.

8. Reconciliation of the information in the report and information in previous reports relating to the oil asset

There are no significant differences in the total estimates set out in the contingent resources report and the total estimates published in the past by the partnerships.

Forward-looking information: The estimates of NSAI in respect of the contingent resources in the Leviathan reservoir are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling operator from drillings in the reservoir and drillings in the adjacent reservoirs, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas consumed may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production.

9. The Company declares that all of the above information has been prepared in compliance with the SPE-PRMS.
10. Opinion of the appraiser

A contingent resources report prepared by NSAI as of December 31, 2011 is attached to this report as a reference to the reserves report attached as Appendix F to the Periodic Report for 2011 of Delek Drilling Partnership, which was published on March 29, 2012 (ref. 2012-01-084516).

J. Contingent resources in the Dolphin discovery

1. Quantitative data

According to a report received by the partnerships from NSAI, which was prepared in accordance with the principles of the SPE-PRMS, the contingent resources of natural gas in the Dolphin 1 reservoir at December 31, 2011 are classified as development on hold, as described below:

Contingent resources	Total in the oil asset (gross) BCF	Total Company share (in concatenation) (net)¹⁴² BCF
Low estimate (1C)	37.2	8.5
Best estimate (2C)	81.3	18.6
High estimate (3C)	177.6	40.6

According to the contingent resources report, the resources are contingent on approval of the development plan for the Dolphin project and demonstration of economic feasibility for the project. NSAI also notes that since it is not possible to determine the economic viability of the reservoir at this stage, a feasibility study is required to estimate the extent of economic viability and commercial potential of the reservoir.

The contingent resources report prepared by NSAI includes a number of assumptions and qualifications: (a) the evaluations have not been adjusted to reflect the commercial risk. (b) The assessor did not visit the drilling site and did not examine the mechanical operations at the site or its state. (c) The assessor did not examine possible exposure arising from environmental events, however, NSAI noted that at the date of the contingent resources report, it is unaware of any possible environmental events that could have a material effect on the amount of reserves estimated in the contingent resources report. (4) The contingent resources are in undeveloped areas and accordingly the estimate is based on assessments in respect of the size of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological properties.

2. The partnerships in the Dolphin 1 discovery will explore different options for commercializing the natural gas in the Dolphin 1 reservoir, as part of the assessment of the options for integrating the reservoir's development plan with development plans of adjacent fields, which may allow such joint development. In view of the estimated scope of contingent resources of natural gas in the Dolphin 1 reservoir, the potential market for these resources is the domestic market and/or the international market, based on and subject to the future development plans in which development of the reservoir may be integrated. For information about the domestic gas market, see section 1.11.3(A) above and for further information about possible export of gas, see the section below.

It is emphasized that at this stage, it is unable to determine an estimated timetable for the formulation and/or implementation of a development plan for the Dolphin 1 reservoir, pending completion of an examination of possible development plans of adjacent fields and the option of integrating the development plan for the Dolphin 1 reservoir.

It is noted that development of the Dolphin 1 reservoir might be integrated with the development plan for the Leviathan reservoir, located 30 km northwest of the Dolphin 1 reservoir, or it may be integrated as part of a future stage in the development of the Tamar reservoir, located approximately 30 km northeast of the Dolphin 1 reservoir.

It is emphasized that each alternative of a development plan has different timetables and construction and operation costs, therefore until the development plan for the Dolphin 1 reservoir is assessed and prepared, the timetables and development budget for the reservoir cannot be estimated.

Forward-looking information: There is no certainty that it will be commercially possible to produce any percentage of the contingent resources.

3. Reconciliation of the information in the report and information in previous reports relating to the oil asset

The immediate report of August 29, 2011 regarding the partnerships' decision to drill the well, which included a report prepared by NSAI, provided information about the

¹⁴² After receiving royalties (at the rate after ROI) and assuming ROI is after the total quantity is sold (for 100% of the rights in the oil asset (of 17.65 BCF) Since the ROI date is affected by the price of gas sales, production capacity, production costs and percentage of royalties, and since the production system has not yet been planned and constructed and agreements for the sale of natural gas have not yet been signed, the ROI date could be materially different from the aforesaid date.

prospective resources at the Dolphin 1 prospect (pre-drilling) as follows: low estimate (1C): BCF 182.6; best estimate (2C) 550.5 BCF; high estimate (3C) 1,630.1 BCF The prospective resources report is based on pre-drilling data, and mainly on a 3D seismic survey ("the seismic survey"), and on the comparison of the formation, as seen in the interpretation of the seismic survey, to various reservoirs in the area and worldwide, and on information obtained from the operator.

The estimate of the contingent resources in the report (which refer to the central fault block in the Dolphin reservoir where the Dolphin 1 drilling was carried out)¹⁴³ is significantly lower than the estimate of the prospective resources in each of the categories. This difference arises from interpretation of the seismic survey, performed prior to the drilling, which assumed and defined (as is customary in interpretation of this type and according to known and proven principles) certain horizons as representing the target top and gas-water contact. Analysis of the actual well results indicates that these assumptions and definitions, which were based, as aforesaid, on pre-drilling information, were inaccurate, and in fact the target top was 30 meters lower than the pre-drilling estimate, and the gas-water contact was in fact 2 meters higher than the pre-drilling estimate. Consequently, the thickness of the layers containing natural gas that were actually discovered in the well is significantly smaller than the thickness of the layers estimated before drilling.

Forward-looking information: The estimates of NSAI in respect of the contingent resources in the Dolphin 1 reservoir are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the drilling operator and drillings in the adjacent reservoirs, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas produced (if produced) may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production.

4. The Company declares that all of the above information has been prepared in compliance with the SPE-PRMS.
5. Opinion of the appraiser

A contingent resources report prepared by NSAI as of December 31, 2011 is attached to this report as a reference to the reserves report attached as Appendix H to the Periodic Report for 2011 of Delek Drilling Partnership, which was published on March 29, 2012 (ref. 2012-01-084516).

K. Prospective resources in the Dolphin 2 and Dolphin 3 prospects

1. On August 29, 2011, the partnerships issued a prospective resources report as of July 31, 2011 for the Dolphin 1, Dolphin 2 and Dolphin 3 prospects, in accordance with the principles of SPE-PRMS.
2. In view of the results of the Dolphin 1 drilling and the contingent resources report in this discovery, only prospective resources (undiscovered) in the Dolphin 2 and Dolphin 3 prospects will be described below, as described in this report as of July 31, 2011:

Prospective resources category	Prospect	Total in the oil asset (gross) ¹⁴⁴ (BCF)
Low estimate	Dolphin 2	101.3
	Dolphin 3	50.7
Best estimate	Dolphin 2	213.2
	Dolphin 3	199.6

¹⁴³ The contingent resources report does not refer to the other fault blocks in the Dolphin reservoir, identified in the prospective resources report, the Dolphin 2 and Dolphin 3 prospects, since according to the professional analysis, they are separate and were not drilled.

¹⁴⁴ After receiving royalties and after ROI

High estimate	Dolphin 2	446
	Dolphin 3	797.9

In view of the differences in data relating to the prospective resources (undiscovered) in the Dolphin 1 prospect, which were included in the prospective resources report, compared to data relating to the contingent resources in the Dolphin 1 well at the date of the report, the partnerships do not consider the Dolphin 2 and Dolphin 3 prospects as significant prospects in which they intend to operate in the near future, including drilling, inter alia, in view of the quantity of resources in the other oil assets held by the partnerships and taking into account the future requirements of these oil assets. It is noted in this context, that the work plan in the Hannah license does not require drilling at the Dolphin 2 and Dolphin 3 prospects, therefore this does not adversely affect the work plan in this license.

L. Prospective resources in the deepwater Leviathan 1 drilling

1. Quantitative data

According to a report that the partnerships received from NSAI, prepared in accordance with the guidelines set out in SPE-PRMS, as of December 31, 2011, the prospective resources in the deep target layers of the Leviathan 1 drilling in the Leviathan reservoir are as follows:

Target	Probability	Total oil/gas asset (gross)			Total Company share (gross) ¹⁴⁵		
		Gas (BCF)	Oil (MMBO)	Total hydrocarbons (MMBOE) ¹⁴⁶	Gas (BCF)	Oil (MMBO)	Total hydrocarbons (MMBOE)
Lower Oligocene	Low estimate	45.6	6.5	14.7	11.5	1.6	3.7
	Best estimate	264.4	39.5	85.2	66.9	10.0	21.6
	High estimate	1,360.1	215.5	441.3	344.1	54.5	111.6
	Mean *	581.2	90.3	187.2 (percentile 27)	147.0	22.8	47.4
Lower Cretaceous	Low estimate	400.1	45.2	111.8	101.2	11.4	28.3
	Best estimate	1,965.2	277.5	605.0	497.1	70.2	153.0
	High estimate	8,432.4	1,297.8	2,703.2	2,133.1	328.3	683.8
	Mean *	3,693.4	563.7	1,179.3 (percentile 29)	934.3	142.6	298.3
Lower Cretaceous	Low estimate	443.4	49.6	123.5	112.2	12.5	31.2
	Best estimate	1,984.8	282.2	613.0	502.1	71.4	155.1
	High estimate	7,563.2	1,204.4	2,464.9	1,913.3	304.7	623.5
	Mean *	3,350.1	512.9	1,071.3 (percentile 31)	847.5	129.7	271.0

2. At the partnerships' request, in addition to the disclosure requirements in the resources report, NSAI included the mean distribution value. The partnerships believe that in this case, this is important information for investors, since Noble and the partnerships have published this information in the past and its publication provides continuity of the partnerships' reports and a full and comparative picture. In view of the aforesaid, the partnerships state the following:

The estimates in the resources report, prepared by NSAI according to PRMS methodology, are based on the following statistical model:

- A) NSAI's technical team defines a range for each parameter in the above table, according to the information available to the team.
- B) A statistical program randomly chooses a value for each parameter (from the defined range) and multiplies the values with each other according to a standard equation.
- C) The statistical program performs the random choice and multiplication stage repeatedly (in this report, multiplication was performed approximately 30,000 times, producing 30,000 values).
- D) Of the 30,000 values produced, PRMS requires that the following values are stated:
 1. Low estimate: 90% of the values exceed this value.
 2. Best estimate: 50% of the values exceed this value
 3. High estimate: 10% of the values exceed this value.

¹⁴⁵ Before payment of royalties

¹⁴⁶ The conversion ratio for energy units is 6 billion cubic feet of gas to million barrels of oil equivalent. (6 BCF = 1 MMBOE).

Forward-looking information: Equivalent units of energy may be misleading particularly if used in isolation. The conversion is based on the energy ratio at the burner and does not represent a value equivalent.

- E) The mean, which is not required by PRMS, is defined simply as the sum total of the 30,000 values, divided by 30,000. It is important to note that generally, the mean is different to the best estimate, and may be higher or lower.

Warning: This mean was not prepared according to PRMS methodology and may take into account, more significantly in reference to the best estimate, extreme scenarios with low probability. It is noteworthy that actual drilling results could be significantly different than the mean.

- F) It is emphasized that the geological and engineering database used to calculate the mean is identical to the database used to calculate the parameters required by PRMS, such that the mean figure is another product of the same statistical method used to calculate the other estimates. As stated in the resources report and the table above,, given the discovery and its development, the probability that the quantity of resources will be equal to or higher than the mean is:
1. 27% for the lower Oligocene target
 2. 29% for the upper Cretaceous target
 3. 31% for the lower Cretaceous target
- G) The report was based on the results of a 3D seismic survey carried out by Petroleum Geo-Services in 2009 and processed in 2010 and on information gathered from the Leviathan 1 well.

- H) Basic parameters used to calculate the different scenarios:

Parameter	Lower Oligocene		Mid Cretaceous		Lower Cretaceous	
	Low estimate	High estimate	Low estimate	High estimate	Low estimate	High estimate
Gross rock volume (acre-feet)	282,515	4,713,247	2,572,271	28,967,372	2,976,639	24,804,310
Net-to-gross ratio (decimal)	0.10	0.700	0.10	0.70	0.10	0.70
Porosity (decimal)	0.12	0.22	0.12	0.22	0.12	0.22
Oil saturation (decimal)	0.55	0.75	0.55	0.75	0.55	0.75
Gas saturation (decimal)	0.55	0.75	0.55	0.75	0.55	0.75
Initial oil formation volume factor (RB/STB)	2.00	1.40	2.00	1.40	2.00	1.40
Initial gas formation volume factor (RB/STB)	0.431	0.505	0.419	0.494	0.418	0.493
Oil recovery factor (decimal)	0.10	0.45	0.10	0.45	0.10	0.45
Gas recovery factor (decimal)	0.50	0.70	0.50	0.70	0.50	0.70
Gross thickness (feet)	48	98	170	379	213	428
Area (acres) ¹⁴⁷	5,917	48,003	15,141	76,449	13,997	57,892

3. Material risks involved in the process The material risks involved in the continuation of drilling at Leviathan 1 are mainly the technical-operational risks involved in the drilling (in particular in view of the high pressure expected in the well and the fact that the drilling is mainly planned to the Oligo-Miocene gas targets, including risk of malfunctions in the drilling operations, electric logs and production tests, if any. If the technological-operational activities are completed without malfunctions, the risks later in the process

147

One acre is the equivalent of 4,050 square meters.

that is required to achieve a commercial discovery include that the porosity and conductivity of the reservoir rock will not be high enough to allow a commercially-significant quantity, penetration of water, which will prevent economically feasible production, and development costs of the discovery. See section 1.11.3(l) below for a discussion of the risk factors involved in exploration.

4. The estimated probability of success of each of the geological risk factors in the exploration process in this drilling and the estimated probability of the presence of hydrocarbons (oil and/or natural gas) are as follows:

Parameter	Lower Oligocene (%)	Mid Cretaceous (%)	Lower Cretaceous (%)
Trap integrity	55	85	85
Reservoir quality	80	40	55
Source evaluation	50	55	55
Migration / timing	40	60	60
Total	9	11	15

5. Estimated probability of development for commercial production: At the date of the report, the partnerships are unable to provide a statistical estimate of the probability for development of the targets for commercial production. However, it can be estimated that the main potential market is the domestic market and international market given an oil discovery and the international market given a natural gas discovery. Accordingly, the partnerships are assessing alternatives for commercializing the hydrocarbons (if discovered and produced), including the option of exporting oil and/or natural gas, and sale to the international market. It is noted that when assessing the potential for commercial production, there may be an option of combining development of a discovery, if there is a discovery in one or more of the targets later in the drilling works, with the development plans of the natural gas reserves reported in the upper part of the drilling (Oligo-Miocene layers). In addition, if relatively small quantities of natural gas and/or oil are discovered in any of these targets, economically-feasible development could require joint development of several discoveries, utilizing regional infrastructure. For further information about the domestic gas market, see section 1.11.3(A) above and for further information about possible export of gas, see section 1.11.29(K) below.
6. The partnerships' explanations of the basic parameters used to calculate the different scenarios: The parameters used to calculate the estimates are mainly based on the results of the 3D seismic survey, information gathered in the Leviathan 1 drilling and general knowledge of the layers and similar reservoirs.

There is no certainty that any part of these potential resources will indeed be discovered, and if discovered, there is no certainty that it will be commercially possible to produce any part of the resources. The prospective information does not lie within the bounds of an evaluation in respect of the contingent reserves and resources, which can only be evaluated after exploration drilling, if at all.

Forward-looking information: The estimates of NSAI in respect of the prospective resources in the different targets following drilling at Leviathan 1 are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the lease operator from the drilling and/or from other drillings, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of hydrocarbons discovered (if discovered) and produced (if produced) may be materially different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production.

7. The Company declares that all of the above information has been prepared in compliance with the SPE-PRMS.

8. Opinion of the appraiser

A contingent resources report prepared by NSAI as of December 31, 2011 is attached to this report as a reference to the reserves report attached as Appendix G to the Periodic Report for 2011 of Delek Drilling Partnership, which was published on March 29, 2012 (ref. 2012-01-084516) and the assessor's consent to include the report in this report is attached.

M. Joint operating agreement for the Ratio Yam project

The joint operating agreement (in this section below: ("the JOA") for the Ratio Yam project covers the same issues included in the JOA for the Yam Tethys project described in section 1.11.4(K) above. Decisions are made by a majority vote in favor of the decision of at least two participants that are not related parties, holding together at least 60% of the rights in the licenses. Noble was appointed as the operator of the licenses. It also states that if a party to the JOA wants to transfer its rights (excluding transfer to a corporation under its control), the other parties to the JOA have the right of first refusal to acquire these rights in accordance with the provisions of the JOA.¹⁴⁸

1.11.7 Exploration operations of the limited partnerships other than in the Yam Tethys, Tamar and Ratio Yam projects

In addition to the production operations of the Yam Tethys project, the development activities of the Tamar project, and operations of the Ratio Yam project, the partnerships are engaged in further oil and gas exploration pursuant to licenses granted them under the Petroleum Law.

Below is a description of the oil and gas exploration operations of the limited partnerships in additional areas:

1.11.8 Ruth licenses

A. General

General information about the oil asset	
Name of oil asset	358/Ruth A 359/Ruth B 360/Ruth C
Location	Offshore assets 45-95 kilometers west of Haifa
Area	The area covered by all the licenses is 1,600 square kilometers
Type of oil asset and description of permitted operations according to that types	License Operations permitted under the Petroleum Law - exploration and production
Original grant date of the oil asset	March 1, 2009
Original expiry date of the oil asset	February 29, 2012
Dates of decision to extend the term of the oil asset	-
Current expiry date of the oil asset	September 1, 2013
Note whether there is an additional option of extending the period of the oil asset: if there is such an option, note the period of the possible extension	Subject to the Petroleum Law, the period can be extended for up to seven years from the grant date, with an option for another two-year extension in the event of a discovery
Note name of operator	Noble
Names of the direct partners in the oil asset and their direct share in the oil asset and, to the best of the Company's knowledge, the names of the controlling	(1) Noble (47.059%); ¹⁴⁹ (2) Delek Drilling Partnership (27.835%) ¹⁵⁰ (3) Avner Partnership (25.106%) ¹⁵¹

¹⁴⁸ The cumulative holdings of Delek Drilling Partnership and Avner Partnership

¹⁴⁹ For further information about Noble, see section 1.11.3(A) above.

¹⁵⁰ For further information about Delek Drilling Partnership, see section 1.11.1(D) above.

¹⁵¹ For further information about Avner Partnership, see section 1.11.1(D) above.

owners in the partners	

General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	¹⁵²
Description of the Company's holding in the oil asset	Through its holdings in the Delek Drilling and Avner partnerships
Effective share of oil asset revenues attributable to equity holders of the Company	<u>In revenue:</u> Before return on investment - 27.201% After return on investment - 30.206% <u>In the right to participate in revenue</u> Before return on investment - 26.18% After return on investment - 26.91% <u>In right to receive royalties:</u> Before return on investment - 1.021% After return on investment - 3.296%
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 3,239

B. Compliance with the terms of the work plan in the Ruth licenses at the date of the report

Period	Description of the work plan defined for the period	Description of work plan items completed in the period	Description of work plan items not yet completed in the period
2009	Mapping potential prospects based on the new seismic survey, seismic facies analysis, rock physics and assessment of potential by December 1, 2009	For further information see the actual and planned work plan for the Ruth licenses.	The operations in the work plan were carried out.
2010	Economic analysis of the prospects up to March 1, 2010	For further information see the actual and planned work plan for the Ruth licenses.	The operations in the work plan were carried out.
2011	Another 2D-3D seismic survey, if required, by March 1, 2011 ¹⁵³ Signing a contract for offshore drilling with a drilling contractor by March 1, 2011 ¹⁵⁴	For further information see the actual and planned work plan for the Ruth licenses.	The operations in the work plan were carried out.

¹⁵² The Ruth licenses were granted on March 1, 2009 instead of the preliminary permit for 197/Ruth

¹⁵³ Completed in 2010

¹⁵⁴ Completed in 2010

C. Binding work plan according to the terms of the oil asset

Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	Company's effective share of the total budget (USD thousands) (divided into the main items)
2012 to September 1, 2013	• Submission of quarterly reports, including exploration results, geological, geophysical and engineering data and details of expenses for works carried out in the license. • Submission of a drilling prospect at least three months before the planned date for drilling in the license area • Submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three months before drilling and no later than March 14, 2013¹⁵⁵ • Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. • Submission of a summary report of the drilling findings no later than three months after completion. • Submission of a report summarizing the operations by June 14, 2013 • As aforesaid, at the date of the report, the Ruth licenses are valid until September 1, 2013.	50,000-70,000 for each drilling	15,430-21,602

D. Actual and planned work plan for the Ruth licenses

The following is a summary of the main activities actually carried out in the Ruth license areas from January 1, 2009 through to the date of the report and a summary of the planned activities in these licenses:

Period	Summary of the operations performed in the period / summary of the planned work plan	Estimated total budget for operations on the level of the oil asset (USD thousands)	Company's effective share in the cost/budget (USD thousands)
2009	• Mapping of the 2D seismic survey in the license areas	234	67
2010	• Feasibility analysis of the prospects • 3-D seismic surveys • Signing a contract for offshore drilling with a drilling contractor	8,368	2,409
2011	• Processing of the 3D seismic survey carried out in 2010 and interpretation of its results. • Processing and interpretation results were received in the fourth quarter of	1,059	313

Period	Summary of the operations performed in the period / summary of the planned work plan	Estimated total budget for operations on the level of the oil asset (USD thousands)	Company's effective share in the cost/budget (USD thousands)
	2011.		
2012 to September 1, 2013	• Submission of quarterly reports for operations carried out in the license • Submission of a drilling prospect at least three months before the planned date for drilling in the license area • Submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three months before drilling and no later than March 14, 2013¹⁵⁶ • Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. Submission of a summary report of the drilling findings no later than three months after completion. • Submission of a report summarizing the operations by June 14, 2013 • As aforesaid, at the date of the report, the Ruth licenses are valid until September 1, 2013.	50,000-70,000 for each drilling	15,430-21,602

E. Disclosure of the effective participation rate in the expenses and revenues in the Ruth licenses

Participation rate	Percentage before return on investment	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of oil asset attributable to equity holders of the Company	29.676%	29.676%	100%	100%	The Company's holdings are through its holdings of participation units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset revenues attributable to equity holders of the Company	26.18%	26.91%	87.8888.21	90.69%	See the calculation in section 1.11.8(H) below.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	29.97%	30.86%	101%	104%	See the calculation in section 1.11.8(H) below.

F. Calculation of the effective share of the oil asset attributable to equity holders of the Company, if gas or oil is discovered in the Ruth license areas

Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical annual revenues of the oil asset after the discovery	100%	100%	
Royalties or payment (derived from revenues after the discovery) related to the oil asset *:			
The State	(11.34%)	(11.34%)	Calculated at the wellhead price according to the calculation in 2011 for the Yam Tethys project
Total	=====	=====	
Adjusted revenues on the level of the oil asset	88.66%	88.66%	
The share of the adjusted oil asset revenues attributable to the equity holders of the Company	29.676%	29.676%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	26.31%	26.31%	
Royalties or payments (derived from revenues after discovery) in respect of the oil asset at the level of the Company			
The share of the equity holders of the Company in the payment to the general partner/another service provider that collects payment at the level of the Company	1.1548%	2.6917%	In the Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In the Avner Partnership – overriding royalties at a rate of 13%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	=====	
Total	1.1548%	2.6917%	
Share of holders of the Company's equity rights in revenues due to additional royalties from the asset	1.021%	3.296%	Overriding royalties at a rate of 3% up to ROI and 13% after ROI, and overriding royalties at a rate of 6% calculated at the wellhead price according to the calculation in 2011 in the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	26.18%	26.91%	

G. Calculation of the effective participation rate of the Company's equity holders in exploration, development and production expenses in the Ruth licenses

Description	%	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical expenses of the oil asset after the discovery	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	4%-1%	The rate in the table refers to exploration expenses. These amounts are for indirect expenses and are in addition to reimbursement of expenses paid to the operator. The rate of payment to the operator decreases as exploration expenses increase. Payment for development expenses is yet to be determined.
Total effective rate of expense at the level of the oil asset	104%-101%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	29.676%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	29.97%-30.86%	
On the level of the Company		
Payments (derived from the expenses) in respect of the oil asset and at the level of the Company (the following percentages will be calculated in accordance with the share of the equity holders of the Company in the oil asset)		
General partner in Avner Partnership		In accordance with the partnership agreement, the general partner is entitled to the higher of 7.5% of the associate partnership's exploration expenses or USD 40 thousand a month on a quarterly calculation.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	29.97%-30.86% ¹⁵⁷	

¹⁵⁷ When the share of Avner Partnership in the exploration expenses exceeds USD 1.6 million per quarter, the effective share will increase to 29.6-30.48%.

H. Royalties and payments paid during exploration, development and production operations for the oil asset (USD thousands)

Description	Total share of equity holders of the Company in investment in the oil asset in this period ¹⁵⁸	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator
Budget actually invested in 2009 (including the payments)	67	0	2
Budget actually invested in 2010 (including the payments)	2,409	0	54
Budget actually invested in 2011 (including the payments)	313	10	0

1.11.9 Alon licenses

A. General

General information about the oil asset	
Name of oil asset	364/Alon A 365/Alon B 366/Alon C 367/Alon D 369/Alon F
Location	An offshore asset, about 50—140 km. North-west of the shores of Nahariya
Area	Approximately 2,400 sq. m
Type of oil asset and description of permitted operations according to that types	License Operations permitted under the Petroleum Law - exploration and production
Original grant date of the oil asset	March 1, 2009
Original expiry date of the oil asset	February 29, 2012
Dates of decision to extend the term of the oil asset	-
Current expiry date of the oil asset	September 1, 2013
Note whether there is an additional option of extending the period of the oil asset: if there is such an option, note the period of the possible extension	Subject to the Petroleum Law, the period can be extended for up to seven years from the grant date, with an option for another two-year extension in the event of a discovery
Note name of operator	Noble
Names of the direct partners in the oil asset and their direct share in the oil asset and, to the best of the Company's knowledge, the names of the controlling owners in the partners	(1) Noble (47.059%) ¹⁵⁹ (2) Delek Drilling Partnership (26.4705%) ¹⁶⁰ (3) Avner Partnership (26.4705%) ¹⁶¹

¹⁵⁸ Including costs for which payments are not made to the operator.

¹⁵⁹ For further information about Noble, see section 1.11.3(A) above.

¹⁶⁰ For further information about Delek Drilling, see section 1.11.1(D) above.

¹⁶¹ For further information about Avner Partnership, see section 1.11.1(D) above

General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	- ¹⁶²
Description of the Company's holding in the oil asset	Through its holdings in the Delek Drilling and Avner partnerships
Effective share of oil asset revenues attributable to equity holders of the Company	<u>In revenue:</u> Before return on investment - 27.0463% After return on investment - 29.829% <u>In the right to participate in revenue</u> Before return on investment - 26.04% After return on investment - 26.66% <u>In right to receive royalties:</u> Before return on investment - 1.0063% After return on investment - 3.1690%
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 5,143 thousand

B. Compliance with the terms of the work plan in the Alon licenses at the date of the report

Period	Description of the work plan defined for the period	Description of work plan items completed in the period ¹⁶³	Description of work plan items not yet completed in the period
2009	Mapping potential prospects based on the new seismic survey (2D survey), seismic facies analysis, rock physics and assessment of potential by December 1, 2009	For further information see the actual and planned work plan for the Alon licenses	The operations in the work plan were carried out.
2010	Economic analysis of the prospects up to March 1, 2010	For further information see the actual and planned work plan for the Alon licenses	The operations in the work plan were carried out.
2011	- Another 2D-3D seismic survey, if required, by March 1, 2011 - Signing a contract for offshore drilling with a drilling contractor by March 1, 2011	For further information see the actual and planned work plan for the Alon licenses	The operations in the work plan were carried out.

¹⁶² The Alon licenses were granted on March 1, 2009 instead of the 198/Alon preliminary permit

¹⁶³ The description of the components of the work plan in the period are for the period up to the report date.

C. Binding work plan according to the terms of the oil asset

Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012 to September 1, 2013	• Submission of quarterly reports for operations carried out in the license • Submission of a drilling prospect at least three months before the planned date for drilling in the license area • Submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three months before drilling and no later than March 14, 2013¹⁶⁴ • Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. • Submission of a summary report of the drilling findings no later than three months after completion. • Submission of a report summarizing the operations by September 1, 2013 • As aforesaid, at the date of the report, the Alon licenses are valid until September 1, 2013.	50,000-70,000 for each drilling	-

D. Actual and planned work plan for the Alon licenses

The following is a summary of the main activities actually carried out in the Alon license areas from January 1, 2009 through to the date of the report and a summary of the planned activities in these licenses:

Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹⁶⁵	Company's effective share in the cost/budget (USD thousands)
2009	Mapping of potential prospects based on a 2D seismic survey conducted in 2008 Performance of 3D seismic surveys (together with the Ratio Yam license areas) ("the 2009 seismic survey")	4,080	1,171
2010	Feasibility analysis of the prospects Seismic survey ("the 2010 seismic survey")	10,109	2,901

¹⁶⁴ If the drilling is carried out by one of the rigs already operating in licenses which Noble holds (Sedco Express, Pride North America and Homer), this document is not required.

¹⁶⁵ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements.

Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹⁶⁵	Company's effective share in the cost/budget (USD thousands)
2011	- Processing and interpretation of a seismic survey in 2010 - Continuation of preparation of drilling prospects - Reprocessing of the 2009 seismic survey - On December 12, 2011, drilling started at the Tanin 1 exploration well in the 364/Alon A license, ending on February 5, 2012 at a final depth of 5,500 m (including water depth). - On February 7, 2012, the partnerships announced a natural gas discovery at the Tanin 1 well.	1,976 36,963	581 10,872
2012 to September 1, 2013	- Submission of quarterly reports for operations carried out in the license - Submission of a drilling prospect at least three months before the planned drilling date in the license area; submission of a document describing the technical specification of the drilling rig and the timetable for drilling, no later than three months before drilling and no later than March 14, 2013¹⁶⁶ - Submission of a drilling plan that includes detailed geological and engineering planning, including risk analysis for the site, at least three months before starting the planned drilling. Submission of a summary report of the drilling findings no later than three months after completion. - Submission of a report summarizing the operations by September 1, 2013 - As aforesaid, at the date of the report, the Alon licenses are valid until September 1, 2013.	50,000-70,000 for each drilling	15,360-21,504

¹⁶⁶ If the drilling is carried out by one of the rigs already operating in licenses which Noble holds (Sedco Express, Pride North America and Homer), this document is not required.

E. Disclosure of the effective participation rate in the expenses and revenues in the Alon licenses

Participation rate	Percentage before return on investment	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of oil asset attributable to equity holders of the Company	29.538%	29.538%	100%	100%	The Company's holdings are through its holdings of participation units of Delek Drilling Partnership and Avner Partnership
Effective share of oil asset revenues attributable to equity holders of the Company	26.04%	26.66%	88.15%	90.27%	See the calculation in section 6 below.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	29.83%	30.72%	101%	104%	See the calculation in section 7 below.

F. Calculation of the effective share of the oil asset attributable to equity holders of the Company, if gas or oil is discovered in the Alon license areas

Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical annual revenues of the oil asset after the discovery	100%	100%	
Royalties or payment (derived from revenues after the discovery) related to the oil asset *:			
The State	(11.34%)	(11.34%)	Calculated at the wellhead price according to the calculation in 2011 for the Yam Tethys project
Total	(11.34%)	(11.34%)	
Adjusted revenues on the level of the oil asset	88.66%	88.66%	
The share of the adjusted oil asset revenues attributable to the equity holders of the Company	29.538%	29.538%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	26.19%	26.19%	
Royalties or payments (derived from revenues after discovery) in respect of the oil asset at the level of the Company			

Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
The share of the equity holders of the Company in the payment to the general partner/another service provider that collects payment at the level of the Company	1.1548%	2.6917%	In the Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In the Avner Partnership – overriding royalties at a rate of 13%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	=====	
Total	1.1548%	2.6917%	
Share of holders of the Company's equity rights in revenues due to additional royalties from the asset	1.0063%	3.1690%	Overriding royalties at a rate of 3% up to ROI and 13% after ROI, and overriding royalties at a rate of 6% calculated at the wellhead price according to the calculation in 2011 in the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	26.04%	26.66%	

G. Calculation of the effective participation rate of the Company's equity holders in exploration, development and production expenses in the Alon licenses

Description	%	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical expenses of the oil asset after the discovery	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	4%-1%	The rate in the table refers to exploration expenses. These amounts are for indirect expenses and are in addition to reimbursement of expenses paid to the operator. The rate of payment to the operator decreases as exploration expenses increase. Payment for development expenses is yet to be determined.
Total effective rate of expense at the level of the oil asset	104%-101%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	29.538%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	29.83%-30.72%	
On the level of the Company		
Payments (derived from the expenses) in respect of the oil asset and at the level of the Company (the following percentages will be calculated in accordance with the share of the equity holders of the Company in the oil asset)		
General partner reported in the Avner Partnership		In accordance with the partnership agreement, the general partner is entitled to the higher of 7.5% of the associate partnership's exploration expenses or USD 40 thousand a month on a quarterly calculation.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	29.83%-30.72% ¹⁶⁷	

¹⁶⁷ When the share of Avner Partnership in the exploration expenses exceeds USD 1.6 million per quarter, the effective share will increase to 29.39-30.26%.

H. Royalties and payments paid during exploration, development and production operations for the oil asset (USD thousands)

Description	Total share of equity holders of the Company in investment in the oil asset in this period ¹⁶⁸	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator
Budget actually invested in 2009 (including the payments)	1,171	0	34
Budget actually invested in 2010 (including the payments)	2,901	0	65
Budget actually invested in 2011 (including the payments)	581	389	118

I. Estimated prospective resources in the Tanin 1 well

On August 30, 2011, the partnerships decided to approve an exploratory drilling at the Tanin 1 well in the 364/Alon A license area.

Further to the aforesaid, the partnership issued an immediate report about the prospective resources in the 364/Alon A license, stating that according to a report each of the partnerships received from NSAI, prepared in accordance with SPE-PRMS guidelines, the prospective (undiscovered) resources in the Tanin 1 prospect in the license area at July 31, 2011 are as follows:

Prospective resources category	Prospect	Total in the oil asset (gross) ¹⁶⁹ (BCF)
Low estimate	A Sands	770.6
	B Sands	46.4
Best estimate	A Sands	1,144.5
	B Sands	62.800
High estimate	A Sands	1,669.2
	B Sands	83.5

Forward-looking information: The above estimates of NSAI in respect of the prospective resources in the Tanin 1 prospect in the license area are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from 3D seismic surveys in the license area and/or from drillings nearby, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas discovered (if discovered) and produced (if produced) may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production projects, including due to continued analysis of the survey findings and due to operational and/or market and/or regulatory conditions.

On February 7, 2011, the partnerships announced that in their opinion, the quantity of gas discovered at the drilling site justifies an analysis and evaluation of the overall quantities of natural gas in the Tanin 1 drilling and an analysis and evaluation of the quantities of natural

¹⁶⁸ Including costs for which payments are not made to the operator.

¹⁶⁹ According to the rate of holding in concatenation of the Company in the asset

gas that can be produced commercially. In view of the aforesaid, the partnerships announced that the Tanin 1 drilling is a natural gas discovery.

1.11.10 Rights in Cyprus¹⁷⁰

A. General information about Block 12

General information about the oil asset	
Name of oil asset	Block 12, Cyprus
Location	The economic territorial waters known as Block 12, located 15-20 km west of the Alon licenses.
Area	Approximately 3,446 square meters ¹⁷¹
Type of oil asset and description of permitted operations according to that type:	Production sharing contract
Original grant date of the oil asset:	October 24, 2008
Original expiry date of the oil asset	October 24, 2011
Decision date for extension of the period of the oil asset	October 23, 2011
Current expiry date of the oil asset	October 23, 2013
Note whether there is an additional option of extending the period of the oil asset: if there is such an option, note the period of the possible extension	The agreement may be extended for two periods of up to two years each on condition that all the conditions required for the ended period are met and after the oil rights area is reduced.
Note name of operator	Noble Energy International, Ltd. ("Noble Cyprus")
Names of the direct partners in the oil asset and their direct share in the oil asset and, to the best of the Company's knowledge, the names of the controlling owners in the partners	1. Noble Cyprus (70%) 2. Delek Drilling Partnership^{1.11.29H}¹⁷² (15%) 3. Avner Partnership¹⁷³ (15%)

¹⁷⁰ For information of the series of agreements concerning Block 12 and transfer of the rights therein, see section 1.11.29.H below.

¹⁷¹ The original license area was approximately 4,446 sq km. Upon renewal of the license, the area was reduced by 25%.

¹⁷² As of the report date, the transfer of the rights by the partnerships is not yet complete, as described in section 1.11.29.H below.

¹⁷³ As of the report date, the transfer of the rights by the partnerships is not yet complete, as described in section 1.11.29.H below.

General information about the Company's share in the oil asset	
Note the acquisition date of the lease for the acquired oil asset	January 22, 2009
Description of the Company's holding in the oil asset	Through its holdings in participation units of Delek Drilling and Avner partnerships.
Effective share of oil asset revenues attributable to equity holders of the Company ¹⁷⁴	<u>In revenue:</u> The effective share of oil asset revenues attributable to equity holders of the Company is 16.64% before ROI and 17.07% after ROI, before deduction of the Republic of Cyprus' share under the provisions of the production sharing contract applicable to Block 12 and after payment of royalties to related parties. For information of the estimated share of the Republic of Cyprus, see section 1.11.10.H below. <u>Participation rights in revenue</u> The effective share of the participation rights in oil asset revenues attributable to equity holders of the Company is 16.01% before ROI and 15.1% after ROI, before deduction of the Republic of Cyprus' share under the provisions of the production sharing contract applicable to Block 12 and after payment of royalties to related parties. For information of the estimated share of the Republic of Cyprus, see section 1.11.10.H below. <u>In right to receive royalties:</u> The effective share of oil asset revenues attributable to equity holders of the Company is 0.628% before ROI and 1.979% after ROI, before deduction of the Republic of Cyprus' share under the provisions of the production sharing contract applicable to Block 12 and after payment of royalties to related parties. For information of the estimated share of the Republic of Cyprus, see section 1.11.10.H below.
Total share of equity holders of the Company in the cumulative investment in the oil asset in the five years preceding the last day of the reporting year (whether recognized as an expense or as an asset in the financial statements):	USD 17,907 thousand.

¹⁷⁴ The Company notes that the disclosure in this section is not according to the full format required under the disclosure guidelines. It cannot fully disclose as required in the guidelines, due to restrictions connected to the process of transferring the Cyprus rights from Noble to the partnerships. Under these circumstances, including: (a) uncertainty concerning the Republic of Cyprus' share in the gas produced, if any, as described in section 1.11.10.H below; (b) the partnerships' share of the potential natural gas resources in Block 12 according to the NSAI report described in section 1.11.10.A below compared to their entire gas reserve; (c) the Company's estimate, based on information in its possession as at the report date (before further operations were performed at Block 12), that development of the Dolphin reservoir will begin before that of Block 12, if at all (information which affects the current value of Block 12 of the partnerships' entire natural gas reserve); given all of these versus the concern that providing disclosure as required in the guideline may harm the process of transferring the rights in Block 12, the partnership discloses in the format set out in this section 1.11.10.

B. Map of oil asset¹⁷⁵



C. Operations in the Block 12 area before the Company held the oil assets¹⁷⁶

Operations performed by	Period of performance of the operations	Summary of the operations	Summary of the operation results [including seismic surveys, drilling results, quantities produced and revoked rights]
Noble Cyprus	2009	D3 seismic survey	
Noble Cyprus	2010	The survey was processed and interpreted.	A drilling prospect was identified.
Noble Cyprus	2011	Preparation and implementation of Aphrodite exploration drilling and initial analysis of the results.	A-1 Aphrodite prospect drilling, initial analysis of the results and announcement of a natural gas discovery.

¹⁷⁵ The map describes the license area defined in the production sharing contract. The actual license area was reduced by 25% upon extension of the license and is 3,400 sq km.

¹⁷⁶ Note that the operations described below are those carried out by Noble Cyprus, based on the parent company's reports.

D. Compliance with the terms of the work plan in Block 12

To the best of the Company's knowledge, as informed by Noble Cyprus, the work plan was fully met up to the report date.

E. Future binding work plan under the terms of the production sharing contract in Block 12

Period	Description of the updated work plan defined for the period	Estimated work plan budget (USD thousands) (divided into the main items)	The Company's effective share of the total budget (USD thousands) (divided into the main items)
2012-2013	To the best of the Company's knowledge, at the date of the report, there is no binding work plan for this period.	-	-

F. Actual and planned work plan for Block 12

The table below includes a summary of the main operations actually performed in the oil asset since January 1, 2009 through to the date of the report and a summary of the operations planned by Noble Cyprus:

Period	Summary of the operations performed in the period / summary of the planned work plan	Actual total cost/estimated total budget for operations on the level of the oil asset (USD thousands) ¹⁷⁷	The Company's effective share in the cost/budget (USD thousands)
2010	The survey was processed and interpreted.	4,667	75
2010	The survey was processed and interpreted.	Approximately 1,667	271
2011	D2 seismic survey On September 8, 2011, exploration drilling began at A-1 ("Aphrodite"). After 73 days, it reached a final depth of 5,860 meters. On March 5, 2012, after the operator informed the partnerships that, in its opinion, the quantity of natural gas discovered at the A-1 drilling site justifies an analysis and evaluation of the overall quantities of natural gas in the reservoir, and an analysis and evaluation of the quantities of natural gas that can be produced commercially, the partnerships announced a natural gas discovery at A-1 well.	1,333 99,920	222 16,655
2012 onwards	Continuation of processing and reviewing the drilling results, based on which an appraisal plan will be determined, including drilling/appraisal, if required, and examination of the development plan, subject to further extension of the license period.	50,000-70,000	8,705-12,187

¹⁷⁷ The amounts for 2009-2011 are amounts that have actually been expended and are audited in the financial statements. It is noted that the estimated budget for operations in 2012 is the Company's estimate, and the Company did not receive an estimate from Noble Cyprus, other than as aforesaid.

G. Disclosure of the effective participation rate in the expenses and revenues in Block 12

Participation rate	Percentage before return on investment	Percentage after return on investment	Rate grossed up to 100% before return on investment	Rate grossed up to 100% after return on investment	Explanations
Effective share of oil asset attributable to equity holders of the Company	16.738%	16.738%	100%	100%	The Company's holdings in the oil asset are expected to be indirect through its holdings in the participation units of the partnerships.
Effective share of oil asset revenues attributable to equity holders of the Company ¹⁷⁸	16.64%	17.07%	99.39%	102.01%	The information is before deduction of the share of the Republic of Cyprus under the provisions of the PSC applicable to Block 12 and after payment of royalties to related parties. For information of the Republic of Cyprus' share, see section 1.11.10.H below.
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	16.91%	17.41%	101%	104%	See the calculation in section 1.11.10.I below.

¹⁷⁸ The Company notes that the disclosure in this section is not according to the full format required under the disclosure guidelines. It cannot fully disclose as required in the guidelines, due to restrictions connected to the process of transferring the Cyprus rights from Noble to the partnerships. Under these circumstances, including: (a) uncertainty concerning the Republic of Cyprus' share in the gas produced, if any, as described in section 1.11.10.H below; (b) the partnerships' share of the potential natural gas resources in Block 12 according to the NSAI report described in section 1.11.10(K) below compared to the their entire gas reserve; (c) the Company's estimate, based on information in its possession as at the report date (before further operations were performed at Block 12), that development of the Dolphin reservoir will begin before that of Block 12, if at all (information which affects the current value of Block 12 of the partnerships' entire natural gas reserve); given all of these versus the concern that providing disclosure as required in the guideline may harm the process of transferring the rights in Block 12, the partnership discloses in the format set out in this section 1.11.10.

H. Calculation of the effective share of the oil asset attributable to equity holders of the Company, if gas or oil is discovered in Block 12.

Description	% Up to return on investment	After return on investment	Summary of the calculation method for royalties or payments (including deduction of expenses and others) (with reference to the agreement)
Theoretical annual revenues of the oil asset after the discovery (%)	100%	100%	
Royalties or payment (derived from revenues after the discovery) related to the oil asset *:			
The State			For information of the Republic of Cyprus' share, see below the table.
	=====	=====	
Adjusted revenues on the level of the oil asset	100%	100%	
Share of the adjusted oil asset revenues attributable to the equity holders of the Company	16.738%	16.738%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company).	16.74%	16.74%	
Royalties or payments (derived from revenues after discovery) in connection with the oil asset at the level of the Company			
On the level of the Company			
Share of the equity holders of the Company in the payment to another service provider that collects payment at the level of the Company.	-	-	
Share of the equity holders of the Company in the payment to the general partner/another service provider that collects payment at the level of the Company.	0.73%	1.64%	In Delek Drilling Partnership – overriding royalties at a rate of 3% up to ROI and 13% after ROI, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state. In Avner Partnership – overriding royalties at a rate of 6%, paid to the owners of the royalty, less wellhead expenses at the rate used to calculate royalties to the state.
	=====	=====	
Total	0.73%	1.64%	
Share of the equity holders of the Company in revenues due to additional royalties from the asset	0.628%	1.979%	Overriding royalties of 3% up to ROI and 13% after ROI and overriding royalties of 6% were calculated at the wellhead price according to the 2011 calculation for the Yam Tethys project.
Effective share of oil asset revenues attributable to equity holders of the Company	16.64%	17.07%	

To the best of the Company's knowledge, based on publications and the model version of the PSC published by the Cypriot government, the average share of the Republic of Cyprus in the natural gas produced, if any (depending, inter alia, on the daily production rate of the reservoir,

the production costs, including the scope of recognized costs, and other factors), which affect the Company's effective share of the natural gas produced is within the accepted range in other countries that adopted the model PSC (for deepwater exploration) and according to an evaluation conducted for the Company, fluctuates between 30%-70% of the gas produced.

It is noted that unlike royalties in Israel, regulated in accordance with legislation published in the Official Gazette, in Cyprus, payments to the authorities are regulated in production sharing contracts with the government of Cyprus. This information is not available to the public. In this context, it is noted that according to the model PSC published by the government of Cyprus on the website of the Ministry of Commerce, Industry and Tourism in Cyprus,¹⁷⁹ which to the best of the Partnership's knowledge is substantially the same as the PSC, the authorities in Cyprus have a share in the income generated for the concessionaire (after deducting expenses using the mechanism set out in the PSC), which is gradual and according to which: (1) for crude oil, this is based on average daily oil production (barrels per day) and the oil price per barrel; (2) for gas, this is based on average daily production on an annual basis (BCF per day). The share of the authorities in Cyprus in the concessionaire's income includes payment of corporate tax to the authorities in Cyprus.

I. Calculation of the effective participation rate of the Company's equity holders in exploration, development and production expenses in Block 12

Description	%	Summary of the calculation method of royalties or payments (including deduction of expenses and others) (reference to the description of the agreement)
Theoretical expenses of the oil asset after the discovery	100%	
Details of payments (derived from the expenses) at the level of the oil asset		
Operator	4%-1%	
Effective rate of expense at the level of the oil asset	104%-101%	
Share of the equity holders of the Company in the oil asset's expenses (linked)	16.74%	
Share of the equity holders of the Company in the effective rate of revenues, at the level of the oil asset (before other payments at the level of the Company)	16.91%-17.41%	
On the level of the Company		
Payments (derived from the expenses) in respect of the oil asset and at the level of the Company (the following percentages will be calculated in accordance with the share of the equity holders of the Company in the oil asset)		
General partner in Avner		
Effective share of expenses for exploration, development or production of the oil asset, attributable to equity holders of the Company	16.91%-17.41%	

¹⁷⁹ At: <http://www.mcit.gov.cy/mcit/mcit.nsf/All/FE3EB5707ADA0E6EC225771B0035B0D2?OpenDocument>.

J. Royalties and payments paid during exploration, development and production operations in Block 12 (USD thousands)

Description	Total share of equity holders of the Company in investment in the oil asset in this period ¹⁸⁰	Of which, the share of equity holders of the Company in payments to the general partner	Of which, the share of equity holders of the Company in payments to the operator (beyond the direct return of expenses)
Budget actually invested in 2009 (including the payments)	759	-	30
Budget actually invested in 2010 (including the payments)	271	0	11
Budget actually invested in 2011 (including the payments)	16,877	0	675

K. Contingent and prospective resources in Block 12

According to the report prepared by NSAI as set out below, some of the resources in the reservoir included in the Block 12 area ("Aphrodite reservoir") have been proven by drilling and are classified accordingly as contingent resources, while others in fault blocks adjacent to the drilling have not been proven and therefore remain classified as prospective resources.

The NSAI resource report specified below noted several assumptions and qualifications, including: (a) the evaluations were not adjusted to reflect the commercial risk; (b) NSAI did not visit the oil field and did not examine the mechanical operation or condition of the well; (c) NSAI did not investigate the possible exposure arising from environmental issues. However, it noted that, as at the report date, it is unaware of possible liability arising from environmental issues which may materially affect the quantity of resources estimated in the resource report; (d) the resources shown in the report are in an undeveloped location and therefore the appraisal is based on estimated volume of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological characteristics and properties.

1. Contingent resources

A) Quantitative data

According to a report from NSAI, which was prepared in accordance with the principles of the Petroleum Resources Management System (SPE-PRMS), the contingent resources in the Aphrodite reservoir as of December 31, 2012 are classified development pending, as described below:

Target	Probability	Total in the oil asset (gross) BCF	Company's total share (gross) ¹⁸¹ BCF
C Sands	Low estimate	225.5	37.7
	Best estimate	1,150.6	192.6
	High estimate	1,952.1	326.7
1 D Sands	Low estimate	19.6	3.3
	Best estimate	232.8	39.0
	High estimate	467.0	78.2
2 D Sands	Low estimate	243.2	40.7
	Best estimate	344.0	57.6
	High estimate	478.1	80.0

B) According to the report, the contingent resources are subject to approval of the project, including an approved development plan and reasonable expectations for

¹⁸⁰ Including costs for which payments are not made to the operator.

¹⁸¹ Before deduction of the Republic of Cyprus' share under the provisions of the PSC applicable to Block 12 and payment of royalties to related parties.

natural gas sales, the report does not include economic analysis of the gas asset and that based on development of similar reservoirs and there is a reasonable chance that the contingent resources in the best estimate category will be financially viable.

- C) In the future, the operator intends exploring different alternatives for developing the Aphrodite reservoir, including the possibility for integrating its development in the development plans of adjacent fields within Israel's territorial waters, including the Leviathan field. Due to the estimated volume of contingent and prospective natural gas resources in the Aphrodite reservoir and the limited scope of the potential domestic gas market in Cyprus, the primary market for these resources is the international market, subject to future fulfillment of a development plan which includes building infrastructure facilities for the export of natural gas. For information about the gas market in Cyprus, see section 1.11.16.B above and for information about the option of exporting gas, see section 1.11.29.K below.
- D) At this stage, it is not possible to set an estimated schedule for the preparation and/or implementation of a development plan for the Aphrodite reservoir until the prospective resources have been assessed and various plans to commercialize and develop the natural gas in the reservoir have been explored and prepared. It is emphasized that each development option has a different timetable and different construction and operating costs, and until the preferred development option is selected, the timetable and budget for development of the reservoir cannot be reasonably estimated. It is also emphasized that every development plan will naturally require extensive regulatory, commercial and financial arrangements, since a substantial portion of the natural gas resources in the Aphrodite reservoir is designated for export.

Forward-looking information: There is no certainty that it will be commercially possible to produce any percentage of the contingent resources.

2. Prospective resources

A) Quantitative data

According to a report received by the partnerships from NSAI, which was prepared in accordance with the principles of the Petroleum Resources Management System (SPE-PRMS), the prospective resources in the Aphrodite reservoir as of December 31, 2012 are as follows:

Target	Probability	Total in the oil asset (gross) BCF	Company's total share (gross)¹⁸² BCF
A Sands	Low estimate	101.3	17.0
	Best estimate	794.6	133.0
	High estimate	2,210.0	369.9
C Sands	Low estimate	686.6	114.9
	Best estimate	1,944.9	325.5
	High estimate	3,731.8	624.6
1 D Sands	Low estimate	99.0	16.6
	Best estimate	383.8	64.2
	High estimate	869.7	145.6
2 D Sands	Low estimate	29.1	4.9
	Best estimate	322.9	54.0
	High estimate	465.1	77.8

¹⁸² Before deduction of the Republic of Cyprus' share under the provisions of the PSC applicable to Block 12 and payment of royalties to related parties.

- B) The report was based on the results of a 3D seismic survey by Petroleum Geo-Services whose processing was completed in 2010 ("the 3D survey").
- C) Basic parameters used to calculate the difference scenarios:

Target	Area (acres)			Gross thickness (feet)			Gross rock volume (acre*feet)		
	High	Best	Low	High	Best	Low	High	Best	Low
A Sands	29,252	24,168	16,250	87	69	27	2,556,533	1,657,456	435,078
C Sands	17,306	12,464	7,678	274	253	188	4,744,578	3,154,862	1,445,248
1D Sands	9,329	6,854	3,485	166	137	99	1,545,632	937,305	343,620
2 D Sands	4,544	2,830	1,061	133	189	59	602,909	534,965	62,483

Target	Gas saturation (decimal)			Porosity (decimal)			Net-to-gross (decimal)		
	High	Best	Low	High	Best	Low	High	Best	Low
A Sands	0.70	0.60	0.50	0.24	0.22	0.19	0.45	0.35	0.25
C Sands	0.69	0.68	0.64	0.22	0.21	0.21	0.46	0.40	0.36
1D Sand	0.68	0.67	0.59	0.22	0.21	0.21	0.33	0.27	0.24
Sand 2D	0.69	0.68	0.64	0.22	0.22	0.21	0.44	0.38	0.34

Target	Gas recovery factor (decimal)			Gas formation volume factor (SCF/RCF)		
	High	Best	Low	High	Best	Low
A Sands	0.70	0.65	0.60	375	375	375
C Sands	0.70	0.65	0.60	378	378	378
1D Sands	0.70	0.65	0.60	378	378	378
2D Sands	0.70	0.65	0.60	379	379	379

- D) Material risks (relates to pre-drilling data) in continuation of the process: At this stage of operations at Block 12 the material risks are geological and in continuation of the process, they are technical operating risks. Risk of faults in the drilling operations, electric logging and production tests, if any. In the event of fault-free technical operating operations, the risks in continuation of the process required to reach a commercial discovery are, inter alia, insufficient permeability of the reservoir sands to allow delivery or delivery in commercially significant quantities, seepage of water into the well which prevents economic production, discovery development costs, etc. For a list of the risk factors of exploration operations, see section 1.11.33.I below.
- E) The estimated probability of success of each of the risk factors in the well and the estimated statistical geological probability of discovering natural gas in the fault blocks where the prospective resources are located are as follows:

Target	Trap integrity	Reservoir quality	Source evaluation	Timing / migration	Total
A Sands	95	60	95	100	54
C Sands	98	85	95	100	79
D1 Sands	98	90	97	100	86
D2 Sands	98	95	98	100	91

- F) Estimated probability of development for commercial production: For information, see subsection (b)-(d) above.
- G) The partnerships' reasons for the basic parameters used to calculate the scenarios: The parameters used to calculate the different estimates are based primarily on the Aphrodite drilling results, the results of the 3D seismic survey and general knowledge concerning targets and similar reservoirs.

There is no certainty that any part of these potential resources will indeed be discovered, and if they are discovered, there is no certainty that it will be possible from the commercial perspective to produce any part of the resources. The prospective information does not lie within the bounds of an evaluation in respect of the contingent reserves and resources, which can only be evaluated after exploration drilling, if at all.

Forward-looking information: The estimates of NSAI in respect of the contingent and prospective resources in the Aphrodite reservoir are forward-looking information as defined in the Securities Law. These estimates are partially based on geological, geophysical and other information received from the operator from the well and from the drilling at adjacent reservoirs, and are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. Actual quantities of natural gas produced (if any) may differ from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production, including due to continued analysis of the findings of the drilling.

- H) The Company declares that all of the above information has been prepared in compliance with the Petroleum Resources Management System (SPE-PRMS).
- I) Opinion of the assessor

The report of the contingent and prospective resources prepared by NSAI as of December 31, 2012 is attached to this report as a reference to the contingent and prospective resources report attached as Appendix I to the periodic report of Delek Drilling Partnership for 2011, which was published on March 29, 2012 (ref. no. 2012-01-084516). Also attached is the assessor's consent to include it in this report.

1.11.11 Discontinued operations

A. Discontinued operations in Israel

Following discussions with the Petroleum Commissioner regarding a number of licenses held by the partnerships and Noble, and in light of the partnerships intention to focus their exploration activities in certain license areas, the partnerships and Noble reached an arrangement with the Petroleum Commissioner on October 26, 2010, whereby they relinquish their rights in the Ruth E, Ruth F and Zurim licenses¹⁸³ and also signed agreements to transfer their rights in a number of other licenses as described below:

Accordingly, on January 9, 2011, an application was made to the Petroleum commissioner, in accordance with section 76 of the Petroleum Law, for approval of the transfer of part of their rights in the 361/Ruth D, 368/Alon E (in this section: "the Ruth and Alon licenses"), 337/Avia and 338/Keren licenses (in this section: the Avia and Keren licenses), so that the total rights of the partnerships will not exceed 25% (12.5% each) and Noble's total rights will not exceed 25%.

On November 29, 2011, the commissioner announced that the Ruth, Alon, Avia and Keren licenses would not be extended, as set out in sections 1.11.29.L and 1.11.20.M below.

Further to the aforesaid, on January 30, 2012, the partnerships appealed the commissioner's decision concerning the Avia and Keren licenses to the Minister of Energy and Water.

1. The partnerships and Noble also asked the Petroleum Council to approve their continued possession of the 360/Ruth C license¹⁸⁴, as an additional license in addition to the 12 licenses, as well as license areas exceeding four hundred thousand (400,000) hectares, in accordance with the provisions of section 17 of the Petroleum Law. As of the report date, a decision has not yet been handed down in this matter.

¹⁸³ It is explicitly stated that Noble had no rights in the Zurim license.

¹⁸⁴ Until December 31, 2011, USD 2,415 thousand have been invested in the Ruth C license (calculated on the basis of the cumulative investment in Ruth A, B, C and D licenses up to December 31, 2012 of USD 9.66 million and the area of the Ruth C license (400 sq km) compared to the total areas of the Ruth A, B, C and D licenses (1,600 sq km)). These amounts were recorded as an expense in the statement of income.

2. The following table summarizes oil assets returned, transferred or expired during 2009-2011:

Name of asset	Expiry date of rights	Reason for expiry
344/Med Ashdod 2 license	July 13, 2009	The Petroleum Commissioner cancelled the license as no agreement was signed for drilling during the license period.
349/Hof license	February 21, 2010	The Petroleum Commissioner cancelled the license as no drilling operations were carried out during the license period.
327/Zurim Halamish Enclave license	December 31, 2010	The partnerships relinquished all their rights to the enclave, as there were no prospects worthy of drilling.
331/Ohad License	June 30, 2010	The license expired, as there were no prospects worthy of drilling.
321/Zerach license – Tzuk Tamrur enclave.	December 31, 2010	The partners to the license contend that they have made a "discovery" within the license area, as defined by the Petroleum Law, and are therefore entitled to receive a license for the area, in contradiction to the commissioner's position. In view of the foregoing, the Petroleum Commissioner announced that the license will expire on December 31, 2010. In view of the aforesaid, the partnerships have appealed the Commissioner's decision to the Minister of Energy and Water. On September 27, 2011, the Minister of Energy and Water notified the license partners that after examining the appeal and professional positions, he decided to dismiss the appeal. The partnerships are considering their steps following the decision. It is noted that to the best of the Company's knowledge, on November 20, 2011, Zerach Oil and Gas Explorations Ltd. Partnership petitioned the High Court of Justice to cancel the Minister of Energy and Water's decision to dismiss the appeal which it filed concerning the license.
361/Ruth D license	February 29, 2012	Expired For additional details, see section 1.11.29.L below.
363/Ruth F license	February 29, 2012	The partnerships relinquished all their rights in the license, as there were no prospects worthy of drilling.
362/Ruth E license	February 29, 2012	The partnerships relinquished all their rights in the license, as there were no prospects worthy of drilling.
368/Alon E license	March 1, 2012	Expired For additional details, see section 1.11.29.L below.
338/Keren license 337/Avia license	March 31, 2012 December 31, 2011	Not yet expired Expired For additional details, see section 1.11.29.M below.

B. Discontinued operations abroad

1. Participation rights in oil assets in the USA

In 2011, Delek Energy Systems US Inc. ("Delek US"), a subsidiary of Delek Energy, signed four agreements for the sale of all of its oil assets in the USA as follows:

- A) On February 14, 2011, a transaction was signed and completed for the sale of part of the oil and gas assets of Delek US, located in Texas ("the sold assets") for USD 11 million in cash. According to the agreement, as from January 1, 2011, the operational results of the sold assets were transferred to the purchasing company.
- B) On February 15, 2011, an agreement was signed for the sale of an additional part of the oil and gas assets of Delek US ("the agreement"). According to the agreement, as from January 1, 2011, the sold assets and the operational results of these sold assets were transferred to the purchasing company. The transaction was completed on March 25, 2011. Delek US was paid USD 31.3 million in consideration for the sale of these assets.
- C) On May 10, 2011, an agreement was signed for the sale of a significant part of the oil and gas assets in the USA of the subsidiary Delek US (in this section: "the agreement"). According to the agreement, as of January 1, 2011, the operational results of the sold assets were transferred to the purchasing company in consideration for USD 120 million (of which USD 95 million was used to repay a loan used to acquire the assets). The transaction was completed on June 9, 2011.
- D) On August 2, 2011 and September 9, 2011, Delek US completed the transaction for the sale of the remaining oil and gas assets in the US in consideration of USD 3.9 million.
- E) The profit from the above transactions amounted to NIS 71.7 million.

2. Vietnam project

- A) Until its sale in July 2009, Delek Vietnam was a wholly owned subsidiary of Delek Energy, and held participation rights of 25% in the exploration project in Block W12 in Vietnam (in this section: "the project").
- B) On July 20, 2009, Delek Energy sold its entire holdings in Delek Vietnam to Premier Oil Group ("Premier"), the parent company of Premier, which is the project operator and one of the partners ("the sale agreement"). Delek Energy received an immediate payment of USD 83.9 million in cash for the sale of Delek Vietnam. In addition to this amount, and subject to the terms set out in the agreement, Premier has undertaken the following contingent payments:

To pay Delek Energy USD 3 million one year after the start of commercial production from the Dua field, if and when there is one.

To pay Delek Energy USD 7 million one year after the start of commercial production from any other field in Block 12W (except for the Chim Sao and Dua fields), if and when there is one.

- C) According to Premier's reports – (1) The Chim Sao field development is complete and production started in October 2011; (2) Premier is continuing to formulate the development plan for the Dua field, including connecting it to the production system at the Chim Sao field. The feed works (design and engineering) of the development plan for the Dua field was completed in May 2011.

3. Rights to oil production in Guinea-Bissau

- A) At the beginning of 2007 Delek Energy International acquired from Premier Oil West Africa B.V., a subsidiary of Premier Oil ("Premier Africa"), 11.43% of the rights in two offshore concessions in Guinea-Bissau in West Africa: the Esperanca concession (Blocks A4 and A5) and the Sinapa concession (Block 2) (in this section: "the concessions"). In 2007, two drillings were carried out within the areas of the concessions, and they were subsequently sealed and abandoned, following which Delek International's project partners decided to relinquish their rights in the licenses.
- B) In view of Delek Energy's policy to concentrate its resources in its core assets in Israel, on December 18, 2009, Delek Energy International signed an agreement with First Australian Resources Ltd. for the transfer of its rights in the concessions. In

consideration for its holdings, Delek Energy International received USD 570 thousand from the buyer to cover its 2009 expenses. In addition, Delek will be entitled to receive repayment amounting to USD 13 million for its past expenses in the concessions, to be paid from the net profits of the buyer, whatever they may be, according to the repayment schedule stipulated in the agreement. It is noted that no commercially-viable discovery has been declared in the concession's areas to date, so there is no certainty that the buyer will derive any profits from the project.

- C) To the best of Delek Energy's knowledge, since the sale of its rights, the concession partners have conducted a 3D seismic survey over an area of about 1,600 sq km and the concessions were extended until 2012.

4. Viking Oil and Gas International Ltd. ("Vogil")

In 2007-2008, Delek Energy International invested USD 19.5 million in Vogil, a private company registered in the Virgin Islands, in exchange for 25% of Vogil's shares. As aforesaid, Vogil has a number of interested parties, which are private investors. Vogil is a holding company that does not retain employees. Due to Vogil's business results, its operations were discontinued in 2009. In 2011, Delek Energy repaid its full debt of USD 8 million for the guarantee provided for Vogil.

1.11.12 Products and Services

A. Israel

In the reporting period, the partnerships supplied natural gas from the Mari B reservoir to the customers listed in section 1.11.13 below:

Furthermore, in the first quarter of 2012, the partnerships signed several agreements for the supply of natural gas from the Tamar reservoir, which is expected to start commercial production in the first half of 2013. As at the reporting date, the partnerships are negotiating with other customers for the sale of natural gas.

B. USA

In the United States, oil and natural gas are commodities. The US market is large and sophisticated with a wide range of customers. Until the sale date of all the oil assets held by Delek Energy in the US (through its subsidiary), it supplied natural gas and fuel to various customers in the US.

- C. As gas and/or fuel is found in the exploration operations of Delek Energy (through its subsidiaries) and/or the limited partnerships, Delek Energy will act to sell them.

1.11.13 Customers

A. Customers in Israel

1. As at the reporting date, the limited partnerships, together with the other partners in the Yam Tethys project, signed agreements to supply natural gas with Israel Electric Corporation ("IEC"), Paz Ashdod Refineries Ltd ("Paz Ashdod Refineries") and Hadera Paper Ltd. ("Hadera Paper"), Delek Ashkelon, subsidiaries of Israel Chemicals Group Ltd. ("ICL Group") and ORL totalling 30.1 BCM.
2. Furthermore, in 2010-2011, the partners in the Yam Tethys project also supplied natural gas to other customers on an occasional basis, especially Nesher Commerce (Cement Marketing) Ltd. and Makhteshim Agan Ltd. At December 31, 2011, 21.93 BCM have been supplied. Revenues of the partnerships from IEC accounted for 79% of all its revenues in 2011, 87% in 2010 and 91% in 2009.
3. Delek Energy and the partnerships are dependent upon IEC, since cancellation or termination of the contract with it would materially impact Delek Energy's operations and profitability. For further information of the partnerships' agreements with IEC, see sections 1.11.13.D(1), 1.11.13.D(2) and 1.11.13.E(1) below.
4. Moreover, in the first quarter of 2012, the partnerships signed several contracts for the supply of natural gas (with IEC, Dalia Power Energies Ltd. ("Dalia"), Ramat Negev Energy Ltd. ("Negev Energy"), Ashdod Energy Ltd. ("Ashdod Energy"), Hadera Paper and Mashav Initiating and Development Ltd. ("Mashav") from the Tamar reservoir which is expected to start commercial production in the first half of 2013, totalling 133.5 BCM.

5. Other potential customers of the partnerships in Israel are significant industrial customers and private power stations. In the event of gas export (whether by pipeline or as LNG), the partnerships' customers may include consumers in the target markets and/or gas marketing companies which purchase the gas either in gas or liquid (LNG) state.

B. Customers in the United States

In 2011, Delek Energy sold oil and natural gas to many customers in the USA.

No single customer in the USA accounted for 10% or more of Delek Energy's total revenues.

C. Contracts with customers for the supply of natural gas in Israel

Long-term agreements which the partnerships have signed for the sale of natural gas¹⁸⁵:

¹⁸⁵

For further information of these agreements, see the reference following the table.

Customer name	Signed on	Agreement expiry date	Total maximum supply quantity under the agreement (BCM)	Quantity supplied until December 31, 2011 (BCM)	Financial value of agreement (as estimated on the contract date)
Agreement for the sale of natural gas from the Yam Tethys project					
IEC	June 25, 2002	July 1, 2014 (or until supply of the total contract quantity)	18	15.81	USD 1.5 billion (100%)
IEC (letter of intent)	July 2, 2009	December 31, 2014	5	3.54	USD 1 billion (100%)
Paz Ashdod Refinery	September 3, 2004	November 28, 2015 or until the total contract quantity is supplied.	1.3	0.66	USD 120 million (100%)
Delek Ashkelon	July 1, 2005	July 1, 2022	2	0.51	USD 160 million (100%)
Hadera Paper	July 29, 2005	June 30, 2011	0.4	0.3	USD 40 million (100%)
Hadera Paper (continuation agreement)	May 15, 2011	June 30, 2013, with rights for extension until total contract quantity is consumed.	0.2	0.03	USD 63 million (100%)
ICL Group	March 25, 2008	September 1, 2014, with rights for extension until total contract quantity is consumed.	2	0.4	USD 260-330 million (100%)
ORL	May 20, 2011	August 31, 2013, with rights for extension until total contract quantity is consumed.	1.2	0.26	USD 350 million (100%)
Agreement to sell natural gas from the Tamar project					
Dalia Power Energies Ltd.	January 8, 2012	As specified in section 1.11.13.E(4) below.	23.28	-	USD 5 billion (100%)
Ramat Negev Energy Ltd.	January 9, 2012	As specified in section 1.11.13.E(5) below.	3.7	-	USD 800 million (100%)
Ashdod Energy Ltd.	January 9, 2012	As specified in section 1.11.13.E(6) below.	1.95	-	USD 400 million (100%)
Hadera Paper (additional agreement)	January 25, 2012	As specified in section 1.11.13.E(2) below.	3.3	-	USD 750 million (100%)
Mashav Initiating and Development Ltd.	February 9, 2012	As specified in section 1.11.13.E(3) below.	2.31	-	USD 680 million (100%)
IEC	March 14, 2012	As specified in section 1.11.13.E(1) below.	78-99	-	Between USD 14-23 billion (100%)

D. Agreements for the sale of natural gas in the Yam Tethys project

1. Agreement to sell natural gas to IEC

- A) On June 25, 2002, the Yam Tethys project partners (in this section: "the sellers") and Israel Electric Corporation (in this section: "the buyer") signed an agreement for delivery of natural gas to IEC.
- B) The agreement is valid through July 1, 2014 or by such date as the sellers have delivered to the buyer a cumulative gas volume equal to 18 BCM (in this section: ("the total contracted volume")), whichever is earlier.

The buyer or the sellers may terminate the agreement should the other party (and for the sellers, any of them) take any bankruptcy action (as defined in the agreement) which is likely to have an adverse effect on the discharge of their obligations pursuant to the agreement, by giving at last 30 days' written notice. The buyer and the sellers agreed not to exercise any right they may have to lawfully terminate the agreement other than in connection with significant or continued breach of material provisions of the agreement, and only after granting a 90-day period to the party in breach to remedy such breach (unless a shorter period is stipulated in the agreement).

- C) Without derogating from the sellers' obligations under the agreement with regard to maintaining reserves, the sellers would not be limited to any sources of natural gas (either from Israel or imported) which they supply to the buyer under the agreement.
- D) The sellers will ensure that at any time during the term of the agreement they shall have available remaining reserves in reservoirs amounting to 130% of the remaining total contract quantity ("the remaining TCQ") (the remaining TCQ after deduction of quantities of gas delivered by the sellers under the agreement). The agreement sets forth instructions for reporting on and supervision of the remaining reserves and for adjustment of certain provisions in the agreement should the sellers fail to maintain sufficient reserves as required. At the date of the report, the sellers are in compliance with the requirements of the reserve balances¹⁸⁶.
- E) The agreement stipulates the annual contracted volume of gas, which changes over the term of the agreement depending, inter alia, on the pace of completion of the transmission system and its connection to IEC power stations for delivery of gas to the stations (in this section: "the annual contract volume").
- F) According to the agreement, gas is supplied on an hourly basis with a minimum and maximum volume per hour, according to procedures and mechanisms set forth in the agreement.
- G) Gas is delivered to the connection point at the INGL pipeline near the permanent receiving terminal on Ashdod shore.
- H) Minimum bill quantity: The agreement specifies the annual minimum bill quantity, at 80% of the annual contracted volume (subject to adjustments) for which the buyer has committed to pay even if it does not consume that volume, subject to provisions of the agreement, ("the minimum bill quantity") as well as instructions for the calculation and adjustments of the minimum bill quantity, including due to force majeure or failure to supply by the sellers. The agreement also specifies a mechanism for the accumulation of excess volume consumed by the buyer in the course of any year, and its use to reduce IEC's undertaking to purchase a minimum quantity, as set forth above, in subsequent years. Furthermore, the agreement specifies provisions and mechanisms allowing IEC to receive gas at no additional charge up to the volume paid for, on account of gas not consumed due to activation of the minimum bill quantity.
- I) At the signing date, the partnerships estimated that the total net receipts (net of royalties to the State and third parties, including interested parties, before tax) from the agreements will be USD 330 million.

¹⁸⁶ The order backlog is based on the minimal gas quantities in the agreements with customers which they undertook to take or pay. According to the partnership, due to the decrease in natural gas supply capacity from the Mari B reservoir, it will not be able to supply the foregoing quantities, but will be able to supply the quantities in the discounted cash flow set out above.

Forward-looking information: The aforementioned estimate by Delek Energy is forward-looking information as defined in the Securities Law, based on the estimates of the limited partnerships' general partners of future gas consumption by IEC. The estimate may not materialize should actual gas consumption by IEC be different than these projections.

- J) Price of gas: The contracted price for the gas is denominated in USD per energy unit (BTU) and is linked to a basket of fuels and to the US Producer Price Index according to the mechanism in the agreement, including minimum and maximum prices. In view of the hedging agreements of the partnerships, after signing the agreement with IEC, the partnerships effectively set the price for gas volumes to be sold at USD 2.47 per million BTU.
- K) Gas quality: According to the agreement, delivery of natural gas will comply with specifications set out in the agreement and according to requirements of the transmission company as approved by the relevant authorities from time to time. The buyer has the right to refuse to receive non-compliant gas until such non-compliance is remedied. All disputes between the parties with regard to gas quality may be submitted to an expert for resolution at the request of any of the parties.
- L) Breach and damages: According to the agreement, should the Sellers fail to supply, at any time, the gas volume ordered by the buyer under the agreement, and should the non-supply exceed the deviation allowed by the agreement, the sellers will compensate the buyer in the subsequent month by selling gas at a discounted price up to the volume of gas not supplied in breach of provisions of the contract. Furthermore, the agreement lists specific breaches by any party for which damages are payable at high rates (including financial compensation). The agreement also sets limits to liability of each party for breach of some of the agreement provisions at amounts specified in the agreement.
- M) Collateral and guarantees: The agreement establishes collateral to be provided and maintained by each of the sellers in favor of the buyer, to guarantee the sellers' obligations under the contract, all at dates, terms and amounts set out in the agreement. Delek Energy's share in the collateral is through a guarantee of USD 30 million, provided to IEC by the Company.
- N) Relationships between the sellers and the sellers' coordinator: The sellers operate jointly on issues such as development of the reservoir, the sellers' facilities and gas production, delivery and supply according to the agreement. Concurrently, the buyer declares that none of the provisions in the agreement will be considered as creating mutual liability among the sellers, and each seller is individually liable to the buyer for its share in the oil rights and in connection with any liability arising from the agreement. Although the buyer may order gas volumes by a single notice to the sellers' coordinator, the volume considered ordered from each of the sellers will be the portion of each of the sellers out of the total volume ordered.
- O) Addendum to the agreement: On August 15, 2006, the sellers signed an addendum to the agreement for the supply of additional quantities of natural gas (in this section: ("the addendum to the agreement")). Pursuant to the addendum to the agreement, the sellers granted IEC an option to purchase additional volumes of natural gas, primarily in response to IEC's gas supply requirements during peak consumption hours. This option referred to additional volumes of gas purchased after June 2006. The validity of the addendum was extended from time to time to March 31, 2009 but in practice the parties acted according to the terms of the addendum to the agreement until June 30, 2009. The purchase price for gas under the terms of the addendum to the agreement is significantly higher than the price at which IEC purchases natural gas under the 2002 agreement, due to the different mechanism according to which the gas price is set and due to an increase in global fuel prices.

2. Letter of intent with IEC

In June 2009, the Yam Tethys project partners and IEC signed a binding letter of intent for the supply of an additional quantity of 1 BCM of natural gas per year for five years (a total of 5 BCM).

At the signing date of the letter of intent, the financial value of the agreement (for 100% of the rights) was estimated at USD 1 billion.

Forward-looking information: The foregoing estimate by Delek Energy is forward-looking information, based on the estimates of the limited partnerships' general partners of future gas consumption by IEC. The estimate may not materialize should actual gas consumption by IEC be different than these projections.

For information of the agreement signed with IEC for the sale of gas by the partnerships and the other partners in the Tamar project, see section 1.11.13.E(1) below.

3. Agreement for the sale of natural gas to Paz Ashdod Refinery¹⁸⁷

- A) On September 3, 2004 an agreement was signed between the Yam Tethys project partners and Paz Ashdod Refinery for the supply of gas to the oil refinery in Ashdod.
- B) The total contract quantity that Yam Tethys group is required to supply to Paz Ashdod Refinery is 1.3 BCM.
- C) The term of the contract is ten years from the end of the trial period specified in the contract, or until Paz Ashdod Refinery consumes the total contract quantity, whichever is earlier.
- D) Paz Ashdod Refinery has a take or pay agreement for a minimum annual quantity of gas according to a mechanism set out in the agreement.
- E) At the signing date of the letter of intent, the financial value of the agreement (for all Yam Tethys project partners) is estimated at USD 120 million.

Forward-looking information: The aforementioned estimate by Delek Energy is forward-looking information as defined in the Securities Law, based on the estimates of the limited partnerships' general partner of future gas consumption by Paz Ashdod Refinery. The estimate may not materialize should actual gas consumption by Paz Ashdod Refinery be different from the aforementioned projections.

- F) Gas supply to Paz Ashdod Refinery started in November 2005.

4. Agreement for the sale of natural gas to Delek Ashkelon

- A) In August 2005, an agreement was signed and approved between Yam Tethys project partners and Delek Ashkelon Ltd., a company controlled by Delek Group, for the supply of gas to Delek Ashkelon's power station adjacent to the desalination plant in Ashkelon ("the 2005 agreement").
- B) Gas supply under the agreement will commence when natural gas is delivered to Delek Ashkelon's power station, subject to terms set forth in the agreement, and will end after 15 years from the end of the run-in period of the power station, or on June 30, 2022.
- C) The annual gas volume to be purchased by Delek Ashkelon is 0.12 BCM.
- D) At the signing date of the 2005 agreement, the total financial value of the agreement (for all Yam Tethys project partners) is estimated at USD 160 million.

Forward-looking information: The aforementioned estimate by Delek Energy is forward-looking information as defined in the Securities Law, based on the estimates of the limited partnerships' general partner of future gas consumption by Delek Ashkelon. The estimate may not materialize should actual gas consumption by Delek Ashkelon differ from these projections.

- E) Gas supply to Delek Ashkelon started in August 2007.
- F) Delek Ashkelon has a take or pay agreement for a minimum annual quantity of gas according to a mechanism set out in the agreement.
- G) On May 16, 2011 an agreement was signed between Delek Ashkelon and the Yam Tethys project partners for the supply of natural gas on an occasional basis ("the spot agreement") for additional volumes supplied as from January 1, 2011 through May 31, 2012. The spot agreement includes general terms for the supply of additional volumes of natural gas, on an occasional basis, beyond those set in the 2005 agreement, and it replaces the addendum to the agreement of 2009 signed between the parties.

¹⁸⁷ The quantities supplied to Paz Ashdod Refinery under the agreement in 2010 and 2011 are 0.15 BCM per year.

- H) The spot agreement is at new prices which are substantially higher than those fixed in the 2005 agreement, as agreed in commercial negotiations between Delek Ashkelon and the Yam Tethys project operator. The agreement does not include an undertaking for supply and/or purchase of natural gas except under the terms applicable to the foregoing supply (if any) and therefore the volumes actually supplied and the total financial value of the transaction are unknown and depend, inter alia, on a range of factors, especially the natural gas volume which will actually be supplied to Delek Ashkelon. Therefore, Delek Energy cannot estimate the total financial value of the agreement.

5. Agreement for the sale of natural gas in the Yam Tethys project to Hadera Paper

- A) On July 29, 2005, an agreement was signed between the Yam Tethys project partners and Hadera Paper for the supply of natural gas to Hadera Paper ("the original agreement"). Gas supply under the agreement commenced in August 2007 upon completion of the pipeline and required facilities, and will terminate on the earlier of five years from commencement of gas flow or upon the purchase of 0.43 BCM, but no later than July 1, 2011.
- B) At the signing date of the original agreement, the total financial value of the agreement (for all Yam Tethys group partners) is estimated at USD 40 million.
- C) On May 15, 2011, the parties signed a continuation agreement under which the agreement period will be extended for a further two years, that is, through June 2013 ("the continuation agreement"). The agreement is for the supply of a total volume of 0.21 BCM natural gas and includes the right of each of the parties to extend the agreement period until the full quantity is consumed if the total quantity has not been consumed by the end of the agreement. The gas price formula specified in the agreement is based on the oil price (Brent per barrel) with a discount component, including a minimum gas price, without any maximum price.
- D) On January 25, 2012, the parties signed an amendment to the continuation agreement, inter alia, extending the agreement period by another month, that is, until July 2013. On the foregoing date, the continuation agreement will expire, even if the full overall volume has not been consumed.
- E) At the signing date of the continuation agreement, the total financial value of the agreement (for all Yam Tethys group partners) is estimated at USD 63 million.

Forward-looking information: The aforementioned estimate by Delek Energy is forward-looking information as defined in the Securities Law, based on the estimates of the limited partnerships' general partner of future gas consumption by Hadera Paper. The estimate may not materialize should actual gas consumption by Hadera Paper be different than these projections.

6. Agreement with ICL Group

- A) On March 25, 2008, the Yam Tethys project partners signed an agreement with a wholly owned subsidiary of ICL Chemicals Ltd. ("ICL"), guaranteed by ICL, for the sale of natural gas to ICL Group.
- B) ICL Group undertook to purchase a total gas quantity of 2 BCM from the Yam Tethys project partners, subject to the adjustments in the agreement ("the contract gas quantity").
- C) Gas supply commenced in December 2009 and will end at the earlier of: September 2014 (subject to the extension specified below); or purchase of the entire contract gas quantity.
- D) The period set out in subclause (3) will be automatically extended by one addition year, if by the end date the entire contract gas quantity has not been consumed. In addition, Yam Tethys partners have an option to extend the period by an additional two years, until the entire contractual gas quantity has been consumed, as set out in the agreement.
- E) The price of gas is based on the price of fuel oil, with a discount including minimum and maximum prices. ICL Group has a take or pay agreement for a minimum annual volume of gas according to conditions set out in the agreement.

- F) The total financial value of the agreement (for all Yam Tethys group partners) is estimated at USD 260-330 million. Actual revenues will be affected by a number of conditions, primarily the price of fuel oil and rate of gas consumption.

Forward-looking information: The aforementioned estimate by Delek Energy is forward-looking information as defined in the Securities Law, based on the estimates of the limited partnerships' general partner of future gas consumption by ICL Group. The estimate may not materialize should actual gas consumption by ICL Group be different than these projections.

7. Agreement for the sale of natural gas to ORL

- A) On May 20, 2011, an agreement was signed between Yam Tethys project partners (in this section: ("the sellers")) and ORL for the supply of natural gas to ORL and its subsidiaries (in this section: ("the agreement")), the main points of which are as follows:
- B) According to the agreement, ORL undertook to purchase 1 BCM of natural gas ("the contract gas quantity"). All proceeds of the agreement will be paid in installments over a period of 27 months as from June 2011 or over a shorter period if ORL consumes the contract gas quantity earlier. If ORL does not consume the contract gas quantity during this period, the supply period will be extended for a further term according to the conditions prescribed in the agreement.
- C) The gas price specified in the agreement comprises a fixed and variable component determined by a formula based on the oil price (Brent per barrel) with a discount component, and includes a minimum price, without any maximum price.
- D) The total financial value of the agreement is estimated at USD 350 million (according to the calculation made on the date of signing the agreement). The actual financial value of the agreement may change as a result of changes in global crude oil prices and ORL's gas consumption rate.

Forward-looking information: The foregoing estimates of the agreement's total financial value and gas supply period is forward-looking information as defined in the Securities Law, and there is no certainty that the supply dates, agreement period and/or total financial value will be as estimated above, as they depend, inter alia, on a range of factors, including the volume, rate and timing of ORL's natural gas consumption, and oil prices.

E. Agreements for the sale of natural gas in the Tamar project

1. Agreement to sell natural gas to IEC

- A) On March 14, 2012, an agreement was signed between the Tamar project partners (in this section: "the sellers") and IEC for the supply of natural gas (in this section "the supply agreement"), the main points of which are as follows:
- B) The sellers undertook to supply IEC with natural gas for 15 years from the date of completion of the run-in period of the Tamar project ("the commercial delivery start date") or until IEC consumes the total gas volume specified in the agreements, that is, 78 BCM (in this section: ("the total contract volume")), whichever is earlier. IEC is entitled to extend the agreement period by up to two additional years, if by the end of 15 years after gas starts to flow from the Tamar project IEC has not purchased the total contract quantity described above, provided that notice is given no later than 13 years after the commercial delivery start date.
- C) According to the agreement, IEC has an option to increase the total contract quantity to 99 BCM (in this section: ("the option")). The option may be exercised until April 2, 2014, under the terms prescribed in the agreement. If the option is exercised, the sellers will be required to take steps to install additional facilities to allow increasing the supply capacity of the Tamar project gas handling and transport system, subject, inter alia, to receiving the authorizations required by law. The sellers undertake to set up these additional facilities within a period of four years from receiving the foregoing authorizations required.
- D) The buyer or the sellers may terminate the agreement should the other party (and for the sellers, any of them) take any bankruptcy action (as defined in the agreement) which is likely to have a material adverse effect on the discharge of their obligations

pursuant to the agreement, by giving at last 120 days' written notice. The buyer and the sellers agreed not to exercise any right they may have to lawfully terminate the agreement other than in connection with significant or continued breach of material provisions of the agreement, and only after granting a 120-day period to the party in breach to remedy such breach (unless a shorter period is stipulated in the agreement). It was also specified that if the gas flow from the Tamar project does not commence by June 30, 2014 (excluding force majeure events), the buyer may terminate the agreement.

- E) The sellers will not be limited to any sources of natural gas (either from Israel or imported) which they supply to the buyer under the agreement.
- F) The agreement stipulates the annual contract gas volume, which changes over the term of the agreement depending on the option, if exercised (in this section: "the annual contract volume").
- G) According to the agreement, gas is supplied on an hourly basis with a maximum volume per hour, according to procedures and mechanisms set forth in the agreement.
- H) Gas is delivered to the connection point at the INGL pipeline near the permanent receiving terminal on Ashdod shore or any other connection point agreed between the parties.
- I) Minimum bill quantity: The agreement specifies the annual minimum bill quantity for which the buyer has committed to pay even if it does not consume that volume, subject to adjustments provided in the agreement (in this section: (the minimum bill quantity"). The minimum bill quantity is the annual quantity calculated as follows: 3.5 BCM per year for the first five years from the commercial delivery start date and 2.5 BCM per year for the remaining contract period, or 5 BCM per year if the buyer exercises the option (subject to adjustments based on the gas sales of the Tamar project partners and the electricity production of IEC). The agreement includes instructions for the calculation and adjustments of the minimum bill quantity, including due to force majeure or failure to supply by the sellers. The agreement also specifies a mechanism for the accumulation of excess volume consumed by the buyer in the course of any year, and its use to reduce IEC's undertaking to purchase a minimum quantity, as set forth above, in several subsequent years. Furthermore, the agreement specifies provisions and mechanisms allowing buyer to receive gas at no additional charge up to the volume paid for, on account of gas not consumed due to activation of the minimum bill quantity.
- J) The agreement includes several preconditions, the main ones being obtaining approval from the Antitrust Authority, the Public Services Authority - Electricity, and the Government Companies Authority.
- K) Price of gas: The contract gas price is denominated in USD per energy unit (BTU) and is set according to a formula that includes a base price and linkage, based mainly on the US consumer price index for all urban consumers (CPI-U) plus 1% per year until 2019 and less 1% per year from 2020.
- L) The agreement stipulates two dates when each party may request adjusting the price (based on the mechanism set out in the agreement) if that party believes that the contract price is no longer appropriate for a long-term contract with a significant buyer: Eight and 11 years after the commercial delivery starts from the Tamar project. At the first adjustment date (after 8 years) the adjustment to the price will be up to 25% (increase or reduction), and at the second adjustment date the adjustment will be up to 10% (increase or reduction).
- M) Gas quality: According to the agreement, delivery of natural gas must comply with the specifications set out in the agreement. The buyer has the right to refuse to receive non-compliant gas until such non-compliance is remedied. All disputes between the parties with regard to gas quality may be submitted to an expert for resolution at the request of any of the parties.
- N) Breach and damages: According to the agreement, the sellers must pay the buyers financial compensation if the gas supply from the Tamar project is delayed beyond the latest date stipulated in the agreement, for a period and amounts set out in the agreement. The agreement also stipulates that should the sellers fail to supply the

gas volume ordered by the buyer pursuant to the agreement, and should the non-supply exceed the deviation allowed by the agreement, the sellers shall compensate the buyer in the subsequent month by selling gas at a discounted price up to the volume of gas not supplied in breach of provisions of the contract. Furthermore, the agreement lists specific breaches for which damages are payable at higher rates. The agreement also sets limits to liability of each party for breach of some of the agreement provisions at amounts specified in the agreement.

- O) Relationships between the sellers and the sellers' coordinator: The sellers operate jointly on issues such as development of the reservoir, the sellers' facilities and gas production, delivery and supply according to the agreement. Concurrently, the buyer declares that none of the provisions in the agreement will be considered as creating mutual liability among the sellers, and each seller is individually liable to the buyer for its share in the oil rights and in connection with any liability arising from the agreement. Although the buyer may order gas volumes by a single notice to the sellers' coordinator, the volume considered ordered from each of the sellers will be the portion of each of the sellers out of the total volume ordered.
- P) The Tamar project partners estimate (based on the formula, estimates of the US CPI-U and a forecast of IEC's gas consumption when signing the agreement) that the cumulative revenues from the sale of natural gas to IEC (relative to 100% of the rights in the Tamar project) are likely to amount to USD 14 billion, and USD 23 billion if the option is exercised. It is clarified that the actual revenues will be derived, inter alia, from the actual gas quantities purchased by IEC, exercise of the option and the exercise date (if exercised), and from the price of gas calculated in accordance with the above formula.

Forward looking information: Delek Energy's aforesaid estimate, including the total financial value of the supply agreement, is forward-looking information as defined in the Securities Law, based on the assessments of the partnerships' general partners and there can be no certainty that it will materialize, in whole or in part, and it might materialize in a different manner, due to various factors including non-fulfillment of the preconditions, in whole or in part, the actual gas consumption by IEC, exercise of the option by IEC and the exercise date (if exercised), the gas price according to the formula in the supply agreement, the behavior of the US CPI-U, etc.

2. Agreement for the sale of natural gas in the Tamar project to Hadera Paper

- A) On January 25, 2012, an agreement for the supply of natural gas was signed between Hadera Paper and the Tamar project partners (in this section: "the sellers"), under which Hadera Paper will purchase natural gas from the sellers, to operate its installations as well as an additional power station of Hadera paper, if constructed (in this section: "the supply agreement"), the main points of which are as follows:
- B) The sellers undertake to supply Hadera Paper with a total of up to 3.3 BCM of natural gas (in this section: "the total contract quantity") over 15 years from mid-2013 (in this section: "the basic agreement period") until Hadera Paper consumes the total contract quantity, whichever is earlier.
- C) The parties may extend the basic agreement period by up to two additional years, if by that date the total contract quantity has not been consumed.
- D) Hadera Paper may reduce the quantities purchased by half of the total contract quantity if it does not construct the foregoing additional power plant.
- E) Hadera has a take or pay agreement for a minimum annual volume of natural gas according to a mechanism set forth in the supply agreement.
- F) The gas price stipulated in the supply agreement will be linked to the cost of generating electricity, as fixed from time to time by the Public Services Authority-Electricity, including a minimum price.
- G) The sellers estimate that the total cumulative revenues from natural gas sales to Hadera Paper (relative to 100% of the rights in the Tamar project) during the basic agreement period (based on the sellers' assessment regarding the natural gas price and the volume purchased throughout the basic agreement period) is likely to amount to USD 750 million, if the total contract quantity is not reduced as set out

above. The actual revenue will be derived from a range of factors, including the actual gas quantity purchased by Hadera Paper and cost of generating electricity.

- H) The supply agreement includes several preconditions, the main ones being finalizing the financing of some of the Tamar project sellers (including the partnerships), and approval by the Public Services Authority-Electricity and the Antitrust Authority (if required).

Forward looking information: The aforementioned estimations concerning the total financial value of the supply agreement, the quantity of natural gas purchased and the supply start date under the supply agreement is forward-looking information as defined in the Securities Law, and there can be no certainty that it will materialize, in whole or in part, and it might materialize in a different manner, due to various factors, including non-fulfillment of the above preconditions, in whole or in part, changes in the volume, rate and timing of natural gas consumption by Hadera Paper, the gas price accordance to the formula in the supply agreement, etc. It is also uncertain as of the reporting date whether Hadera Paper will construct another power station, as set forth above.

3. Agreement to sell natural gas to Mashav

- A) On February 9, 2012, the Tamar project partners (in this section: "the sellers") signed an agreement with Mashav for the supply of natural gas for the operation of its Ramla installations and expansion of its Ramla power station, should it be extended (in this section: "the supply agreement"), the main points of which are as follows:
 - B) The sellers undertake to supply Mashav with up to 0.2 BCM of natural gas per year over 15 years starting from the second half of 2013 or until Mashav consumes the total contract quantity stipulated in the supply agreement, whichever is earlier (in this section: ("the supply agreement period").
 - C) Mashav has the right, which can be exercised for a period of up to two months from the date of signing the supply agreement, to reduce the total contract quantity of natural gas under the supply agreement to approximately 40% thereof, if it does not expand its power station, as noted above. If during a period of three years after exercising this right to reduce the annual volume Mashav decides to expand its power station, the sellers may increase the volume by written notice to Mashav.
 - D) Mashav has a take or pay agreement for a minimum annual volume of gas according to a mechanism set forth in the supply agreement.
 - E) The gas price stipulated in the supply agreement will be linked to the cost of generating electricity, as fixed from time to time by the Public Services Authority-Electricity, including a minimum price.
 - F) The sellers estimate that the total cumulative revenues from gas sales to Mashav (relative to 100% of the rights in the Tamar project) during the supply agreement period (based on the sellers' assessment regarding the natural gas price and the supply agreement period) is likely to amount to USD 680 million, if the total contract quantity is not reduced as set out above. The actual revenue will be derived from a range of factors, including the actual gas quantity purchased by Mashav and the cost of generating electricity.
 - G) The supply agreement includes several preconditions, the main ones being finalizing the financing of some of the Tamar project sellers (including the partnerships), and approval by the Public Services Authority-Electricity and the Antitrust Authority (if required).

Forward looking information: The aforementioned estimations concerning the total financial value of the supply agreement and the supply start date under the supply agreement is forward-looking information as defined in the Securities Law, and there can be no certainty that it will materialize, in whole or in part, and it might materialize in a different manner, due to various factors, including non-fulfillment of the above preconditions, in whole or in part, changes in the volume, rate and timing of natural gas consumption by Mashav, the gas price according to the formula in the supply agreement, etc. It is also uncertain at this stage whether Mashav will expand the power plant as set out above.

4. Agreement to sell natural gas to Dalia

- A) On January 8, 2012, an agreement was signed between the Tamar project partners (in this section: "the sellers") and Dalia Power Energies Ltd. for the supply of natural gas to operate the power station which Dalia plans to construct (in this section: "the supply agreement"), the main points of which are as follows:
- B) The sellers undertake to supply Dalia with up to 1.38 BCM of natural gas per year over 17 years starting from commencement of commercial operation of the power station which Dalia plans to build or until it consumes the total contract quantity stipulated in the supply agreement, whichever is earlier (in this section: ("the supply agreement period").
- C) The parties may extend the supply agreement period by up to two additional years, if by that date the total contract quantity has not been consumed.
- D) Dalia has a take or pay agreement for a minimum annual volume of natural gas according to a mechanism set forth in the supply agreement.
- E) The gas price stipulated in the supply agreement will be determined according to a formula based primarily on the cost of generating electricity, as fixed from time to time by the Public Services Authority-Electricity, including a minimum price.
- F) The sellers estimate that the total cumulative revenues from gas sales to Dalia (relative to 100% of the rights in the Tamar project) during the supply agreement period (based on the sellers' assessment regarding the gas price during the supply period) are likely to amount to USD 5 billion. The actual revenue will be derived from a range of factors, including the actual gas quantity purchased by Dalia and the cost of generating electricity.
- G) The supply agreement includes several preconditions, the main ones being finalizing the financing of Dalia, finalizing the financing of some of the Tamar project sellers (including the partnerships) and approval by the Public Services Authority-Electricity and the Antitrust Authority (if required).
- H) The gas supply start date under the supply agreement is estimated by Delek Energy for the second half of 2014.

Forward looking information: The aforementioned estimations concerning the total financial value of the supply agreement and the supply start date under the supply agreement is forward-looking information as defined in the Securities Law, and there can be no certainty that it will materialize, in whole or in part, and it might materialize in a different manner, due to various factors, including non-fulfillment of the above preconditions, in whole or in part, changes in the volume, rate and timing of natural gas consumption by Dalia, the gas price according to the formula in the supply agreement, etc.

5. Agreement to sell natural gas to Ramat Negev

- A) On January 9, 2012, the Tamar project partners (in this section: "the sellers") and Ramat Negev signed an agreement for the supply of natural gas to operate a power station which Ramat Negev plans to construct (in this section: "the supply agreement"), the main points of which are as follows:
- B) The sellers undertake to supply Ramat Negev with up to 0.22 BCM of natural gas per year over 16 years starting from commencement of commercial operation of the power station which it plans to build or until it consumes the total contract quantity stipulated in the supply agreement, whichever is earlier (in this section: ("the supply agreement period").
- C) The parties may extend the supply agreement period by up to two additional years, if by that date the total contract quantity has not been consumed.
- D) Ramat Negev has a take or pay agreement for a minimum annual volume of gas according to a mechanism set forth in the supply agreement.
- E) The gas price stipulated in the supply agreement will be linked to the cost of generating electricity, as fixed from time to time by the Public Services Authority-Electricity, including a minimum price.

- F) The sellers estimate that the total cumulative revenues from gas sales to Ramat Negev (relative to 100% of the rights in the Tamar project) during the supply agreement period (based on the sellers' assessment regarding the gas price during the supply period) are likely to amount to USD 800 million. The actual revenue will be derived from a range of factors, including the actual gas quantity purchased by Ramat Negev and the cost of generating electricity.
- G) The supply agreement includes several preconditions, the main ones being finalizing the financing of Ramat Negev, finalizing the financing of some of the Tamar project sellers (including the partnerships) and approval by the Public Services Authority-Electricity and the Antitrust Authority (if required).
- H) The gas supply start date under the supply agreement is estimated by Delek Energy for the second half of 2014.

Forward looking information: The aforementioned estimations concerning the total financial value of the supply agreement and the supply start date under the supply agreement is forward-looking information as defined in the Securities Law, and there can be no certainty that it will materialize, in whole or in part, and it might materialize in a different manner, due to various factors, including non-fulfillment of the above preconditions, in whole or in part, changes in the volume, rate and timing of natural gas consumption by Ramat Negev, the gas price according to the formula in the supply agreement, etc.

6. Agreement to sell natural gas to Ashdod Energy

- A) On January 9, 2012, the Tamar project partners (in this section: "the sellers") and Ashdod Energy signed an agreement for the supply of natural gas to operate a power station which Ashdod Energy plans to construct (in this section: "the supply agreement"), the main points of which are as follows:
- B) The sellers undertake to supply Ashdod Energy with up to 0.11 BCM of natural gas per year over 16 years starting from commencement of commercial operation of the power station which it plans to build or until it consumes the total contract quantity stipulated in the supply agreement, whichever is earlier (in this section: ("the supply agreement period").
- C) The parties may extend the supply agreement period by up to two additional years, if by that date the total contract quantity has not been consumed.
- D) Ashdod Energy has a take or pay agreement for a minimum annual volume of gas according to a mechanism set forth in the supply agreement.
- E) The gas price stipulated in the supply agreement will be linked to the cost of generating electricity, as fixed from time to time by the Public Services Authority-Electricity, including a minimum price.
- F) The sellers estimate that the total cumulative revenues from gas sales to Ashdod Energy (relative to 100% of the rights in the Tamar project) during the supply agreement period (based on the sellers' assessment regarding the gas price during the supply period) is likely to amount to USD 400 million. The actual revenue will be derived from a range of factors, including the actual gas quantity purchased by Ashdod Energy and the cost of generating electricity.
- G) The supply agreement includes several preconditions, the main ones being finalizing the financing of Ashdod Energy, finalizing the financing of some of the Tamar project sellers (including the partnerships) and approval by the Public Services Authority-Electricity and the Antitrust Authority (if required).
- H) The gas supply start date under this agreement is estimated by Delek Energy for the second half of 2014.

Forward looking information: The aforementioned estimations concerning the total financial value of the supply agreement and the supply start date under the supply agreement is forward-looking information as defined in the Securities Law, and there can be no certainty that it will materialize, in whole or in part, and it might materialize in a different manner, due to various factors, including non-fulfillment of the above preconditions, in whole or in part, changes in the volume, rate and timing of natural gas consumption by Ashdod Energy and the gas price according to the formula in the supply agreement.

1.11.14 **Marketing and distribution**

- A. The Tamar project partners are taking steps to market gas to potential customers beyond the present ones. The partners are in various stages of negotiations with potential customers to sign binding agreements for the sale of natural gas from the reservoir.
- B. Delivery of gas to some additional customers also depends on the completion of the national gas pipeline being built by Israel Natural Gas Lines ("INGL"). At the reporting date, INGL has yet to complete the pipeline for the delivery of gas to all potential customers.
- C. At the date of the report, the power stations and the partnerships' customers connected to the national pipeline are as follows: Delek Ashkelon, Paz Refineries Ashdod, Hadera Paper, ICL Group at the Dead Sea, ORL, and the IEC power stations in Ashdod, Tel Aviv (Reading), Gezer, Hagit Haifa, Alon Tavor, Ramat Hovav and Zafit.
- D. The partnerships also signed a memorandum of understanding with potential buyers to assess an agreement to sell natural gas in the Tamar project to convert the gas to liquefied natural gas (LNG) using a floating liquefaction facility (in this section: "the liquefaction facility") and export it to South Korea and/or other countries. Pursuant to the foregoing memorandum of understanding, these potential buyers signed a letter of intent according to which negotiations will be conducted and non-exclusivity to sell and purchase LNG liquefied through the liquefaction facility will be granted. For further information of these agreements, see section 1.11.29.K above.
- E. The US oil market is highly developed, with appropriate infrastructure for delivery of oil and natural gas. Therefore marketing and distribution are conducted by means of existing infrastructure, and Delek Energy is not required to make any material investments in additional facilities.

1.11.15 **Order backlog**

- A. As at December 31, 2011, the order backlog for 2012 and 2013, as stipulated in binding contracts for the supply of natural gas, is as follows:¹⁸⁸

Minimum total annual quantity in the agreements BCM	
2013	2012
3.4	3.4

- B. As of December 31, 2010, the order backlog for 2010 and 2011, as stipulated in binding contracts for the supply of natural gas, was as follows :

Minimum total annual quantity in the agreements BCM	
2011	2010
3.1	2.8

- C. The supply of natural gas in 2011 was 4.34 BCM. The consideration received from the sale of gas in 2011 amounted to USD 722.8 million (100%).

1.11.16 **Competition**

- A. Israel
 - 1. A number of companies have been selling natural gas in Israel for many years. The sale of natural gas is primarily intended for local markets, therefore the competition is with parties operating in these markets.

¹⁸⁸ The above order backlog is based on the minimal gas quantities stipulated in the agreements for the supply of natural gas in the Yam Tethys project which the customers undertook to take or pay. According to the Company, due to the decrease in supply of natural gas from the Mari B reservoir, the partnerships will not be able to supply the quantities which they committed to in the agreements with respect to the period until completion of the development works in the Tamar project. In the matter of the Company's evaluation concerning the quantities to be supplied by the partnerships, see the quantities in the discounted cash flow set out above. The above order backlog excludes the quantities set out in agreements to sell gas from the Tamar project, due to the fact that they are contingent agreements whose conditions for them entering into force have not yet been met as of the reporting date.

2. In addition to the Yam Tethys group, there is one other group supplying natural gas in the Israeli market: East Mediterranean Gas Company¹⁸⁹ ("EMG"). EMG imports gas from Egypt and has signed gas supply agreements with several Israeli customers, the largest of which are the IEC and companies affiliated to Israel Corp. For the past year, EMG's supply of natural gas has been disrupted many times, following political unrest and/or security developments in Egypt. Moreover, the media have published information regarding the intention of the Egyptian authorities to reexamine the sales prices of the gas imported from Egypt. These events have implications for the competition in Israel's natural gas economy.
3. Moreover, British Gas has discovered natural gas reservoirs off the Gaza shore, which are of similar size to existing discoveries at Yam Tethys. However, they are currently not involved in marketing natural gas to the Israeli market.
4. In view of the commercial discoveries at Tamar, Dalit, Dolphin, Tanin and Leviathan, the partners to these discoveries (including the partnership) could become significant suppliers of natural gas to the Israeli market.
5. In addition to these discoveries, under the terms of the licenses issued by the commissioner to numerous parties, several exploration drillings are expected to be conducted in the forthcoming year. If these drillings lead to discoveries of significant quantities of natural gas, the competition for natural gas supply in the Israeli market will increase.
6. Natural gas suppliers also compete with other fuels, including coal, and the level of gas consumption and price are affected by the prices of these fuels. In addition, in the future, LNG is expected to be imported into the Israeli market.

Oil sales are less limited to local customers, and may be made on the global markets, where there is greater competition, but also more sales options. However, oil is a commodity with a price dictated by global fluctuations in supply and demand, therefore competition with other oil producing companies is not expected to have a material impact on the oil sales of the partnerships, if any.

B. Cyprus

1. At the report date, Cyprus is almost completely dependent on imported oil products and electricity production in Cyprus is mainly based (90%) on burning oil and oil products. The Cypriot energy market is characterized by high dependence on importing oil and oil products and fast growth in demand for energy. Furthermore, Cyprus has difficulty in connecting to the European energy infrastructures due to its geographic location. In 2007, the Cypriot government set up the Natural Gas Public Company (DEFA). Under regulations established in 2007 concerning the Cypriot natural gas market, this gas company has exclusivity to import and distribute natural gas in Cyprus. The Cypriot government and electric company are taking steps to promote replacing the use of oil and oil products with the use of natural gas to generate electricity. However, at the report date, Cyprus does not use natural gas. The Aphrodite discovery created a possible local source of natural gas in Cyprus. However, due to the large investments required to develop the discovery and the small volume of the potential Cypriot local market, it appears that developing the discovery and supplying natural gas to the local market depends on the capacity of the Cypriot authorities to promote establishment of export infrastructures to justify development and commercialization of the discovery.
2. In February 2012, the Cypriot government published a tender for 12 hydrocarbon exploration licenses in the territorial waters of Cyprus ("the license tender"), some of which border on Block 12. According to the information published by the Cypriot authorities, the licenses will be granted on a competitive basis under the rules published in the license tender documentation. The license tender is subject to Cypriot law and regulations published in Cyprus, and the latest submission date is May 11, 2012. At the report date, the partnerships have not yet formulated their position with respect to participation in the license tender.
3. After completion of the tender and allocation of the licenses to the winning parties, there may be additional natural gas discoveries in Cyprus. Since the Cypriot local market is

¹⁸⁹ EMG imports gas from Egypt and has signed gas supply agreements with several Israeli customers, the largest of which are the IEC and companies affiliated to Israel Corp.

small, the economic justification of developing discoveries depends on the ability to export the natural gas. At this stage, in the absence of relevant regulation in Cyprus in all matters concerning natural gas export facilities, it is impossible to estimate how additional discoveries may affect, if at all, the manner of exporting gas from Cyprus and the competition, if it develops, in all matters concerning the local market and access to export infrastructures.

1.11.17 Seasonality

- A. In Israel, IEC's gas consumption fluctuates, inter alia, with seasonal changes in demand for electricity and with IEC's maintenance plan. In the third quarter of each year (the summer months) power consumption is highest, therefore IEC consumes more gas during that quarter.
- B. The following information describes the distribution of natural gas sales to IEC over the past two years:¹⁹⁰

	Q1 (BCM)	Q2 (BCM)	Q3 (BCM)	Q4 (BCM)
2011	0.7	1.16	0.9	0.7
2010	0.4	0.6	1.0	0.7

- C. The seasonality of gas and oil consumption by customers in the USA had no material effect on Delek Energy's revenues from projects in the United States in the reporting periods of the financial statements.

1.11.18 Facilities and production capacity

The production system of the Yam Tethys project includes a production platform connected to eight wells, of which three are producing wells, a 42-km offshore pipeline for transmission of gas, and a permanent receiving terminal in Ashdod, which was completed in 2008. The production platform is anchored to the seabed at a water depth of approximately 236 meters. The upper part of the production platform, above sea level, contains all the platform decks. The four decks, 60 m long and 35 m wide, contain include production facilities planned for a maximum gas supply of up to 600 million cubic feet per day, equal to 6 BCM per year. The platform also includes generators, compressors, connection outlets for a gas pipeline, gas well heads, space for a drilling machine, helipad, employee living quarters and work area, a raised gas removal facility, antennas, fire extinguishing facilities, life boats and security devices, measuring and other facilities associated with the platform production and handling system.

For information of the reduced production capacity of the Mari B, see section 1.11.4.H(1) above.

For information of the planned development plan of the Tamar lease, see section 1.11.5.E(2) above.

1.11.19 Human resources

- A. The following employees were employed at Delek Energy, its subsidiaries and the partnerships at December 31, 2011 and 2010:

Department	No. of employees per day December 31, 2011	No. of employee at December 31, 2010
Management and headquarters	12	7
Finance	5	3
Professional	2	-
Total	19	10

- B. The increase in the number of employees in 2011 compared to 2010 arises from an increase in scope of the partnerships' operations due to significant discoveries in their oil assets.

¹⁹⁰ The information refers to total natural gas sales of the entire Yam Tethys group, rounded off to the nearest tenth of a BCM.

- C. Delek Energy also receives professional consultation service from various consultants, including geologists, geophysicists, lawyers, media consultants and financial advisors, as required.
- D. It is also noted that under the operating agreements in most of the projects to which the partnerships and/or the Company are partners, the project operator employs staff for management and operation of the projects. There are no employee-employer relations between employees of the project operator and the partnerships and/or the Company, and the partnerships and/or the Company have no direct liability towards them for severance.
- E. In the reporting year, management services were provided to Delek Energy and a wholly-owned subsidiary, as described in article 22 of Chapter D.
- F. Generally, the staff of the Company, subsidiaries and partnerships are employed under personal employment contracts. Officers and senior management staff are employed under terms agreed with each of these office holders, including monthly salary, company car, mobile phone, and provisions for executive insurance and study fund.
- G. Options for senior officers
 - 1. For the options allotted to Gideon Tadmor, former CEO of Delek Energy, see article 22 in chapter D of the report.
 - 2. On August 23, 2007 Delek Energy's board of directors and audit committee decided, subject to approval of Delek Energy's general meeting, which gave its approval on December 10, 2007, to approve the allocation of 55,345 unquoted options exercisable for 55,345 ordinary shares of Delek Energy, to the former chairman of Delek Energy, Gabriel Last. On January 17, 2010, Gabriel Last announced his resignation as chairman of Delek Energy's board of directors, effective from February 1, 2010 and Delek Energy's board of directors resolved to appoint him as deputy chairman of the board of directors as from that date. On January 17, 2010, subject to the approval of the general meeting, which was given on March 3, 2010, it was resolved that in view of the change in Gabriel Last's position, the terms of the options plan will be revised, such that subsequent to the changes, Gabriel Last will have 44,276 options. If Gabriel Last exercises all the options, the shares will account for 0.9% of Delek Energy's issued and paid up share capital, assuming the exercise of all of Delek Energy's convertible securities.
 - A) On January 17, 2010, Delek Energy's board of directors resolved, subsequent to the resolution of the audit committee meeting of January 14, 2010 and subject to the approval of the general meeting, which was given on March 3, 2010, to approve the allotment of phantom units amounting to 2% of the Delek Energy's issued and paid up share capital (at the approval date of the agreement), which is, 100,108 phantom units, in four equal tranches, to the chairman of Delek Energy, Dr. Yoram Turbowicz. On May 3, 2011, the general meeting approved termination of Dr. Yoram Turbowicz's employment as director in Delek Energy as from the approval date of the general meeting. According to the employment agreement with the chairman, upon termination of his employment by Delek Energy, he was entitled to exercise only the first lot of the package of phantom units he received, that is, 25,027 phantom unit representing 0.5% of the issued and paid up share capital of Delek Energy at an exercise price of NIS 1,007 each, even through two years had not yet passed since his appointment as Delek Energy director.
 - B) On August 23, 2011, Delek Energy's board of directors resolved, subsequent to the receiving approval of the audit committee and the board of directors of the general partner in Delek Drilling Partnership, to approve the allotment of phantom units ("the phantom units") at the value of the underlying asset (the participation units which grant participation rights in the rights of the limited partner in Delek Drilling Partnership) amounting to USD 15 million, to the CEO of Delek Drilling Partnership's general partner, Yossi Abu. The phantom units will vest in three lots ("the total package"), while each lot included in the total package will be exercisable during the vesting period, independently and/or together with other lots which vested previously, subject to adjustments. Subject to that set forth in his employment contract, Yossi Abu's eligibility concerning each of the three lots will only be effective upon completion of one full year of employment concerning that lot or in the case of the first lot, three full years.

1.11.20 Suppliers and raw materials

A project operator is appointed for each drilling project in which Delek Energy has rights. The operator contracts with professional contractors, which have the relevant equipment, for each project. There are no contractors in Israel involved in drillings, offshore seismic surveys development and infrastructure works of the type conducted by the limited partnerships together with their partners in the various projects. Therefore, the partnerships need to contract with foreign contractors for the necessary services. Offshore drilling equipment is chartered and transported from all over the world according to availability, project type and special needs of each project. Another important parameter that has impact on this matter is the price of crude oil: an increase in the price of crude oil usually affects the availability of contractors and required equipment and visa versa. The partnerships and/or the Company do not directly contract with suppliers or professional contractors, and such contracting is left to the project operators. Steel is a significant raw material in exploration and production equipment, used for pipes, drill bits and platform structures. Global metal prices have increased significantly in recent years.

1.11.21 Working capital

- A. The partnerships extend credit to their customers for periods of between 20 and 75 days. The average customer credit period in 2011 was 23 days.
- B. The average scope of customer credit in 2011 was USD 17.9 million.
- C. Payments of the partnerships and/or the Company to operators of the joint ventures are made under the terms in each operating agreement.

1.11.22 Investments

The Company also owns 29.3% of the shares in Matra Petroleum Plc ("Matra"), a public company registered in the UK, which has rights in an exploration and production project in Russia, 2.77% of the shares in Nexus Energy Ltd. ("Nexus"), an Australian oil and natural gas exploration and production company (and the full share capital of Delek Energy Systems (Gibraltar) Limited ("Delek Gibraltar"), a wholly owned subsidiary of Delek Energy, registered in Gibraltar, which has rights in an exploration project in the North Sea.

1.11.23 Financing

A. General

- 1. Delek Energy's operations are financed primarily by raising debentures in Israel, bank loans obtained in Israel and long term loans received from the Company.
- 2. Delek Energy examines from time to time options for receiving additional financing from the banking system and/or by way of the capital market in Israel. It is noted that there is no certainty that Delek Energy will receive additional financing as aforesaid.
- 3. The oil and gas exploration operations of the Limited Partnerships (as opposed to development and production) are financed from revenues received from the sale of the Yam Tethys project natural gas, funds from the Yam Tethys financing agreement (as defined below) and from short term loans that the partnerships received from Delek Energy.
- 4. In view of the development plan for the Tamar project, the additional investments required in the Yam Tethys project and further exploration efforts, the partnerships are expected to require significant sums of money to finance their operations, and this in accordance with the work plan and budgets that will be approved from time to time under the joint operating agreements applicable to the oil assets that they hold.
- 5. The partnerships intend taking action to raise the finances required to meet their obligations, among other things, by raising capital by way of a rights issue. It is further noted that there is no certainty that the partnerships will receive this financing.
- 6. Furthermore, it is noted that should the Company decide to maintain the rate of its holding in the partnerships, it will have to participate in the forgoing efforts to raise capital and to inject the funds required for its relative share in the partnerships.
- 7. On February 21, 2012 the general meeting of the holders of participating units of Delek Drilling and of Avner approved the issue of participating units and/or securities convertible into participating units during 2012, in an amount and on dates that will be fixed as will be decided by the general partner in either Partnership, for the purpose of raising the amounts required, in the opinion of the general partner in either Partnership, for financing

the ongoing operations of the entire partnership, including investment in the oil assets specified in section 5.1 of the Limited Partnership Agreement and repayment of its liabilities, and for empowering the general partner of either Partnership to decide on the structure, volume and timing of the issue, at its exclusive and absolute discretion, provided that a maximum amount will be set according to which the issue will not exceed USD 125 million. In addition, such issue may be made at any time under one or more prospectus and/or shelf offering memorandum, as the general partner of either Partnership will decide.

8. Pursuant to a permit granted by the Income Tax Authority to the partnerships close to the date of their establishment, the Limited Partnerships has committed not to obtain loans exceeding 3% of the amount raised from investors in the Limited Partnerships without prior consent of the Income Tax Authority.¹⁹¹

¹⁹¹

See below concerning the approvals received from the Income Tax Authority for receiving additional loans.

B. Breakdown of loans received by Delek Energy and the Limited Partnerships as of December 31, 2011

Partnerships

Designation	Borrower	Lender	Loan received date	Loan repayment date	Amount of loan	Interest	Linkage	Collateral	Balance as of December 31, 2011	Balance at February 29, 2012
Tamar financing	Partnerships	Consortium of banks	June 2010	June 2012	USD 190 million	3-month Libor + 5.75%	USD	See section 1.11.23 (e) below.	USD 184.6 million	USD 186.2 million
Yam Tethys financing	Partnerships	Consortium of banks	June 2011	June 2014	USD 109 million	3-month Libor + 2.75%	USD	See section 1.11.231.1 1.23D.2 (d) below.	Delek - USD 69.4 million Avner - USD 68.9 million	USD 53 million
Leviathan financing	Partnerships	HSBC Bank Plc	December 2011.	Until June 2014	USD 250 million	3-month Libor + 3.5%-4.5%	USD	See section 1.11.23 (f) below.	-	¹⁹²

- C. Breakdown of average and effective interest rates on loans, effective during 2011 and which are not intended for specific use by Delek Energy and the partnerships

		Average interest rate	Effective Interest rate
		Long-term loans	Long-term loans
Banking sources	Dollar loans	3-month Libor + 1.75%-4.5%	3-month Libor + 1.75%-4.5%
Non-banking sources	Index-linked shekel loans from the parent company	7.25%	7.25%
	Dollar debentures at fixed interest	7.9%	8.42%
	Shekel index-linked debentures	5.15%-5.5%	5.58%-5.87%
	Shekel debentures at fixed interest	7.19%	7.63%

		Average interest rate	Effective Interest rate
		Long-term loans	Long-term loans
Banking sources	Dollar loans	3-month Libor + 3.65%	3-month Libor + 3.65%

D. Material financing agreements

1. Debenture issue for financing the Yam Tethys project

On March 9, 2005 agreements to obtain non-recourse financing for the share of Israeli partners in Tam Tethys project (the partnerships and Delek Investments) were concluded, totaling USD 275 million. The share of Delek Drilling Partnership and Avner Partnership in this amount is USD 130 million and USD 120 million, respectively. At the beginning of May 2011, these debentures were repaid by early redemption in accordance with their terms. The objective of early redemption was, inter alia, to allow the partnerships to obtain new financing as specified below.

2. Yam Tethys project financing agreement

- A) On June 7, 2011 a new loan agreement was signed ("the Yam Tethys financing agreement") between the Israeli partners in the Yam Tethys project (the partnerships and Delek Investments) and a consortium of banks headed by Morgan Stanley & Co. International Plc ("the Yam Tethys financing banks") according to which each of the partnerships would receive a non-recourse loan in the amount of USD 109 million ("the loan").
- B) The Loan will be used to finance the share of the partnerships in the operating costs for oil rights held by the partnerships. Concurrently, with the financing agreement signed by the partnerships, a financing agreement with the same terms was signed between the Yam Tethys Financing Banks and Delek Investments for a loan of USD 23 million.
- C) The loan is for up to three years, depending on the rate of gas sales. If the sales exceed the amount set in the basic model appended to the loan agreement, part of the surplus proceeds can be used for early repayment of the loan. The partnerships are entitled to repay the loan prematurely at any time and at no charge.
- D) The dollar-denominated loan bears an annual variable interest rate of three-month Libor plus a margin of 2.75%. According to the Yam Tethys Financing Agreement, the loan will be repaid starting from October 2011 in eleven unequal quarterly payments based on the repayment schedule set by the parties, and depending on the forecast for gas sales set in the basic model. In addition, when the loan is received, the partnerships paid a one-time fee of 2% of the loan as set out in the financing agreement.

E) To receive the financing, the partnerships established a special purpose company: Delek Drilling Partnership established Delek Drilling (Tamar Financing) Ltd. and Avner Partnership established Avner Exploration (Tamar Financing) Ltd. (in this section for each of the SPCs: ("the SPC"). In accordance with the Yam Tethys Financing Agreement, the loan provided to the SPC will be a back-to-back loan for each limited partnership.

3. Collateral

To secure repayment of the loan, each partnership placed a lien on its rights to the assets related to the Mari reservoir in the Ashkelon lease, primarily: its rights in the Ashkelon lease, in the shares of Yam Tethys Ltd., in the JOA in the Ashkelon lease, including its rights in the project equipment and facilities, in agreements for sale of natural gas signed by the partners in the Ashkelon lease, the shares of the special purpose company and the assets and agreements related to the project (such as insurance policies). The loan is a non-recourse loan and the lenders have no right of recourse against the partnership's assets that have not been pledged in their favor.

4. Early redemption

As customary for this type of financing transaction, events of default were defined in the financing agreement, other than increased sales of gas as aforesaid, which if they occur the partnerships are committed to early repayment of the loan, in whole or in part, including, inter alia, the following key events: the loan becoming illegitimate; transfer of control in the partnerships; significant damage to the project; a decrease in the ratio of debt service for the remaining the loan period; decrease to below the minimum quantity of gas in the reserve.

5. Restrictions applicable to the partnerships

The partnerships have accepted standard covenants, including the following main commitments: compliance with a ratio of debt service for the remaining the loan period, a commitment to pay all taxes and levies owed by the partnerships, the partnerships' compliance with commitments under agreements to sell gas and the JOA, which were pledged, compliance with safety requirements, the commitment of each partnership to function as a partnership in accordance with the laws of the State of Israel, restrictions concerning structural changes in the partnership, restrictions on changes in agreements for the gas sales and the JOA, protection of pledged assets, and refraining from any breach or change of any of the significant terms of agreements,

6. Events of default

The financing agreement sets out standard events of default, which if they materialize (subject to remedial periods as provided by the financing agreement) the Yam Tethys financing banks may call for immediate repayment of the loan. The breach events include the following main events: nonpayment of amounts due to lenders; breach of covenants; breach of representations; insolvency events; events that could have a material adverse effect on the ability of the limited partnerships to fulfill their material obligations in respect of the financing agreement or the pledged agreements for sale of gas, events that could have a material adverse effect on their assets or main businesses or the financial position of the partnerships.

7. The Yam Tethys financing agreement was signed subsequent to receipt, on June 1, 2011, of the income tax authorities approval of the partnerships' application to take loans for the purpose of exploration, development and establishment of the following oil assets: Ashkelon Holding, Tamar Holding, Rachel license, Amit licenses, Hannah license, Alon A and Alon C licenses ("the June 2011 approval"), in addition to the limitation set in the previous approval received from the income tax authorities and which regulated the status of each of the partnerships as a partnership according to the definition prescribed in the Income Tax Regulations (Rules for Tax Calculations for Ownership and Sale of Participation Units in an Oil Exploration Partnership), 1988 ("the original approval").

8. According to the June 2011 approval, the partnerships may obtain loans in the amount of USD 109 million for exploration, development and establishment of the foregoing oil assets and which are payable by December 31, 2014.

E. Bridging loan for Tamar financing

- A) On June 24, 2010, agreements were signed for a bridging loan ("the interim financing agreement") between one of the partnerships (through wholly-owned SPCs as set out below) and Barclays Bank Plc and HSBC Bank Plc¹⁹³ ("the interim financing banks"). Subsequent to the interim financing agreement each of the partnerships received a non-recourse loan for financing part of the Tamar field development costs ("the Tamar project") up to an amount of USD 190 million (in this section - ("the loan"). Concurrent with the signing of the interim financing agreement by the partnerships, a financing agreement with the same terms was signed between the interim financing banks and Dor Gas (for a loan of USD 50 million), to finance its share in part of the development costs of the Tamar project.
- B) The loan is for the period until the agreement is signed for long-term non-recourse project finance to fully finance each of the partnerships' share in the development costs of the Tamar project ("the project financing") or for a period of 18 months ("the original loan period"), according to the earlier date (with the option of extending it, under certain conditions, for an overall period of 24 months¹⁹⁴).
- C) On December 22, 2011 the original loan period was extended by an additional six months, i.e. until June 24, 2012 or until the signing of the project financing, according to the earlier date the new loan period").
- D) The loan will be repaid in a bullet payment at the end of the new loan period.
- E) The partnerships may repay the loan prematurely, subject to the terms set out in the interim financing agreement.
- F) The loan bears an annual variable interest rate of three-month Libor plus a margin of 2.75%.
- G) The funds of the loan were transferred to each partnership on a current basis, in accordance with the payment requirements issued by the operator to the partners in the Tamar project for development costs of the Tamar project (cash calls) and to finance the loan costs.
- H) The partnerships intend to take steps to raise financing for the project before the new loan agreement expires, such that the project finance will repay the loan. The end of the project finance raising is also affected, inter alia, by the agreement with the Israel Electric Corporation for the supply of natural gas from the Tamar project as set forth below.
- I) To receive the financing, the partnerships established a special purpose company: Delek Drilling partnership established Delek Drilling (Tamar Financing) Ltd. and Avner partnership established Avner Exploration (Tamar Financing) Ltd. (in this section for each of the SPCs: ("the SPC"). In accordance with the interim financing agreement, the loan provided to the SPC will be a back-to-back loan for each limited partnership.
- J) Collateral

To secure the loan, each of the partnerships pledged its rights to the assets related to the Tamar project. The main points are as follows: their rights in the Tamar and Dalit leases ("the leases"), rights in the Tamar project JOA, rights in any future agreements for the sale of natural gas from the Tamar project, shares of the SPC and accompanying agreements of the Tamar project (such as insurance policies and equipment).

The loan is a non-recourse loan and the lenders have no right of recourse against the partnerships' assets that were not pledged in their favor. These pledges are subject to royalty rights of the State and other entities that are entitled to receive royalties from the partnerships (including interested parties). To establish legal certainty regarding priority of claim in the event of insolvency of the limited

¹⁹³ After granting the financing, the interim financing banks syndicated part of the loan to other banks.

¹⁹⁴ The main terms for extending the loan are approval of a budget and development plan by the Tamar project partners and submission to the Commissioner within one year from the loan date, and start of development drilling by the end of June 2011.

partnership, the financing agreements prescribe, based on requirement of the banks, that the leases will be pledged in favor of the entities entitled to royalties for the term of the interim financing agreement as collateral for the right to royalties.

K) Restrictions applicable to the partnerships

As is standard in this type of financing, the partnerships have undertaken standard covenants, including the following main commitments¹⁹⁵: Restrictions on taking additional loans (other than non-recourse loans, loans from related parties and loans of up to USD 20 million); compliance with liquidity tests¹⁹⁶; compliance with the reservoir to debt ratio¹⁹⁷; restrictions on the change in operations; restrictions on the transfer of control in the partnerships; restrictions on signing contracts that may adversely affect the partnerships' ability to raise project financing; maintaining the pledged assets and avoiding breach or change of conditions of the material agreements, including agreements not to vote in accordance with the JOA in a way that may adversely affect the ability of each limited partnership to raise the project financing (including with respect to replacing the operator); purchase of insurance in accordance with the JOA; conditions for the purchase of additional rights in the Tamar project; and restrictions on approval of sole risk operations in the Tamar project.

F. Events of default

As customary in financing transactions of this nature, the interim financing agreement defined events of default, which if occur (subject to recovery periods set out in the interim financing agreement) confer on the financing banks the right to call for immediate repayment of the interim financing loan, including the following main events: failure to pay amounts owed to lenders; breach of covenants; breach of representations; insolvency events; occurrence of events that may have a material adverse effect on the ability of the partnerships to fulfill their material obligations in respect of the interim financing agreement or the Tamar project, events that may have a material adverse effect on their assets or main businesses or the financial condition of the partnerships or events that could have a material adverse effect on their ability to raise the project financing; cancellation or inability to receive material approval required for the Tamar project; meeting of additional milestones set according to agreed deadlines (project development approval; gas sales agreement with IEC; planning approval for establishment of the gas receiving terminal; availability of drilling rigs for development drilling); and a continuing force majeure event in connection with the Tamar project.

Concurrent with signing the interim financing agreement, each limited partnership appointed the interim financing banks as exclusive consultants and organizers for project financing, and granted them exclusive rights or participation according to certain conditions set out in any hedge transactions that the limited partnership may perform and the right of refusal for financial services and other consulting services to each of the partnerships, in respect of the Tamar project.

The interim financing agreement was signed subsequent to receipt, on March 25, 2010, of the income tax authorities approval of the partnerships' application (which was submitted together with Isramco) to obtain loans for the purpose of exploration, development and establishment of the Tamar project ("the March 2010 approval"), in addition to the limit set in the original approval.

In accordance with the March 2010 approval, the partnerships can finance their part in the production infrastructure plan at the Tamar project through a loan and/or issuance of debentures, without the required financing and/or investments made by the partnership in the production infrastructures canceling the partnership's status granted under the foregoing original approval.

The partnerships received the approval from the Tax Authority for exemption from withholding tax to the foreign lenders for interest paid on the loan.

¹⁹⁵ As aforesaid, the loan was provided as a short-term bridge loan until project funding is received. Therefore, the financial covenants prescribed for the loan have no significant implications, however the main points of the financial covenants in the agreement are set out below, with reference to those that are significant.

¹⁹⁶ According to this test, the partnerships are required to show sources for financing the payment requirements for a short period set out in the agreement.

¹⁹⁷ See below.

G. Leviathan project financing agreement

1. On December 22, 2011 a new loan agreement was signed ("the Leviathan financing agreement") between the partnerships and HSBC Bank Plc ("the Leviathan financing bank"), according to which each of the partnerships would receive a non-recourse loan in the amount of USD 250 million ("the loan"). The loan funds would be used, in addition to financing the operations of the partnerships in the Leviathan project, to also finance investments in the Yam Tethys project, including drilling at the satellite reservoir of the Mari B reservoir in the Ashkelon lease, the Noa North field in the Noa lease (if the partnerships decide to develop it) and to finance the partnerships operations at the Tamar lease (subject to conditions and clarifications prescribed in the financing approval as set forth in section (2) below) and to pay various expenses relating to the loan.

The loan is made available in two facilities, as follows:

Facility A in the amount of USD 75 million, which will be available for withdrawal after the fulfillment of a number of preconditions primarily, the approval of the Commissioner for a lien on the partnerships' rights in the 349/Rachel and 350/Amit licenses ("the Rachel and Amit licenses").

The Commissioner's approval with regard to the Rachel and Amit licenses was received on February 27, 2012. The Commissioner's foregoing approval was given subject to terms and clarifications prescribed therein, which include compliance with the terms set for the first withdrawal of loan funds under a long term non-recourse finance project for full financing of the part of each partnership in the development costs of the Tamar project, excluding in the event of unexpected deviation from the Tamar project establishment budget and after receiving the Commissioner's approval.

The payment date of Facility A is 24 months after signing of the Leviathan financing agreement.

Facility B in the amount of USD 175 million, which will be available for withdrawal upon closing the full project financing for the Tamar project and repayment of the bridging loan (provided to the partnerships with respect to the Tamar project) and no later than on June 24, 2012. The payment date of Facility B is 24 months after the first withdrawal therefrom, and no later than on June 24, 2014.

2. The partnerships may repay the loan prematurely, subject to the terms set out in the Leviathan financing agreement, without premature repayment fees.
3. The loan is in dollars and bears annual interest calculated at Libor for three months plus a margin of between 3.5% and 4.5% (not including fees).
4. To receive the Leviathan financing agreement, the partnerships established a special purpose company: Delek Drilling partnership established Delek Drilling (Leviathan Financing) Ltd. and Avner partnership established Avner Exploration (Leviathan Financing) Ltd. (in this section for each of the SPCs: ("the SPC"). In accordance with the Leviathan financing agreement, the loan provided to the SPC will be a back-to-back loan for each limited partnership.

5. Collateral

To secure the loan, each of the partnerships pledged its rights to the assets related to the Leviathan project. The main points are as follows: its rights in the Amit and Rachel licenses ("the licenses"), its rights in the Leviathan project joint operating agreement (in this section - ("the JOA")), the shares in the special purpose company and the assets and agreements related to the Leviathan project (such as insurance policies).

The loan is a non-recourse loan and the Leviathan financing bank has no right of recourse against the partnerships' assets that were not pledged in their favor. These pledges are subject to royalty rights of the state and other entities that are entitled to receive royalties from the partnerships (including interested parties).

To establish legal certainty regarding priority of claim as aforesaid, in the event of insolvency of one of the partnerships, the Leviathan financing agreement prescribes, based on the Leviathan financing bank's requirements, that the licensees will be pledged as collateral for the right to royalties in favor of the entities entitled to royalties for the term of the Leviathan financing agreement.

6. Restrictions on the partnerships

As is standard in this type of financing, the partnerships have undertaken covenants including, inter alia, the following main commitments: Restrictions on taking additional loans (other than non-recourse loans and credit of up to USD 20 million); compliance with the reservoir to debt ratio; restrictions on the change in operations; restrictions on the transfer of control in the partnerships; restrictions on signing contracts that may have a material adverse effect; maintaining the pledged assets and avoiding breach or change of conditions of the material agreements, including agreements not to vote in accordance with the JOA in a way that may adversely affect the ability of each partnership to fulfill their material obligations in respect of the Leviathan financing agreement; purchase of insurance in accordance with the JOA; conditions for the purchase of additional rights in the Leviathan project; and restrictions on approval of sole risk operations in the Leviathan project.

7. Events of default

As customary in financing transactions of this nature, the Leviathan financing agreement defined events of default, which if occur (subject to recovery periods set out in the Leviathan financing agreement) confer on the Leviathan financing banks the right to call for immediate repayment of the interim financing loan, including the following main events: failure to pay amounts owed to the Leviathan financing bank; breach of covenants; breach of representations; insolvency events; occurrence of events that may have a material adverse effect on the ability of the partnerships to fulfill their material obligations in respect of the Leviathan financing agreement or the Leviathan project, events that may have a material adverse effect on their assets or primary businesses or the financial position of the partnerships; events that could have a material adverse effect on the ability of the partnerships to sell the Leviathan project so as to enable them to repay the loan on due date; cancellation or inability to receive material approval required for the Leviathan project; and repeated force majeure events relating to the Leviathan project.

The partnerships appointed the Leviathan financing bank as sole consultant and coordinator of the long-term loan (which will replace, inter alia, the loan which is the subject of this report) and granted it the right to provide various services (whether alone or with the cooperation of other banks) in respect of the Leviathan project.

The approval of the Income Tax Authority for the loans was received in March.

8. Financial criteria

As part of receiving the loans and credit from banking and/or non-banking sources, Delek Energy undertook to comply with the following financial criteria:

9. Delek Energy's loans from Israeli banks

Financial covenant	Method of calculation	Tested ratio as of December 31, 2011 ¹⁹⁸	Remarks
Minimum shareholders equity of Delek Drilling and Avner partnerships	The balance of shareholders equity of Delek Drilling and Avner partnerships will not fall below USD 60 and 70 million, respectively.	Shareholders' equity of Delek Drilling Partnership: USD 252 million Shareholders' equity of Avner Partnership: USD 249 million	The balance is calculated only on the basis of the published audited financial statements and/or the condensed interim financial statements.
The shareholders equity to balance sheet ratio of Delek Drilling and Avner Partnerships	The rate of the shareholders equity of Delek Drilling and Avner partnerships out of the total balance sheet of Delek Drilling and Avner partnerships will not fall below 30%.	The ratio for both partnerships is 40%.	The shareholders equity to balance sheet ratio is calculated only on the basis of the audited financial statements and/or the condensed interim financial statements.
Minimum shareholders' equity	The shareholders' equity plus components shall not fall below NIS 250 million.	The balance of shareholders' equity plus components is over NIS 400 million.	The foregoing covenant is calculated only on the basis of the audited financial statements and/or the condensed interim financial statements.
Shareholders equity to balance sheet ratio	The shareholders equity (plus components) to balance sheet ratio shall not fall below 13%-15%.	The ration ranges between 16% and 21% ¹⁹⁹ .	
The debt to collateral ratio	The bank debt balance to market value of the pledged participating units of the Delek Drilling and Avner partnerships shall not fall below 25% - 40%.	The ratio ranged between 5% to 22% in the various banks ²⁰⁰ .	This is measured on a daily basis.
The market value of the Company's entire holdings in the participating units of the Delek Drilling and Avner partnerships to the Company's debt (stand-alone).	The Company's financial debt in its stand-alone balance sheet divided by the market value of its entire holdings in the participating units of Delek Drilling and Avner partnerships shall not exceed 50%.	The ratio is lower than 25%.	

¹⁹⁸ The date on which compliance with the financial criteria was examined by the lender (if such date is set).

¹⁹⁹ During November 2011, it became apparent that for one of the Company's lenders, the foregoing ratio was lower than required by 2%. The lender notified the Company that it waives its rights with respect to this covenant until publication of the Company's annual financial statements for the period ended December 31, 2011. Furthermore, the lender noted that the foregoing stay is subject to the Company continuing to comply with its undertakings to maintain the financial indices it committed to for other lenders as well, other than the foregoing event of default that was approved. In view thereof, the loans received from the bank were reclassified as current liabilities. On March 26, 2011 the Company reached agreements with a bank according to which the covenant with the bank was amended. Under the agreements, new covenants were added, as specified below.

²⁰⁰ The scope of the pledged participating units proximate the date of publication of the financial statements with regard to loans received from banks and with respect to credit facilities used subsequent to the balance sheet date is 24% of the participating units held by the Company directly and indirectly in Delek Drilling Partnership and 12% of the participation units held by the Company in Avner Partnership.

10. Debentures (Series C - E)

Financial covenant	Method of calculation	Tested ratio as of		
		December 31, 2011 ²⁰¹	December 31, 2011	February 28, 2012
Debt to collateral ratio	The market value of participating units pledged for debentures to the balance of debenture principal debt ratio shall not fall below 1.1.	The participating unit to net debenture debt ratio is calculated monthly on first trading day of each calendar month during the debenture period.	Series C 1.8 Series D 1.8 Series E 1.8	

11. Yam Tethys financing agreement

Financial covenant	Method of calculation	Tested ratio as of ²⁰²	
		January 31, 2012 ²⁰³	December 31, 2011
Revenue to debt service	Total revenues (from last payment date through to current payment date) from sale of natural gas from the reserve to debt service of the next payment based on the payment schedule set in the agreement (including payments for acceleration) ratio will be greater than 1.	1.7	1.7
Revenue to debt service (for purpose of withdrawal of funds)	- The debt service ratio (total revenue to debt service) for the three months prior to the payment date will be less than 1.15. - The debt service ratio (total revenue to debt service) for the three months prior to the payment date will be less than 1.15. - The current value of the total net revenue for the loan balance to the debt balance on the distribution date ratio will be lower than 1.3.	1.7 1.5 1.3	1.7 1.5 1.3
The debt service to total loan period balance ratio	The foregoing calculation will be attached to the annual financial statements that are submitted to the lenders as of the annual financial statements one after the first withdrawal of the funds, which is the financial statements for 2012.	=	=

²⁰¹ The date on which compliance with the financial criteria was examined by the lender (if such date is set).

²⁰² As stipulated in section 1.11.4[J](1)c above, there has been a significant decline in the ability to produce natural gas from the Mari B reservoir in recent months. This decline in production ability is expected to have an adverse effect on the financial results of the partnerships, and inter alia, on the financial covenants. At this stage the partnerships are unable to estimate, with high certainty, the full implications of the decline in production ability and supply and the scope of the effect on the financial results of the partnerships, which is liable to constitute grounds for closing the funds in the pledged accounts and even cause for immediate repayment of the loan. It is further noted that, in some of the events the partnership has, under the agreements, the option to amend the relevant ratio by way of partial early repayment on account of the loan. The net loan balance (less pledged deposits) as of reporting date amounts to USD 26 million (constituting 24% of the original loan). The partnerships are coordinating the actions with the banks

²⁰³ The date on which compliance with the financial criteria was examined in accordance with the loan agreement (if such date is set).

12. Tamar financing agreement

Financial covenant	Method of calculation	Tested ratio as of December 31, 2011 ²⁰⁴
Liquidity test	The ability to comply with the next payments for the Tamar project over the coming 60 days.	The partnerships are in compliance with the required ratio.
Value of reservoir to debt balance	The value of the reservoir (for the purpose of the financing agreement only) to debt balance ratio will not fall below 2 ²⁰⁵ .	4

13. Leviathan financing agreement

Financial covenant	Method of calculation	Tested ratio as of December 31, 2011 ²⁰⁶
Value of reservoir to debt balance	The value of the reservoir (for the purpose of the financing agreement only) to debt balance ratio will not fall below 2 ²⁰⁷ .	As of reporting date, the loan has not yet been withdrawn.

²⁰⁴ The date on which compliance with the financial criteria was examined in accordance with the loan agreement (if such date is set). It is hereby clarified that as of publication date of this report, there is no material change in the results of the tested ratio.

²⁰⁵ It is clarified that the value of the reservoir for the purpose of this financial covenant was calculated according to arbitrary parameters that were set and defined only for the purpose of this agreement and therefore it serves this purpose only and does not reflect the financial value of the reservoir in any way.

²⁰⁶ The date on which compliance with the financial criteria was examined in accordance with the loan agreement (if such date is set). It is hereby clarified that as of publication date of this report, there is no material change in the results of the tested ratio.

²⁰⁷ It is clarified that the value of the reservoir for the purpose of this financial covenant was calculated according to arbitrary parameters that were set and defined only for the purpose of this agreement and therefore it serves this purpose only and does not reflect the financial value of the reservoir in any way.

14. Credit facilities

A) Breakdown of the main terms of the credit facilities provided to Delek Energy:

Lender	Date facility extended	Credit facility period	Amount of credit facility	Commission for allocating credit (calculated on the unused credit)	Collateral	Used credit balance as of December 31, 2011	Used credit balance as of reporting date	Additional details
Local Bank	January 5, 2010	until June 30, 2012	USD 36.2 million	0.65%	Participating units of Delek Drilling Partnership:	-	USD 36.2 million	See section B) below.

- B) On January 24, 2012 Delek Energy used the full credit facility extended to it by the lender ("the loan" or "the loan agreement"). The loan principal will be repaid in a lump sum on January 1, 2014 and the interest will be paid every three months as of the date of receipt of the loan. Delek Energy has the right to make early repayment on account of the loan, on any of the interest payment dates, by giving prior notice of 7 business days, provided that the amount of the early repayment will not be less than USD 2.5 million and subject to payment of early payment commission as set forth in the loan agreement. To secure the foregoing loan, inter alia, Delek Energy deposited with the Lender an amount that will not be less than two consecutive interest payments for the loan.
- C) As customary for this type of loan agreement, the lender is entitled to call the loan for immediate repayment under any of the events noted in the loan agreement (subject to the terms of the loan agreement) and including in the following events: breach of Delek Energy's undertakings towards the Lender (subject to the breach amendment period); change in the structure of Delek Energy and/or Delek Drilling Partnership and/or any entity controlled by Delek Drilling Partnership, directly or indirectly (together - "the corporations"), without receiving prior written consent of the lender; liquidation proceedings and/or receivership proceedings and/or foreclosure proceedings and/or execution procedures regarding the assets of one of the Corporations; insolvency events stipulated in the loan agreement relating to any of the Corporations; change in holdings in Avner Partnership and/or change of control in Delek Drilling Partnership and/or change of control in Delek Energy and/or change of control in Delek Investments, as stipulated in the loan agreement; if any of the Corporations are required to repay debts and liabilities in an amount exceeding USD 1 million immediately and/or not in accordance with the original repayment schedule of any of the foregoing Corporations towards other creditors; a stay or cessation in trading of securities of Delek Drilling Partnership for a consecutive period of 3 days or delisting of its securities from trading, etc.
- D) Amendment of promissory note dated March 26, 2012 - under agreements reached with the bank as set forth in section 1.1.5 above, the following financial covenants were added:
- E) Delek Energy's shareholders' equity shall not fall below NIS 100 million.
- F) Delek Energy's shareholders equity to stand-alone balance sheet ratio will not fall below 15% at any time.
- G) Delek Energy's total financial debt in its stand-alone balance sheet divided by the market value of its holdings in the participating units of Avner Partnership and of Delek Drilling Partnership will not exceed 50%.

1.11.24 Taxation

For information of the terms of taxation of Delek Energy profits, see Note 42 to the financial statements.

1.11.25 Environmental risks and means for their management

- A. Drilling and production operations carry environmental risks associated with oil gushing and/or oil spill and/or natural gas leak.
- B. In Israel, the Petroleum Law and its regulations stipulate that, inter alia, the drilling shall be accomplished with due caution so as to prevent seepage of liquids and gases into the ground or uncontrollable gushing, as well as to prevent their penetration from one geological layer to another.. Furthermore, it is forbidden to abandon a well unless it is plugged in accordance with instructions of the Petroleum Commissioner. The operator purchases insurance to cover environmental damage incurred by uncontrolled gushing of oil and/or gas in oil and gas drilling and/or production.
- C. In March 2011, the Ministry of Environmental Protection published preliminary draft guidelines for new and existing gas and oil drillings with the aim of settling the environmental aspects of oil and gas drilling from the exploratory drilling stage, through the development drilling stage to the production drilling stage. These guidelines apply to a range of environmental aspects of the drillings, including prevention of pollution of the ground and water sources and treatment of polluting incidents; regulating the chemicals permitted for use; method of waste removal on land, whether originating in land drillings or marine drillings; pool for temporary collection of

drilling sludge until removal; means for storage of diesel, fuels, and crude oil; requirements for removal destinations and for testing quality of removed drilling liquids and sludge, quality of drilling chips and any other waste whether originating in land or in marine drillings; and setting procedures for treating leak and spill incidents. The guidelines are to be implemented throughout all the oil drilling stages, from submitting of applications through production stages and drilling abandonment. As of reporting date, the draft guidelines are being discussed by professionals. The guidelines could have an effect on the costs and the way Delek Energy and/or the partnerships operate, the scope of which as of reporting date cannot be estimated.

- D. In addition to the foregoing guidelines, on December 14, 2011 the Marine and Coastal Beach Division of the Ministry of Environmental Protection sent a letter to all the oil and gas exploration partnerships and companies relating to environmental regulation for offshore oil and gas exploration, drilling and production operations (including rigs, offshore underwater installations, pipelines and any other facility, whether or not operating under the permits granted by the Ministry of Energy and Water under the Petroleum Law, including supervision and control of all the installations and monitoring of the offshore environment), which includes initial instructions and guidelines concerning the drilling operations. The foregoing letter also states that companies operating in offshore drillings will be required to regulate their operations in accordance with the existing legislature, which includes obtaining permits for marine pumping or for dumping of effluents and waste into the sea in accordance with the provisions of the Prevention of Sea Pollution from Land-Based Sources Law, 1988 and the Prevention of Sea Pollution (Dumping of Waste) Law, 1983, and a poisons permit pursuant to the provisions of the Hazardous Substances Law, 1993. Furthermore, in cases where gas or oil is transmitted via sub-marine pipelines, a permit is required under the Water Regulations (Prevention of Water Pollution) (Fuel Pipelines), 2006, and the partnerships' drilling operations may require monitoring of the marine environment (background and ongoing monitoring), as part of the process for obtaining the marine pumping or marine effluents and waste dumping permits. In addition, the letter also states that companies involved in offshore drillings will be required to prepare and submit an emergency plan for treating oil spill marine pollution for approval of the Ministry of Environmental Protection as well as a comprehensive environmental survey of all the operations involved in laying marine infrastructures. Delek Energy estimates that the foregoing arrangements (particularly if it will adopt the Ministry of Environmental Protection guidelines) could affect costs and the way Delek Energy and/or the partnerships operate, the scope of which as of reporting date cannot be estimated.
- E. As set forth above, under licenses and permits obtained by the Yam Tethys project partners in connection with construction of the project's production system, the partners are required to operate in compliance with environmental protection standards set forth in the licenses and permits. Following an oil seepage event in 2010 in the Gulf of Mexico, requirements and supervision were tightened for offshore oil and gas exploration off the coast of Israel.
- F. On March 22, 2011 a private bill, called the Petroleum Law (Amendment - Environmental Protection), 2011 bill, was tabled in the Knesset, which deals with prescribing essential environmental regulation and control mechanisms concerning oil and gas exploration and production. The objective of this proposed bill is to anchor representation of environmental issues, primarily the Ministry of Environmental Protection, as entities determined by law and to instill environmental considerations into decision making under the Petroleum Law. The bill also stipulates that it will be able to set restrictions in the terms of the license or preliminary permit with the purpose of preventing and minimizing damage to the environment and that it will be able to take measures against the holders of licenses or oil rights, which caused or may cause environmental damage. In the opinion of Delek Energy, if the proposed bill is adopted in its current format, if at all, it is not liable to adversely affect the businesses of Delek Energy and/or the partnerships.
- G. On January 9, 2012, the Ministry of Energy and Water drafted an initial environment and safety code for onshore natural gas production ("the Environmental Code"), which was distributed for review by the companies, green organizations and relevant entities in the industry. This code is intended to ensure, inter alia, that onshore oil and natural gas exploration and production are carried out using the best safety and control measures to prevent breakdowns and damage to the environment and workers. At the same time, the Ministry of Energy and Water is drafting a similar code for offshore oil and natural gas drillings, which will also be distributed for public review. Since the environmental code refers, as of reporting date, only to onshore natural gas production, it is not liable to have an adverse effect on the businesses of Delek Energy and/or the partnerships.

- H. In addition to the guidelines of the Ministry of Energy and Water and the Ministry of Environmental Protection, the operations of the partnerships may be subject to provisions relating to ecological matters that may be issued from time to time on behalf of public or private entities, including the Israel Lands Administration, the Antitrust Authority and the Ministry of Interior.
- I. The cost of operations related to environmental protection is included in the budgets for the different projects. At the report date, no additional material costs are anticipated. As of reporting date, the Delek Energy is not aware of any non-compliance or deviation from the ecological requirements in the projects in which the partnerships have rights.
- J. As of reporting date and to the best of Delek Energy's knowledge, there are no legal and/or administrative proceedings concerning environmental protection issues against Delek Energy (including against its officers) and/or the partnerships and/or any of the officers of the partners in the partnerships.
- K. The partnerships, which operate in the various projects through an operator, have strategic ecological policies for protecting the environment and for complying with the provisions of the law in general and the environmental laws in particular. These policies include the operator's strict compliance with internal procedures for dealing with the environmental hazards of its operations, and includes appropriate training of human resources, based on a work program for minimizing environmental damage and preventing failures and accidents.
- L. Cyprus - pursuant to the Cypriot Impact on the Environment from Certain Plans and/or Programs Law (2005), which was adapted to relevant EU directive, strategic environmental assessment is required with regard to government decisions concerning activities or programs that may affect the environment. The Cypriot Ministry of Energy assigned the preparation of the strategic environmental assessment report to companies operating in the industry (following a tender) with regard to oil and natural gas exploration and production in Cyprus and in the Cypriot exclusive economic zone (EEZ). The exploration license granted requires operating in accordance with the strategic environmental assessment report.

1.11.26 Restrictions on and supervision of the partnerships' operations

A. Israel

- 1. In Israel, oil and gas exploration and production are primarily regulated under the Petroleum Law and its Regulations, as specified below:
 - A) Exploration is conducted under preliminary permits, licenses and leases (as defined in the Petroleum Law), which are granted by the competent authorities and include, inter alia, preliminary testing, work plans, time schedules and various restrictions.
 - B) Moreover, the Petroleum Law stipulates that a lease holder must pay royalties to the State at a rate of one eighth of the quantity of oil produced from the leased and exploited field (excluding the quantity of oil and/or natural gas used by the lease holder in operating the lease area), and in any case no less than the minimum royalty set in the Petroleum Law.
 - C) The Authority (as defined in the Petroleum Law) may rescind the rights if the owner of the rights does not comply with any of the provisions of the law or the terms of the oil rights or does not act according to the work plan that it submitted or was late in execution or did not invest the amounts it committed to invest in oil exploration.
- 2. In Israel, transmission, distribution and marketing of natural gas are regulated by the Natural Gas Sector Law. The establishment and operation of a natural gas pipeline or natural gas distribution network or LNG and/or natural gas storage facility are dependent upon obtaining licenses from the Ministry of Energy and Water. Furthermore, the Natural Gas Sector Law stipulates that the period of the foregoing license shall not exceed 30 years, subject to the discretion of the Minister of Energy.
- 3. Announcements made through the various media in May 2011, stated that the Ministry of Energy and Water is examining the option of introducing price controls on the natural gas sold in Israel. If such price controls are introduced and a maximum price is fixed that is lower than the prices set in the natural gas sales agreements of the partnerships, if such fixed price will be legally upheld, this could have an adverse effect on the businesses of Delek Energy and/or the partnerships, the volume of which derives from the maximum price that is set. On the other hand, price controls may make it more difficult for

competing suppliers to enter the market, thereby assisting the businesses of Delek Energy and/or the partnerships.

4. In May 2011 the Ministry of Energy and Water published a draft Petroleum Regulations (Transfer of Oil Rights), 2011, as amended in October 2011 ("the Rights Transfer Regulations"), the purpose of which is to regulate procedures for applications for the transfer of oil rights and/or benefits relating to oil rights (as defined in the transfer of oil rights regulations) by prescribing guiding terms and conditions according to which the Commissioner may accept such application, stipulate various conditions or reject it. Delek Energy estimates that approval of the current version of the transfer of rights regulations, if they are approved at all, could adversely affect operations in the oil and natural gas exploration and production sector in Israel, and this includes the operations of Delek Energy and/or the partnerships.
5. In addition, in October 2011 a committee was established to examine government policy relating to the natural gas sector and its future development in Israel. The committee is headed by Shaul Zemach, CEO of the Ministry of Energy and Water ("the Zemach Committee") and its objectives are - (1) to examine government policy models for the natural gas sector in countries with similar characteristics, while taking into account the unique geopolitical aspects of the State of Israel; (2) to examine and analyze domestic supply and demand based on a variety of scenarios; (3) to examine the appropriate policy to encourage and offer incentives for natural gas exploration and for developing the natural gas sector in Israel and maintaining reserves for supplying the domestic consumption needs and export of natural gas. As at reporting date, the Zemach Committee has not yet published its recommendations.
6. On January 30, 2012 the Ministry of Energy published draft Petroleum Regulations (Permission to deviate from the Planning and Building Law provisions) 2012, (below in this section - ("the draft regulations"), regarding onshore oil and natural gas exploration and which include orderly planning procedures which will apply to the regulation at all oil and natural gas exploration and drilling in Israel. It should be noted that Delek Energy is unable to assess whether the draft regulations will be adopted or not, nor to what extent. Since the draft regulations deal with onshore oil and natural gas exploration, as of reporting date, it is not expected to affect the businesses of Delek Energy and/or the partnerships.
7. Permits and licenses for production and transmission systems: As part of the development of the gas discoveries of the Yam Tethys Project partners, the partners in the Yam Tethys Project received permits and licenses under the Petroleum Law and Natural Gas Sector Law requiring the establishment, installation and operation of natural gas production platforms and pipeline from the production platform to the reception terminal close to the Eshkol power station in Ashdod.
8. Commissioner's directives regarding applications for receiving and/or transferring oil rights

From time to time the Commission of Petroleum Affairs publishes guidelines for submitting applications to be discussed by the Petroleum Council dealing with, inter alia, granting of rights, including minimum prerequisites for obtaining oil asset rights and the transfer of oil asset rights ("the Commissioner's guidelines"). These prerequisites include proof of professional and economic abilities, presentation of agreements for the project in the application, participation of an experienced operator holding at least 5% of the oil rights, etc.

Furthermore, the guidelines also stipulate that applications for the transfer of oil rights and/or benefits relating to oil rights will be discussed on the basis of the principles set forth in the transfer of rights regulations.

9. Petroleum Profits Taxation Law, 2011 ("the Petroleum Profits Taxation Law").

On April 12, 2010 the Minister of Finance appointed a committee to examine the fiscal policy relating to oil and gas resources in Israel ("the Sheshinski Committee"), with the aim of examining the fiscal system customary in Israel relating to oil and gas resources in Israel and recommending updated fiscal policies. The Sheshinski Committee recommendations were adopted by the government in January 2011.

As a result of the Sheshinski Committee recommendations, the Petroleum Profits Taxation Law was approved at the end of March 2011.

Legislation of the Petroleum Profits Tax Law resulted in a significant increase in the tax burden on the owners of the participation units and adversely affected the partnerships' businesses and operations. The partnerships are assessing their legal measures, specifically in respect of the applicability of the Petroleum Profits Taxation Law on oil rights granted to the partnerships prior to legislation of the foregoing law. For further information pertaining to the Petroleum Profits Taxation Law see Note 42A to the financial statements.

10. Cyprus

Oil and gas exploration operations are subject to regulation which includes requirements for permits, licenses or rights to perform the operations, requirements for the scope of investment and schedule for exploration, payment of royalties to the state, safety and environmental quality.

Hydrocarbons exploration and production operations in the Republic of Cyprus ("Cyprus") are regulated in the Hydrocarbons (Prospection, Exploration and Exploitation) Law, 2007 ("the Cypriot Law") and the Hydrocarbons (Prospection, Exploration and Exploitation) Regulations, 2007, 2009 ("the Cypriot Regulations"). The Cypriot Law and the Cypriot Regulations regulate operations in Cypriot territorial waters and in Cypriot exclusive economic zone. Furthermore, Cyprus is a full member of the EU and the EU directive concerning granting and use of hydrocarbon exploration and production permits (Directive 94/22/EC) and other relevant European legislature that also regulates hydrocarbon exploration and production operations in Cyprus and the Cypriot EEZ are applicable.

In 1988, Cyprus adopted the UN Convention on the Laws of the Sea (UNCLOS 82) and signed a number of agreements with its neighboring countries with regard to defining the Cypriot EEZ. Such agreements were signed with Egypt, Lebanon and Israel.

Under Cypriot Law and the Cypriot Regulations, a hydrocarbons exploration license is granted for an initial period of three years, which may be extended for two further two year periods. An exploitation license is granted under the Cypriot Law and the Cypriot Regulations, for 25 years and may be extended for a further 10 year period. An exploitation license relating to a commercial discovery during exploration will be issued following approval of a development and production plan, as set forth in the Cypriot Law and the Cypriot Regulations.

The relationship between the Republic of Cyprus and the license holder is prescribed under a production sharing contract ("the concession contract"). The concession contract prescribes the relationship, the liabilities and rights of the license holder and the fiscal terms applicable to the license holder.

11. USA

In the USA, oil and natural gas exploration and production rights are usually acquired from the landowners. Typically, only the oil and gas exploration and production rights are acquired, with other ownership rights in the real estate remaining with the land owner. In exchange for acquisition of exploration and production rights, the landowner usually receives current lease payments as well as royalties from the buyer if oil or gas is produced. The buyer of the rights is committed to minimal exploration operations to keep the exploration and production rights. If these commitments are not fulfilled, the landowner may sell these rights to a third party. Oil and gas exploration operations are subject to various laws, including environmental protection laws. These laws include provisions for prevention of land, water and air pollution.

1.11.27 Antitrust

- A. On October 11, 2000, the Antitrust Commissioner consented to a transaction in which the Israeli partners acquired the Reading & Bates rights in Yam Tethys project. This consent, as updated, is restricted by several conditions, and includes a condition that any purchase of holdings by the Company (including affiliates of the Group) of 5% or more in a corporation engaged in exploration, production, transmission, marketing or sale of natural gas in Israel, requires prior approval of the Antitrust Commissioner, if the corporation possesses any natural gas discoveries. It is hereby emphasized that the provisions of this sub-section do not apply to the Yam Tethys joint venture.

- B. On August 28, 2006, the Antitrust Commissioner consented to the transfer of the partnership rights in the Matan and Michal licenses to Noble as specified in section 1.11.5 above. The Antitrust Commissioner's decision was contingent on the following major conditions:
1. The "local corporations" (as defined below) would not hold jointly, whether on their own or with additional holders, any gas rights other than those directly and exclusively arising from the Matan and/or Michal licenses, without the express prior written consent of the Antitrust Commissioner. By December 31, 2006, the "local corporations" shall terminate any joint holding in gas rights, other than those directly and exclusively arising from the Matan and/or Michal licenses, which they held jointly on the decision date, whether on their own or with other holders, unless such joint holding is expressly permitted in writing by the Antitrust Commissioner.
 2. In any arrangement, agreement or understanding, oral or in writing, with regard to setting a mechanism or system for decision making between holders of Matan and Michal licenses for marketing natural gas produced under the Matan and Michal licenses, none of the "local corporations" shall individually own, directly or indirectly, any right or power to prevent the other holders from taking any decision or action for marketing natural gas produced under the Matan and Michal licenses.
 3. Definitions: the "local corporations" – Delek Group and Isramco; Delek Group – Avner Oil Exploration Limited Partnership and/or Delek Drilling Limited Partnership and/or any person affiliated with any of them; Isramco – and any affiliate.
- C. On September 6, 2011, each of the partnerships received a letter from the Antitrust Commissioner concerning a hearing on (1) the possibility of pronouncing it to be a monopoly together with its partners in the Yam Tethys project with regard to the current supply of natural gas from the project and together with its partners in the Tamar project with regard to the future supply of natural gas from the project; and (2) the possibility of, prior to such announcement, as a party in a restrictive arrangements with its partners in the Ratio Yam licenses.
- If the partnerships are pronounced to be a monopoly and restrictions are imposed on their operations, it will adversely affect the businesses of Delek Energy and/or the partnerships.
- D. If the partnerships are pronounced, following a hearing, to be a monopoly (with regard to the Yam Tethys project), Chapter D of the Antitrust Law will be applicable and restrictions may be imposed on their operations. If this does in deed take place, it could have an adverse effect on the businesses of Delek Energy and the partnerships.
- E. If the Antitrust Commissioner decides, following a hearing, to pronounce the partnerships as a future monopoly (with regard to the Tamar project) and/or decide that it is a party to a restrictive arrangement - Delek Energy believes that it has good legal and economic arguments against such pronouncement and/or decision.

1.11.28 Liens and guarantees

For further particulars relating to liens and guarantees, see Note 33 to the financial statements.

1.11.29 Material agreements

Below is a list of the material agreements to which Delek Energy and/or the partnerships are a party, including agreements that were in force during the period from January 1, 2011 through to reporting date or which affected the operations of Delek Energy and/or the partnerships during this period:

- A. For further information pertaining to the sale of natural gas from the Yam Tethys and Tamar projects see section 1.11.13(C) above.
- B. For details regarding the joint operating agreement in the Yam Tethys project see section 1.11.4(K) above.
- C. For information pertaining to the joint operating agreement in the Tamar project see section 1.11.5(L) above.
- D. For further information regarding the joint operating agreement in the Ratio Yam project see section 1.11.6(M) above.
- E. For details concerning the agreements for obtaining finance for the Yam Tethys project see section 1.11.23(D)(2) above.

- F. For information concerning the agreements for obtaining finance for the Yam Tethys project see section 1.11.23(E) above.
- G. For information pertaining to the agreement to obtain finance foregoing in the Leviathan project see section 1.11.23(F) above.
- H. Agreements pertaining to Block 12 in Cyprus
1. On January 22, 2009, the general partners in the limited partnerships signed an agreement (amended on March 2, 2010) with a related company of Noble ("Noble Cyprus") in which Noble Cyprus undertook to transfer to the general partner of each partnership 15% of a production sharing agreement with the Cypriot government ("the PSA"), subject to the approval of the Cypriot authorities ("the transfer agreement"). The PSA grants oil and/or gas exploration and production rights in the Cypriot territorial waters known as Block 12, located 15-20 km west of the Alon licenses (Block 12") and inter alia, the agreement stipulates the agreement period (which was set according to the progress of the work stages), the project area, project work plan, guarantees to be provided to ensure that the work will be carried out, tax provisions, bonuses payable according to project development stages, and the right of Cyprus to a share in any oil and/or gas that may be recovered, if recovered, according to the arrangements defined in the PSA.
 2. Subsequently, on January 22, 2009 each of the partnerships engaged in an options agreement with its general partner (which was amended on December 29, 2009, on December 20, 2010 and on August 7, 2011), ("the option agreement") to receive all the rights that will be transferred to the general partner under the aforesaid transfer agreement, once these have been granted.
 3. On August 21, 2011, an agreement was signed between Noble Cyprus and the general partner of each partnership (who engaged in an agreement in the name of the general partner and in the name of each partnership), amending the transfer agreement, and which specified that, subject to obtaining approval of the Cypriot government, each of the general partners will transfer to the partnership all of their rights, obligations and liabilities under the transfer agreement. The aforesaid agreement also stipulates that each partnership will bear 15% of the amounts expended by Noble due to operations carried out in Block 12 under the PSA, and also prior to obtaining approval of the Cypriot authorities for transferring the rights into the names of the partnerships and without them being a party to the PSA. This agreement also states that until the Cypriot authorities approve the transfer of the rights to the partnerships as aforesaid, the partnerships will not have any access to information or data relating to the activities in Block 12 and which are confidential under the PSA and that Noble has absolute discretion in carrying out such activities and that the partnerships have no say in the decision concerning the drilling, drafting of the drilling plan or fixing drilling dates. The transfer agreement will terminate on the earlier of the following dates: (1) expiry of the PSA; (2) with regard to each general partner, the date on which the transfer of rights to each of them is completed; and (3) August 1, 2013. If, prior to August 1, 2013, any of the general partners will choose to transfer its rights to any third party that is acceptable to Noble, and which will undertake the provisions of the transfer agreement, and such transfer will be approved by the Cypriot government, the provisions of the agreement will apply to the foregoing transfer, respectively.
 4. Concurrent with the signing of the transfer agreement, the general partners and Noble Cyprus signed a JOA applicable to Block 12, in order to regulate the operation if the foregoing transfer is approved. The JOA covers the same issues included in the JOA for the Yam Tethys project described in section 1.11.4(K) above, wherein resolutions are adopted by a decisive majority vote of at least two participants that are not related parties and that jointly hold at least 65% of the license rights. In addition, Noble was appointed as the operator.
 5. It is noted that under Regulation 8 of the Income Tax (Deductions from revenues of oil rights holders) Regulations, 1956, the Commissioner of Petroleum Affairs has confirmed the applicability of the regulations to the partnerships on Block 12 as well, subject to the conditions set by him.
 6. On December 9, 2011, a letter was received at Noble Cyprus offices from the Minister of Commerce Industry and Tourism of Cyprus (in charge of energy issues in Cyprus), which states that on November 29, 2011 the Council of Ministers of the Republic of Cyprus

decided, based on Noble's application of July 11, 2011 (and the information specified therein and attached thereto) to partially assign the rights in the PSA and exploration license for Block 12 (in this section - "the License") and to approve assignment of 30% (15% to Avner Partnership and 15% to Drilling Partnership) of revenues to which Noble is entitled under the PSA and the license ("the assignment"). According to the foregoing letter, the above assignment is subject to the following terms: (1) the participation of the partnerships will not be as an operator as defined in the PSA and the license; (2) all the other obligations and rights of Noble under the PSA and the license will remain unchanged and Noble Cyprus will continue serving as the only operator and will exclusively bear all the obligations under the PSA and the license. The partnerships and Noble Cyprus are working with the authorities in Cyprus to complete the rights transfer process so that the partnerships will be a party to the PSA and the license.

I. Agreements concerning royalty payments to Delek Energy by Delek Drilling Partnership

1. Delek Energy and Delek - The Israel Fuel Corporation Ltd. ("Delek Israel" and "the transferors", accordingly) and the general partner of Delek Drilling Partnership, on behalf of the partnership, signed an agreement in 1993 for the transfer of rights. On March 30, 2000, the right of Delek Israel was transferred to Delek Investments as part of reorganization in the Company.
2. Under the agreement, the transferors transferred to Delek Drilling Partnership rights in several licenses and Delek Drilling Partnership undertook to pay the royalties to the transferors, at rates set forth below, out of the Delek Drilling Partnership's share of oil, gas or any other material of value produced and used from the oil assets in which Delek Drilling Partnership has or will have an interest (before deduction of any royalties, but after deduction of oil used for production).
3. The rates of the royalties paid to the transferors are as follows: until such date as the investment of Delek Drilling Partnership is recouped, royalties will be paid at a rate of 5% of onshore oil assets and 3% of offshore oil assets. After this date royalties will be paid at a rate of 15% of onshore oil assets and 13% of offshore oil assets.

The term "investment return date" means the date, subsequent to the signing of the rights transfer agreement, on which the value of revenues (net) (as defined below) which Delek Drilling Partnership received or is entitled to receive for oil and/or gas and/or any other material of value produced and used from the oil asset (i.e. license or lease) under which the discovery is found, calculated in USD (at the representative exchange rate published by Delek Israel), will be equivalent to the full value of the amount expended by Delek Drilling Partnership in that oil asset (as defined below), calculated in USD (at the foregoing exchange rate).

The term "value of revenues (net)" means the value of all revenues, as confirmed by the accountants of Delek Drilling Partnership, for oil and/or gas and/or other material of value produced and used from the oil asset (i.e. license or lease) ("the value of revenues (gross)") less all the production costs and royalties paid for them.

The term "value of the amount expended by Delek Drilling Partnership" means all the expenses expended by Delek Drilling Partnership in the oil asset (i.e. license or lease) in which the oil and/or gas and/or other material of value was produced, excluding expenses (up to the value of the royalties (net)) deducted from the value of revenues (gross) for the purpose of determining the value of all revenues (net) and as will be confirmed by the accountants of Delek Drilling Partnership.

4. The transferors or any of them will be entitled to receive the foregoing royalties or part thereof in kind, i.e. to receive in kind part of the oil and/or gas and/or other material of value produced and used from the oil assets in which Delek Drilling Partnership has an interest (up to the rate noted above). If one or both of the transferors choose to receive royalties in kind, the parties will settle the manner and dates on which the transferors will be expected to receive the royalty. Should one of the transferors choose not to receive royalties in kind, Delek Drilling Partnership will pay that transferor the market value, in USD, or (if under the law it is only able to pay in Israeli currency) in Israeli currency, calculated in USD at the representative exchange rate of the USD upon actual payment, of the royalties due to the transferor. Such payment will be made once every month. The quantities of oil and/or gas and/or other material of value produced or used from the oil asset for the purpose of calculating the royalties due to the transferor will be measured in accordance with the customary principles in the oil industry.

5. Delek Drilling Partnership will keep full and precise records of its share in the oil and/or gas and/or other materials of value produced and used from the oil assets in which it has an interest. Each of the transferors will be entitled to appoint an accountant who will be entitled to review, examine and copy, during regular business hours, the ledgers of Delek Drilling Partnership and other documents and records pertaining to the transferors' rights to receive royalties under the rights transfer agreement.
 6. The right to receive royalties as aforesaid will be linked to Delek Drilling Partnership's share in each of the oil assets in which it has an interest. If Delek Drilling Partnership will transfer its rights in an oil asset in which it has an interest, Delek Drilling Partnership will cause the receiver of the transfer to undertake all the obligations to pay royalties as aforesaid. The foregoing does not apply in the event of forfeiture of an asset due to Delek Drilling Partnership being past due.
 7. In 2002, the agreement between Delek Drilling partnership and the transferors appointed an expert arbitrator to determine the correct meanings of certain definitions and terms relating to royalties owed by Delek Drilling Partnership as aforesaid, and mainly relating to the definition of "the investment return date" with regard to the Yam Tethys project. The appointed arbitrator expressed his opinion, inter alia, on the calculation method and different elements that should be considered when determining the investment return date, including
 - A) that only revenue received for oil and/or gas and/or other materials of value ("the oil and/or gas") which is produced and used from the oil assets (and confirmed as such by the accountants for Delek Drilling Partnership) should be taken into account; and
 - B) that only the value of the expenses expended by Delek Drilling Partnership in the oil asset (license or lease) in which the oil and/or gas was produced (and confirmed as such by the accountants for Delek Drilling Partnership) should be taken into account; and that should expenses be expended in more than one oil asset as aforesaid, the expense should be split between the oil assets in which it was expended and/or which it was meant to serve. Thus, an expense which was expended in oil asset A from which, at the end of the day, no oil and/or gas was produced, will not be taken into account for the purpose of determining the investment return date for oil asset B from which oil and/or gas was produced; and
 - C) that the expense with regard to exploration operations (including onshore drillings) will be taken into account as an expense in the oil asset within which it was expended for the purpose of determining the investment return date, and this is also the rule for development as well as for exploration to find the boundaries of the field; and with regard to installations (onshore and on the continental shelf), including for production, treatment, transmission, measurement, storage, operations, maintenance and operating costs, and marketing and sales costs (including sales agreements) of the gas; and
 - D) that with regard to an expense taken into account for the purpose of determining the investment return date, the expense expended must be taken into account in full (without amortization) and financing expenses are not to be taken into account; and
 - E) that the investment return date is determined only once, and once it is determined there is no going back, even if another situation is created where the expenses in the oil asset exceeds revenues received from the production of oil and/or gas from that oil asset.
- J. Delek Drilling Partnership and Avner Limited Partnership agreements
1. Each of the partnerships were incorporated under the agreement between their general partner and their limited partner. Most of the provisions in the limited partnership agreements of Delek Drilling and of Avner are essentially similar. Below is a summary of the main provisions of the above agreements ("the limited partnership agreement"):
 - A) The limited partnership agreement was signed between the general partner and the limited partner (and trustee).
 - B) The goals of the partnerships are to participate in oil and/or gas exploration in geographical regions specified in the limited partnership agreement.

- C) The main expenses of the partnerships will be "exploration and development expenses" as defined in the Income Tax Regulations (Rules for Tax Calculation on Holding and Sale of Participation Units in an Oil Exploration Partnership), 1988.
 - D) The general partner of each partnership is entitled to 0.01% of revenues and is liable for 0.01% of expenses and losses of the limited partnership, as well as for expenses and losses of the limited partnership for which the limited partner may not be liable, due to restrictions pertaining to the limited partner.
 - E) According to the limited partnership agreement, the general partner will manage all of the limited partnership affairs at its discretion and to the best of its ability, and shall endeavor to implement the goals of the limited partnership as set out in the limited partnership agreement. A supervisor is appointed to each partnership and given certain specific supervisory authority intended to protect the interests of holders of participation units. The general partner is entitled to monthly management fees of USD 40,000 and to reimbursement of certain direct expenses allowed under the limited partnership agreement.
 - F) The limited partnership agreement stipulates that all of the limited partnership's profits, which are lawfully distributable by the partnership as profits after deduction of amounts (excluded in determining the profit) required by the partnership - will be distributed to the partners, pro rata to their rights, as set out in the limited partnership agreement.
 - G) The general partner and/or employees and/or management shall not be liable to the limited partnership nor to the limited partner for any act or omission made on behalf of the limited partnership under authority granted to the general partner within or pursuant to the agreement or by law, unless the acts were committed fraudulently or willfully or constitute gross negligence. The limited partnership agreement also includes provisions relating to insurance and indemnification of the general partner.
 - H) The term of the limited partnership remains in effect as long as the limited partnership owns, directly or indirectly, a valid oil asset or rights therein or in any oil or gas to be produced. The limited partnership shall be terminated before the specified dates if it is disbanded earlier by order of the limited partnership agreement or by law or by the partners' consent.
2. It is noted that the limited partnership agreement of Avner Partnership stipulates that the general partner may serve as operator of oil exploration operations in areas where the limited partnership has interests, and will be eligible to be appointed operator in areas where it may have interests in the future.
 3. Furthermore, the limited partnership agreement of Avner Partnership specifies the right to royalties at 6% of the entire share of Avner Partnership in oil and/or gas and/or any other material of value produced and exploited from oil assets where Avner Partnership has, or may have in the future, an interest (before deduction of any royalties, but after deduction of oil used for production. It should be noted that Delek Investments is eligible to 1% of the aforementioned 6%

K. Agreement concerning the export of LNG

1. On November 13, 2011 the partners in the Tamar and the Dalit projects, including the limited partnerships, (in this section - "the Tamar Project Partners") signed a Memorandum of understanding with Daewoo Shipbuilding and Marine Engineering Co. Ltd.²⁰⁸ ("DSME") and D&H Solutions AS²⁰⁹ ("D&H") (together - "the buyers") which came into effect on November 22, 2011 with regard to examining an agreement whereby the Tamar project partners could sell natural gas to the Buyers for converting it to LNG and

²⁰⁸ To the best of the Company's knowledge, DSME is a foreign company registered in South Korea (the company's head office is located in Seoul), which owns a leading international shipyard in South Korea. DSME has business connections with large shipping companies and oil companies worldwide and is known as a leading world class company specializing in shipbuilding and as an offshore contractor with over 30 years experience. DSME has the resources required and modern facilities enabling it to build and establish the complex infrastructures required for a FLNG (floating liquefied natural gas) venture.

²⁰⁹ To the best of the Company's knowledge, D&H is a joint venture incorporated as a registered partnership in Hungary between DSME and Hemla II. D&H operates in the development of solutions for natural gas reserves around the world in collaboration with strategic partners and with owners of gas reserves.

exporting it to South Korea and/or other countries that will be agreed by the parties ("the memorandum of understanding").

Main points of the memorandum of understanding

The buyers intend to liquefy the natural gas using a floating liquefied natural gas facility to be constructed and financed by the buyers and positioned in the Tamar and/or Dalit gas field and from there, to be transported in special tankers to target markets ("the FLNG facility").

The parties to the memorandum of understanding decided that in the first stage, which is expected to continue for three months, the initial front-end engineering design (pre-FEED) will begin to define the parameters required for the detailed plan ("the first stage").

After the first stage (if the Tamar project partners and the FLNG partners so decide), the second stage of the detailed front end engineering design (FEED) will begin, which is expected to continue for nine months ("the second stage").

At the end of the second stage and subject to a decision on the final investment (if the Tamar project partners and the FLNG partners so decide), construction of the FLNG facility in Korea, development drillings and construction of a special production system at the Tamar and/or Dalit gas field will begin. This stage is expected to continue for three or four years.

Concurrent with the foregoing detailed engineering planning, the parties intend to negotiate an agreement for the supply of natural gas by the Tamar project partners to the FLNG for 15 to 20 years, in quantities required to produce 2-3 million tons per annum (MTPA) of LNG, meaning estimated annual gas sales of between 3 BCM and 4.5 BCM.

The price that the buyers will pay for natural gas is expected to be a factor of LNG selling prices by the buyers and the expected costs of liquefaction and transportation. According to indications and certain assumptions provided by the buyers, including current LNG prices, and based on the price of USD 100 per barrel of oil, it is expected that the Tamar project partners will be paid between USD 7 and USD 9 per MMBtu of natural gas. Actual revenue will be a factor of a range of considerations, including those described above and the prices of fuels when supplied.

Each of the partners in the Tamar project will be given the right to participate in the establishment of the FLNG facility in a scope and under terms to be agreed between the parties.

It is further emphasized that this is a memorandum of understanding only and development through the FLNG facility, including the actual supply of gas, is subject to engineering and economic feasibility studies as well as negotiations for a series of contracts, including a binding contract for the sale of gas, and obtaining all the approvals required by law.

2. Subsequent to the memorandum of understanding, the buyers are currently carrying out the pre-FEED planning to examine and define the required parameters for the detailed planning. At the same time the buyers, through a special purpose company established together with Next Decade LLC for marketing LNG ("the marketing company") to manage negotiations with potential buyers of LNG that will be liquefied at the FLNG facility.

Subsequently, on March 21, 2012 a memorandum of understanding was signed between the marketing company and Gazprom Marketing & Trading Switzerland AG ("Swiss GM&T"), a subsidiary of Gazprom Marketing & Trading Limited²¹⁰, according to which the parties will negotiate exclusivity for selling and buying LNG liquefied at the FLNG facility ("the letter of intent"). The main points of the negotiations are for supply starting in 2017 of MTPA2-3 of LNG at a price that will be calculated on the basis of fair LNG market prices in Asia or other pricing mechanisms that will be agreed upon by the parties.

²¹⁰ To the best of the Company's knowledge, Gazprom Marketing & Trading Limited is a company is registered in the UK and is a wholly owned subsidiary of the Gazprom Group, which is the largest global gas company (based on assets) that holds approx. 17% of the gas reserves worldwide and 70% of the gas reserves in Russia. Gazprom Marketing & Trading Limited, whose management is based in London, was established in 1999 to manage marketing and trading operations in deregulated markets in Europe and since 2005 is responsible for all aspects of marketing, transmission and trading of LNG for the Gazprom Group. Swiss GM&T was established in 2011 as a base for the development of trade in oil, LPG and LNG with the advantages in being located in Switzerland, in central Europe.

It is noted that under the memorandum of understanding, the Tamar project partners will be granted the right to participate in the marketing company and in the FLNG facility, under terms that will be agreed upon by the parties.

It is further emphasized that this is a non-binding memorandum of understanding only and that the execution of the foregoing FLNG project, including the actual supply of gas, is subject to engineering and economic feasibility studies as well as negotiations for a series of contracts, including binding contracts for the sale of gas and the sale of LNG, and obtaining all the approvals required by law.

Forward looking information: The above estimates concerning the partnerships' engagement in the memorandum of understanding and regarding the letter of intent is forward looking information as defined in the Securities Law, and there is no certainty that it will materialize, in full or in part, in the aforesaid manner, and may materialize in a substantially different manner, in particular (1) it is not at all certain that a binding contract will be signed under the terms set out above or under other terms, and the signing as aforesaid is subject, inter alia, to agreement between the parties of the terms of the binding contract and receipt of approval from the certified authorities and required permits under any law, if required; (2) the FLNG facility is innovative technology which is still in development stages and there is still no certainty regarding its reliability, its effectiveness, the costs involved and its suitability for the Tamar and Dalit leases; (3) also, following signing of a binding contract, there is no certainty that the partners in the FLNG facility or the Tamar project partners will decide to continue with the project; (4) and, following the signing of a binding contract and completion of all the project stages, there is no certainty concerning the actual supply of gas, and there is no certainty concerning the volume of supply and/or that the scope of revenue for the natural gas will be as estimated above, and these are dependent upon, inter alia, the terms of the supply contract, the size and scope of the operations of the project operations, the LNG supply volume, the global prices of fuels and LNG, the costs of the project, or if any of the risk factors involved in the partnership's operations and the development of the Tamar project will materialize (the lack of means for development and production, the realization of technological risks, regulatory changes, etc).

L. Agreements for the sale of rights in the Ruth D and Alon E licenses

1. On February 23, 2011, the partners in the 361/Ruth D and 368/E Alon licenses ("the Ruth D and Alon E licenses") signed contingent agreements with third parties for the sale of part of their oil rights in the Ruth D and Alon E licenses (in this section: "agreements for sale of the rights"). According to these agreements, the partners in the Ruth D and Alon E licenses will transfer (each according to their proportionate share in the licenses), 50% of the participation rights (out of 100%) in each of the Ruth D and Alon E licenses, subject to fulfillment of the preconditions.

2. The buyers of the rights in Ruth D and Alon E licenses, and their proportionate share in each of them (after transfer of the rights, to the extent that this is completed) are as follows:

17.5% Israel Land Development Co. – Energy Ltd. ("ILDC – Energy") (in the Alon E license, 5% of the rights were acquired by Israel Land Development Co. Ltd. – "ILDC").²¹¹

17.5% ProSeed Venture Capital Management (1999) Ltd.²¹²

15.0% - Ellomay Capital Ltd.²¹³

According to the sales agreement, the consideration for the rights in the Ruth D and Alon E licenses is as follows:

²¹¹ To the best of the partnership's knowledge, ILDC – Energy Ltd. is controlled by ILDC, which owns 69.69% of its shares. ILDC is a public company traded in Israel, controlled by Yaakov Nimrodi, who owns 42.45% of its shares and Ofer Nimrodi, who owns 28.43% of its shares.

²¹² To the best of the Company's knowledge, ProSeed Venture Capital Management (1999) Ltd. is a private company registered in Israel. The company is fully controlled by Landlan Investments Ltd., which is controlled by Ligad Rotlevy, Yair Rotlevy and Yeschayahu Landau through a private company.

²¹³ To the best of the company's knowledge, Ellomay Capital Ltd. ("Ellomay") is an Israeli company traded on the NASDAQ. The controlling shareholders are Shlomo Nehama, who holds 37.3% of its shares and Kanir Joint Investments (2005) Limited, holding 33.3% of its shares.

3. At the completion date of the transaction: 1) reimbursement of USD 588 thousand to the Delek Drilling Partnership and Avner Partnership for prior expenses in the Ruth D and Alon E licenses; 2) reimbursement of expenses covered by the partnerships for their proportionate share in purchase of the rights in the Ruth D and Alon E licenses, from the signing date through to the completion date.
4. For the first drilling in the Ruth D and Alon E licenses ("the initial drilling"), if it is drilled: the partnerships will be entitled to creditor's rights for 30% of their rights, so that the buyers will cover, in addition, their proportionate share in the expenses of the first drilling, with an additional share equivalent to 7.5% of the cost of the first drilling up to the total cost (100%) of USD 50 million ("the creditor's rights").
5. Overriding royalties of 3% of the rights transferred by the partnerships in the Ruth D and Alon E licenses for all oil and gas produced.
6. The partnership may convert, up to the start date of the first drilling, the balance of their partnership rights to overriding royalties of 3% of the transferred rights.
 - A) It is clarified that the rights transfer agreements are subject to approvals, including approvals that are required according to the limited partnership's agreements and the partnership's escrow agreements, approvals of the certified organs of the buyers and the approval of the Commissioner of Petroleum Affairs to transfer the transferred rights in the Ruth D and Alon E licenses, at the dates set out in the agreements. After approval of the transfer of the transferred rights to the buyers, each partnership will own 12.5% of the rights in the Ruth D and Alon E licenses.
 - B) Furthermore, with regard to the arrangement applicable to the holders of royalty rights relating to the transferred rights in the Ruth D and Alon E licenses, see below.
 - C) On November 29, 2011, the Commissioner of Petroleum Affairs gave notice that since the application for the transfer of rights required in the Ruth D and Alon E licenses was not completed, these licenses would not be extended. Delek Energy is of the opinion that all the preconditions for obtaining the Commissioner's approval for the transfer of rights under the Ruth D and Alon E licenses have been fulfilled and therefore Delek Energy intends taking action to transfer the rights in the Ruth D and Alon E licenses and to examine the legal options open to it to exercise its rights in these licenses, including examining the option of filing an appeal.

M. Agreements for the sale of rights in the Avia and Keren licenses

1. On February 23, 2011, the partners in the 337/Avia and 338/Keren licenses ("the Avia and Keren licenses") signed contingent agreements with third parties for the sale of part of their oil rights in the Avia and Keren licenses. According to the agreements, the partners in the Avia and Keren licenses (each according to their proportionate share in the licenses) will transfer, subject to the fulfillment of preconditions, 75% of the participation rights in each of the Avia and Keren licenses. ("the contingent agreement")
2. The buyers of the rights in the Avia and Keren licenses, and their proportionate share in each of them (after transfer of the rights, to the extent that this is completed) are as follows:
 - 50%: ATP East Med Number 1 BV²¹⁴ and ATP Oil & Gas Corporation²¹⁵ (together: "ATP")
 - 10%: Modiin Energy Limited Partnership²¹⁶
 - 10%: Ellomay Capital Ltd.²¹⁷
 - 5%: Odin Energy Ltd.²¹⁸

²¹⁴ To the best of the Company's knowledge, ATP East Med BV Number 1 is a private company registered in Holland, and is wholly owned by ATP East Med BV, which is wholly owned (through Netherlands) by ATP Oil & Gas BV) of ATP Oil & Gas Corporation.

²¹⁵ To the best of the Company's knowledge, ATP Oil & Gas Corporation is a public company traded on the NASDAQ and registered in Texas, USA. The company has no shareholders owning more than 25%.

²¹⁶ To the best of the Company's knowledge, the controlling shareholder in the partnership is Modiin Energy Management (1992) Ltd, controlled by Yitzhak Sultan and IDB Development Company Ltd.

²¹⁷ For further information about Ellomay, see section 1.11.29(L) above.

²¹⁸ To the best of the Company's knowledge, Odin Energy Limited is a private company registered in Israel. The company is owned by ARIB Energy (2011) Ltd. (a company wholly owned by Ram Belinkov, owning 50% of the company, and by Adonan Ltd. (a company wholly owned by Benny Rosenberg), owning 50% of its shares.

3. According to the sales agreements, consideration for the rights in the Avia and Keren licenses will be as follows:
 - A) At the completion date of the transaction: 1) reimbursement of expenses of USD 2.671 million to the partnerships for prior expenses in the Avia and Keren licenses; 2) reimbursement of expenses covered by the partnerships for their proportionate share of the purchase of the rights in the Avia and Keren licenses, from the date of signature through to the completion date.
 - B) For the first drilling in the Avia and Keren licenses (in this section: ("the initial drilling")), if it is drilled: the partnerships will be entitled to creditor's rights for 30% of their rights, so that the buyers will cover, in addition, their proportionate share in the expenses of the first drilling, with an additional share equivalent to 7.5% of the cost of the first drilling up to the total cost (100%) of USD 50 million ("the creditor's rights").
 - C) Overriding royalties of 3% of the rights transferred by the partnerships in the Avia and Keren licenses for all oil and gas produced.
 - D) The partnership may convert, up to the start date of the first drilling, the balance of their partnership rights to overriding royalties of 3% of the transferred rights.
4. In the sale of rights in the Avia and Keren licenses, it was agreed that ATP would be appointed operator of the joint venture in the license areas, according to the provisions of the JOAs that were signed when the agreement was signed, which will come into effect after approval and completion of the transfers.
5. It is clarified that the agreements are subject to approvals, including approvals that are required according to the limited partnership's agreements and the partnership's escrow agreements, approvals of the certified organs of the buyers and the approval of the Commissioner of Petroleum Affairs to transfer the transferred rights in the licenses and to appoint ATP as operator of the Avia and Keren licenses, at the dates set out in the agreements. After approval of transfer of the transferred rights to the buyers, the percentage of the participation rights of the partnerships in the Avia and Ruth licenses will be 12.5%.
6. On September 19, 2011, ATP informed the partnerships that it was canceling the contingent agreement prior to receiving the approval of the Commissioner of Petroleum Affairs for the transfer of rights as specified above, and this even though, to the best of Delek Energy's knowledge, all the preconditions for obtaining the approval of the Commission for the transfer of rights were fulfilled as aforesaid.
7. On November 29, 2011, the Commissioner gave notice that the Avia and Keren licenses would not be extended for the following reasons: failure to comply with the terms of the work plan in the foregoing licenses; to date the transfer of rights process is incomplete; an amended application was not submitted following the withdrawal of the proposed operator and prior to receiving clarifications in view of the Antitrust Commissioner's announcement as set out below.
8. The partnerships are of the opinion that all the conditions for obtaining the approval of the Commissioner for the transfer of rights were fulfilled and that the Commissioner's delay in deciding led to the withdrawal of the proposed operator.
9. On November 16, 2011 the partnership proposed an alternative operator to the Commissioner. Edison International S.P.A. ("Edison") and requested his urgent approval.
10. On January 30, 2012, the partnerships submitted an appeal to the Minister of Energy to the decision of the Commissioner not to freeze the work plan under the terms of the Avia and Keren licenses and not to extend their validity.
11. On March 19, 2012, the partnerships signed a contingent agreement with Edison for the sale of part of its oil rights in the Avia and Keren licenses, according to which, inter alia, the partnerships will transfer, subject to compliance with preconditions including acceptance of the appeal submitted by the partnerships to the Minister of Energy as aforesaid, and renewal and extension of the Avia and Keren licenses, 50% of the participation rights in each of the Avia and Keren licenses

N. Rights of the royalty holders in the rights transferred in the agreements set forth above:

Furthermore, the partnerships and the holders of royalty rights, as set out in section 1.11.29(S) above (in this section - "the royalty rights holders"), have an agreement concerning the transferred rights, as follows:

The royalty rights holders will be entitled to royalties at a rate of 13% of the royalties that the partnerships will be entitled to under the rights sale agreements (9.75% to Delek Energy and 3.25% to Delek Investments), similarly the royalty rights holders will also be entitled to a pro rata share in the value of the rights actually paid, at a rate equivalent to the rate of the royalty. It is hereby clarified that if the partnerships decide to convert their rights in the licenses for additional royalties as aforesaid, the same arrangement as specified above will also apply to these royalties.

1.11.30 Legal proceedings

In the matter of the claim filed at the Tel Aviv District Court against Yam Tethys Ltd. and a number of other defendants, see Note 32(A)(6) to the financial statements.

1.11.31 Business objectives and strategy

Delek Energy believes that the scope of the significant natural gas resources discovered in the projects which the partnerships are involved in, especially in the Tamar and Leviathan discoveries, along with the oil assets and other explorations held by the partnerships in the territorial waters of Israel and Cyprus, preserve the partnerships' status (together with their partners) as the industry leaders in Israel and Cyprus and also incorporate potential for growth and generation of value.

In view of the aforesaid, the partnerships' operating strategy and objectives are to expand and assimilate the use of natural gas in the Israeli economy and supply its needs alongside promoting and developing markets and infrastructures to allow exporting natural gas.

A. Yam Tethys project

Maximum production of natural gas from the Mari B reservoir with the aim of bridging the customers' requirements until delivery of gas from the Tamar reservoir.

Development of the Noa reservoir and the Leviathan reservoirs of Mari B (Pinnacles), if natural gas in sufficient quality and quantity is discovered there, using the production facilities of the Yam Tethys project to assist in bridging the customers' needs.

Preparing the production facilities of the Yam Tethys and the Mari B reservoir as part of the Tamar project development plan, including providing strategic and operating storage services of natural gas for the Mari B reservoir.

B. Tamar project

Developing the Tamar project, with the aim of enabling commencement of the supply of natural gas from the project to the Israeli economy in the first half of 2013.

Exercising of signed agreements, and negotiations and additional agreements for the sale of natural gas to potential consumers in Israel.

Promoting construction of the floating facility (FLNG), which will be located on a dedicated ship above the Tamar reservoir. The partnerships intend to continue reviewing and promoting the terms required to establish this type of project, including reviewing the FLNG technologically, signing agreements to sell natural gas and/or LNG as part of the project, financing establishment of the facility and ensuring the appropriate regulatory conditions.

Raising non-recourse project finance for the partnerships' share in the Tamar project development costs. Raising this finance might be affected by regulatory aspects and the Israeli and global capital markets.

C. Ratio Yam project

Continuing the review and assessment of the Leviathan reservoir and preparing a gas commercialization plan to allow outlining the development plan of this reservoir and other adjacent discoveries. Ensuring the export of critical mass natural gas, which requires setting up of export infrastructures, is an essential economic condition for development drilling of the Leviathan reservoir and adjacent discoveries (including Dolphin and Tanin).

D. Block 12, Cyprus

Continuing the evaluation of the Aphrodite reservoir resources along with promoting the examination of alternatives for commercializing the gas both for the Cypriot market and for export, including the option of integrating the development of the reservoir with that of Leviathan.

E. Oil and gas exploration in the exploration areas

Continuing the exploration efforts in the offshore oil concessions off the coast of Israel, focusing on the oil licenses with the greatest potential and performing additional exploration drillings, taking into account the results of the drillings and surveys conducted by the partnerships, including moving the Leviathan 1 well. Without securing the commercialization horizon of natural gas through export, there is no economic justification to continue exploration for natural gas.

F. Export

Following the discovery of considerable gas reserves in the Tamar and Leviathan reservoirs and additional discoveries, and due to the potential in other exploration areas in which the partnerships operates, they are examining various options for commercializing the gas, including the option of exporting and selling it on the international market. The partnerships are examining, inter alia, the option of exporting the gas in two main ways: (1) pipelines; (2) liquefaction and delivery as liquid natural gas (LNG) in dedicated tankers, and are negotiating with various parties which may participate in projects, as set forth above. In general, the infrastructure costs for delivering the gas as set out above are very high.

Pipeline: The partnerships are assessing the option of exporting natural gas through a pipeline to various countries, mainly Turkey, Greece and Cyprus, to supply natural gas to these markets and/or to connect the existing and/or planned pipeline of these countries to that of other European countries. A preliminary examination carried out for the partnerships indicates that installation of a pipeline to these countries, and from these countries to other European countries, is an extremely complex and expensive engineering project. The partnerships are also exploring the option of supplying natural gas to the Palestinian Authority and neighboring countries to meet the demand for natural gas in these markets. In addition, the partnerships are also exploring the option of exporting natural gas for the existing LNG plants in Egypt.

Liquefaction (LNG): The partnerships are exploring the option of liquefying the gas and transporting it as LNG in designated tankers to countries where there is a demand and infrastructure for importing LNG and to countries that are examining the option of establishing infrastructure to import LNG. The total global LNP trade in 2010 amounted to 297 BCM and from initial data, it appears that in 2011 the trade exceeded 330 BCM, an increase of 11%. The main market that consumed more than half of this quantity is in East Asia. The consumption leaders in East Asia in 2011 were Japan, which following the Fukushima nuclear reactor disaster and as an alternative to nuclear energy, increased its consumption of natural gas from 93 BCM to 100 BCM; South Korea, which consumed 50 BCM and Taiwan which consumed 16 BCM. Another significant market for LNG is Europe, which is responsible for 25% of the total LNG consumption worldwide. The European LNG consumption leaders in 2011 are the UK (26 BCM), Spain (24 BCM), France (14 BCM) and Italy (8.6 BCM).

Establishment of a conventional onshore liquefaction plant requires allocation of land close to the coastline and involves more substantial costs. The partnerships have started examining potential onshore sites to establish a conventional liquefaction facility. Another outline under examination by the partnerships is establishment of a floating liquefied natural gas facility (FLNG) on a dedicated ship in the gas field area. The partnerships have signed a memorandum of understanding with potential buyers to assess an agreement to sell natural gas in the Tamar project to convert LNG using a floating liquefaction facility and export it to South Korea and/or other countries to be agreed upon. Pursuant to the foregoing memorandum of understanding, these potential buyers signed a letter of intent according to which negotiations will be conducted and non-exclusivity to sell and purchase LNG liquefied through the liquefaction facility will be granted. For further information of these agreements, see section 1.11.29.K above.

Forward looking information: FLNG is a new technology which is currently still in its development stages and there is no certainty regarding its reliability, costs and its compatibility with the partnerships' projects. The partnerships' objectives and strategy, as described above, are general intentions and goals, and as such there is no certainty that they will be realized,

inter alia, due to changes in the projects, changes in the market situation, regulatory and tax law changes, changes in priorities resulting from findings of future drilling and surveys as well as due to unexpected events and a range of risk factors connected to natural gas exploration.

In view of the aforesaid, the partnerships have started carrying out test, including techno-economical evaluation of gas liquefaction alternatives and economic and other conditions in the possible target markets, in order to define the technical feasibility and economic attractiveness of the alternatives for exporting natural gas from Israel, also taking into account recent developments in the global natural gas market.

Additionally, under certain circumstances, various products can be produced from natural gas (such as methanol and ammonia), which are easier to transport.

- G. The investments required for the partnerships' operations require them to invest substantial finances and to purchase know-how and other skills in current and future areas of operation. The partnerships intend to explore and take the necessary steps required to raise funds by the means available to them, including issuing rights and/or obtaining bank loans and/or issuing debentures.
- H. In view of the know-how and experience, specific technical and engineering capabilities, access to target markets and substantial investments required to establish an export infrastructure, the partnerships are exploring, including in cooperation with its partners in the Leviathan project, options for investments by strategic parties in their various assets and collaboration with them to allow them, inter alia, to promote developing the export of natural gas, continue maintaining their lead in their area of operation and contribute to their continued growth. It is uncertain whether the partnerships will succeed in their efforts to raise these finances and/or in creating these strategic collaborations.
- I. Furthermore, in view of the regulatory changes and challenges facing them, the partnerships are examining the option of structural changes and the option to be listed for trade or to list all or some of their assets for trade on another stock exchange around the world more suitable for natural gas exploration, production and export operations. It is uncertain whether the partnerships will succeed in these processes.
- J. The partnerships' objectives and strategy, as described above, are general intentions and goals, and as such there is no certainty that they will be realized, inter alia, due to changes in the projects, including the Tamar and Leviathan reservoirs, changes in the market situation, regulatory and tax law changes, changes in priorities as a result of drilling and survey findings as well as due to unexpected events and the risk factors described in section 1.11.33 below.

1.11.32 Insurance coverage

The partnerships and Delek Investment purchased insurance coverage for drilling and production in the Yam Tethys project, as set out below (the amounts of the insurance are correct as of the preparation date of the report). The insurance amounts and liability limits represent the share of the Israeli partners in the Yam Tethys project:

Insured amount in USD millions	Description of coverage
411	Offshore property, the Group's share in the production rig and offshore pipeline.
21	Onshore property including the Group's share in the onshore facilities.
<u>432</u>	Total property insurance
(1) 100 (2) 25 The total insurance amount will not exceed USD 100 million. (3) 5	Loss of income insurance: (1) For a covered event at the policyholder's facilities; (2) as the result of an event at IEC's facilities; (3) dedicated insurance for overriding royalties.
335 100	Political risk insurance including war and terror risk: (1) onshore and offshore property; (2) loss of income.

Delek Energy also purchased, together with the partnerships, Delek Investments and subsidiaries, liability insurance to cover their current operations and physical and property damage to third

parties due to drilling and production operations of these companies, including accidental pollution damage. This insurance has a liability limit of USD 25 million per case and cumulative for the insurance period covering the share of the partners in each of the projects, further coverage of USD 25 million per case and cumulative for the insurance period covering the share of the partners in each of the projects and a third coverage of USD 100 million per case and cumulative for the insurance period in terms of 100% of the rights.

Furthermore, Delek Energy, together with the other companies listed above, has purchased control of well insurance for drilling operations in the following insurance amounts:

For Yam Tethys and Noa drilling, a total amount (for 100% of the rights) of USD 150 million per case. For Leviathan 1, a total amount (for 100% of the rights) of USD 800 million per case. For Tamar, Dalit 1, Karish, Tanin, Block 12 in Cyprus, and Leviathan 2 and 3, this insurance covers a total amount (for 100% of the rights) of USD 200 million per case. For the Tzuk Tamrur drilling, this insurance has a liability limit (for 100% of the rights) of USD 25 per case and cumulative for the insurance period.

Delek Energy also purchased, together with others, all-risk insurance for the Tamar field development project of USD 2.2 billion for 100% of the rights.

Some of the insurance coverage described above was drawn up independently and some as part of Noble's insurance policies.

The insurances are subject to mortgage agreements and assignment of rights according to financing agreements that are prepared from time to time.

It is noted that from time to time, Delek Energy monitors changes in the value of the policyholder's property, to adapt the scope of insurance purchased to the exposure relative to the cost of the insurance and the insurance available internationally for the energy segment. Consequently, Delek Energy can decide to reduce the coverage purchased and/or the amount of the insurance purchased and/or can decide not to purchase any insurance for one risk or another.

1.11.33 Risk factors

Oil and gas exploration and the development of oil and gas discoveries involve large financial outlays with a high financial risk, primarily for reasons set forth below. This is even more significant for offshore oil exploration and production operations.

- A. Fluctuations in the dollar exchange rate: Delek Energy is exposed to fluctuations in the dollar exchange rate. As from January 1, 2008, the limited partnerships measure their results in US dollars, therefore every erosion in the dollar-shekel exchange rate will lower the revenue, net expenses and assets of Delek Energy, and consequently, will lead to a decrease in the equity and profits of Delek Energy. On the other hand, in 2007, Delek Energy started to raise dollar loans, therefore, every revaluation in the shekel-dollar exchange rate will result in revenue from exchange rate differences due to these loans. Furthermore, significant fluctuations in coal prices may lead to a change in the IEC's usage model, which could mean preference given to power stations fueled by coal compared with power stations fueled by natural gas and vice versa. In addition, the price of gas in some of the gas supply contracts signed by the Tamar project partners was derived from the price of electricity as defined by the Public Services Authority - Electricity from time to time (as set out in section 1.11.13(E) above), therefore a decrease in the electricity price will result in a decrease in the partnership's revenue from these agreements.
- B. Dependence on global fuel prices: The prices paid by consumers for natural gas in reservoirs in which the partnerships are party, are derived, inter alia, from prices of alternative energy sources to gas, such as oil and coal. A decrease in prices of alternative fuels could have an adverse impact on the price which the partnerships are able to obtain from its customers for natural gas sold by the partnerships and/or may influence the economic viability of production from the reservoirs discovered in the Tamar and Ratio Yam projects and any other reservoirs that may be discovered by the partnerships. Furthermore, significant fluctuations in coal prices may lead to a change in the IEC's usage model, which could mean preference given to power stations fueled by coal compared with power stations fueled by natural gas and vice versa.
- C. Competition for gas supply: To the best of Delek Energy's knowledge, at the reporting date there are three major competitors for gas supply in Israel (for further information, see section 1.11.16(A) above). However, further discoveries may lead to the entry of other competitors. In view of the relatively small gas sector in Israel, this competition may impair the ability of the partnerships and Delek Energy to market the gas reserves discovered by them or that will be

discovered in the future, having an adverse effect on the revenue of the partnerships and Delek Energy.

- D. Market size compared with size of reservoirs: The natural gas reservoirs discovered in the Tamar and Ratio Yam projects, Alon licenses and Cyprus project are considerably larger than the potential market in Israel and Cyprus, which is relatively limited. Accordingly, the operational results of the partnerships and Delek Energy are largely dependent on the possibility of commercializing the gas, including the possibility of exporting gas and selling it on the international market. The possibility of gas export and sales depend on several factors with high uncertainty, such as establishment of an export and transportation system subject to regulatory approvals, economic feasibility of establishing this system, identification of potential customers in the international market, and financing investments in development and establishment of the export system.
- E. Uncertainty regarding the construction of the national gas pipeline: The ability of the partnerships and Delek Energy to supply gas to other potential consumers and to increase the gas volume supplied to IEC is dependent, inter alia, on the completion and expansion of the national gas pipeline and the regional distribution networks.
- F. Absence of insurance cover: Although the Delek Energy and the partnerships have insurance policies to cover possible damages with regard to their operations, these policies do not cover all potential risks and therefore the insurance payout may not cover the full scope of damages and/or all potential losses (for third-party damages as well as for potential loss of income and establishment costs of the production system in the case of an event that causes damage to the production system). Accordingly, in the event of a large-scale disaster, the insurance amounts and liability limits set out in section 1.11.32 above may not cover the full amount of the damages. Furthermore, there is no certainty that appropriate policies may be purchased in the future under reasonable commercial terms, if at all. Moreover, for certain insurances, Delek Energy and/or the partnerships may decide not to take them out at all.
- G. Operational risks: Oil and gas exploration and production operations are exposed to all risks involved in exploration and production of oil and gas, such as uncontrolled gushing from the well, explosion, collapse and conflagration of the well, malfunctions, accidents and other events that could impair the performance of the production and delivery system. Any of these could damage or destroy the oil or gas wells, production facilities, exploration equipment as well as cause bodily injury and damage to property. There is also a risk that equipment could be trapped in the oil drill, preventing the continuation of drilling operations or incurring significant expenses. Should any of these events occur at sea, consequences could be extremely severe and major damage could be incurred. Furthermore, there is risk of liability for pollution damage due to gushing and/or leaking of oil and/or gas. There is no certainty that all required insurance to cover these risks can be obtained, nor that coverage provided by the insurance policies obtained will be sufficient. The decision on the type and scope of insurance policy is usually made separately for each drilling, taking into account, inter alia, the cost of insurance, nature and scope of the proposed coverage and the anticipated risks. The operator of a specific project could decide not to take out certain policies.
- H. Dependence on contractors, equipment and professional services: There are no contractors in Israel involved in drillings, development or offshore seismic surveys of the type conducted by the limited partnerships. Therefore, the partnerships are required to contract with foreign contractors for the necessary services. Furthermore, there are few machines capable of drilling and carrying out development operations at sea in general, and in deep water in particular, compared to the large demand, and there is no certainty that proper vessels will be available for drilling when required. Therefore these offshore operations could involve high costs and/or significant delays in schedules set in the work plans, or part thereof. Most of the suitable equipment and human resources for these operations can be ordered for short periods, therefore it is often necessary to order equipment and professional human resource services from abroad, which is expensive and causes significant delay in operations. Contracting with foreign contractors for offshore oil exploration, development and production operations (including maintenance and repairs contractors) could sometimes be difficult, also due to the security and geopolitical situation in Israel.
- I. Exploration risks and reliable on incomplete data and assumptions: Oil and gas exploration is not an exact science, therefore there is a high risk, since failed exploration drillings could result in a loss of investment. The geological and geophysical means and techniques do not provide an accurate forecast as to the location, shape, features or size of oil or gas reservoirs. Therefore, determining exploration prospects and estimating the size of existing reservoirs and

gas reserves could be based, to a large extent, on partial or approximate data and on unproved assumptions. It is obviously impossible to ensure that oil or gas will be found at all as a result of exploration operations, or that it will be commercially viable for production and exploitation. Furthermore, there is shortage of direct geological and geophysical information for some of the offshore areas of the oil assets of the partnerships and/or Delek Energy. This is due, inter alia, to the limited number of drillings in these areas and the sparse information that could be derived from them. Estimates of proved gas reserves and resources that can be produced from the reservoirs could also change from time to time. The estimated oil and gas quantities in producing reservoirs during the reporting period is calculated each year, inter alia, based on assessments of oil and gas reserves by external experts. The estimation of the gas reserves and gas resources according to the above principles is subjective, based on different assumptions and incomplete information, and the estimates of experts could vary significantly. There are numerous assumptions and data that affect the results of the estimated reserves and changes in these assumptions and/or data could result in significant changes in the assessments. In view of the aforesaid, it is noted that the information in this report regarding the gas reserves and gas resources in the different reservoirs is based on assessment only and should not be considered as information regarding precise quantities. Estimates of the proved and developed gas reserves in the Mari gas field are used to determine the depreciation rate of assets in financial statements of the limited partnerships. Depreciation of investments associated with discovery and production of proven and developed gas reserves is based on the depletion method, in other words, in each accounting period the assets are depreciated at a rate determined by the number of units of gas actually produced, divided by the proven and developed gas reserves remaining according to estimates. Given the fundamental importance of the depreciation, these changes could significantly affect the operating results and financial situation of the partnerships and of Delek Energy.

- J. Estimated costs and schedules and potential shortage of means: Estimated costs and schedules for exploration and development are based on general forecasts only and there could be significant variances. Exploration plans could change significantly due to the findings of these explorations, causing significant deviations in schedules and estimated costs of these operations. Malfunctions during exploration and production, and other factors, could extend the operations far beyond schedule and expenses for completing exploration could be significantly higher than forecasted. Proposed exploration operations could also involve financial outlay which the partnerships may not be able to cover. According to JOAs, late payment of the share of Delek Energy, the limited partnerships and/or the Company, as relevant, of an approved budget for a work plan is a breach which could lead to forfeiture of rights of the partnerships and/or Delek Energy in the oil asset to which the operating agreement applies. Each party to the JOA is liable for timely payment of its relative share. Should other parties to the agreement fail to pay the amounts due and are in breach of the agreement, the partnerships could be liable for payments significantly exceeding their proportional share in the oil assets relative to the breach. If such payments are not made on time, the partnerships could risk forfeiture of all their rights in the assets. Particularly high costs of offshore drilling and development could result in deviations in the budget (expected or unexpected). This could prevent the partnerships and/or Delek Energy from fulfilling its financial obligations, resulting in forfeiture of its rights.
- K. Risks in the development of a field in the event of a discovery: The decision-making process for continued investment in development and commercial production, intermediate operations prior to commercial production, and implementation of development and commercial production (if feasible) could continue for a long period and involve heavy expenses. Development and production in very deep waters (such as the depth in the Tamar and Leviathan discoveries) is extremely complicated and requires technology for construction of special production platforms.
- L. Dependence on permits from external entities: Operations of some of the limited partnerships' areas requires different permits. To the best of Delek Energy's knowledge, the main permits required are those pursuant to the Petroleum Law and Natural Gas Sector Law, permits from the security forces, Nature and National Parks Protection Authority, environmental quality authorities, Civil Aviation Authority, local authority and/or planning and construction committees, the Ministry of Agriculture and Rural Development – Aquaculture Department, Ports Authority and shipping department in the Ministry of Transportation. Attaining these permits could entail additional expenses beyond the budgets allocated for such operations, or cause delays to schedule of planned operations. Notwithstanding the aforesaid, some of the limited partnerships' operations are subject to coordination and scheduling with the security

forces. Dependence on security forces could disrupt plans of the partnerships with regard to such operations, both in terms of their ability to carry out planned activities and in terms of the schedule and costs of these operations.

- M. Regulatory changes: Operations of the partnerships and Delek Energy in Israel require numerous regulatory permits, primarily from the competent authorities pursuant to the Oil Law and Natural Gas Sector Law, as well as permits from state institutions (including the Ministry of Defense, Ministry of the Environment, Tax Authority and planning authorities). In recent years, a number of bills were presented for amendments to the relevant laws and regulations relating to the core operations of Delek Energy and the limited partnerships. In 2010-2011, the Petroleum Commissioner issued new rules and procedures for granting oil rights and restrictions on the transfer of rights in oil assets. Implementation of these rules and procedures could have an adverse effect on the operations of the partnership and Delek Energy. As part of Delek Energy's international operations, primarily in undeveloped countries, there is a risk that regulations will be changed in a way that could harm the Company.

These regulatory changes could have an adverse effect on the operations of the limited partnerships. For further information see section 1.11.26 above.

- N. Dependence on weather and sea conditions: Rough seas and difficult weather could delay schedules of offshore work plans and extend the time for their completion. These delays could increase expected costs and could also cause non-compliance with mandatory schedules to which the partnerships' committed.
- O. Tax risks: The tax issues related to operations of the limited partnerships have yet to be litigated in Israeli courts and it is impossible to determine or to anticipate how the courts will rule on such issues, if and when they are brought before them. Furthermore, for some of the legal issues there is no way to anticipate the position of the tax authorities. Since the operations of the partnerships are subject to special taxes, changes arising from changes in legislation, regulations or a change in the position of the Tax Authority, as set out above, could have material implications on the tax applicable to the partnerships and holders of partnership units. In addition, the Petroleum Profits Tax Law, which was passed at the end of March 2011, will significantly increase the tax burden on the partnerships' profits, and consequently, will have an adverse effect on the partnerships' business and operations.
- P. Financing liabilities: The limited partnerships have financing agreements as set out above. According to these financing agreements, the limited partnerships have place liens, inter alia, on their rights in the Ashkelon lease, Tamar Lease, Dalit lease and Rachel and Amit licenses, agreements for the sale of natural gas with Yam Tethys project partners, the joint operating agreement for the relevant projects, facilities, shares of subsidiaries and rights according to insurance policies. Should the limited partnerships fail to comply with their liabilities under the aforementioned financing agreements, this could lead to a demand for immediate repayment of amounts due under the financing agreements, as well as to liquidation of the collateral provided by the limited partnerships.
- Q. Dependence on a major customer: The limited partnerships and IEC signed an agreement for the sale of natural gas. IEC is currently the largest single consumer in Israel and today the main gas consumer of the partnerships. Payments received from IEC under the IEC agreement are currently the main source of revenue for the limited partnerships. Failure of IEC to comply with its undertakings for timely payment of the amounts payable under the agreement with IEC could lead to a breach of the financing agreements and consequently to demands for their immediate repayment. It is impossible to anticipate the changes to IEC's operating license, nor how these changes would affect the financial status of IEC. It is noted that the government's policy to increase competition in Israel's energy market by introducing new, private power producers, as well as the government's intention to privatize IEC, could adversely affect IEC's financial robustness, thus affecting its ability to meet its liabilities under the agreement. The 2002 agreement with the IEC has several provisions relating to force majeure events, which, should they occur, would release the IEC from its obligations to continue making payments under the agreement.
- R. Dependence on the operator: The partnerships rely to a large extent on Noble, in the oil rights it uses as the Operator, including in the Yam Tethys project, due to the provisions in the JOAs as well as because of the Operator's experience in projects of this scope in other countries and the partnerships relative lack of experience in these types of project. If Noble withdraws from the Yam Tethys project and/or the Tamar project and/or the Ratio Yam project and/or the project in Cyprus and/or other licenses held by the partnerships, or changes its status in way

that it will no longer be the operator, this could have an adverse effect on the ability of the partnerships to meet their liabilities according to the work plan of the oil assets and/or under the agreement for the sale of gas and could affect the production costs of the project.

- S. Late payment for joint operations: According to agreements with the other partners in the partnerships' oil assets, any party that does not pay its debts in full, under the agreements, shall forfeit their rights in oil assets to which the agreement applies, without any compensation.
- T. Minority decisive vote: In most transactions that the partnerships are party to, their participation holdings are low and therefore also its voting rights. Since the decisions are taken by majority vote (by a majority as defined in the JOAs), the partnerships have no influence over the decisions that are made. In addition, these transactions contain the option that if one of the partners withdraws and the other partners do not assume its share (of unapproved expenses) in exploration or development operations, this could lead to the termination of these operations before completion of the plan defined in the transaction and the return of the oil assets in which these operations are performed.
- U. Shortage of production and development resources and participation in operation: Commercially viable discoveries and their production require the partnerships to invest significant amounts, which exceed the means currently available to them. These costs, especially with regard to offshore discoveries (such as the Tamar, Dalit, Leviathan, Dolphin and Tanin discoveries), are extremely high and the operations also entail risks, including operational risks. Although the partnerships could hold a valuable asset if there is a commercial discovery, there is no certainty that collateralizing this asset would be sufficient to obtain financing for development and production. It is noted that due to the royalty payments due by the limited partnerships to the State of Israel, Delek Energy, the Company and to others, there is no certainty that, in the event of a commercially viable discovery, development of the oil or gas field can be financed or that oil production would be financially feasible for the limited partnerships. A sharp rise in production expenses, a material increase in the tax burden or a sharp drop in oil and gas prices could have an adverse effect on the production viability.
- V. Inclusion of additional participants and dilution of the share of the partnerships in the revenues: The limited partnership may, with the approval of the Commissioner, transfer part of the rights in the oil assets to other parties. Exploration and production operations require substantial capital which in many cases cannot be raised within the frame of loans or debt, therefore in certain cases it may be required to include additional partners in various oil assets of the partnerships and/or of the Company, leading to dilution of their share in these assets and in any of the oil and gas revenues deriving from them.
- W. Cancellation or expiry of oil rights and assets: Oil rights are granted according to the Petroleum Law for a limited term, and are contingent on fulfilling commitments on dates specified in terms of the oil assets. Non-compliance with the commitments could lead to cancellation of the oil rights. An extension of the oil right is at the discretion of the competent authorities, according to the Petroleum Law, which may refuse an extension, restrict the oil right or add other conditions. The ability to exploit oil assets depends, inter alia, on the ability of the partnerships to finance various operations and the availability of suitable equipment and personnel. The absence of equipment or personnel could increase the costs or even prevent fulfillment of the terms of the oil rights or the preliminary permit, prevent or restrict the extension of rights to assets or cause them to expire. Failure to meet the terms stipulated in the oil rights could result in a loss of the rights and loss of investment. In respect of the partnerships' rights in Block 12 in Cyprus, it is uncertain when and if the process for transferring the rights in Block 12 in Cyprus will be completed (as set out in section 1.11.29(H)). The Cypriot authorities are responsible for deciding whether to complete the process for transferring the rights in Block 12 and non-completion could affect the partnerships' rights in Block 12 in Cyprus.
- X. Migrating reservoirs: It is possible that oil or natural gas reservoirs that are discovered or will be discovered in the areas in which the limited partnerships have rights will migrate (in terms of the geological formation and size of the reservoir) into other areas where Company or the limited partnerships have no rights, and vice versa. If gas migrates to areas in which others have rights, negotiations could be required for an agreement on joint exploitation and production from the reservoir, to achieve maximum efficiency of the oil or natural gas reserves.
- Y. Security risk: The production platform of the Yam Tethys project is located relatively close to the maritime border between Israel and Gaza, therefore it is exposed to security risks,

including acts of terror. The permanent receiving terminal in Ashdod is exposed to security risks including acts of terror.

- Z. Belonging of Delek Energy to the Company and the controlling shareholder, Yitzhak Tshuva: Delek Energy belongs to the Company and the controlling shareholder, Yitzhak Tshuva, which could affect the ability of Delek Energy to raise credit, inter alia, due to the single borrower limitation, which could limit Delek Energy's sources of bank credit in Israel, and other regulatory limitations imposed on the banks and institutions by the Ministry of Finance and the Bank of Israel.

The table below presents a summary of risk factors by type (macro risks, sector-specific risks and company-specific risks for Delek Energy and/or the partnerships and/or the Company), according to the estimates of the Company based on the degree of their effect on the Company: major, moderate or minor effect.

	Impact of risk factors on the Company's business		
	Major	Moderate	Minor
Macro risks			
Fluctuations in the dollar exchange rate		X	
Dependence on global oil prices	X		
Sector risks			
Competition for gas supply	X		
Market size compared with size of reservoirs	X		
Uncertainty regarding construction of the national gas pipeline		X	
Insurance		X	
Operational risks	X		
Dependence on contractors	X		
Exploration risks	X		
Estimated schedules and costs		X	
Field development on discovery	X		
Dependence on permits from external entities	X		
Regulatory changes	X		
Dependence on weather and sea conditions		X	
Risks specific to the Company			
Tax risks	X		
Financing liabilities	X		
Dependence on primary customer	X		
Dependence on the Operator	X		
Arrears in payments for joint operations			X
Minority decisive vote:			X
Shortage of production and development resources and participation in operation	X		
Inclusion of additional participants and dilution of the partnership's share			X
Cancellation or expiration of oil rights and assets		X	
Migrating reservoirs		X	
Security risk	X		
Belonging of Delek Energy to the Company and the controlling shareholder, Yitzhak Tshuva		X	

The impact of these risk factors on the energy sector is based on estimates alone and may actually differ.

Glossary

Appraisal well: a drilling carried out as part of the appraisal drilling plan, to determine the physical size, oil or gas reserves and the production rate of the field

AVO analysis: An AVO analysis is used by geophysicists to determine the thickness of rock layers, porosity, density, velocity, lithology and fluid content in rocks.

BCF: billions of cubic feet, which is 0.001 TCF or 0.0283 BCM

BCM: billions of cubic meters, which is 35.3 BCF or 0.0353 TCF

BOE: barrel of oil equivalent, being the amount of energy produced from gas that is the same as the amount of energy produced from one barrel of oil

BOEPD: BOE per day

Commercial quantities: a quantity of oil, sufficient for production on a commercial basis

Confirmation well: a drilling to confirm the existing of the oil reservoir that was discovered in the discovery drilling, and verification of the production tests in the discovery drilling.

Cretaceous layer: rocks from a geological period dating from about 145 million years to 65 million years ago. Lower Cretaceous layers are the deepest layer and are the earliest of the Cretaceous layers.

Development: drilling and equipping of the oil asset area to determine its production capacity and for oil production and marketing

Directional drilling: diagonal drilling towards the target layer, compared to regular vertical drilling

Discovery: discovery of oil in a drilling

Exploration: operations related to the search for oil and gas

Horizontal drilling: drilling of a well that travels horizontally through a producing layer

Hydrocarbons: carbons, a generic name for oil and gas, which are coal and hydrogen compounds

Jurassic layer: rocks from a geological period dating from about 144 million to 208 million years ago

Lease: as defined in the Petroleum Law

LGN: liquid natural gas

License: As defined in the Petroleum Law

Logs: electric logs recorded during drilling, providing a continuous record of rock properties and content, to locate the potential layers that could contain oil or gas reserves

MMCF/D: millions of cubic feet per day

MMCF: millions of cubic feet, which is 0.001 BCF or 0.0003 BCM

Oil asset: the lease, direct or indirect, in a preliminary permit, license or lease; in another country – the lease, direct or indirect, in a similar right granted by a competent party. The oil asset is also regarded as the right to receive benefits arising from the lease, direct or indirect, in the oil asset or in a similar right (as the case may be).

Oil exploration:

- (1) Test drilling
- (2) Any other operation for oil exploration, including geological, geophysical and geochemical tests, and drilling to achieve geological information only

Oil field: an area with geological layers under which an oil reservoir lies with potential for commercial production

Oil right: a license or lease, as defined in the Petroleum Law

Oil: any petroleum fluid, whether liquid or gaseous and includes oil, natural gas, natural gasoline, condensates and (carbons) hydrocarbons and also asphalt and other solid petroleum hydrocarbons when dissolved in and producible with fluid petroleum

Oligocene layer: rocks from a geological period dating from about 34 million years to 23 million years ago. Lower Oligocene layers are the deepest layer and are the earliest of the Oligocene layers.

Petroleum Resources Management System (2007) (SPE-PRMS): as published by the Society of Petroleum Engineers, the American Association of Petroleum Geologists (AAPG), the World Petroleum Council (WPC) and the Society of Petroleum Evaluation Engineers (SPEE) and as revised from time to time.

Petroleum; Prospective Resources; Discovered; Discovery; Reserves; Contingent Resources; Proved Reserves; Probable Reserves; Low Estimate; Best Estimate; High Estimate; 1C,2C,3C Contingent Resources; On Production; Approved for Development; Justified for Development; Development Pending; Development Unclassified or on Hold; Well Abandonment; Development not Viable; Dry Hole; 1P/2P/3P Reserves: as defined in SPE-PRMS

Preliminary permit: As defined in the Petroleum Law

Priority right to obtain a license: as defined in the Petroleum Law

Probable reserves: reserves believed to exist with reasonable certainty based on reasonable evidence of the presence of recoverable hydrocarbons in a known formation or reservoir, or based on assumptions regarding contact between fluids (water and oil), with a lower probability than that of proved reserves deriving from lower supervision of the wells in the area and/or lack of production test. These reserves could include laterals of proved reservoirs or other reservoirs where no production tests have been carried out at a commercial rate or recoverable reserves using methods to increase production not yet assessed at the reservoir or at reservoirs where the implementation of the plan is uncertain.

Proved reserves: oil/gas reserves that to a high level of certainty are recoverable, according to the regulations of the Securities and Exchange Commission (SEC) and the regulations of the Society of Petroleum Engineers and World Petroleum Council (SPE/WPC)

Proved, developed and non-producing reserves (PDNP): proved reserves in reservoirs in a producing field, where commercial production has not commenced. The development and production drillings produced from other reservoirs in the same field, however these reserves are in reservoirs that are closed behind pipe. Depletion of producing reservoirs results in depletion of closed behind pipe reservoirs

Proved, developed and producing reserves (PDP): proved reserves produced by development and production drilling

Proved, undeveloped reserves PUD): proved reserves in reservoirs, where there is no development drilling in continuation of or adjacent to the reservoirs with proved, developed and producing reserves

Reserves: Amounts of producible oil and/or gas in a reservoir

Seismic facies analysis: analysis of seismic data distinguishing between the different rock layers.

Seismic survey: a method that allows (on land or offshore) subterranean imaging and detection of geological formations. The survey is carried out by inserting subterranean seismic waves and returning them from the different aspects in the tested profile. 2D and 3D surveys are common today. The 2D surveys are mainly used to obtain preliminary underground information in the survey area, and for general detection of formations that could serve as oil traps. The 3D surveys are carried out in areas identified as having potential in the 2D surveys. These surveys are more expensive than the 2D surveys and produce higher-quality results. The image received is detailed and allows, inter alia, detection of the optimal location for drilling and a more accurate assessment of the size of the formation.

TCF: trillions of cubic feet, which is 1,000 BCF or 28.32 BCM

Test drilling: drilling of test wells to find oil or to determine the size or edges of the oil field

The Commissioner, or the Petroleum Commissioner: the Commissioner of Petroleum Affairs appointed under the Petroleum Law, 1952

The Natural Gas Sector Law: the Natural Gas Sector Law, 2002

The Petroleum Law: the Petroleum Law, 1952

Working interest: an interest in an oil asset granting its owner the right to participate, pro rata, in the exploration, development and production of oil, subject to payment of a corresponding percentage of the expenses arising from these works, after acquiring the working interest.

Conversion table for units used in the report:

MMcf	BCF	BCM
35310.7	35.3107	1

BCM	MMcf	BCF
0.0283	1000	1

BCM	BCF	MMcf
0.00003	0.001	1

1.12 Insurance and Finance in Israel

1.12.1 Acquisition of holdings in the insurance field in Israel

In 2005 and 2006 the Group, through Delek Investments and Delek Capital,²¹⁹ and in two transactions, acquired control of The Phoenix²²⁰, for a total consideration of approximately NIS 1,882 million. As of the report date, Delek Group holds 56% of shares in The Phoenix and 55% of the voting rights. The purchase agreement signed with Meir Group stated that it hold shares in The Phoenix which entitle them to 20% or more of the capital and voting rights in the company ("Holding A"), or less than 20% but not less than 10% ("Holding B"), Delek Capital and Delek Investments will use their means of control in order to bring about a situation whereby two directors will serve on The Phoenix's Board of Directors in the case of Holding A, or one director in the case of Holding B, who will be recommended by Meir Group and will be acceptable to Delek Capital and Delek Investments. Currently, four directors recommended by The Phoenix are serving on the Company's Board of Directors, out of a total of eight directors (including two external directors). In addition, the agreement sets forth, inter alia, the terms for purchasing the shares, the manner in which the purchase is to be carried out, and an obligation by Delek Capital concerning future indemnification and insurance in The Phoenix.

1.12.2 General information on the operating segment

A. Structure of the operating segment and changes therein

The Phoenix was incorporated in 1949 as a private company and became a public company in 1978. Currently, The Phoenix 1 share is traded under the Tel Aviv 75 index, the Tel Aviv 100 index, the Tel Aviv Insurance index, and the Tel Aviv Finance index.²²¹ At the date of the report, most of The Phoenix's activity is in insurance, including various sub-segments, and is carried out through the subsidiary, The Phoenix Insurance Company Ltd. ("The Phoenix Insurance"). This activity includes operations in life insurance and long-term savings, and most sectors of general insurance, compulsory automobile insurance, property vehicle insurance, and other general insurance, and health insurance. The Phoenix Insurance also holds The Phoenix Agencies, which coordinates The Phoenix's insurance agent operations. In addition, The Phoenix engages in the management of provident funds, mainly through Excellence Investments Ltd. ("Excellence")²²² and pension funds, as well as various finance-related activities on the capital markets. Alongside its insurance and finance operations, The Phoenix provides non-bank credit, and engages in investments in companies, investments in real estate, artworks, and other investments. The Phoenix's non-insurance investments and investment management activity take place mainly through the subsidiary, The Phoenix Investments and Finances Ltd. ("The Phoenix Investments"). In managing its above operations, The Phoenix employs risk management methods. The Phoenix focuses on managing the risks to which it is exposed, so as to identify and assess their potential influence on the future financial positions of the various companies in The Phoenix Group.

As of December 31, 2010, total assets under The Phoenix's management (including Excellence) amounted to approximately NIS 106.7 billion, divided as follows: approximately NIS 21.5 billion in life insurance, not including guaranteed-yield policies (and approximately NIS 31.5 billion including guaranteed-yield policies); approximately NIS 19.5 billion in provident funds; approximately NIS 5.5 billion in pension funds; approximately NIS 19.1 billion in ETFs; approximately NIS 17.5 billion in mutual funds; approximately NIS 8.1 billion in portfolio management; and approximately NIS 5.5 billion in other nostro accounts.

²¹⁹ Following the liquidation of Delek Capital in 2010, its holdings in The Phoenix were transferred to Delek Investments.

²²⁰ In this section, "The Phoenix" refers to The Phoenix Holdings Ltd. and all the companies consolidated in its financial statements.

²²¹ Pursuant to a decision of the TASE Board of Directors, on January 26, 2012, The Phoenix's shares of NIS 5 par value ("The Phoenix 5 Shares") were delisted from trading after 24 months elapsed from the date on which trading in the Phoenix 5 Shares ceased on the main list and they were transferred to the preservation list, and at the end of this period the conditions for resuming trading under the main list were not met.

²²² Excellence was first consolidated in The Phoenix's financial statements on March 31, 2009, at a rate of 80.88%. For details regarding the agreement pertaining to the acquisition of control in Excellence, see Note 14 to the financial statements. As of the date of the report, The Phoenix holds 73.32% of Excellence's issued share capital, after having acquired the "first installment" (as determined in the settlement agreement) of Excellence shares to the amount of 20.44%, in return for approximately NIS 342.6 million, and after acquiring additional shares through transactions outside the TASE.

The Phoenix is active in four principal segments:

1. Life insurance and long-term savings – life insurance is primarily intended for the long-term and guarantees insurance coverage for the occurrence of the insured event, including, *inter alia*, the death of the policyholder or the policyholder reaching the age set forth in the insurance policy. In addition, coverage for various risks during the lifetime of the individual (such as death, handicap and/or work disability) may be added to the aforesaid policies. These policies may also include, at the insured party's discretion, a savings component. Life insurance including a savings component constitutes one of the three main alternatives for long-term savings – life insurance, pension funds and provident funds. Provident funds are savings instruments which do not include an insurance component, which in the past offered policyholders a capital track. Today, under the 2008 legislation, these funds offer an allowance track. In addition to its life insurance activities and its provident fund activities (mainly carried out through Excellence)²²³ which are of a substantial scope in The Phoenix, The Phoenix also conducts pension-related activities. Pension funds grant the policyholder a monthly allowance upon his retirement or earlier, and also permits insurance coverage in the event of death and/or disability.
2. General insurance, including three insurance sectors:

Compulsory motor insurance - this branch includes the Phoenix's activity in providing insurance cover pursuant to the provisions of the law (Motor Vehicle Insurance Ordinance) (New Version), 1970, resulting from the use of a motor vehicle, and it provides cover for physical injury (to the driver of the vehicle, passengers in the vehicle or pedestrians) resulting from the use of a motorized vehicle, under the Law for the Compensation of Road Accident Victims.

Vehicle property insurance – this focusses on cover for property damage to the insured vehicle, and includes The Phoenix's activity in the sale of insurance policies for property damage to the insured vehicle, which includes cover for property damage to the vehicle (for example, resulting from an accident and/or theft) ("Comprehensive Insurance") and cover for property damage caused by the insured vehicle to third parties ("Third Party Insurance").

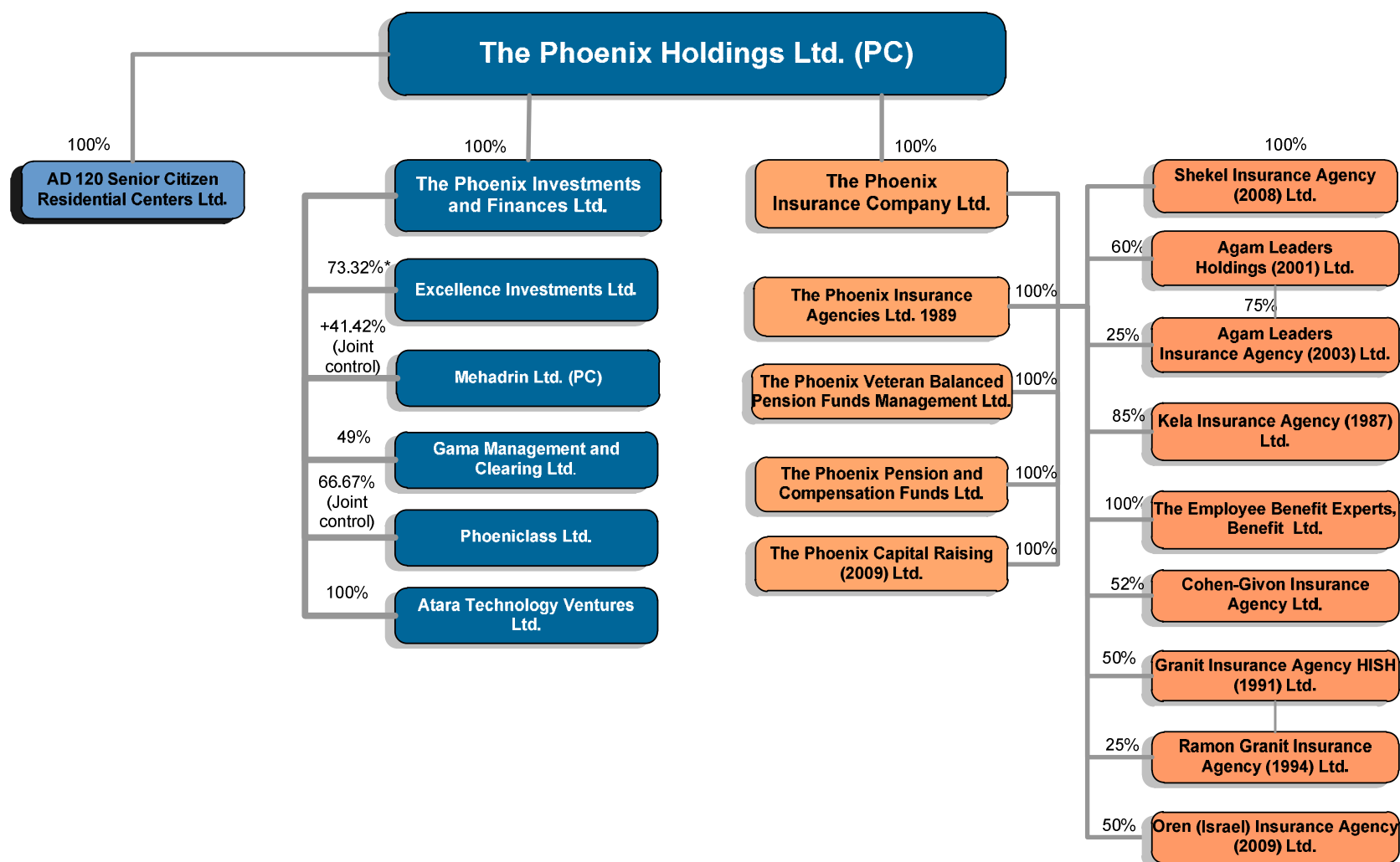
Other general insurance – this includes The Phoenix's activity in the sale of various insurance policies in three main sectors: property insurance (that is not vehicle related) for physical damage to the policyholder's property (such as apartment insurance and business insurance); liability insurance that is generally sold together with property insurance for businesses and covers the insured for his liability towards third parties (such as third party liability, employer liability, professional liability including directors and officers liability and liability for faulty products) and other general insurance areas (such as personal accident insurance and contract work insurance).
3. Health insurance – this includes The Phoenix's activity in insurance for individual and collective illness and hospitalization as well as dental insurance. The policies sold in these areas of insurance cover various forms of harm sustained by the policyholder due to illness and/or accident (except for death). It also includes The Phoenix's activity in nursing care insurance and insurance for chronic illness, travel insurance, foreign employee insurance and sick days insurance.
4. Financial services – This segment includes the Excellence Group's activities consisting mainly of financial asset management services: marketing and management of investments for customers, underwriting and investment banking, issue of structured products, issue of financial products, management of mutual funds, issue of ETFs, and provision of stock exchange and trade services.

²²³ It should be noted that in addition to the provident funds, Excellence manages pension funds and short-term savings (through Excellence Invest policies – savings policies which do not include an insurance component).

Following is a summary of financial data for the areas of insurance provided by The Phoenix for 2010-2011 (in NIS millions):

	2011	2010
Profit (loss) from life insurance and long-term savings	(14)	64
Profit (loss) from health insurance	126	104
Profit from general insurance	142	220
Profit from financial services	95	112
Total pre-tax profit (loss) from operating segments	349	500
Income less expenses not attributed to operating segments	(131)	(9)
Profit (loss) before income tax	218	491
Income tax	149	158
Profit (loss) for the period	69	333
Attributable to:		
The Phoenix shareholders	53	309
Minority interests	16	24
Profit (loss) for the period	69	333

Structure of the principal holdings in insurance and finance in Israel:



The structure of the holdings includes the principal companies in the Phoenix Group. Inter alia, the following have not been included: subsidiaries of the insurance agencies, companies established for real estate investments and some of the subsidiaries of Phoenix Investments, which are not fundamental.

* Based on the agreement with Mssrs. Roni Biram and Gil Deutsch, The Phoenix will acquire a further 10% of Excellence shares. For details see Note 14 to the Financial Statements.

B. Legislation, standardization and special constraints

1. Insurance activities are subject to comprehensive regulation under law, as well as to supervision by the Capital Market Commissioner and the Commissioner of Insurance ("the Commissioner"). The extensive regulation is a factor which has considerable influence on activity; in recent years, regulation increased considerably and changed the nature of activity and competition, mainly in life insurance and long-term savings. For details of regulations governing insurance in general, see section 1.12.17 below; for details of regulations governing life insurance and long-term savings, see sections 1.12.2(D) and 1.12.3(A)(2) below.
2. Restrictions on the distribution of dividends and capital requirements

According to the provisions of various laws, the insurance operations of the Phoenix are subject to minimum equity requirements, as prescribed in the Supervision of Financial Services (Insurance) (Minimum Equity Required from an Insurer) Regulations (Amendment), 1998- ("Minimum Equity Regulations"). The purpose of an insurer's equity is to serve as a cushion for absorbing losses stemming from the materialization of unforeseeable risks to which it is exposed, and that it failed to identify specifically or that were inadequately evaluated. The purpose of this cushion is to enable the insurer to continue operating as a going concern in times of distress and to meet its obligations to policyholders and other debtors even in the event of liquidation. The equity required of The Phoenix as of December 31, 2011, according to the Commissioner's regulations and directives is NIS 2,441 million. The equity balance as of the aforesaid date, calculated according to the equity regulations is NIS 3,039 million (about NIS 1,823 million basic tier 1 capital, NIS 671 million complex tier 2 capital and NIS 545 million deferred tier 2 capital). Of these amounts, NIS 330 million are non-distributable surpluses. For additional details about the minimum equity required from an insurer, including details of the provisions of the Minimum Equity Regulations and the instructions of the Commissioner of Insurance, see Note 35 to the Company's Financial Statements.

New pension fund management companies and provident fund management companies

In February 2012, a circular concerning capital requirements from management companies ("the Circular"), the Supervision of Financial Services (Provident Funds) (Minimum equity required from a provident fund or pension fund management company) Regulations, 2012, and the Income Tax (Rules for approving and managing provident funds) Regulations (Amendment no. 2), 2012, were published (hereinafter in this sub-section: "the Regulations"). Accordingly, the equity requirements for management companies were updated, so as to include equity requirements based on the sum of the company's expenses over the last 12 months, and based on the volume of assets under management that it holds, but no less than initial equity of NIS 10 million. The regulations set forth investment rules for the minimum required equity which include, inter alia, a minimum required holding of liquid assets, a prohibition on holding intangible assets against the required equity, and a prohibition on pledging the assets held against the required equity. Furthermore, a management company will be required to provide additional equity in respect of the sum of the assets held in contravention of the provisions of the Ways of Investing Required Equity Regulations or in contravention of the Commissioner's instructions. A management company may distribute a dividend only if its equity is at least equal to the equity it is required to hold according to the Regulations. Under the Regulations, transition provisions were prescribed whereby a management company that received a license before publication of the circular, and whose equity on the commencement date of the Regulations was less than the minimum equity required, as noted above, must gradually increase its equity to the requisite amount by December 31, 2014, based on the formula in the Regulations. The Regulations will take effect in March 2012. The Phoenix believes that the new regulations will lead to a reduction of about NIS 67 million in the equity required of the provident fund management companies, according to the data in the financial statements as of December 31, 2011, due to the elimination of the equity requirements for deferred acquisition costs.

According to the Income Tax Regulations, a provident fund management company is required to hold equity of NIS 1 million (linked to the CPI for November 2001, i.e. NIS 1.2 million). The Phoenix Pension and Provident's equity for all pension and provident fund operations as of December 31, 2011 amounts to NIS 89 million; Excellence Provident and Pension's equity for all provident fund and pension operations as of December 31, 2011 amounts to NIS 100 million.

Provisions concerning restrictions on the distribution of a dividend by insurance companies:

In March 2009, the Commissioner issued a letter stating that as of the financial statements for 2008 and until December 30, 2010, insurance companies and managing companies will not distribute dividends except with the Commissioner's prior approval. According to this letter, as a general rule, no approval will be granted for the distribution of dividends exceeding 25% of the distributable profit. A letter of clarification that was published in December 2011, concerning criteria for approval of a dividend distribution by an insurer, stipulated that an insurance company may submit a request to the Commissioner for approval of a dividend distribution, from the date of publication of the Periodic Reports for 2011, subject to holding equity of at least 105% and to submittal of an annual profit forecast for the ensuing two years, an updated service debt plan approved by the board of directors of the holding company that holds the insurance company, an action plan for raising capital approved by the insurance company's board of directors, and minutes of the meeting of the insurance company's board of directors at which the distribution of the dividend was approved. Concerning the distribution of a dividend that does not require the Commissioner's prior approval, the ratio between total equity after distribution of the dividend and the amount required in the second clarification, was revised to 115%.

3. Repurchase of shares – In the ordinary course of their business, Excellence's ETF companies and profit-sharing policies buy shares in The Phoenix and the Company. The purchases are performed as part of the investment permits for "The Phoenix Method" plan, given by the Commissioner of Insurance in the Ministry of Finance. For information on the application of Section 309 of the Companies Law in connection with these activities, see Section 1.4.3 above.
4. On March 24, 2011, the Board of Directors of The Phoenix approved the distribution of a cash dividend to the amount of NIS 50 million. On May 1, 2011, the general meeting of The Phoenix approved the dividend distribution, and on May 15, 2011 the dividend was distributed to The Phoenix shareholders.

C. Changes in the scope and profitability of segment operations

The most material changes in the insurance business are taking place in life insurance and long-term savings. This is due, inter alia, to a series of far-reaching regulatory initiatives, which began with the Bachar legislation, which was approved in 2005 and continued with additional reforms which were approved subsequent years, and in planned future reforms. For details, see section 1.12.2(D) below. In addition, operating results are materially affected by the economic situation and the capital markets in Israel and abroad. Similar to the situation in 2009 and 2010, the first half of 2011 was characterized by relatively strong macro-economic data. Nevertheless, as the year progress, figures began to be published indicating a slower rate of growth, and 2011 as a whole was largely characterized by a negative trend due to a challenging worldwide macro-economic environment. From the beginning of the year, Israel's stock market showed low levels of trade, and all the leading share indices posted negative returns for 2011 as a whole. This state of affairs led to lower profits for The Phoenix compared with 2010, mainly due to a negative yield rate. In 2011, the results from The Phoenix's operating segments amounted to a profit of about NIS 349 million (compared with a profit of about NIS 500 million in 2010 and a profit of about NIS 440 million in 2009).

D. Market developments in the operating segments

The Bachar reforms

In July 2005, legislation was enacted for implementation of the Bachar Commission recommendations: the Increase of Competition and Reduction of Centrality and Conflicts of Interests in the Israeli Capital Market Law (Legislative Amendments), 2005 ("the Competition Law"); the Supervision of Financial Services Law (Provident Funds), 2005 ("the Provident Law"); the Supervision of Financial Services Law (Activity in Pension Consultancy and Pension Marketing), 2005 ("the Consulting and Marketing Law"). These laws ("the Bachar Legislation") were intended to implement the Bachar Commission recommendations in the following areas:

1. A structural change in the capital market, with the aim of separating activities with a potential for competition, and especially the enactment of a prohibition against the holding of provident funds, trust funds or insurers by banks; reduction of the concentration and

conflicts of interests in the capital market, especially due to holdings by major banks in trust companies, provident funds and underwriting companies; distinction between a consultant and a marketer, and regulation of their roles and duties towards the client; establishment of a new sales model and the duty of best advice – that is, adapting the product to the client's needs; a permit for banks to provide consultancy and distribute pension savings products; establishment of the employee's exclusive right to choose a provident fund or a pension scheme. For additional details with regard to the Bachar Legislation, see section 1.12.17(C) below.

The laws entered into force in the fourth quarter of 2005 and the first half of 2006, and caused material developments in a number of areas:

- A) The banks sold most of the provident funds and trust funds which they had previously owned. Most of the provident funds were acquired by the various insurance groups.
- B) Along with the separation of the provident funds and trust funds from the banks, the Bachar Legislation enabled banks to enter the field of consultancy and distribution of pension products. This possibility was opened to the banks gradually, subject to their compliance with various conditions. In 2006 - 2008, several medium-sized banks began to deal in pension consultancy, with regard to pension and provident funds and the large banks also received licenses to give pension advice.
- C) The institutional entities have developed systems which support the Best Advice model, in cooperation with the banks, and have trained their employees to comply with the licensing requirements for pension marketing.
- D) Public awareness regarding the yield of the financial products has increased – among other things, due to the handling of this subject by the media, including quotation of monthly and annual yields, and due to the introduction of systems which compare financial savings products.

Amendment No. 3 to the Provident Fund Law

January 28, 2008 was the date of publication of Amendment No. 3 to the Provident Fund Law, which has material implications for the activity in the field. The amendment includes a series of amendments to the Provident Fund Law, the Supervision Law and the Income Tax Ordinance. The objective of the amendment is to ensure a more transparent and sophisticated market for all persons saving up for retirement, by unifying the taxation rules applying to pension products, making significant decisions by savers close to retirement age with regard to the amounts in savings, ensuring that all savers have a pension component in their savings, and increasing competition in the pension market for the benefit of consumers.

The amendment sets forth, *inter alia*, provisions regarding the classification of provident funds into two types of pension provident funds: a pension provident fund which pays a pension directly to eligible persons, pursuant to the fund regulations, and a pension provident fund which does not enable direct withdrawal of monies deposited therein, except for monies from the severance pay component, monies from pension components that were deposited prior to December 31, 2007 and monies unlawfully withdrawn from the pension component, unless by transfer of those monies to a provident fund which pays a pension.

Portability of pension savings

In March 2008, the Knesset Finance Committee approved the Supervision of Financial Services (Provident funds) (Transfer of monies between funds) Regulations, 2008, ("Pension Portability Regulations") which govern transfers between the various pension savings products: provident funds, life insurance schemes and pension funds. The new regulations enable consumers to move from one pension savings product to another, or to replace the entity which manages the savings with another managing entity, at any time, without payment when transferring monies between the products and in accordance with their preferences. The objective of the law is to encourage competition, increase the efficiency of the pension products, and improve the service given to consumers. Pension monies cannot be moved from group pension plans to capital plans, in line with the Commissioner's policy to encourage group pension channels over capital channels, as also expressed in Amendment No. 3 to the Provident Fund Law, as set forth above.

The provisions of the regulations governing the portability of pensions include, *inter alia*, provisions concerning the relevant dates for transfer of monies and insurance liability from the

transferor fund to the recipient fund, the calculation method for the transferred amounts, the transfer method of the monies, consolidation and splitting of accounts, the status of members in the transferor fund (active / inactive), and the types of funds.

Compulsory pension arrangement

On November 19, 2007, a general collective agreement for pension insurance in Israel's economy was signed by the Coordination Office of Economic Organizations and the New Histadrut – Israel General Federation of Labor. The agreement includes a requirement for employers to deposit monies in a pension provident fund on behalf of their employees, as set forth in the collective agreement, starting in January 2008, and thereafter.

On December 30, 2007, the Minister of Industry, Trade and Labor enacted an expansion order for comprehensive pension insurance pursuant to the Collective Agreements Law, 1957 ("the Expansion Order") which expands the application of the provisions of the collective agreement to all employees and employers in the market, applied retroactively from January 1, 2008. As of the reporting date, a significant number of additional employees have joined as policyholders in the pension funds, and The Phoenix believes that there is potential for further growth in deposits in light of the gradual increase in the deposit rate under the collective agreement. It is noted that during the period 2008-2010 the number of new members who joined the pension funds declined following the application of the compulsory pension extension order, arising from the gradual exhaustion of potential new members under the agreement. Nevertheless, a noticeable percentage of those who joined the new pension funds in 2010, did so as part of the extension order.²²⁴ In September 2010, a collective agreement was signed between the Histadrut (Labor Federation) and the Coordinating Bureau of Economic Organizations, amending the existing agreement for pension insurance in the economy, and according to which in 2014 the rates of deposit under the compulsory pension arrangement will increase to 17.5%. In September 2011, the Minister for Industry and Trade published an order adopting the aforementioned collective agreement for all employees in the economy.

Adapting the pension savings track to member characteristics ("the Chilean [adapted savings] Model").

The Chilean Model (adapted financial savings) is the name given to the reform the purpose of which is to adapt pension savings to member characteristics, and to age in particular. The model was formulated in the wake of the global financial crisis and the problems that emerged from this crisis, and as a result of existing failings in the present method of managing the investments of pension savings, to the extent that the investments are managed jointly for all savers, without taking into account their different characteristics. In July 2009, July 2010 and January 2012, the Superintendent of Capital Markets, Insurance and Savings published a draft circular that discusses the adaptation of savings tracks to member characteristics, and draft Supervision of Financial Services (Provident Funds) (Setting up Default Tracks) Regulations, 2009. According to these drafts, institutional entities (provident funds, pension funds and insurance funds) will be required to establish separate investment tracks for savers of different ages. Additionally, the institutional entities will be entitled to expand the model and will also be able to separate the money belonging to savers according to other characteristics, e.g.: risk preference, financial situation, etc. Similarly, savers who join a pension savings product will be associated to the Chilean (adapted savings) model by default, if they have not chosen any other investment track. The drafts propose that the process of transferring savers to tracks suited to their characteristics will be gradual, extending over a several years, and initially, recipients of pensions will be the first to be transferred to the tracks best suited to them, followed by the older savers and finally the younger savers. It is noted that The Phoenix is ready to implement the above provisions through "The Phoenix Method Products" (for details, see Section **Error! Reference source not found.** below).

The long-term savings clearing house

In 2010, The Long-Term Savings Clearing House Ltd. was established, under joint ownership of several banks and insurance companies. The purpose of this company is to establish and manage an information and payment clearing house to serve customers, distributors, and manufacturers in the long-term savings market. According to the Ministry of Finance Capital Market Division, a pension-savings clearing house will streamline activities related to the transfer of information and funds, by providing a common technological base for all entities

²²⁴ From the reports of the Superintendent of the Capital Market, Insurance and Savings for 2009 and 2010.

involved in the pension-savings market, and regulating work processes. The Government is promoting the clearing house's establishment through legislation and in 2011 and until the date of the report, law amendments, announcements and draft circulars were published by the Commissioner, regulating, inter alia the licensing of the Company to operate a pension clearing system, mechanisms for supervising the system, information security for the system and any action that must be taken therein. The Phoenix believes that the clearing house's effects on the pension savings market are not clear at this stage, due to the fact that the process is still in its relatively early stages. It seems that full implementation of the clearing house's operations will lead to increased transparency in the industry and increased competition. The clearing house will make it easier for members of the different provident funds to review the pension products, and thus sensibly plan the savings and insurance coverages relevant for them. It is also likely to facilitate the activity of pension advisors in general, and particularly of the banks in the pension sector. On the other hand, in the short term, it may limit or delay the development of new technologies or products due to operational constraints in the clearing house. The activity of the clearing center may also affect the number and mode of operation of agents that are part of the arrangement. The scope and nature of these effects depend, inter alia, on the final manner in which the clearing center will operate.

Ministry of Finance plan for increasing competition in the pension-savings market

On November 30, 2010, the Minister of Finance presented the highlights of his plan for increasing competition in the pension savings market.

The Ministry of Finance intends to reduce the differences between pension savings products, so as to assist policyholders in comparing different products. Furthermore, in order to facilitate decision making after joining a pension-savings program, the Ministry of Finance will act to maximize transparency in institutional entities for policyholders. The plan will apply to pension-savings products, except for those sections of the program covering agents and consultants' remuneration and commissions. As part of the implementation of the plan, in February 2012, the Knesset Finance Committee approved an amendment to the Supervision of Financial Services (Provident Funds) (Management fees) Regulations, 2012, in which from January 2014 the upper limit for maximum annual management fees on provident funds and managers insurance that do not guarantee a yield will be reduced. In relation to insurance policies, the amendment states that the limit to management fees will not apply to insurance policies that were issued before January 1, 2013. Additionally, as part of the Finance Committee's deliberations, it was agreed that legislation would be enacted to set a fixed amount for minimum management fees. This move is dependent on the completion of various regulatory procedures. As far as The Phoenix is aware, and based on various publications, this decision refers only to the maximum amount of management fees for provident funds and managers insurance, and it does not apply to the management fees collected on the management of study funds and pension funds. The Phoenix is reviewing a series of measures that it may take to moderate the effect of the expected reduction in the management fees. The Phoenix believes that the aforementioned amendment will significantly affect the management fee revenues of the provident fund and insurance fund management companies. Furthermore, this amendment is likely to affect on-going profits in the future and the embedded value (EV) in respect of new life insurance policies to be sold, including indirectly affecting part of the life insurance portfolio of The Phoenix. On the other hand, materialization of the publications regarding agreement to set a fixed amount for the management fees may somewhat moderate the possible impact on the revenues and profit of the management companies. The Phoenix is examining the possible impact of the implementation of the regulations on its operations and financial position, including the need to make provision for impairment of value.

Aside from the aforesaid material developments, the following trends in long-term savings have become evident in recent years: increased transparency of pension products; encouragement of savings for pension purposes; increase in consumers' awareness and heightened competition; and increased enforcement by the Capital Market Division.

The Committee for Socioeconomic change

In September 2011, the Committee for Socioeconomic Change, headed by Prof. Trajtenberg, which was appointed in the wake of the social protests throughout Israel during the summer of 2011, submitted its recommendations to the government. The Committee's recommendations included, inter alia: raising corporate tax to 25% commencing in 2012, at the same time halting the planned cuts in the corporate tax rate that had previously been determined; raising the tax

rate on capital gains (including tax on interest and dividends) from 2012, and tightening the control of monopolies. In light of the foregoing, in December 2011, the Change in the Tax Burden (Legislative amendments) Law, 2011 was published, which from 2012 raises the tax rate on capital gains and the interest on CPI linked assets and on dividends by 5%. In January 2012, the Ministry of Finance published two law memorandums in which it proposed, inter alia, indirectly amending the Antitrust Law, which authorizes the Antitrust Court to order owners of a monopoly to sell all or part of an asset in its possession, should the court find that this may prevent harm or concern of significant harm being caused to business competition or to the public, and in the context of a concentration group, also if this is required to significantly enhance competition between members of the group or in a particular sector or to create conditions for significantly enhancing such competition. At the date of the report, except for legislative amendments that have already been completed, there is no certainty as to which of the Committee's recommendations will be implemented, and how, nor has a time frame been defined for implementation of these recommendations. Consequently, aside from the effect arising from the change in the tax rates mentioned above, The Phoenix is unable to estimate the extent to which it will be affected by these recommendations.

The Committee for Increasing Competition in the Economy (the Concentration Committee)

In February 2012, the Committee, which was established to review the present structure of the economy and its influence on the level of competition ("the Concentration Committee"), submitted its final recommendations, including, inter alia, the following:

2. Concerning real and financial holdings: a corporation that is not a financial corporation and whose effective sales turnover exceeds NIS 6 billion or whose effective credit exceeds NIS 6 billion ("A Significant Real Entity"), or one who controls such an entity, will not control or hold, at a rate exceeding the rate to be determined, a financial entity, whose overall assets exceed NIS 40 billion ("a Significant Financial Entity"); a Significant Financial Entity that is not a bank will not control one who controls a bank that is a Significant Financial Entity.
3. Concerning control through a pyramidal holding structure: control of companies in a pyramidal holding structure including more than two layers is forbidden (transition provisions will apply); for companies in a third layer or higher in existing pyramidal structures, a transition period will be determined at the end of which a pyramidal structure consisting of more than three layers will not be permitted; recommendations on the number of directors and independent directors in the board of directors.
4. Concerning financial institutions: a requirement that, as part of their investment policy, institutional investors will be obligated to take into consideration the quality of the corporate governance, inter alia, and the granting of loans intended for leveraged buyouts; institutional investors will also be required to determine "warning signs" which, when met, will require taking action vis-a-vis the company; creating supervision and regulation of entities that advise institutional investors with regard to how to vote at meetings (including from the aspects of eligibility and conflicts of interests).

At the date of the report, there is no certainty as to which of the committee's recommendations will be implemented and how; The Phoenix is therefore unable to estimate the extent to which these recommendations will affect it. Nevertheless, assuming that the recommendations are adopted and implemented as is, their adoption and implementation (particularly those recommendations that address companies with a pyramidal structure, if and insofar as there are any) may affect the identity of the controlling shareholder of The Phoenix, taking into account any limitations that may be imposed on the Company. The instructions concerning institutional investors will apply to the subsidiary The Phoenix Insurance as an institutional investor. Furthermore, The Phoenix, its control of public companies and its ability to acquire or dispose of holdings in public companies, may be directly affected.

Reduction of maximum annual management fees in provident funds and executive insurance

In February 2012, the Knesset Finance Committee approved an amendment to the Supervision of Financial Services Regulations (Provident funds) (Management fees), 2012, in which context limitations were set on the maximum annual management fees charged by provident funds and executive insurance that do not guarantee a yield. The regulations are due to take effect gradually from 2013 (with respect to insurance policies, it was determined that the maximum management fees limit will not apply to insurance policies that were issue

before January 1, 2012). To the best of The Phoenix's knowledge, this decision relates only to the maximum management fees in the provident funds and executive insurance policies, and it does not apply to the management fees collected on management of the study funds and pension funds. Based, in part, on estimates prepared by Excellence, in which most of The Phoenix's provident fund is concentrated, The Phoenix believes that this amendment will significantly affect revenues from provident fund management. The Phoenix estimates that the direct impact of these regulations in forthcoming years will be a reduction of 11%-12% in its revenues from provident fund management in 2011. It should be emphasized that this calculation refers to the direct impact of the regulations only, based on data at December 31, 2011. Likewise, the amendment is likely to affect on-going profitability in the future and the embedded value in respect of new life insurance policies to be sold, including indirect effects on part of the life insurance portfolio of The Phoenix Group.

The actual scope of the decline in revenues may be affected by other factors as well, for example the volume of raisings and deposits in the relevant years, yields in the relevant years, and other offsetting factors such as updates to supplementary regulatory provisions, a review of the way in which the Company costs its products and changes in such, a review of possibilities for developing revenue centers that supplement this segment, etc.

Furthermore, The Phoenix is examining a series of measures that it will take to moderate the effect of the anticipated reduction in management fees. Consequently, The Phoenix reduced the goodwill attributed to provident fund activity in its financial statements by NIS 113 million.

E. Critical success factors in the field of activity

The critical parameters for success are: economic, employment and capital market conditions; regulation, including supervision on prices; market competition; customer loyalty and portfolio retention; investment management quality; financial risks quality; distribution channels, including their ability to increase demand and create new markets; the range of products and the ability to adapt products to market conditions and customer needs; quality of service to policyholders, members, and agents; The Phoenix's positioning as a leading company in the life insurance and long-term savings market, while creating a brand that will strengthen its competitive standing; recruitment and retention of quality human capital; IT and technological resources; operational efficiency and operating, marketing and sales expenses; effective controls; integrity and stability.

Specifically, the following success factors can be named for insurance and pension operations: underwriting quality; management fees permitted by law and actually charged; actuarial quality in determining costs and reserves; the frequency and scope of claims, including disasters; quality of the various aspects of the claims management process; hedges and reinsurance costs; changes in life expectancy; the scope of tax benefits granted to customers (in the life insurance and long-term savings segment; technological and other developments in medicine, including medical inflation; changes in the health services package.

F. Principal entry and exit barriers in the segment

The principal entry barriers for the insurance operations are: licensing for The Phoenix, pursuant to the provisions of the Supervision of Financial Services (Insurance) Law and the licensing requirements for provident funds; legislative and regulatory requirements with regard to insurers' equity; expertise, knowhow, and experience required in insurance operations, mainly in the fields of actuary and risk management. Familiarity is also required with segment markets, including the reinsurance market; minimum size (critical mass) - a minimum amount of revenue is required to cover the high fixed operating costs required to operate insurance and investment mechanisms, including the need to meet changing regulatory requirements in the various segments.

The principal exit barriers are long-term liabilities towards policyholders and members, the long period of time required in some sectors for settlement of past claims (runoff), and regulatory requirements.

G. Substitutes for products in the segment and changes therein

In the general insurance segments, substitutes for The Phoenix's products are being offered by other insurance companies issuing similar products. The principal differences between the products in these fields are rates and scope of coverage. In the long-term savings segment, there is a relatively high level of substitution between the pension savings products (except for study funds). This interchangeability of products is due to their meeting similar needs for the

same target audience, in particular as regards executive insurance and comprehensive pension. A lesser level of substitution exists between segment products and other financial products (such as long-term deposits), as these products usually do not include two material elements (which are found in segment products - tax benefit and combining risk with savings). In the financial services segment, substitutes are the selection of an alternative management method, financial instruments offered by banks and other investment houses, raisings on overseas exchanges, and issue of loans from banks or non-bank organizations.

H. Structure of competition in the segment and changes therein

The five major insurance groups in the insurance market (which, as set forth above, also hold pension funds and provident funds) are The Phoenix Group, Clal Group, Migdal Group, Harel Group and Menorah – Mivtahim Group. According to Ministry of Finance data, in 2011 these groups held a joint market share of approximately 93% of total life insurance premiums and approximately 74% of all general insurance premiums (including health insurance). Further details of the competition structure appear in the description of the various sectors below.

1.12.3 Products and services

Financial information with regard to the insurance segments in 2010 and 2011 (in NIS millions):

	Life insurance and long-term savings ²²⁵		Compulsory vehicle		Property vehicle		Other general		Health	
	2011	2010	2011	2010	2011	2010	2011	2010	2011	2010
Gross premiums	3,670	3,065	374	389	728	668	949	893	1,146	1,071
Premiums less reinsurance (on retention)	3,606	3,002	360	374	728	668	534	496	984	910
Payments and changes in liabilities for insurance and investment contracts, gross	2,479	5,364	292	368	513	420	540	540	705	783
Payments and changes in liabilities for insurance and investment contracts (on retention)	2,442	5,317	306	375	513	420	276	280	649	632
Pre-tax profit (loss)	(14)	64	67	52	(12)	60	87	109	126	104
Total insurance liabilities, gross	30,414	29,527	1,981	1,977	483	416	2,272	2,193	1,339	1,317

The following table summarizes the financial results for the finance segment, as presented in The Phoenix's financial statements:

	2011	2010*
Total revenues		
From externals	375	398
From other operating segments	-	-
Total revenues	375	398
Total attributed costs:		
Costs that are not revenue for other operating segments	276	291
Costs that are revenues for other operating segments	-	-
Total costs	276	291
Write down of original differences	4	10
The Phoenix's share in the net results of investee companies	(1)	15
Pre-tax profit	95	112
Minority share in revenues from externals operating segment	14	20

* Operations in this segment are carried out through Excellence, for which The Phoenix has consolidated its results starting 2009.

²²⁵ Including Excellence provident and pension funds.

A. Life insurance and long-term savings

1. General: The Phoenix operates in all long-term savings areas and in all types of pension funds and provident funds, including study funds. Most of The Phoenix's operations at this date are in life insurance and provident funds (provident fund activities are mostly carried out through Excellence) and it operates in a more restricted fashion but in increasing volumes, in the pension sector.

Life insurance - A range of life insurance policy products are offered to customers, including an option of integrating insurance covers (e.g. insurance against death, work disability as well as other coverage) with retirement savings which the policyholder can redeem upon retirement or at another time. This allows the policyholder to choose the most appropriate component in these policies from the insurance covers ("Risk") and the financial accrual for retirement ("Saving"). Until January 1, 2008, policyholders also had the option of choosing policies known as insurance funds, pursuant to the provisions of the Income Tax Regulations (Rules for Approval and Management of Provident Funds), 1964, how benefits would be received – a capital track allowing a one-time withdrawal of funds from the age of 60 or an allowance track offering the policyholder a monthly allowance from the age of 60. Following Amendment No. 3 to the Provident Fund Law, at January 1, 2008, it is no longer possible to choose between a capital track and a pension track and retirement savings are offered on a pension track only (except for the severance pay component). Policies with a savings component are divided into several major types, which are distinguished by the way investments are made by the insurance companies, the types of cover and the management fees or expenses charged by the insurance companies.

The activity in the life insurance sector includes a combination of sales of new policies and provision of service to policyholders under existing policies which have been sold from the starting date of The Phoenix's activity until this day .

The life insurance sector has undergone extremely significant changes, starting in 2000, with regard to a number of aspects. These include the types of schemes operated, the rules of taxation which apply to the insurance schemes, and how the monies of policyholders are invested. The year 2005 was characterized by considerable changes in regulations, including the Bachar Legislation, which led to a comprehensive structural change in the capital market in general and the long-term savings sector in particular. In addition, in 2007 and 2008, the life insurance sector underwent additional significant changes as a result of the reform which enabled mobility of pension savings, Amendment No. 3 to the Provident Fund Law and the compulsory pension arrangement. For further details concerning the aforementioned reforms, and additional reforms, see section 1.12.2(D) above.

In life insurance and long-term savings, The Phoenix markets executive insurance, individual life insurance, group life insurance, work disability insurance, a range of insurance plans and savings policies.

Provident funds – provident funds offer savers (hereinafter in this sub-section: "the member"), an additional option for long or medium-term savings, entitling them to various tax benefits and an option (under certain conditions) to withdraw money that has been accrued as a lump sum. There are several types of provident fund: provident funds for personal compensation - long-term provident funds (a lump sum may be withdrawn only for amounts arising from deposits that were made until the end of 2007, and regarding deposits made from January 2008 and thereafter, they function as provident funds that do not pay an annuity); salaried members - in these funds, both the employer and the employee make regular monthly contributions from the employee's salary, whereas for self-employed members, only the member contributes to the fund; study funds - medium-term provident funds. Funds accumulated in a study fund may be withdrawn for study purposes from the end of the third year of membership in the fund, and after six years' membership the funds may be withdrawn for any purpose; individual severance-pay provident fund - for varying terms depending on the period of employment and the member's preferences; central severance pay funds - the employer sets money aside to guarantee severance pay for his employees. In these funds the member is the employer and the money is accumulated in a coordinated manner in the employer's name on behalf of his employees (under the provisions of the amended Provident Fund Law these funds were closed to new deposits for employees for whom no deposits were made in 2007, and under these provisions they were closed entirely to deposits from 2011 onwards);

provident funds for other purposes, such as for sick pay, convalescence, vacation, etc. - these are usually short-term provident funds for certain categories of member only; individually managed provident funds and study funds - through which self-employed members can manage their savings as defined in the regulations and money in study funds, through individually managed provident funds, to be managed by the member or a portfolio manager representing him, under investment restrictions to be monitored by the management company managing the savings. Companies managing provident funds derive their revenues from management fees that they charge on the assets. Since the management company does not charge fees as a percentage of profits, the effect of the yield on the revenues from management fees is indirect, and derives from the effect of the yield on the volume of assets which forms the basis for the management fees charged. The management company's principal source of profit is the difference between revenues from the actual management fees and the marketing, operating and service expenses incurred by the company.

The Phoenix manages provident funds and study funds through The Phoenix Pension and Provident Fund and through Excellence Provident and Pension, which manage remuneration and compensation funds, study funds, and a central severance pay fund.

In addition, The Phoenix manages pension funds on a smaller, although gradually increasing, scale. Pension funds allow policyholders to save for pension in the long term (old-age pension) and also provide cover for disability (disability pension) and death (survivors' pension). Old-age pension is an allowance paid to members from their retirement and for the rest of their lives. Disability pension is an allowance paid to members who have lost their ability to work, according to the decision of the fund's medical committee. The amount of the allowance is determined as a percentage of the effective income for disability and survivors, as defined in the fund's articles and based on the level of disability. Survivors' pension is an allowance paid to the survivors (widow and orphans) of members who have died during the insurance period or after the member becomes a pensioner. Like a disability pension, the survivors' pension is a percentage of the effective income for disability and survivors, as defined in the fund's articles.

Pension funds are divided into three types: senior pension funds (under special management/ ordinary management), new comprehensive pension funds, and new general pension funds. Remuneration fees received from pension fund members are divided into risk components (in the event that insurance coverage was purchased), a savings component, and a management fee component. Companies managing pension funds derive their revenues from management fees (from the contribution fees and from the accrued amounts), and the profit margin is the difference between the net management fees (after discounts, if they are given) and the management company's actual operating and marketing expenses. Pension fund claim payments (including annuity payments) do not directly affect the managing company's profits, as the insurance is mutual insurance and the policyholders bear the risk for claim payments.

2. Regulation:

Aside from the legal provisions set forth above, life insurance and long-term savings activities are subject to two principal legal frameworks:

The first framework includes the Insurance Contract Law, 1981; the Supervision of Financial Services (Insurance) Law, 1981; the Provident Funds Law; the Consultancy and Marketing Law; and regulations, orders and Commissioner's circulars issued by virtue of those laws. This legal framework governs material issues in The Phoenix's activity in the field of conclusion of an insurance contract, the duties of the parties to insurance contracts, terms and conditions of insurance schemes, due diligence for policyholders, and ways of operation for insurance agents, pension marketers and pension consultants. The legal framework also governs issues such as the corporate regime of institutional entities, the rules of investment, reports to policyholders and to the public, and so forth .

The second legal framework deals with the tax benefits of the pension instruments and includes the Income Tax Ordinance and the Income Tax Regulations (Conditions for Approval and Management of Provident Funds), 1964 ("the Provident Fund Regulations"). This legal framework confers a special status on provident funds, which also include pension funds and insurance funds, with regard to tax credits and deductions and exemptions from capital gains tax, with the aim of encouraging the public to save for retirement by means of provident funds and insurance funds. Life insurance schemes

which include an insurance component, and which are recognized as insurance funds ("managers' insurance policies" and "benefit policies for self-employed persons"), also benefit from the special status conferred upon provident funds by the Income Tax Ordinance and the Provident Fund Regulations. The Income Tax Ordinance and the regulations enacted by virtue thereof, generally speaking, set forth rules and tax provisions with regard to insurance schemes marketed by The Phoenix.

Within the framework of Amendment No. 3 to the Provident Funds Law, the tax rules which apply to the various pension savings products were unified, such that all products entitle savers to the same tax benefits, so that the public are able to make decisions based on their pension needs, with no bias due to tax considerations. The tax benefits primarily include the possibility of a tax credit for the policyholder / member, as well as a deduction permit for the employer. In addition, savings for retirement, pursuant to the tax provisions, enable exemptions from pension tax and capital gains tax.

It is further noted, that in February 2011, a committee was established headed by the Director General of the Ministry of Finance, for examining the tax benefits model for pension savings. The committee is to examine the feasibility of the "Life Cycle" model, which allows policyholders greater flexibility in enjoying tax benefits throughout their years of employment, and also grants tax benefits to some employees who do not currently receive them. The committee is also to examine the ability of the various organizations to implement this model quickly, and to recommend a tax benefit model for pension savings from among the alternative models.

For additional information about the regulatory restrictions in the life insurance and long-term savings segment, and reforms that are expected to affect this activity, see Section 1.12.2(A) above.

3. Changes in the scope of activity and profitability:

The scope of activities in the long-term savings segment has a high correlation to the conditions in the local economy.

Life insurance - The profitability of the life insurance sector is affected to a great degree by the results of investment in the capital market. According to data from the Ministry of Finance, at December 31, 2011,, assets under management in the life insurance branch amounted to NIS 211 billion, compared with NIS 205 billion at December 31, 2010, a 3% increase. The relatively low increase in the volume of assets under management in 2011 derives principally from the negative impact of the capital market and the yields attained in the capital market in 2011, which offset part of the net accrual for this year. It should be noted, that due to the negative yield in profit-sharing policies, accrued during the prior period, no variable management fees can be charged until a positive yield is achieved which will offset the negative real yield so far accumulated in profit-sharing policies between 1991 and 2003. Therefore, in 2008 and 2009, The Phoenix did not charge management fees. In 2010, The Phoenix charged variable management fees in the amount of approximately NIS 15 million and in 2011 it again did not charge variable management fees on profit-sharing policies that were marketed until 2004, due to the negative yields in the capital market in that year. As of December 31, 2011, the estimated uncharged management fees due to negative yield until the investment losses on these policies are covered amounted to NIS 279 million, compared with NIS 38 million at December 31, 2010. As of the end of February 2010, this amount was NIS 199 million.

Provident funds – According to Ministry of Finance data, the volume of assets managed in provident funds increased in 2011 by 4% over 2010, as compared to an increase of 9% in 2010 over 2009. Most of the decline in the volume of assets in the provident segment in 2011 can be attributed to negative yields attained in the capital market in 2011, and to a net negative accrual.

Pension funds – According to Ministry of Finance reports, total assets in the pension segment grew in 2011 by 8% over 2010, with accelerated growth continuing in the new pension funds segment, which grew by 13% in 2011, following 42% year-on-year growth in 2010. It is safe to assume that this elevated growth rate in assets is due to the rise in public awareness to pension savings in general and to retirement pension in particular, transfer from other long-term savings channels (mainly the pension funds segment), entry of insurance agents who began selling pension plans, and the coming into effect of the compulsory pension arrangement. The moderation in the rate of growth in 2011 compared with 2010 is principally the result of negative yields resulting from

developments in the capital market in 2011. In recent years, the pension funds have offered their customers discounts on the management fees, a trend that has contributed to lowering profitability in this segment.

2011 saw a 27% increase in remuneration fees and a 19% increase in assets under management in The Phoenix's new pension funds. In the reporting year, remuneration fees to provident funds managed by The Phoenix amounted to NIS 2,070 million, compared to NIS 1,488 million in 2010. Assets under management of The Phoenix's provident funds, that were affected by negative yields in the capital market and by non-recurring deposits in individually managed study funds declined compared with 2010.

4. Competition: In recent years, there have been changes in the long-term savings sector which have increased competition. The sector has become affected by substitute products that meet the need for retirement savings. The purpose of Ministry of Finance plan to enhance competition in the pension savings market, detailed in Section 1.12.2(D) above, is, inter alia, to increase transparency of the financial institutions towards savers, and this has been the guideline for the ministry's regulatory activity in recent years. The Bachar reform, which separated the provident funds and trust funds from the banks and allowed them to enter the pension product sector, also contributed to increased competition in the sector. Other reforms, such as annulment of the capital savings tracks under Amendment 3, increasing transparency and the mobility regulations also serve to increase market competition in the segment.

Life insurance - In Israel, there are five principal insurance groups in the life insurance sector: The Phoenix, Migdal, Clal, Harel and Menorah, as well as a number of smaller insurance companies. According to data provided by the Ministry of Finance, the five key insurance groups receive about 93% of total premiums in this segment in 2011, with The Phoenix in third place with regard to insurance premiums, with a market share of 16.2%, compared with market shares of 16% and 14.9% in 2010 and 2009, respectively. The market shares of the other principal groups in 2011 were as follows: Migdal (32.6%); Clal (22.2%); Harel (14.5%); and Menorah (8%).

Provident funds – The requirements set forth by the Bachar legislation for the sale of provident funds (and trust funds) by the banks, has led to a structural change in ownership in the provident funds segment, and a large portion of the provident funds offered for sale were acquired by the various insurance groups. Furthermore, due to expected regulatory demands by the Ministry of Finance, such as a increased equity requirements, and a requirement to reduce the number of funds held by a managing company (one fund of each type), the decline in the number of organizations managing provident funds continues. According to Ministry of Finance data, while the number of controlling corporations totaled 58 in 2008, this number went down to 49 in 2009 and 45 in 2010 and 2011, respectively.

Pension – The pension funds segment is characterized by increasing competition. As public awareness of pension savings has risen, so has the public's focus on investment management quality in the pension funds and on the yields delivered, as important factors when choosing a fund. The main players in the pension market (2011 data) are Menorah Mivtachim, (31.3%), Makefet Personal (Migdal Group) (24.5%), Meitavit – Atudot (Clal Group) (18%), Harel Pension (15%), and The Phoenix Pension and Provident Fund (including Excellence) (7.2%).

5. Investment management:

Investment management operations are subject to the provisions of the Supervision of Insurance Law and the Supervision of Financial Services Law (Provident Funds), 2005, and the regulations enacted thereunder, and are carried out through a number of designated investment managers. A distinction is made between the Nostro funds of the Group's companies, and management of policyholder and member funds (in The Phoenix Insurance and The Phoenix Pension and Provident Funds). In profit-sharing policies issued since 2004, the yield on the investments is attributed to the policyholders, while the insurer is entitled to fixed management fees only. In profit-sharing policies issued up to December 31, 2003, the yield on investments is attributed to the policyholders, while the insurer is entitled to fixed management fees and variable management fees on the real yield after deduction of the fixed management fees. In non-profit-sharing life insurance policies (for that part of the life insurance portfolio which is not backed by designated bonds), there is no direct correlation between the linkage basis prescribed for

assets and the linkage basis for liabilities. In pension and provident funds, the yield on investments, less of management fees from accrual after discounts, is attributed to members.

In 2011, The Phoenix's policy for investing in shares focused on gradually increasing the overseas share component; in the government bonds channel, most of the activity was concentrated in the shekel channels, while maintaining a medium-short average duration; activity in the corporate channel focused on the purchase of bonds issued with a high rating, and on the other hand selling bonds and bank debentures and capital notes bearing relatively low yields. In the share channel, the investment portfolio is weighted in favor of Israeli shares over foreign shares.

6. Principal segment products: In the life insurance segment, The Phoenix markets executive insurance, individual and group life insurance, disability insurance, a range of insurance plans and savings policies. The Phoenix offers the following basic insurance policies:

Executive insurance: This insurance includes a retirement savings component and consists of provisions made by both parties - both employee and employer (compensation and remuneration components). Premiums paid on the insurance policies are assigned to the various risks (mainly - death and disability) and to retirement savings. The retirement savings component could have been withdrawn as a capital component until December 31, 2007. Following Amendment 3 to the Provident Funds Law, retirement moneys can now only be withdrawn through an annuity track, except for the capital savings component for retirement accrued up to December 31, 2007, which remains a capital component. These policies target employers and their employees. Executive insurance is approved as an insurance fund under the Income Tax Regulations, and is entitles both employers and employees to various tax benefits.

Personal insurance: There are two types, intended for the self-employed and private individuals: compensation for self-employed individuals – policies governed by the Provident Fund Regulations that enjoy tax benefits at the time of deposit and withdrawal; personal insurance policies not approved as provident funds, which do not enjoy tax benefits, apart from a 25% credit for premium paid for death coverage. The terms for the personal policies sold from 2004 were brought in line with those for executive insurance.

Other insurance policies offered by The Phoenix are pure risk life insurance, work disability insurance and more.

Guaranteed-yield policies carry a charge for the difference between the guaranteed yield for the insured and the actual yield. In profit-sharing policies, management fees are charged according to the particular policy. These management fees are calculated according to the Commissioner's instructions based on the policies' yields, and are charged from the accumulated savings of the insured in the profit-sharing portfolio. Management fees for policies sold until December 31, 2003 include fixed management fees of 0.6% a year of the accrued assets, plus up to 15% of the real yield net of the fixed management fees ("variable management fees"). If a real loss accumulates, the insurance companies are not entitled to variable management fees, and this until the accrued loss is covered. The management fees for policies that were sold from 2004 onwards include fixed management fees from the accrued assets that are independent of investment performance, i.e. they are not variable management fees. For insurance policies that are sold as an insurance fund, these management fees shall not exceed 2% a year. For information regarding the estimate for management fees not charged due to negative yields, see section 1.12.3(A)(3) above.

The Phoenix operates in the pension and provident fund segments through The Phoenix Pension and Provident Funds and through Excellence Nessuah Provident and Pension. Provident funds are operated according to the Income Tax Regulations (Rules for Approval and Management of Provident Funds), 1964. The main provident fund products are personal provident funds for rewards and compensation, which serve for reward and compensation payments for salaried employees and self-employed individuals. Excellence offers personal funds under various tracks according to the level of savings chosen by the member; central provident funds for compensation, which target employers seeking to accumulate funds to guarantee severance pay for their employees. These funds are closed to new members as of January 1, 2006, and as of January 2011 no new moneys are deposited in these funds; study funds, targeting salaried employees and self-

employed individuals, and which allow members to accumulate moneys for continuing education and to receive tax benefits. Moneys accumulating in the fund can be withdrawn for continuing education purposes starting three years after the initial deposit. After 6 years of membership in the fund, the moneys can be withdrawn for any purpose; individually managed provident fund / study fund - in these funds, members can manage their savings independently and/or through an investment manager of their choice, under investment restrictions to be monitored by the company managing the savings. At the date of this report, The Phoenix Pension and Provident Funds manages five provident funds and Excellence Provident and Pension Funds manages 4 personal pension and compensation funds (that include 15 different investment tracks), 3 study funds (that include 13 different investment tracks) and 11 central compensation funds.

In 2006-2008, Excellence acquired the provident fund operations which were previously managed by Mizrahi-Tefahot Bank, as well as additional provident funds managing assets whose value is not material for Excellence.

The Phoenix Provident and Pension manages the following pension funds: The Phoenix Comprehensive Pension, which in 2011 operated 14 insurance channels differing in their level of coverage, the nature of coverage, and the retirement age, and 5 investment channels; The Phoenix General Pension, which operates together with the comprehensive pension fund and any deposits above the aforesaid maximum are made to this fund. The fund operates two savings channels, is not entitled to designated debentures, but is not subject to restrictions on maximum deposits, and permits one-time deposits. Furthermore, the Amit Pension Fund for Veteran Associates, which is closed to new members, is managed by The Phoenix Pension Company For Managing Balanced Pension Funds Ltd.

Excellence Provident and Pension manages the following two pension funds: Excellence Nessuah Pension, a comprehensive pension fund which includes the three pension components (old-age, disability, and survivors) and offers, in addition to its savings component, a variety of pension channels, including insurance coverage for disability and death; and Excellence Nessuah Pension Savings, a basic-type (savings) new general pension fund. The fund does not include the insurance components, and so allows greater accumulation of monies for savings. Furthermore, the fund permits one-time deposits. The fund invests 100% of its assets in non-guaranteed investments.

"The Phoenix Method" for investment management – In 2009, The Phoenix launched "The Phoenix Method" for managing long-term savings ("The Phoenix Method" or "the Method"). This program implements a well-known methodology implemented around the world (mainly in the United States and Europe) for managing pension savings investments. "The Phoenix Method" is based on the establishment of personal pension savings portfolios using the Life Cycle method, which is customized to the preferences and characteristics of each particular client (mainly based on the client's risk range and risk perception). In this way, the pension portfolio can be customized to the characteristics and preferences of each customer, unrelated to and independently of the other savers in the same fund. Asset allocation for each customer is carried out using indices. In "The Phoenix Method", the investment portfolio is managed in a way that does not require the client's active intervention, based on a unique model developed by The Phoenix, in collaboration with members of academia, and based on research in Israel and abroad. It should be noted that the method fits the possible future shape of the investment management system as determined in several drafts published by the Commissioner concerning a long-term savings model adapted to the saver's age as described in Section 1.12.2 above.

Policies whose investment portfolios are managed according to "The Phoenix Method" accounted for the bulk of The Phoenix's total executive insurance sales in the reporting year. As of December 31, 2011, insurance schemes whose investment portfolios are managed according to "The Phoenix Method" accumulated NIS 1,371 million. Furthermore, starting in 2010, The Phoenix's pension customers have also been offered the possibility of managing their investments according to "The Phoenix Method". From 2011 sales of pension policies where the customers prefer to manage their investments according to this method, account for 85% of the fund's total sales.

7. Clients: The Phoenix markets its products to a wide range of customers, divided into three main groups – employers and employees, individuals and self-employed and cooperatives. The Phoenix Insurance is not materially dependent on any single customer.

In 2011, the breakdown of life insurance premiums was as follows: employers (executive insurance) – 74%, individuals and self-employed – 23%, collectives – 3%. In the pension segment, the number of members in The Phoenix Pension and Provident grew by 18% in 2011 compared to 2010, following a 28% increase in the number of members in 2010 over 2009. A considerable part of this increase can be attributed to new policyholder subscriptions following the compulsory pension arrangement. Excellence Provident and Pension saw a decrease of 7%.

In 2011, members in The Phoenix Pension and Provident and in Excellence Provident and Pension's provident funds were distributed according to the following types: in study funds: employees - 75% and 75%, respectively. Self-employed individuals - 25% and 25%, respectively; in funds for compensation and remuneration: employees - 67% and 71% respectively. Self-employed individuals - 33% and 29%, respectively.

8. Marketing and distribution: Until the Bachar reforms, most life insurance plans were sold by insurance agents, including independent agents and agencies, and agencies owned by insurance companies. The Bachar legislation in general, and the Consultancy and Marketing Law in particular, led to changes in the sale and distribution of life insurance schemes and pension and provident fund products and is expected to lead to additional material changes in the future. The aforesaid legislation prescribed two tracks for distribution of pension products: pension consultancy (a person or corporate entity providing consultancy to an individual with regard to the feasibility of savings for that individual by means of a pension product to which the person or entity providing consultancy has no affinity); and pension marketing (which is carried out through a pension insurance agent or a pension marketing agent, defined as the employee of an institutional entity, with an affinity to the pension products which he or she markets). Pension consultants, including banks, will receive a distribution commission at the rate of up to 0.25% of the assets and will distribute pension products including all products in the sector, which they will be required to adjust to the client's needs. There is a limit on the commission for pension consultants, whereas there is no limit for pension marketers who may receive various commissions. On January 1, 2008, an amendment to the Consultancy and Marketing Law came into effect, allowing pension consultants who are banking corporations to give advice in respect of all long-term savings products – pension funds, provident funds and life insurance and they will receive a uniform distribution commission for this from the institutional entities. The purpose of this amendment is to enhance the consultant's objectivity, to prevent a general tendency on the part of the consultant in favor of certain types of pension products for which he receives a commission, and to improve the quality of service to the public. The Bachar reform sought to separate the banks, as the entity producing the products (provident funds only) from the entity that distributes the products. At the same time, it enabled the banks to increase their presence as the distributors of pension products and to allow them to operate as pension consultants, and as an important new entity in the distribution of pension products. Nevertheless, the Bachar legislation imposed limitations regarding the banks activity as distributors of pension products (the Advice and Marketing Law defined restrictions pertaining to pension consultancy licenses granted to banks). The banks' entry into the pension consultation market can potentially lead to a significant increase in the sales of segment products due to new target markets being exposed to the institutional entities. However, it is also liable to significantly cannibalize existing marketing channels. At the date of this report, and to the best of The Phoenix's knowledge, the banks that received a pension consulting license from the Ministry of Finance are Union Bank, Mizrahi-Tefahot, Discount Bank, FIBI - First International Bank of Israel, Mercantile-Discount, Otsar Hahayal, Bank Poaley Agudat Israel (PAGI), Arab-Israel Bank, Bank Leumi and Bank Hapoalim.

The Phoenix life insurance policies are marketed mainly by agents who receive handling fees and commissions at various rates. The rate of the commission is determined by the type of product, the scope of performance of the agent, the profitability of each agent's insurance portfolio, and according to negotiations with each agent. The insurance agents work with sales managers who are employed by The Phoenix Insurance and serve as mentors on sales matters and help resolve on-going problems. The commissions paid are generally determined as a percentage of the management fees, the premium and/or accrual or the margins on each policy. Commissions are also paid for the sales activity of the respective agent. The percentage of commissions paid to agents with regard to all

kinds of life insurance and long-term insurance mentioned above varies (some commissions are paid as advances during the first year of the lifespan of the policy).

Starting January 1, 2004, changes have been made in new life insurance schemes marketed by The Phoenix Insurance, which are based in part on reducing the premium component for coverage of expenses and profit. These changes led to changes in the commission agreements with the agents, principally involving a reduction in the commissions paid to agents in the first year of the policy and an extension of the period over which the commissions are spread out. As a result, most of the commissions and handling fees for the majority of the new "track" policies are spread out over the lifespan of the policy, on an ongoing basis, as long as the policy remains in force.

In addition, The Phoenix customarily provides loans in various amounts to its agents (irrespective of their commitment to performance). The loans to agents are secured with various collaterals. The regulations for investment methods and the Commissioner of Insurance's circulars set limits on the granting of loans to agents.

Likewise, The Phoenix Pension and Provident's pension funds are usually marketed through agents, and The Phoenix Pension does not have any exclusivity agreements with its agents. The remuneration structure for agents usually consists of handling fees to a certain percentage of the management fees, and in certain cases a volume-based commission at a variable rate from new sales. The provident funds are also marketed through agents. The provident funds do not have exclusivity agreements with any agent whatsoever. The agents' fees in this segment consist of a certain percentage of the management fees.

Additionally, The Phoenix Pension and Provident signed distribution agreements for its products with most of the banks. Under these agreements distribution of pension and provident products is carried out in consideration for a distribution commission at the maximum rates prescribed by the consultancy regulations.

It should be noted that as part of the Ministry of Finance's plan to enhance competition in the pension savings market, it has been proposed that a limit be placed on the size of the commissions, bonuses and prizes paid to insurance agents that are linked to sales targets, concurrent with the possible increase in distribution fees paid to pension consultants, including banks. If these proposals are advanced, they will bring about changes in the mix of the distribution channels so as to increase the feasibility of distribution by pension consultants and banks, and reduce the feasibility of distribution by small and medium-sized agents.

Excellence's pension and provident funds' activities are marketed through a number of primary distribution channels: (1) pension marketers for Excellence Nessuah Pension and Provident Funds, through self-initiated contact with potential customers, and mainly by contacting companies and organizations employing a large number of employees; (2) insurance agents and independent marketers; (3) investment consultants and pension consultants in banks, working with those banks that have signed a distribution agreement.

B. Compulsory vehicle insurance

1. General: Compulsory vehicle insurance is required of every person using or allowing others to use a motor vehicle, pursuant to the Motor Vehicle Insurance Ordinance (New Version), 1970 ("the Motor Vehicle Insurance Ordinance"), and covers and it covers the vehicle owner and the driver against any liability they may incur under the Compensation for Road Accident Victims Law, 1975 ("The Road Accident Victims Law") and against any other liability they may incur on account of physical injury caused by or as a result of the use of a motor vehicle to the driver, passengers, or pedestrians who were injured by the vehicle.

Pursuant to the Motor Vehicle Insurance Regulations (Establishment and Management of Databases), 2004, a database operator has been established in the compulsory vehicle insurance field, who is responsible for managing the database and producing user reports, inter alia, to assess the risks in the compulsory vehicle insurance sector and determine the pure risk cost on the basis of which the compulsory insurance tariffs are determined.

Circulars issued by the Commissioner of Insurance establish various parameters which the insurer may use in setting the tariffs, such as engine capacity and driver age and/or sex and

driving experience, and the procedures according to which the insurer is required to act in all matters relating to approval of premium and maximum tariffs which may be collected by the insurer ("Differential Tariff"). The insurance companies have been permitted to use different tariff formulas for vehicle fleets and collectives with approval from the Commissioner of Insurance.

The following entities are also active in compulsory vehicle insurance: (a) residual insurance ("the Pool") - the Pool provides cover for compulsory insurance for the owners of motor vehicles for extraordinary risks that commercial insurance companies have no interest in insuring (mainly motorbikes and ATVs), as these are generally loss-making items. The pool is an arrangement based on insurance shared by all the insurers and is regulated in the Motor Vehicle Insurance (Residual insurance arrangement and mechanism for setting the tariff) Regulations, 2001, by virtue of which a joint corporation of the insurers was established which manages the Pool. The pool operates as an insurer and its tariffs are set by the Commissioner of Insurance, and they are higher than the tariffs of the other insurers. In 2011, The Phoenix's share of the compulsory vehicle insurance market declined, so that its relative share in the 2012 underwriting year will decline from 8.9% in 2011 to 8.4% in 2012. It should be noted that recently an amendment to the Motor Vehicle Insurance Ordinance was approved, which is likely to increase the Pool's losses and raise the burden on the insurance companies to cover these losses; (b) Karnit – The Fund for Compensation of Road Accident Victims – a corporation established under the Road Accident Victims Law to pay compensation to road accident victims who are entitled to compensation under the law but cannot claim compensation from the insurance companies. Pursuant to the provisions of the Compensation for Road Accident Victims Ordinance (Financing of the Fund) (Amendment), 2003, the insurance companies are required to transfer to Karnit 1% of the risk premiums for compulsory motor vehicle insurance policies which come into effect.

Standard policy – In January 2010, the Minister of Finance published the Supervision of Financial Services Regulations (Insurance) (Terms of a Motor Vehicle Insurance Policy) 2010 ("the Regulations"), which replace and annul the Motor Vehicle Insurance Regulations (Insurance Certificates) 1970. The Regulations prescribe minimum mandatory terms for compulsory vehicle insurance (the Standard Policy) and include, inter alia, provisions regarding the form and terms of the insurance certificate including the requirement for special emphasis of those sections detailed in the Regulations and the option to emphasize additional sections. Furthermore, the Regulations state that insurance companies may add an expansion appendix regarding the scope of coverage, but are prohibited from changing the wording of the standard policy or the insurance certificate, or changing the order of the sections in the standard policy.

2. Characteristics of compulsory vehicle insurance: The sector contains one product: insurance cover under the Motor Vehicle Insurance Ordinance for the owner of a vehicle and its driver against any liability which they might incur under the Road Accident Victims Law and any liability which they might incur following bodily harm caused by or as the result of use of the motor vehicle to the driver of the vehicle, passengers therein or pedestrians injured by the vehicle as the result of use thereof. The characteristics include absolute liability of the insurer, limit of compensation, entry of the insurance into force only after full payment of the premium, legal proceedings conducted over a long period of time, uniformity of coverage and competition on tariffs, obligation to insure, and separation of grounds (persons granted grounds for claims under the Road Accident Victims Law, must sue for damages strictly and only under this law). As aforesaid, in January 2010 the Commissioner of Insurance published the Supervision of Financial Services Regulations (Insurance) (Terms of a Motor Vehicle Compulsory Insurance Policy), 2010. These regulations prescribe a standard policy for compulsory motor vehicle insurance and the wording of the compulsory insurance for trading in vehicles.
3. Clients: The Phoenix's clients are private clients, business clients, collectives, large vehicle fleets, and Israel Railways. In 2011, the distribution of (gross) insurance premiums paid by The Phoenix's clients was 13.8% by large vehicle fleets, collectives and Israel Railways, and 86.2% by the remaining policyholders (mostly individual policyholders), compared with 14.2% and 85.8%, respectively, in 2010.
4. Competition: All insurance companies offer compulsory vehicle insurance. As the insurance coverage is uniform and market volume is limited, competition in compulsory vehicle insurance focuses on insurance tariffs, service provided to the policyholders, the

percentages of commissions paid by the various companies to their insurance agents, and correct segmentation of the population groups of drivers and pricing of the policies offered to them. According to data from the Ministry of Finance for the first nine months of 2010, The Phoenix's share of the compulsory vehicle sector in 2011 was 8.3% for gross insurance premiums for the sector, compared to 9.2% in 2010. The Phoenix is ranked fifth after Menorah (13.7%), Clal (12.8%), Harel (12.6%), and Eliahu (9.5%). The Phoenix is working to increase its market share, taking care to maintain the quality of its portfolio and profits, while applying command and control instruments to improve and enhance the underwriting systems.

5. Financial data - distribution of profit (loss) on retention for products and services in the field of compulsory vehicle insurance in 2011 and 2010 (in NIS millions):

	2011	2010
Gross premiums	374	389
Premiums less reinsurance (on retention)	360	374
Gross claims	292	368
Claims on retention	306	375

The decline in premiums in 2011 over 2010 was largely the result of a decline in premiums charged for the compulsory vehicle transaction of a large policyholder, and lower tariffs during the second half of the year. The decline in claims in 2011 compared with 2010 is due, inter alia, to a decline in estimates for outstanding claims in respect of old years, and due to a decline in the outlay for medical expense payments for the 2009 to 2011 underwriting years.

C. Property vehicle insurance

1. General: Vehicle insurance (known as CASCO or comprehensive insurance) is the most common optional insurance within the field of general insurance. Property vehicle insurance includes cover for property damage to the insured vehicle ("Comprehensive Insurance") and for damage caused by the insured vehicle to third parties ("Third Party Insurance").
2. Characteristics of property vehicle insurance: The Phoenix markets property vehicle insurance which covers property damage caused to the insured vehicle and property damage caused by the insured's vehicle to a third party. As aforesaid, property vehicle insurance is optional insurance. The insurance policy for a private vehicle and a commercial vehicle weighing up to 4 tons is based on the terms of the standard policy which are determined in the Supervision Regulations of Insurance Businesses (Terms of a Private Vehicle Insurance Contract) 1986. The wording of the standard policy is binding and it is possible only to improve its terms and add expansions in respect of the scope of cover, risks, property and liabilities of policyholders. The property vehicle insurance tariff is a differential actuarial tariff (variable and risk-adjusted) which is subject to approval from the Commissioner of Insurance. This tariff is determined on the basis of a number of parameters which include, among others: model of vehicle, engine capacity, year of manufacture, protection type, number of drivers, sex and age of the drivers, experience, and previous claims. Standard policy terms include coverage in case of accident, theft, fire, malicious damage, damage by natural elements, property damages caused to third parties, etc. The Phoenix Insurance offers various expanded coverages, such as coverage for earthquake risks, riots and strikes, as well as ancillary services such as towing, replacement vehicle in case of accident or theft, and glass breakage insurance. The Phoenix also offers a variety of insurance options for commercial vehicles weighing more than 4 tons, at terms which are customary in Israel and at tariffs which are reviewed periodically. The size of the potential market is limited to the number of vehicles in Israel and so the market is relatively stable and the competition focuses on reducing tariffs and improving service. The sector is also characterized by the short period of time taken to complete the processing of claims.
3. Clients: Most of The Phoenix's clients are individuals, corporate clients, collectives and vehicle fleets. The bulk of The Phoenix's premiums in this sector are derived from individual and corporate clients (92.6% in 2011 and 92.3% in 2010), while the remaining premiums (7.4% in 2011 and 7.4% in 2010) come from large vehicle fleets and collectives.

4. Competition: The property vehicle insurance sector is characterized by fierce competition, mainly due to little difference in the insurance covers offered by the different companies, which is reflected mainly in the reduction of tariffs and increase in commissions. The competition is principally focused on insurance tariffs, service, the percentages of commissions paid by the various companies to their insurance agents, and correct segmentation of the population groups of drivers and pricing of the policies offered to them. According to data from the Ministry of Finance, in the first nine months of 2011, The Phoenix's market share is 12.2% (fourth place in the sector), an increase of 0.4% over 2010, after Harel (15.7%), Menorah (15.2%) and Clal (12.2%).
5. Financial data for products and services in the property vehicle segment in 2010 – 2011 (in NIS millions):

	2011	2010
Gross premiums	728	668
Premiums less reinsurance (on retention)	728	668
Gross claims	513	420
Claims on retention	513	420

Premiums rose steadily in 2011 over 2010 due to the expanding volume of the insured motor vehicle portfolio. The average premium declined due to competition in this segment. The increase in claims is mainly due to the expanding volume of the insured motor vehicle portfolio.

6. Recommendations of the committee to increase competition in the vehicle sector (Zelekha committee):

In February 2012, the Committee to increase competition in the vehicle sector submitted its report. The report contained, inter alia, recommendations pertaining to the manner in which insurance companies operate vis-à-vis "arrangement garages", and changes in the method of choosing assessors (including, a prohibition on the insurance companies' involvement in choosing the assessor and determining his fee). The Company believes that if these these recommendations are adopted as part of binding legislation, they may increase the scope of compensation paid by The Phoenix on vehicle property claims. Nevertheless, at this stage, the Company is unable to estimate the full ramifications of the aforementioned recommendations, if they are accepted, in part as, at present, they are only recommendations and there is no way of knowing whether they will be passed as binding legislation and what the wording of such legislation will be.

D. Other general insurance

1. General: Other general insurance includes a wide range of insurance cover, which may be divided into three principal sectors:

Property insurance: Provides coverage against loss or physical damage to property owned by the policyholder or for which he is responsible. It includes insurance for residences, business premises, and engineering insurances. The principal risks covered by property insurance policies are fire, explosion, and risk of burglary, earthquake and natural disasters. Property insurance includes coverage for direct damages to the policyholder's property caused by the realization of those risks set forth in the policy, and coverage for indirect damages (insofar as additional coverages have been purchased). Generally speaking, the term of the policy is one year, with a limitation period of three years from the entitling event for property insurance claims. Claims against property insurance policies are clarified shortly after the occurrence of the insurance event (and so this sector is considered as having a "short claims tail").

Liability insurance:

In the case of liability insurance, the insurer indemnifies policyholders for their financial liability towards third parties, up to the limit of liability stated in the policy. Liability insurance includes third-party liability insurance, employers' liability insurance, professional liability insurance (including directors' and officers' liability insurance) and product liability insurance. The limitation period in liability policies does not end so long as the third party's claim against the policyholder remains valid. In general, the term of the policy is one year, but in light of the long period of time which passes from the date of the

incident, and the formulation and filing of the claim, as well as the length of time required for factual and legal clarification of the claim, this sector is considered as having a "long claims tail", and recognition of profits is postponed for a period of at least three years.

In some types of liability insurance (primarily third-party liability insurance and employers' liability insurance), the cover is on a per-event basis. In other words, cover is given to events which occurred during the term of the insurance, and the claim may be filed after the term of the insurance has expired, subject to the statute of limitations. In other types of liability insurance (primarily professional liability insurance, directors' and officeholders' liability insurance, and product liability insurance), the cover is based on the date the claim is filed. In other words, cover is given to claims which were initially filed during the term of the insurance, even if the grounds for these claims arose prior to the term of the insurance, but after the date prescribed in the policy as the retroactive date.

Other insurance: This category includes types of insurance coverage which are not property or liability insurance, such as short-term personal accident insurance (which covers death or permanent full or partial disability resulting from an accident and/or temporary work disability resulting from an accident or illness) or contractor work insurance (coverage for losses or unexpected physical damage to the project).

The scope of activity in the field of other general insurance is related to factors such as the frequency of the event insured (for example: increase in the number of burglaries of business premises or residential properties), the economic situation of the potential policyholders, their willingness to take out insurance policies, as against other means of managing and reducing risks, and the overall scope of economic activity in Israel. Insurance policies in this field often provide insurance packages ("umbrella" insurance) which include various types of cover – both property and liability insurance.

2. Clients: In 2011, most of The Phoenix's clients in the other general insurance sector were private policyholders and business clients (98%). The remaining 2% of the gross insurance premiums come from large corporate clients. The comparative figures in 2010 were 95.9% and 4.1%.
3. Financial data of "other general insurance" products for 2011-2010, broken down by sectors (in NIS millions):

Property insurance

	2011	2010
Gross premiums	575	531
Premium less reinsurance (on retention)	255	242
Gross claims	328	266
Claims on retention	101	85

The segment shows on-going growth. The increase in premiums in 2011 over 2010 is evident in most branches, but focuses on household and engineering. In 2011, gross claims increased due to a large claim in the property loss branch that was covered by reinsurance.

Liability insurance

	2011	2010
Gross premiums	347	329
Premium less reinsurance (on retention)	254	238
Gross claims	193	256
Claims on retention	166	185

The increase in premiums in 2011 is marked in all sectors, but mainly in the professional liability branch. The decline in claims, gross and on retention, in 2011 compared with 2010 is mainly due to closure without payment of a large claim and to the release of reserves.

Other insurance

	2011	2010
Gross premiums	27	33
Premium less reinsurance (on retention)	25	15
Gross claims	19	18
Claims on retention	9	10

The decline in premiums in 2011 centers on personal accident insurance, due to the fact that this activity was transferred to the health segment. The increase in premiums on retention in 2011 is due to a change in the reinsurance arrangements. The source of the decline is gross claims compared with 2009, originating with the non-renewal of loss-making transactions in the personal accident branch.

4. Competition: The general insurance sector is characterized by fierce competition which is reflected in the adaptation of the insurance policies to clients' needs, entry into specific insurance niches, reduction of tariffs and special discounts. The Phoenix's competitors in the general insurance sector are most of the insurance companies. According to data from the Ministry of Finance for the first nine months of 2011, The Phoenix is in third place in this field, with 12.7% (compared to 12.4% in 2010) after Clal (21%) and Harel (17.8%).

E. Health insurance

1. General: Health insurance policies are intended to indemnify or compensate policyholders for medical expenses in cases of harm to their health. These policies include cover for transplant expenses, medication which is not subsidized by the state, private medicine and hospitalization expenses. Moreover, this segment includes nursing care insurance, insurance for serious illness, dental insurance, sick day insurance, travel insurance, insurance for Israelis overseas, insurance for foreign workers living in Israel, and personal accident insurance. For the above insurance schemes, the insurance term is greater than one year (personal accident insurance for periods of up to one year is included under general insurance). Health insurance in Israel is divided into three layers: first layer - state-subsidized health services; second layer - additional health services, which expands or substitutes the state-subsidized health services and is provided solely by the HMOs; third layer - private health insurance purchased from insurance companies. The health insurance market is a growing market, which is a part of the total national expenditure on health in Israel, and the percentage of persons purchasing private insurance policies is constantly increasing. The Phoenix offers a range of insurance plans which are updated in accordance with the rate of technological progress and medical treatments in Israel and worldwide. The health insurance policies marketed by The Phoenix are under the "Health Line" brand. The Phoenix also operates a customer relations center which handles enquiries from policyholders, answers questions regarding the various insurance plans, and markets and operates the various policies.

According to Ministry of Finance data, in the first nine months of 2011, there was a 14.2% increase in the volume of gross insurance premiums earned in the health insurance sector compared with the corresponding period in 2010. This compares with a 11.7% increase in 2010 over 2009.

Premiums for The Phoenix Insurance's health insurance activities increased in 2011, amounting to NIS 1,147 million compared with NIS 1,085 million in 2010, an increase of 5.7%. The increase is due mainly to marketing efforts in private policies and an increase in insurance for collectives.

Activity in health insurance, similar to other fields of insurance, is subject to the legal provisions which apply to insurers and the directives from the Commissioner of Insurance. The trend in regulation in recent years has been toward standardization of the basic terms of the insurance policy and increased transparency in the terms of insurance policies.

2. Principal products: The Phoenix markets health insurance, illness and hospitalization insurance, nursing care insurance, dental insurance, insurance for foreign workers living abroad, chronic illness insurance, sick day insurance, insurance for Israelis overseas, travel abroad insurance, and personal accident insurance (for periods of more than one

year). Health insurance includes compensation or indemnification for expenses related to surgery, transplants and/or special treatments in other countries, cover for drugs which are not included in the State "health basket", alternative treatments, compensation for serious diseases, medical services using advanced technologies, ambulatory medical services, etc., all according to the insurance schemes purchased for or by the policyholders. Supplementary products are added to the insurance schemes which offer a wide range of options for expanding the insurance cover in accordance with the needs of the policyholder.

3. Clients: Health insurance clients can be divided into three principal groups: individual policyholders who can construct a customized insurance scheme, both as regards insurance coverage and as regards premium payments; group insurance for employees and families and employees, unions and major companies in Israel; members of Israel's HMOs who purchase coverage for additional health services. The Phoenix's additional health service operations include nursing care coverage to Meuhedet Healthcare Services members as part of the "Meuhedet Gold" coverage plan. In 2011, the distribution of premiums was as follows: 51.3% from private clients; 35.7% from group insurance clients; and 13% from members of Israel's HMOs, compared with 49.8%, 34.8% and 15.3%, respectively, in 2010.
4. Competition: The health insurance segment is characterized by stiff competition due, inter alia, to the numerous competitors and the similarity between products. The share of the collective insurance schemes in the segment is growing consistently. The dominant insurance group in the field of health insurance is Harel. At the end of 2011, Harel held 41% of that market. This market share is due, inter alia, to Harel's holding 100% of Dikla Insurance Co. Ltd., which provides group nursing care insurance for the members of the Clalit Health Services HMO, as part of that HMO's additional health services.

The other main competitors in this area are Clal, Migdal and Menorah and the supplementary service programs of Israel's HMOs. The Phoenix has increased its market share in recent years. According to data from the Ministry of Finance for the first nine months of 2011, The Phoenix is ranked third in this field from the standpoint of gross insurance premiums, with 18.6%, after Harel (41.1%) and Clal (22%), and before Migdal (10.1%).

The Phoenix copes with competition in the field by pricing its products properly, taking into account, among other things, distribution and sales commissions, operating costs, cost of risk, the existence of high-quality information concerning risks on the basis of past experience and the analysis thereof, use of reinsurance contracts for the transfer of risks, aggressive marketing, improving service, and offering attractive products to policyholders, including policyholders with special coverage needs.

In 2011, The Phoenix launched a new and improved personal accident insurance policy that meets the growing need for a personal accident insurance product among customers and agents, and a product offering weekly compensation resulting from an accident that provides a fixed, pre-determined sum insured for loss of function that causes work disability. In January 2012, The Phoenix launched a package of coverages for coping with cancer. The package includes a service note entitling policyholders who have cancer to personalized management of their medical file and the constant care and supervision of a team of specialists from the Assuta Hospital during the course of the illness.

5. Financial data of health insurance products for 2010-2011 (NIS millions):

	2010	2010
Gross premiums	1,147	1,085
Premiums less reinsurance (in retention)	984	925
Increase in liabilities and payments for insurance contracts	705	784
Increase in insurance liabilities and payments for insurance contracts (retention)	649	633

The high increase in retention premiums compared with gross premiums in 2010 is due to the termination of cover for medicines for members of Maccabi Healthcare Services, which was reinsurance intensive. The decline in gross claims (and the more moderate

increase in retention claims) can be attributed to the decline in the insurance reserve due to a decline in the incidence rates, principally on surgery and hospitalization products.

F. Financial services

1. General

The Phoenix operates in the financial services segment through Excellence, 78.56% of whose shares are held by The Phoenix as of the report date²²⁶.

Excellence is a public company and its shares are listed for trading on the TASE. Excellence, through companies under its control (jointly: "Excellence"), is involved in a variety of activities in the capital market: marketing and management of investments for customers, management of mutual funds, underwriting and investment banking, issuing of structured products, issuing of financial products, and provision of stock exchange and trading services. In addition, Excellence is engaged in the management of provident and pension funds as detailed in section (A) above.

- A) Investment marketing and portfolio management for clients – This field includes the following Excellence activities: marketing and investment management services in Israel and abroad; management of mutual funds; and a real estate investment trust (REIT).

Investment portfolio marketing and management operations are carried out through Excellence Nessuah Investment Management Ltd., which is licensed to manage and market investments under the Consultation and Marketing Law. In addition, some of the portfolio management activities are carried out through a strategic partner Invesco Asset Management Ltd.

Trust fund management operations are carried out through Excellence Nessuah Trust Fund Management Ltd.

On June 9, 2009, Excellence and the companies under its control finalized their agreement with Prisma Investment House Ltd. ("Prisma") to acquire Prisma's trust fund, index-linked certificates and portfolio management operations. Upon the completion of the Prisma transaction, and after integrating its operations in Excellence, Excellence continued the process of merging similar funds on the one hand, and setting up new funds, including index funds, on the other. At the date of publication of this report, The Phoenix manages 141 mutual funds through Excellence Mutual Funds (previously Prisma Mutual Funds Ltd.) in most of the existing investment management channels.

- B) Underwriting and investment banking – Excellence, through Excellence Nessuah Underwriting (1993) Ltd., provides services in underwriting, management, consultancy and distribution for public and private offerings in Israel. The company engages in securities transactions (including offers of sale) and distribution of securities, brokerage and consultancy in securities and financing transactions. Excellence also takes part in the management of IPOs and serves as manager of an underwriter or distributor consortium and/or as an underwriter or distributor, as applicable.
- C) Issue of structured products – Beginning in 2002, Excellence is involved in the issue of negotiable structured securities on the TASE. All structured securities were issued through a private company whose shares are not listed and shall not be listed for trade on the TASE and the company's sole activity is the issue of bonds and dealing with assets mortgaged in favor of those holding the bonds (in this section; "the Issuing Companies"). The issuing companies are controlled by Excellence and are special purpose companies (SPCs) established for the issuing of bonds, and which are prohibited from undertaking any other activity.

In January 2011, Shaharit Capital Markets Ltd. and Shaharit Issuances Ltd, that issued 2 series of active debentures that are traded on the TASE, were acquired. On February 2, 2011, Excellence reported that it had reached agreement in principle with Clal Finance Underwriting ("Clal Underwriting") to acquire all the holdings of Clal Underwriting in the following companies: Gilboa Dollar Ltd., Eden Dollar Ltd., Galila

²²⁶ Regarding the Excellence transaction, in which The Phoenix will purchase a further 10.22% of Excellence's share capital, see Note 14 to the financial statements.

Deposits Ltd., and Galileo Debentures Ltd. ("the Acquired Companies"), which issued structured debentures and deposit certificates to the public in consideration of NIS 8.5 million. At December 31, 2011, the assets under management of the Acquired Companies was NIS 2.263 million. In view of the above, and after the date of completion of the transaction, The Phoenix expects to be the largest group in the structured products sector traded on the Stock Exchange.

- D) Issue of financial instruments – Excellence, through a number of KSM companies, is involved in the issue of and trading in index-linked certificates, composite certificates, short certificates, commodity certificates and coverage options for the public. Each of the series of index-linked certificates was issued through a company with just one commercial activity – the issuing of index-linked certificates and dealing with assets mortgaged in favor of those holding the certificates. The KSM companies specialize in the management of index-linked products. Excellence began issuing certificates of deposit in 2004, through KSM Jambo, Paz Foreign Deposit Ltd., Paz Foreign Deposit 2 Ltd. and KSM Currencies Ltd. Furthermore, Prisma Currencies Ltd. was purchased in 2009. All certificates of deposit are issued through a company with just one commercial activity – the issuing of certificates of deposit and dealing with assets mortgaged in favor of those holding the certificates of deposit. Certificates of deposit are linked to the rate of exchange for a variety of currencies against the Israeli shekel (excluding KSM Jumbo) and bear interest.
- E) Brokerage and trading services – Excellence, through a TASE member company, is involved in marketing and investment services and brokerage services (trading in securities and derivatives) for local and foreign customers in Israel and abroad. Excellence specializes in all trade channels including shares, bonds in Israel, bonds abroad, derivatives, foreign securities, issues and distributions. Excellence Nessuah Brokerage Services Ltd. ("Excellence Nessuah Brokerage" or "the TASE Member") is licensed to market investments pursuant to the Consultancy Law and it has been a member of the stock exchange since August 1978. The TASE Member provides services in investment marketing and securities trading on the TASE and in overseas markets and market making in shares and government bonds for local and foreign clients. It should be noted that in light of the amendment to the Joint Investments Trust Law from February 2010, whereby a fund manager may only enter into agreement with a trading company for payment of commissions from the assets of a fund that it manages for transactions performed in the fund's assets, by way of a tender, many fund managers suspended their engagements with trading companies and transferred this activity to the banks. As a result, the scope of the institutional brokerage activity with respect to activity with related parties and vis-a-vis institutional entities that are not affiliates was reduced, leading to a decline in revenues.

Details of the Excellence's revenue, by field of activities, the costs attributed to each field of activity and the operating profit from each field, at December 31, 2010 and 2011 (in NIS millions):²²⁷

	TASE and trading services		Issue of structured products		Provident and pension funds		Investment underwriting and banking		Investment management		Issue of financial products	
	December 31, 2010	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Total revenue	47	46	7	20	219	230	8	20	171	200	132	120
Costs												
Variable costs that are not revenue in another segment	4	4	1	4	46	41	1	5	63	64	17	18
Fixed costs that are not revenues in another segment	27	26	6	10	106	114	3	3	70	73	41	43
Total costs	31	30	7	14	452	155	4	8	133	137	58	61
Operating profit	16	16	-	6	67	75	4	12	38	63	74	59
Total assets	287	271	788	1,210	414	426	27	23	316	410	19,526	18,127
Minority interest in segment revenues	-	-	-	-	-	-	-	-	-	3	7	5

In 2010 and 2011, Excellence's total assets amounted to NIS 20,651 million and NIS 21,567 million, respectively. Total liabilities amounted to NIS 19,949 million and NIS 20,763 million respectively. Turnover amounted to NIS 637 million and NIS 584 million, respectively. Operating profit amounted to NIS 231 million and NIS 199 million, respectively, and net profit amounted to NIS 148 million and NIS 108 million, respectively.

²²⁷ Data taken from Excellence's financial statements.

2. Limitations, legislation, standardization and special constraints

Excellence's operations in various areas in the capital market are subject to comprehensive regulation. The trust fund management segment is regulated under the provisions of the Joint Investments Trust Law and regulations made thereunder. Supervision of entities in this field and the enforcement of legislation are carried out by the Israel Securities Authority. Furthermore, the Bachar legislation set forth limitations on holding the means of control and on market shares for mutual fund managers. In November 2011, the Corporate Governance for Fund Managers and Portfolio Managers Law (Legislative amendments), 2011 ("Corporate Governance Law") was published in the Official Gazette, in which context indirect amendments were made in the Joint Investments Trust Law. The purpose of the Corporate Governance Law is, inter alia, to improve the set of corporate governance obligations that apply to mutual fund managers, that are not public companies. The principal amendments are: ensuring that the fund trustee is independent of the fund manager, clarification of the supervisory obligations that apply to the trustee, and improving the control, supervision and monitoring mechanisms in the fund manager. The Corporate Governance Law will take effect 6 months from its publication in the Official Gazette. The underwriting and investment banking segment is regulated under the Securities Law, and the regulations made thereunder, and specifically under the Securities Regulations (Underwriting), 2007. In addition to the provisions of the securities legislation, underwriting operations are subject to limitations prescribed under antitrust laws, and are also influenced by provisions applicable to institutional investors. Operations in the issue of structured products and financial instruments segment are subject to the provisions of the Securities Law and the regulations made thereunder. These operations are further subject to the provisions and limitations set forth under deeds of trust signed by each SPC issuing structured products or ETFs with the bondholders' trustee. Furthermore, each of the "Haharim" companies, which carry out issuings of structured vehicles, is obligated towards the ratings company to act according to certain principles and obligations. It is noted that the Israel Securities Authority has issued interim recommendations submitted by an inter-departmental team charged with examining the preparations mandated by the significant increase in the production and marketing of hybrid financial products to the general public. The team recommends to apply various regulatory mechanisms which, inter alia, will route hybrid, high-risk financial products to the 'TACT Institutional' market, and so apply comprehensive regulation for management entities and increase supervision of financial brokers. As of the reporting date, Excellence is negotiating with the Israel Securities Authority so as to allow the issue of structured vehicles to the general public in a manner similar to the way these vehicles were issued in the past. The outcomes of these negotiations are, at this time, uncertain. Operations in the ETF and deposit certificates segment are subject to the Companies Law, the Securities Law and the regulations made thereunder, and the directives issued by the TASE; the main laws which apply to the trade and brokerage services segment are the provisions TASE rules and regulations, the Consultation Law and the Israel Securities Authority directives issued thereunder. Several regulatory changes have been made over the last two years in an effort to increase the supervision of index-linked certificates and deposit certificates. Thus for example, in 2010, the Securities Authority published a bill to amend the Joint Investments Trust Law in connection with the entry of the companies that issue index-linked certificates under the supervisory regime of the Joint Investments Trust Law. At the beginning of 2012, the Securities Authority published the main points of a supervisory model for this sector. Additionally, and at the time of the publication of the report, the Securities Authority published two collections of regulations pertaining to Amendment no. 16 to the Joint Investments Trust Law that help lay the judicial foundations for including index-linked certificate activity in this law. Furthermore, Amendment no. 17 to the Companies Law was recently published, obligating the KSM companies to appoint, inter alia, 2 external directors who have no interest in the controlling shareholder, following the approval of the Audit Committee, and to appoint an internal auditor. The KSM companies have implemented the provisions of the amendment. In February an amendment was published to the Supervision of Financial Services (Provident Funds) (Direct expenses for performing transactions) Regulations, prescribing, inter alia, restrictions on the expenses that an institutional entity may charge directly to the assets of a provident fund or to money held against yield-dependent obligations, for performing transactions. Excellence believes that this amendment may lead to a reduction in the volume of the asset managed by institutional investors in index-linked certificates on indices in Israel and as a

direct consequence, Excellence's revenues in this segment may decline. At this stage it is impossible to estimate the precise scope of the effect on the Company's revenues and its profits in this segment. The principal laws as they relate to TASE services and trading are the Consultation Law, insofar as they relate to investment marketers, and the provisions of the Prohibition on Money Laundering Law and the Prohibition on Money Laundering Order (duty of identification, reporting, and maintaining records of a TASE member), 2001. The TASE member operates according to the TASE members' statute, and is subject to supervision by the TASE; the provisions of the Provident Funds Law, the Supervision Regulations, and the Provident Funds Management Regulations apply to the provident fund segment. Provident funds are subject to supervision by the Commissioner of Capital Markets, Insurance and Savings in the Ministry of Finance. In addition to these laws, various reforms and legislative amendments that have taken place in recent years affect Excellence's operations. The Bachar reform, which is described in Section 1.12.2(D) above, has led to material changes in the capital market, including changes in the structure of ownership in the capital market, and to reforms in all matters related to consultation and marketing of financial and pension-related products and trust funds. See also a description of the changes and regulatory reforms from the last year, as described in Section 1.12.2(A). In 2007 and 2008, the TASE enacted changes in the TASE statute, which affected the structured products and financial instruments segments. Furthermore, in July 2007, a reform was carried out in the underwriting industry, which mainly dealt with changes to the method of underwriting and the manner of offering securities in Israel. As detailed above, also during the course of 2010 and up to the date of publication of the report, regulatory provisions were promulgated in an effort to increase supervision of the activity of mutual funds and index-linked certificate companies. Furthermore, in January 2011, the Knesset passed the Law for Effective Enforcement Procedures in the Securities Authority (Legislative Amendments), 2011 ("Improved Enforcement Law"), which applies to all areas of activity by companies operating in the capital market - public companies, reporting corporations, index-linked certificate companies, companies that issue financial products, investment consultants and marketers, portfolio managers and mutual fund managers. The law establishes an administrative enforcement mechanism designed to deal with securities offenses where the level of intent rises no higher than negligence. Among the sanctions that the Securities Authority is authorized to impose are heavy administrative fines on individuals and companies, exclusion from the capital market and from positions of authority, and payment to the victims of the offense.

3. Changes in the scope of operations and profitability of the segment

Excellence operates in various segments in the local capital market, which are characterized by high volatility, inter alia due to the effect of political, security-related and economic factors in Israel and abroad, which are outside of Excellence's control. Inter alia, this volatility affects the scope of the public's activity in the capital market, and the prices of securities and financial products.

In light of the economic recovery in 2009 and 2010, the volume of assets managed by Excellence grew, as did the scope of its operations, mainly in the underwriting and asset management segments. Nevertheless, 2011, which saw renewed volatility in the capital markets in Israel and worldwide as the financial crisis intensified and spread, mainly in the eurozone, affected Excellence mainly with respect to the following: (1) the volume of assets under management declined due to falling market indices; (2) in assets under management - assets were diverted to less risky investment channels on which the management fees are lower; (3) growth and the volume of sales in the various operating segments slowed. As of December 31, 2011, Excellence held total assets under management of NIS 63.4 billion, compared with NIS 63.5 billion as of December 31, 2010.

Investment marketing activity and investment management for customers in 2011 declined sharply relative to share indices in Israel and the rest of the world, resulting in negative yields that affected the overall annual yield for assets under management. Concern over the direct impact of the global crisis on the Israel economy also affected Israel's capital markets, fueling the fears of investors who shifted assets managed in more volatile channels to those perceived as less risky, such as cash and cash substitutes, government bonds, on which management fees are lower.

From the second quarter of 2011, a marked slowdown was felt in the domestic capital market in underwriting and investment banking activity, reflecting the negative developments in the global economy, and particularly the negative economic events in

Europe. In the local capital market, prices of securities and the volume of trade fell, and there were large redemptions, particularly in the mutual fund sector. Accordingly, there has been a marked decline in the number and volume of capital raisings, as well as in the change in the mix of issuances and issuers, resulting in fewer share issuances. This was accompanied by an increase in the weight of capital issuances by way of rights, which under normal circumstances do not involve underwriters or distributors. Likewise, there was a noticeable reduction in the issuance of unrated corporate bonds or bonds that have relatively low rating levels. This sequence of events cast a shadow over the operating segment and led to a decline in the volume of activity and profitability therein in 2011. In 2011 Excellence took part in 56 issuances, serving as underwriter in 3 of them (as consortium manager), and in 53 issuances it served as the distributor.

Excellence did not issue any additional structured products to the public during the course of 2011. The restrictions on the volume and class of structured bonds that the company is permitted to issue, that were adopted by the Securities Authority as aforementioned, led to a decline in the volume of Excellence's activity and a significant decline in its revenues from this segment in 2010 and 2011. At the date of the report, Excellence has issued 15 series of structured debentures that have not yet been redeemed, of which two series were registered for trade on the TASE and 13 were private placements that were not registered for trade.

The scope of operations in the financial instrument issuing segment is derived from the condition of the capital market, the range of issued instruments, the awareness of the investing public and the marketers of financial instruments, the issuing rate and the volume of investment, changes in public preferences as regards investments specializing in overseas markets, commodities and financial derivatives in Israel and abroad. During the course of 2011 the volume of assets under management in this segment declined by about NIS 1.2 billion, compared to 2010 following the falling values of the indices to which the index-linked certificates are linked.

Operations in the trade and brokerage services segment are also influenced by capital market conditions. From the second quarter of 2011, prices of securities in the local capital market and the volume of trade fell, and there were large redemptions, particularly in the mutual fund sector. Likewise, in 2011 the Israeli banks increased their holdings of brokerage activity, which in turn led to lower profits from activity in this segment relative to 2010.

4. Customers

Customers in the trust funds, structured products and financial products segments are the general public. Structured products which are not listed for trade on the TASE are sold mainly to institutional customers. Customers in the portfolio management segment include both institutional and private customers. Customers in the investment banking and underwriting segment are mainly private and public companies seeking to raise capital or offer securities to the public. Customers in the trade and brokerage services segment are mainly institutional entities in Israel and abroad, as well as individual customers and customers whose moneys are managed by portfolio managers.

5. Marketing and distribution

In the investment marketing and management segment, portfolios are marketed through Excellence employees, a distributor network of independent agents, and a telemarketing mechanism which recruits customers through cold calling. Mutual funds are marketed mainly to investment consultants in the various banks, as well as through advertising on the various media. The structured and financial instrument issuings segment is subject to advertising restrictions as issuings are made according to a prospectus. Marketing efforts in this segment are concentrated immediately prior to issuing, and include presentations to institutional entities, to investment consultants and to portfolio managers. Investment banking and underwriting operations are marketed through Excellence employees, and targets the management of large-scale enterprises and the managers of their finances. Operations in the trade and brokerage services segment are marketed mainly by Excellence employees, as well as through independent agents who are entitled to commissions for customers recruited.

6. Competition

The following is a short description of the competition in Excellence's segments of operation:

Investment management and marketing – There are numerous organizations in Israel specializing in portfolio management and in the provision of investment marketing services. In recent years, there has been a significant increase in the number of organizations operating in this market, which has increased competition. Clal Finance, Peilim Capital Markets, Psagot, IBI, Altshuler Shaham, DS, and Migdal Capital markets are portfolio managers which Excellence estimates to be its main competitors in the portfolio management segment. Excellence estimates that it is among the leading companies in the portfolio management segment in Israel. Excellence believes its main competitors in the mutual fund segment are primarily those companies which were formerly controlled by the banks, such as Psagot Mutual Funds, Harel-PIA Trust Funds, Menorah Mivtahim Mutual Funds, DS Mutual Funds, and privately-owned companies (which were not controlled by the banks) including Meitav, Clal Finance, Migdal Capital Markets, IBI, Analyst, Altshuler-Shaham, Epsilon and others.

Issue of structured products – In light of the regulatory restrictions and requirements introduced by the Securities Authority relating to the issue of structured products, the scope of activity in this segment has declined considerably, as has competition in the segment. As mentioned above, Excellence reached agreement in principle with Clal Underwriting to acquire all the holdings of Clal Underwriting in companies that issue structured bonds and deposit certificates to the public. To the best of Excellence's knowledge, following completion of the transaction, Excellence will be the largest player in the market for structured products that are traded on the Stock Exchange.

Issue of financial products – Excellence estimates that there are 4 other organizations which have issued index-linked certificates to the public, led by Meitav-Mabat, owned by Meitav Investment House, Tahlit-Index, owned by DS Investment House, Psagot, and Harel. Excellence estimates that it is the largest player in the index-linked certificates segment, with a market share of approximately 33%.

Underwriting – In the underwriting segment, there are currently three dominant players (Clal Finance and Underwriting, Poalim IBI Underwriting and Issuing, and Leumi Partners), approximately three or four mid-size issuing managers (including Excellence), and other smaller organizations.

Trade and brokerage services – Competitors are TASE members, which at December 31, 2011 include 12 TASE members who are Israeli banks, 13 TASE members that are not banks, two TASE members that are foreign banks and one remote member. Competition focuses on commissions, quality and diversification of services provided to customers.

1.12.4 Customers

There are many and diverse customers in the insurance industry. No single insurance customer provides The Phoenix with 10% or more of the Company's total income. For a description of the typical customer in each field of insurance, see above.

1.12.5 Marketing and distribution

In the insurance industry, most marketing and distribution is performed by insurance agents and agencies. Most of the insurance agents have agreements with a number of insurance companies in order to provide solutions for the wide range of their customers' needs. When choosing the insurance company they intend to work with, the main factors considered by the agents are the rates of commissions, the quality of service provided by the insurance company, innovative products and services, and the suitability of the insurance products to the agent's customers. The insurance company's principal considerations when choosing agents to represent them are the agent's fields of activities, specialties and relative advantages, the potential for commercial cooperation with the insurance company; rates of commission; the agent's customer base; and the agent's integrity.

The vast majority of insurance policies sold by The Phoenix Insurance are marketed through agents, most of which also market policies issued by other insurance companies. Insurance agents work directly with The Phoenix's insurance clusters.

The Phoenix Insurance also works through pension arrangement agencies and agencies employing sub-agents. As a rule, these agencies work with a number of insurance companies. The

Phoenix grants such agencies issuing and underwriting authority at different levels. In most cases, when The Phoenix Insurance signs an agreement with an agency working with sub-agents, The Phoenix Insurance also signs agreements with the sub-agents operating through the agency. For additional information about agents' activities, see Section 1.12.3(A)(8) above.

The Phoenix also operates an internet website which enables users to purchase automobile insurance (compulsory and property), travel insurance, and receive personalized and marketing information. The Phoenix operates a customer service call center which assists its sales operations and provides a quick response to customers' requests, as well as supportive Facebook community, enabling, inter alia, dialog on insurance subjects and supplementary aspects relating to health, savings, and protection of property belonging to policyholders. Additionally, The Phoenix develops new digital tools for communication by means of smartphones and providing customer service, such as at the time of an accident.

The Phoenix Insurance owns a number of insurance agencies. As is standard practice in the insurance industry, these agencies do not work exclusively with The Phoenix Insurance and work with a number of different insurance companies. These agencies have technologies that facilitate the transfer of financial activity between the employers and the pension producers. In 2011, about 18.3% of total life insurance premiums and 22.1% of total contributions for pension business were received through the insurance agencies controlled by The Phoenix. In health and general insurance operations, these agencies do not account for a material portion of The Phoenix's premiums.

Agent activities are supervised by the Commissioner of Insurance, and interactions between agent activities are regulated under the Insurance Contract Law, the Supervision Law, and the Pension Marketing Law.

1.12.6 Seasonality

Seasonality has no material effect on profitability in any of The Phoenix's sectors of activity.

In the general insurance industry, seasonality in the premium payment cycle throughout the year is affected in the first quarter, because most policies (mainly vehicle insurance policies) organized for employee groups and for car fleets are renewed at the beginning of the year. Seasonality in the payment cycles for premiums on profits is neutralized by the reserve mechanism for risks that have not yet elapsed. It is noted that a severe winter season may cause an increase in claims, especially in the property vehicle segment. The following table provides details of the general insurance premiums earned in each quarter in the period 2010-2011:

	2011		2010	
	NIS millions	%	NIS millions	%
1st quarter	655	31.9	661	33.9
2nd quarter	450	21.9	439	22.5
3rd quarter	479	23.4	439	22.5
4th quarter	467	22.8	411	21.1
Total	2,051	100.0	1,950	100.0

The following table provides details of seasonality in health insurance. These details indicate that seasonality does not affect the health insurance sector. Premiums in health insurance by quarter:

	2011		2010	
	NIS millions	%	NIS millions	%
1st quarter	259	22.6	269	24.8
2nd quarter	266	23.2	244	22.5
3rd quarter	277	24.2	251	23.1
4th quarter	345	30.0	321	29.6
Total	1,147	100.0	1,085	100.0

In the life insurance sector, revenue from premiums are not characterized by clear seasonality. However, as the provisions for life insurance benefit from tax benefits, a substantial part of the new sales is made at the end of the year. The following table provides details of the life insurance premiums received in each quarter in the period 2009-2010:

	2011		2010	
	NIS millions	%	NIS millions	%
1st quarter	861	23.4	751	24.5
2nd quarter	815	22.2	741	24.2
3rd quarter	861	23.5	731	23.9
4th quarter	1,133	30.9	842	27.4
Total	3,670	100.0	3,065	100.0

1.12.7 Reinsurance

Israel's insurance companies usually cover a substantial part of their insurance risk that they undertake through foreign reinsurers. The Phoenix reinsurers have an influence on insurance capacity, policy conditions, tariffs and profitability. Notwithstanding the aforesaid, reinsurance agreements do not derogate from the contractual rights accruing to the insurance company's policyholders and do not absolve the insurance company from any liability towards policyholders. Therefore, the stability of the reinsurers has an effect on the insurance company. Moreover, conditions to agreements made with reinsurers affect the insurance company's profits.

A possible deterioration in the position of the reinsurance market is likely to have a number of consequences: First, an insurance company which enters into a reinsurance agreement is directly exposed to the reinsurer's ability to comply with its commitments if an insurance event occurs. Second, a deterioration in the robustness of a reinsurer is likely to cause the insurance company to request that it be replaced with another reinsurer. This entails the addition of costs to the original reinsurance costs and the risk that the original terms of cover will not be achieved, which in turn leads to the recording of an accounting loss because of a suspicion that the reinsurer will be unable to meet its obligations. Third, a deterioration in the position of the reinsurance market is liable to lead to a decline in reinsurance capacity which harms the insurer's ability to conduct its insurance business, and a rise in reinsurance tariffs and other agreements terms with the reinsurer, thereby causing additional costs or harming the quality of the insurance cover. In addition to the aforesaid, an absence of the reinsurance required by an insurance company is liable to cause a failure in its ability to comply with its regulatory capital requirements.

2011 was characterized by a large number of significant natural disasters worldwide. These included earthquakes in New Zealand and Japan, and floods in Europe and Thailand. 2011 is considered one of the most difficult years regarding the volume of catastrophe losses, which at this stage are estimated at approximately USD 108 billion. Despite this enormous sum, so far the financial rating of the reinsurers has not been downgraded. The worsening trend in the international capital markets and the decline in revenues from investments also reduced the profitability of the reinsurers, resulting in a significant increase in reinsurance prices before the start of 2012.

Since 2002, The Phoenix Insurance signs agreements with reinsurers graded A- and above, as rated by one of two rating companies – Standard and Poor's and AM Best. It is noted that towards 2011, The Phoenix's Board of Directors updated The Phoenix's policy for managing its exposure to reinsurers. The reinsurer market at the ratings relevant to The Phoenix Insurance includes more than 200 insurance companies. The Phoenix Insurance regularly works with approximately 60 reinsurers. For further details about The Phoenix's largest reinsurers, see Note 28 to the financial statements.

In general, the reinsurance rate in the life insurance sector is significantly lower than the reinsurance rate in the general insurance sector. This is due to the majority of insurance premiums in the life insurance sector including a savings component, for which there is no reinsurance. In addition, statistics on risks are more reliable in life insurance. In the general insurance sector there is also variability in the scope of reinsurance acquired, with reinsurance being less prevalent in sectors characterized by high-dispersion homogenous risks (e.g. – the vehicle sectors - compulsory and property), and more prevalent in sectors characterized by high variance, low dispersion and large-scale risks (e.g. – other property insurance).

Contracts are through various types of reinsurance²²⁸. Reinsurance contracts for the general insurance sector are usually made on an annual basis. Reinsurance contracts in the life, health and

²²⁸ **Contractual reinsurance**, made between the insurance company and the reinsurer, is made according to a reinsurance agreement under which the reinsurer, according to certain prescribed terms, assumes all the risks/ businesses transferred to it by the direct insurer without need to approve each risk/ business separately. Contractual reinsurance is divided into **relative reinsurance**, in which the division between the assumption of risks (claims coverage) and the premium is identical, and **non-relative reinsurance**, in which the assumption of risk (claims coverage) by the reinsurer is not directly correlated to its share in the premium. Relative reinsurance is sub-divided

nursing care insurance sectors are usually made for a set period and apply for the entire lifespan of the covered policies issued during that period. In the life insurance sector, The Phoenix Insurance engages various reinsurers through relative reinsurance contracts, both for compulsory insurance and for optional insurances, for protection of the risk component in the life insurance portfolio only. Starting from mid-2005, a non-relative reinsurance contract is purchased, which protects from physical injuries, loss of life and disability due to catastrophic events. In the compulsory and property vehicle insurance sectors, The Phoenix Insurance undertakes "excess of loss" reinsurance contracts. In the general insurance sectors, The Phoenix Insurance undertakes the following types of reinsurance contracts: relative, excess of loss, and quota. In the health insurance sectors, The Phoenix Insurance undertakes quota-type relative reinsurance contracts, for protecting the risk components in the health insurance portfolio. A relative reinsurance agreement has been signed for a number of large-scale collective insurance policies.

For more information regarding reinsurance, see Notes 28 and 30 to the financial statements.

1.12.8 Suppliers and service providers

The Phoenix enters into agreements with a large number of suppliers and service providers in different insurance fields, mainly claim settlement. These are selected on the basis of the nature and quality of their service, availability, and areas of expertise. The various types of agreements with these suppliers and service providers include payments according to all inclusive tariffs, by activity, according to a percentage of the risk, according to hourly rates and per opinion. These contracts are usually for indefinite periods of time and do not include exclusivity. The Phoenix also has IT agreements, with several hardware and software suppliers who provide hardware, software and maintenance services. The Phoenix also has agreements with various suppliers of development and maintenance services. Agreements with the suppliers may consist of a fixed price per project, payment at an hourly rate, and a price per unit. The Phoenix also has outsourcing agreements with several service suppliers such as for the development, maintenance, operation, storage and processing of data or information systems or infrastructure on a random and/or on-going basis. Due to the knowledge accumulated by suppliers in the course of providing services, a short-term dependence may develop on a particular supplier, as the replacement of IT service providers requires time and money. Such dependence may, for example, arise due to a need to complete a project within a limited time frame in response to regulatory changes or in a field in which the supplier's accumulated knowledge provides that supplier with an advantage.

1.12.9 Actuarial responsibility and risk management

The purpose of The Phoenix's risk management is to support and protect it from unforeseen losses that may prevent it from attaining its business goals. The present risk management system is founded on risk management and control principles that include, inter alia, reasonable involvement and understanding of risk management by The Phoenix's board of directors, providing tools for estimating and measuring risks, and arranging for means to supervise and control such risks. The Control of Financial Services (Insurance) Law, 1981, determines that an insurer, including a company managing a pension fund, must appoint a responsible actuary for each field of insurance in which the company is involved and that the insurer and any pension fund under the insurer's management must appoint a "risk manager". The responsible actuary's tasks include making recommendations to the Board of Directors and the CEO concerning the insurer's level of insurance liabilities or concerning the actuarial balance in the pension fund managed by the insurer, as applicable. The risk manager's tasks include, inter alia, advising the Board of Directors and CEO concerning the risks facing the insurer and any pension fund that it manages. Rules pertaining to the functions, powers and operation of responsible actuaries and risk managers, and the interactions between them have been detailed in a number of circulars published by the Commissioner. In 2014, the Solvency II regulatory directive is expected to come into force. The Solvency II directive regulates the capital requirements and risk management processes for insurance companies. Under the various circulars and letters to the market concerning the

into **quota share contracts**, in which the reinsurer undertakes coverage at a fixed portion of each claim in a certain segment for an identical fixed portion of the premium, and **surplus contracts**, in which the reinsurer undertakes coverage at a variable portion of any claim up to a predetermined limit for an identical portion of the premium. Non-relative reinsurance is sub-divided into **excess of loss contracts**, in which insurance is granted for single claims, where up to a certain predetermined residual amount the direct insurer incurs the cumulative damages, and above that amount the excess loss is incurred by the reinsurer, and into **stop loss contracts**, where the reinsurer indemnifies for a portion/ amount of damages in excess of the predetermined portion/ amount. In addition to contractual reinsurance, there is also facultative reinsurance, which is divided across a number of reinsurers.

preparation for Solvency II, the Commissioner of Insurance required that companies initiate processes to guarantee organizational preparedness for implementing the proposed directive. The Phoenix is in the process of implementing a work plan that will promote and expand the instruments used to manage and monitor the various risks to which it is exposed. At the same time The Phoenix complies with the regulatory requirements and its business needs. This activity is an integral part of the deployment to implement Solvency II in Israel in coming years. The board of directors of The Phoenix is monitoring progress of the work plan and preparations for implementation of the directive.

1.12.10 Property, plant and equipment

The Phoenix's property, plant and equipment consists mainly of office buildings, computers, software and equipment.

Offices of The Phoenix Group, Derech Hashalom, Givatayim: The Phoenix Insurance holds the right to be registered as the owners of 15 floors of office space in 53 Derech Hashalom, Givatayim, with a total area of 18,745 square meters (gross), storerooms with a total area of 699 square meters and 300 parking spaces in an underground parking lot, which serve as The Phoenix's offices. According to The Phoenix's financial statements, the building's depreciated cost amounts to NIS 177 million.

The Phoenix owns additional real estate assets with an immaterial adjusted value.

Information Systems: The Phoenix has information systems which comprise hardware, software and additional equipment with an amortized cost at December 31, 2011 of NIS 606 million. In 2011, The Phoenix invested NIS 173 million in software and computers. The Phoenix's information systems-related current expenses totaled NIS 180 million in 2011, up NIS 13.3 million from 2010. This increase in current expenses stems primarily from increased depreciation of computers. The Phoenix's IT department provides all IT services for The Phoenix in-house, and as necessary through subcontractors and various software suppliers. The Phoenix's IT infrastructure serves its employees throughout the country and provides The Phoenix's pension funds with computer services and work environments using The Phoenix Group's computer systems. Additionally, the IT infrastructure supports the agents and their employees who spread all over the country and use the various telecommunications infrastructures.

The Phoenix Group's central IT infrastructure is based on IBM UNIX computers and serves approximately 7,000 users simultaneously. The Phoenix's IT center is in its main building in Givatayim. The Phoenix has a backup computing site in Netanya, which serves as a live backup site, including UNIX computers and data storage units. This site guarantees business continuity in the event that the main site goes offline.

1.12.11 Intangible assets

"The Phoenix" name is a registered trademark. The Phoenix has trademarks for a number of brands and insurance products and operates databases registered as required by the Privacy Protection Law, 1981. The databases are vital to the running of The Phoenix business activities and include databases for the salary data of The Phoenix Insurance's employees, life insurance, elementary insurance, policy expenses and claim payments. Through its employees and suppliers, The Phoenix develops software for in-house use and holds copyright for that software. In accordance with an agreement from August 2006 between The Phoenix Insurance and Excellence, Excellence granted The Phoenix Insurance the right to use "the Excellence" name for its "Excellence Invest" policies in consideration of the management fees stipulated in the agreement, for as long as the management agreement for management of the investment portfolios for the abovementioned policies remains valid. Furthermore, The Phoenix has recorded goodwill and surplus costs, mainly through the acquisition of Excellence, Prisma (by Excellence), and insurance agencies, to the amount of NIS 1,165 million, net, net of amortization.

1.12.12 Human capital

A. Organizational structure

The Phoenix is a holdings company and does not employ salaried employees. The Phoenix employees are employed by The Phoenix Insurance, with some employees being employed by the other investees. The CEO of The Phoenix also serves as CEO of The Phoenix Insurance and an additional subsidiary in The Phoenix Group, and answers to The Phoenix's Board of Directors. The Board of Directors outlines Company policy and supervises the performance and activity of the CEO.

The Phoenix has the following main units: insurance segments - life insurance and long-term savings segment (including The Phoenix Pension and Provident); the general insurance and health segments; the customers division; and the headquarters and finance divisions. In addition to these divisions there are the claims department; the investments department; the IT division; the marketing and business development unit, and the administrative and logistics department. The Phoenix's agency operations are coordinated by The Phoenix Agencies and by the Company's secretariat, which provide secretary services for The Phoenix, The Phoenix Insurance, and additional companies in The Phoenix Group.

The Phoenix's financial service operations are carried out through Excellence, which is a public company controlled by The Phoenix, which operates independently.

B. Workforce at The Phoenix

The following table provides details of The Phoenix workforce at December 31, 2010.

	December 31, 2011	December 31, 2010
Management	16	19
Customer Division	909	819
General Insurance	74	76
Life Insurance and Long-term Savings	43	48
The Phoenix Pension and Provident	47	32
Health	40	39
Claims Department	207	195
Functional Headquarters, Headquarters and Finance Division, and Other Headquarters Functions	404	389
The Phoenix Investments	27	28
The Phoenix Insurance Agencies	1	1
Total for The Phoenix excluding The Phoenix-owned insurance agencies and excluding financial services (Excellence)	1,768	1,646
Financial Services (Excellence)	345	323
Excellence – Provident and Pensions	243	229
Insurance agencies controlled by The Phoenix	611	496
Total The Phoenix	2,967	2,694

During 2011, the workforce at The Phoenix increased by 122 employees (excluding Company-owned insurance agencies and excluding Excellence). The increase in employees in 2011 was mainly due to recruitment in the customer relations center and service departments, in the customers division, and in the pension fund. These recruitments were aimed at improving the service given The Phoenix's policyholders and agents, inter alia, due to increased sales volume and the growth in operations.

The increase in the number of Excellence employees in the finance segment is largely due to the expansion of existing operations, expansion of infrastructure and the addition of new operations (insignificant at the date of the report); in the provident and pension fund segments, most of the increase is due to more temporary staff in the sales and service units; the increase in the number of employees in the arrangement agencies is due to the acquisition of new agencies, the setting up of new ventures and an increase in the scope of activity.

C. Benefits and employment agreements

In accordance with the policies previously employed at The Phoenix, veteran employees do not have signed employment agreements. Beginning in 2002, and after the Employee Information (Work Conditions) Law, 2002 came into effect, new employees are given a form listing their conditions of employment and as required by the law. Beginning in 2004, the labor relations were written into personal employment agreements which list their conditions of employment and the ancillary conditions, including social benefits and the employee's rights and duties. The Phoenix's employees are entitled to social contributions, which are generally deposited in policies, pension and study funds, and various provident funds. The majority of The Phoenix employees receive holiday bonuses (of one half of their monthly salary), paid twice a year. Furthermore, some of the Company's employees are entitled to a company car.

Salary supplementation and employee remuneration are determined by The Phoenix's overall remuneration policy, which is determined by The Phoenix's Board of Directors.

It should be noted that The Phoenix Insurance is a member of the Israel Association of Life Insurance Companies Ltd., which is a member of the Coordinating Bureau of Economic Organizations. Consequently, all the collective labor agreements that are signed by the Bureau apply to it.

D. Officers and senior management and option plans for employees and officers

Officers and senior management staff are employed in accordance with personal employment agreements and benefit from a range of remuneration methods, including wage increases and bonuses determined annually by The Phoenix's board of directors, principally according to business results. In 2007, The Phoenix adopted an employee and officer payment plan through which it can grant its employees and officers and those in the companies under its control, either directly or indirectly, at no cost, option warrants not listed for trading on the stock exchange. These options warrants are exercisable as ordinary shares in The Phoenix, each with a par value of NIS 1. In 2010, the option warrant allotment terms were changed as regards the rules for determining the base price for exercising the warrants. Furthermore, warrants were granted to 4 of The Phoenix's officers. On December 30, 2010, The Phoenix's board of directors adopted a multi-year compensation plan for The Phoenix's investment employees and senior officers, based on the principles set forth in the Commissioner's circular for determining a company's compensation policy. The incentive plan attempts to balance the fixed and variable elements of compensation and to reflect the risk level entailed in attaining the yields on the various investment channels. The incentive plan is based on a series of parameters and profitability that, as a rule, are based on cumulative, long-term results for three years, performance in the various investment channels compared to competitors, with reference to the relative risk level in the different channels on a series of parameters, and the relative risk level.

The Phoenix has given letters of indemnity and insurance to its directors and to senior officers who are not directors.

- E. 2011 and up to the date of the report saw personnel changes in The Phoenix's senior management, which included changes in the composition of The Phoenix's board of directors, and personnel changes in some of The Phoenix's executive positions. In April 2011, Dr. Moshe Bareket ("Dr. Bareket") was appointed Chairman of the Board of Directors of The Phoenix Insurance, replacing Dr. Ehud Shapira who resigned following his appointment as a director of Bank Leumi Ltd. The terms of Dr. Bareket's tenure (through a wholly owned management company) entered into force on April 10, 2011 and will be effective for three years; they include monthly management fees, updated every quarter, an annual bonus based on a mechanism that was determined, a refund of expenses for car maintenance, per diem expenses and hosting, according to general practice at The Phoenix, mobile phone, landline, and laptop. Mr. Eyal Lapidot serves as CEO of The Phoenix, The Phoenix Insurance, The Phoenix Investments and Finance, and other subsidiaries of The Phoenix Group. Mr. Lapidot's terms of employment went into effect on June 6, 2009, and will remain in effect for a period of five years. These terms include a monthly salary, social benefits, ancillary benefits, annual bonus, options, and reimbursement for expenses. For details regarding the terms of Mr. Eyal Lapidot's employment, see the detail according to Regulation 21 in Chapter D to this report.

1.12.13 Management of investments

The Phoenix manages the following investments:

1. General insurance liability funds
2. Funds from life insurance policies with guaranteed yield
3. Equity and surplus capital
4. Funds from life insurance policies participating in the profits
5. Funds from members of pension funds
6. Funds from members of provident funds

The monies for the different types of insurance liabilities are invested in a range of assets, according to the nature and type of liability and subject to the regulations on the manner of such investments, which determine, inter alia, provisions referring to the types of assets that an insurer

is entitled to hold against the insurers various liabilities and various limitations and facilities adapted to the nature and types of the various liabilities.

The Supervision Law and the provisions referring to the manner of such investments determine, inter alia, that the board of directors of an insurer shall appoint two investment committees. One committee shall manage the investment portfolio for the monies that will cover performance-based liabilities (monies belonging to members / policyholders – in the insurance company's participatory portfolio) (the participatory investments committee). The second is the committee for the investment of the insurer's equity and the investment of monies covering insurance liabilities, which are not performance-based liabilities (monies from general insurance, life insurance with a guaranteed yield, capital and surplus capital) (the "Nostro Investments Committee").

The Provident Funds Law and the Provident Funds Regulations prescribe methods for investments of savings as part of pension and provident activities, including the different types of assets, the limitations and the different investment frameworks.

Investment management services in the Group are concentrated in The Phoenix Investments.²²⁹ Accordingly, management agreements have been signed for investment management services for both member and nostro monies, and the operation of these investments in consideration for management fees. Such agreements have been signed between The Phoenix Investments and The Phoenix Holdings, The Phoenix Insurance, The Phoenix Pension and Provident, and The Phoenix Balanced.

Investments are managed by a number of designated investment managers with separation between the management of the nostro monies belonging to The Phoenix companies and the management of the monies belonging to policyholders and members (in The Phoenix Insurance and The Phoenix Pension and The Phoenix Provident). The investment managers are supported by the internal economics department and use surveys and analyst reports from banks and investment houses in Israel and abroad.

The Phoenix also engages in various financing operations, including various forms of commercial credit (debentures and non-marketable loans), with or without guarantees, structured financing including asset-backed debentures, other structured products, financial derivatives and hybrid assets, deposits and capital notes. In 2009, with the market's recovery from the economic crisis, efforts were directed towards new investments in non-marketable debt. This trend continued in 2010 and 2011, focusing on issuing secured loans to the commercial sector. The Phoenix Investments makes specific provisions for doubtful and bad debts so as to changing market conditions, and also employs internal controls so as to minimize the risks related to the extension of such credit facilities. In 2011, The Phoenix's policy for investing in shares focused on gradually increasing the overseas share component; in the government bonds channel, most of the activity was concentrated in shekel channels, while maintaining a medium-short average duration; activity in the corporate channel focused on the purchase of bonds issued with a high rating, and on the other hand selling bank debentures and capital notes bearing relatively low yields. In the share channel, the investment portfolio is weighted in favor of Israeli shares over foreign shares. The Phoenix focused on expanding its loans and non-marketable credit portfolio and establishing the infrastructure for broadening its real-estate investments. The Phoenix seeks to expand its long-term income-generating real estate investments, in Israel and abroad. These activities are carried out through a direct investment in real estate controlled and managed by The Phoenix, and through a direct investment in real estate assets together with experts, mainly in those segments which The Phoenix's management believes to require expertise. The main segments in which The Phoenix operates are commercial real estate and offices.

1.12.14 Investments

The Phoenix has investments in real estate, companies and a range of other assets. The major investments of The Phoenix include ownership of 41.42% in the public company Mehadrin Ltd, which is active principally in the agriculture industry, as well as ownership of 49% of the issued and paid-up share capital of Gama Management and Clearing Ltd. ("Gama"). Under a 2010 agreement signed between The Phoenix Investments and the shareholders in Gama, it was agreed that if either party wishes to sell all its holdings in Gama shares, such party will have right to obligate the other party to sell its holdings in Gama with it. This agreement prescribes a mechanism for calculating the consideration to be received by the party that is obligated to sell its holdings. Gama Management and Clearing Ltd. is a private company which engages, inter alia, in financing, discounting, clearing and management of credit card vouchers, in providing various types of credit

229

Management of some of the portfolios also includes the purchase of specific investment management services.

facilities, in check clearing and factoring. Gama's main operations consist of credit card discounting services, which allow Gama's customers to sell goods against credit card payments and receive the sum of the transactions in cash.

In addition, The Phoenix holds full ownership of the assisted living chain "Ad 120", which develops, constructs and manages up-market assisted living centers, as well as 50% of "Pen-Tau", a limited partnership that holds 50% of the rights in the Mall Hayam mall in Eilat.

Furthermore, in recent years, The Phoenix Insurance has focused on acquiring agencies dealing in pension-related investments. These agencies include Shekel, Agam and Kela, which are some of the largest arrangement management agencies engaged mainly in the marketing and distribution of life insurance and long term savings and health insurance. These agencies are held through The Phoenix Agencies, which is wholly-owned and controlled (100%) by The Phoenix Insurance. For details concerning these agencies' operations, see Section 1.12.5 above.

1.12.15 Financing

- A. The Phoenix finances its activities, inter alia, from external sources, including the issue of promissory notes and bonds, and through short- and long-term loans from banks and non-bank sources (total loans and short and long-term credit at December 31, 2011 are NIS 3,971 million). The following table provides details of the average nominal interest rates for loans taken from bank and non-bank sources, valid during 2011, but not intended for exclusive use by The Phoenix:

	Average interest rate for for loans not intended for exclusive use by The Phoenix			
	Average Rate	Deferred promissory notes	Long-term loans	Short-term loans
Banking sources* – CPI linked	4.59%	4.56%	5.05%	5.05%
Banking sources – non-linked	4.47%	n/a	5.86%	3.85%
Non-banking sources** – CPI-linked	4.32%	4.10%	4.50%	4.00%
Non-banking sources** - non-CPI-linked	5.52%	6.00%	4.73%	5.95%

* Including, inter alia, deferred promissory notes issued to banks in February 2008 and September 2009.

** Including bonds issued in 2007 to institutional entities, and including promissory notes issued by The Phoenix Capital Raisings.

B. Debt resources

In February 2012, the Company performed a private issue of NIS 31,225,605 par value debentures (Series 1) to a private investor, in consideration of NIS 40 million. The debentures are from the same series in which it issued NIS 600,000,000 par value Debentures (Series 1) in 2007. The Debentures (Series 1) are CPI linked and bear annual interest of 4.5% which is payable once a year until 2019.

In August 2009, a special purpose company known as The Phoenix Capital Resources (2009) Ltd., which engages in raising funds in Israel for The Phoenix Insurance ("The Phoenix Capital Resources"), raised NIS 500 million through a prospectus, in which promissory notes (Series A) were offered to the public. Promissory notes are linked to the Israeli CPI, and bear an annual interest of 4.4% paid twice-annually each year between 2010 and 2018. The Phoenix Insurance undertook to meet the payment terms of the promissory notes (Series A) issued by The Phoenix Capital Resources.

It should be noted that under the control permit, The Phoenix is subject to restrictions on the issue of "means of control".

In September and October 2010, The Phoenix raised NIS 400 million in capital through the issue of debentures, half of which are repayable in one lump sum on September 30, 2022, (with an option for early redemption after nine years), bearing an annual interest of 3.6%, and linked to the CPI for August 2010 ("Debentures (Series B)"); and the other half of which are repayable in one lump sum on September 30, 2020 (with an option for early redemption after 7 years), and bearing an annual interest of 6% (unlinked) ("Debentures (Series C)").

Debentures (Series B) and Debentures (Series C) have special features as instructed by the Commissioner of Insurance, in part with respect to the deferral of payments, early redemption and supplementary interest.

In November 2011, The Phoenix raised NIS 213,712,000 par value Debentures (Series B), and NIS 143,501,000 par value Debentures (Series C) by way of an expansion of series, and in the total amount of NIS 361.5 million.

The consideration from from Debentures (Series B) and Debentures (Series C) was recognized by the Commissioner of Insurance as hybrid tier-2 capital for The Phoenix Insurance, subject to limitations on the maximum rate of tier-2 capital, as mentioned in the Commissioner's circular with respect to the equity of insurers.

C. Credit rating

On October 16, 2011, S&P Maalot upgraded the financial robustness rating for The Phoenix Insurance from ilAA to ilAA+ (the rating outlook remained stable). Maalot therefore upgraded the rating for the The Phoenix Insurance's deferred promissory notes from ilAA- to ilAA, and the hybrid tier-2 capital of The Phoenix Insurance from ilA+ to ilAA-.

In November 2011, and February 2012, Maalot affirmed its Aa3 rating for Debentures (Series 1) of The Phoenix and Debentures (Series B and C) of The Phoenix Capital Resources.

1.12.16 Taxation

See: Note 42 to the financial statements.

1.12.17 Restrictions and supervision of The Phoenix's operations

A. The Insurance Contract Law, 1981 ("the Insurance Contract Law")

The Insurance Contract Law mainly regulates the relationship between the insurer and the policyholder, including the status of the insurance agent, and also determines the main provisions in respect of the nature of the Insurance contract, the duty of disclosure and the results of non-disclosure, the insurance period and the terms for its termination or abbreviation, the status and rights of the beneficiaries, the provisions relating to the payments of the insurance premiums and their dates, provisions in the matter of changes in the risk of the policyholder, provisions for the manner of payment of insurance benefits including their prescription date, and various provisions relating specifically to the various types of insurance.

B. The Supervision Law and its provisions

The Phoenix and The Phoenix Insurance are subject to the regulations of the Financial Services (Insurance) Supervision Law, 1981 ("the Supervision Law" or "the Law") and its provisions ("the Supervision Provisions"). The Supervision Law and the Supervision Provisions regulate, inter alia, the following matters:

1. **Powers of the Commissioner of Insurance** – According to the Supervision Law, the Commissioner of the insurance and savings capital market in the Ministry of Finance will be the Commissioner of Insurance. The Law determines the roles and powers of the Commissioner including empowering him to issue directives concerning methods of operation and management of the insurers, insurance agents, their officers and anyone in their employ, to ensure the proper management and preservation of the interests of the policyholders or clients and to prevent harm to the insurer's ability to fulfill its obligations.
2. **Business licenses in the various insurance fields** – Engaging in insurance and insurance brokerage requires a license. The Supervision Law determines provisions in respect of licensing insurers and insurance agents, including the power to revoke licenses.
3. **Holding means of control** – The Supervision Law determines provisions for permits to hold the means of control of an insurer and insurance agency as well as provisions pertaining to prohibitions on material holdings in the long-term savings sector For information concerning the permit for controlling and holding the means of control in an insurer - The Phoenix Holdings Ltd. and its subsidiaries - issued by the Ministry of Finance Commissioner of the Capital Market, Insurance and Savings to Mr. Yitzhak Sharon (Tshuva) on December 30, 2010, see Section 1.6.4 above.
4. **Supervision of insurance businesses** – The Supervision Law determines various provisions in respect of supervision of insurance businesses, including provisions pertaining to restrictions on business management, provisions in the matter of organs and officers in the

insurer, handover of reports and directions in the matter of separation of life insurance businesses from other businesses of the insurer. The Law also qualifies the Minister of Finance to enact regulations in various matters connected with supervision of insurance such as types of assets to be held by the insurer against liabilities and methods of their investment; duty of the insurer to hold insurance reserves and the manner of their calculation, operating as an overseas insurer; determining insurance terms for insurance plans and premiums and provisions in respect of maintenance of stability of insurance companies.

5. **Provisions in respect of policyholders' interests** – The Supervision Law qualifies the Minister of Finance to enact regulations pertaining to preservation of the interests of policyholders, including the Commissioner's power to investigate public complaints, provisions regarding the rates of premiums and other payments which the insurer may collect from the policyholders; provisions regarding terms in an insurance contract and their wording as well as provisions regarding the structure and form of an insurance policy.

The following regulations were promulgated pursuant to the Supervision Law:

- A) Supervision of Insurance Businesses (Minimum equity required of an insurer) Regulations, 1998 ("the Minimum Equity Regulations") regulate the minimum capital required of an insurer, pursuant to the various definitions relating to the capital of the insurance companies. For further details see Section 1.12.2(B)(2) above and Note 35 to the Company's Financial Statements.
- B) Supervision of Insurance Business Regulations (Methods of investing an insurer's capital and reserves and liability management), 2001 ("the Investment Methods Regulations") include provisions concerning the types of assets that insurers are permitted to hold against various liabilities, restrictions regarding an insurer's investment in a subsidiary or investee, a holder of means of control in that insurer, an principal shareholder, another insurer or in any other corporation engaged in insurance brokerage.
- C) Supervision of Insurance Business Regulations (Methods for calculating provisions for future claims in general insurance), 1984, include regulations concerning the insurer's obligation to hold insurance reserves, the manner in which they are calculated and provisions for pending claims.
- D) Supervision of Insurance Business Regulations (Report details), 1998, provide for the content, details and accounting principles used to draw up an insurer's financial statements.
- E) Supervision of Insurance Business Regulations (Ways of separating accounts and assets of a life insurer), 1984 determine guidelines for the methods used to separate the accounts and assets of life insurance businesses from the insurer's other insurance businesses, and separation of assets of life insurance businesses participating in profits from assets from all other life insurance business assets.

C. Legislation Implementing the Bachar Committee Recommendations

As explained in section 1.12.2(D), in July 2005, legislation was passed for the implementation of the Bachar Committee Recommendations. The following are the principal points of law for implementation of those recommendations:

1. Increased Competition Law: The definition of long-term saving assets and the determination of a market share ceiling (15%, about NIS 49 billion); the determination that the banks shall act solely in an advisory capacity (pension and investment advice); definition of the roles of the advisor (pension / investment) and marketer (pension / investment) and a clear distinction between the two; mandatory licensing for institutional employees; a ban on a union of employees or employers serving as a pension agent; higher requirements for fiduciary duties of an agent and advisor; closer supervision of insurers.
2. Consulting and Marketing Law: Firm distinction between a consultant and a marketer and the same licensing obligations for both functions; the determination that a pension insurance transaction can be executed only within an advisory or marketing capacity; the obligation to adapt the product to the client's needs; the licensee's obligation to provide the client with written documents explaining why the pension saving scheme is worthwhile, the advisor's recommendation, the obligation of due disclosure concerning conflicts of interest; obligatory documentation of advisory and marketing activities; the

license holder's obligations to trust and due care; the obligation to draw up a written agreement between the advisor and the client; the obligation to maintain confidentiality between a client and an agent; monetary and/or criminal sanctions for the breach of obligations by a licensee.

3. Provident Funds Law: Firm establishment of an employee's right to choose the fund in which his or her pension savings shall be invested; application of the principle of mobility between provident funds for payments and compensation; instructions on investment of the annuity fund monies; the obligation to collect distribution commissions from the member for pension advice/marketing; wide-ranging obligations to supervise the managing companies; civil and criminal sanctions

D. Additional legislation:

1. Streamlining of Enforcement Proceedings in the Israel Securities Authority (Legislative Amendments), 2011, published in January 2011, seeks to streamline the enforcement of those laws entrusted to the Israel Securities Authority (the Securities Law, the Regulation of Investment Consulting Law and the Joint Investments in Trust Law). The Law adds two new enforcement mechanisms as well as various sanctions.
2. On October 19, 2010, the Increased Enforcement in the Capital Market Bill (Legislative Amendments), 2010, was published. This bill aims to guarantee the proper management of institutional entities and to safeguard public interest in savings and prevent damage to the institutional entities' ability to meet their obligations. The bill proposes changes to the current enforcement arrangements under the supervision laws, expanding the Commissioner's supervisory powers, and granting him administrative inquiry powers in order to investigate violations of the supervision laws.
3. For details about the possible impact of the Concentration Committee's recommendations, if accepted, on The Phoenix, see Section 1.12.2(D) above.
4. In March 2012, the Knesset Finance Committee approved draft Supervision of Financial Services (Provident Funds) Regulations (Investment rules that apply to management companies and insurers), 2012, which equate the legislative arrangement for insurance with the laws applicable to pension and provident funds; at the same time, various changes were made in some of the existing investment rules, in an effort to adapt them to Ministry of Finance policy relating to the capital market's method of operation in general, and the activity of the institutional investors in particular. The draft regulations define rules for the gradual transition from the currently existing provisions to the investment restrictions as defined in the new regulations.

1.12.18 Material agreements

For details regarding the agreement pertaining to the acquisition of Excellence, see Note 14 to the financial statements.

1.12.19 Legal proceedings

As part of the regular course of business of The Phoenix in the insurance sector, The Phoenix is involved in a number of legal proceedings. Furthermore, at the reporting date, there are a number of motions pending for certification of class actions suits against The Phoenix. The exposure from these lawsuits, and in particular if The Phoenix loses these class actions, if certified, could have a material effect on the results of The Phoenix's operations. For details about pending legal proceedings against The Phoenix and Excellence, including a table of claims which have been approved as class actions, and applications for approval as class actions, see Note 32(A)(4) to the Financial Statements.

1.12.20 Business objectives and strategy

The Phoenix aims to position itself as a leading company in the various insurance segments and in the finance segment, inter alia, as regards innovativeness and service, to expand its operations and increase its market share and profitability. Furthermore, The Phoenix seeks attractive investment opportunities while regularly examining its investments in non-core segments, and the suitability of such investments to The Phoenix's goals and core investments. The Phoenix believes that in forthcoming years, the financial services segment will be influenced mainly by an erosion of management fees, fees in the various operating segments, and stiffer regulations. An important component of Excellence's business strategy will include dealing with the repercussions of these trends.

1.12.21 Risk factors

- A. **Market conditions** – The general market condition has an effect on The Phoenix's businesses. A recession, also caused by a deterioration in the security or global economic situation, could cause a decline in the volumes of deposits in the various long-term savings channels and even withdrawal of pension and medium-term savings (study funds) to meet present needs, increase in lost debts, reduction of the cover purchased in insurance policies, increase in the number of insurance events and claims (because of an increase in the number of break-ins and frauds), filing of claims on earlier dates, and increasing competition in the various segments of operation.
- B. **Employment level** – The national level of employment has a significant influence on The Phoenix business interests, principally in the field of long-term savings, as it influences the allocation of funds to the various savings channels. Furthermore, the drop in the number of employed (an increase in unemployment) and in wage levels has a negative effect on the volume of new sales and cancellation rates in insurance portfolios.
- C. **Market risks** – The materialization of principle market risks, such as: share risks, interest risks, spread risks, currency risks, and inflation risks, may lead to the devaluation of assets held by The Phoenix.

1. **Capital markets in Israel and around the world** – A significant proportion of The Phoenix assets portfolio is invested in securities in capital markets in Israel and other countries and in financial derivatives which typically suffer from fluctuations caused by market risks and political and economic events in Israel and around the world.

The Phoenix Insurance manages the negotiable assets held, inter alia, against insurance liabilities, while taking into account market risks and the nature of the liabilities, such as linkages and the yield required. Sharp fluctuations in investment asset prices are liable to affect the reported value of the negotiable securities portfolio on The Phoenix's capital and on its reported profits. In view of the investments in financial and other assets, changes in the capital markets and the value of capital market assets have a significant influence on The Phoenix's results, both in terms of profits stemming from profit-sharing insurance policies and in terms of The Phoenix's nostro portfolios. In addition, a crisis in the capital markets in Israel and abroad is liable to cause the collapse of key financial institutions and this increases the risk in The Phoenix's agreements with these entities (counterparty risk).

2. **Interest risks** – Losses which could arise from changes in the interest curves in Israel and abroad. The Phoenix Insurance holds linked, shekel and foreign-currency debentures against its insurance liabilities. Therefore, a rise in the interest curves in Israel and abroad will result in losses in the portfolio caused by the drops in debenture prices. Furthermore, increased interest rates may increase proceeds in the long-term savings segment in general and in the guaranteed-yield policies in particular.
3. **Spread risk** – The loss that is liable to be generated as a result of changes in the spread risk between marketable concern-related debentures and government bonds (no risk). Spread risk changes are meant to reflect the changes in accumulated borrower insolvency and changes caused by market volatility.
4. **Exchange rate risks** – The Phoenix Insurance's investments abroad are exposed to changes in the exchange rates for those currencies in which the investments were made and principally, changes in the rates for the US dollar, euro, sterling and yen. Moreover, changes in exchange rates affect the value of assets in foreign currencies included in The Phoenix's investment portfolio, insurance liabilities and activities conducted with reinsurers (when the cover price is in dollars).
5. **Inflation risks** – Among other things, The Phoenix holds non-linked financial assets and a rise in the CPI will result in the erosion of their value. Moreover, as the majority of The Phoenix's insurance liabilities are CPI-linked, holding non-linked assets may have a negative effect on The Phoenix's profitability in the event of an increase in the CPI (see also ALM risks below).
6. **ALM risks** - Risks due to a discrepancy between insurance liabilities and assets held by The Phoenix Insurance. Such a discrepancy may arise, inter alia, from timing differences (duration differences between liabilities and assets), in scope (a liabilities value which is materially higher than the value of assets), in currency (assets and liabilities held in different currencies),

and in linkage to the CPI. In this context, The Phoenix is exposed mainly to inflationary risks (and duration differences in life insurance and long-term savings).

- D. **Liquidity risks** – Inability to sell assets immediately or without having a detrimental effect on their value due to low marketability may lead to losses upon realization of such assets. The Phoenix Insurance holds, inter alia, non-marketable assets and low-marketability assets. These holdings include corporate bonds, loans, non-marketable shares, low-marketability shares and alternative investments. The marketability issue is exacerbated in times of crisis, when deteriorating market conditions have a negative effect on the liquidity of assets.
- E. **Credit risks** – The risks for financial losses due to counterparts not meeting their obligations or a downgrading of their credit rating. The Phoenix invests part of its assets in the provision of credit, loans and mortgages to corporations, agents and various other borrowers; in various types of deposits in the Israeli banking system; in negotiable and non-negotiable securities; in financial instruments such as credit trusts, CDOs and more. Furthermore, The Phoenix Insurance is exposed to the credit risks of the reinsurers with which it has signed insurance contracts. Defaults on obligations by counterparts to the agreement as a result of insolvency, and impairment of the debt due to a drop in a borrower's credit rating or in their repayment ability, will have an adverse effect on The Phoenix profits.
- F. **Changes in public preferences** – The public's tendency to choose substitute products in the different fields (pension, provident funds, or executive insurance) or the public's tendency not to undertake insurance policies may have an effect on demand for The Group's products and its profitability in the different fields.
- G. **Regulation** – The Phoenix's activities are subject to extensive regulatory demands. There is a continuing trend towards greater strictness and the addition of more regulatory demands as well as stronger enforcement of these demands. Non-compliance with regulatory demands might result in a range of sanctions and damage to the Company's goodwill. Changes in regulatory provisions have an effect on financial reporting, the Company's operations, and its profitability. Some of The Phoenix Group's companies operate in accordance with permits and licenses granted to the companies in accordance with the law by the Commissioner of Insurance. Non-compliance with the permit and license conditions might result in sanctions or even cancellation of the licenses. Furthermore, regulation in the insurance industry has a significant effect on the structure of the products sold and the premiums collected for the different products. The provisions in law, instructions and agreements pertaining to the structure of savings in the economy and principally, those pertaining to pension savings, including the associated tax implications, have an effect on changes in the volume of activity in the market and the substitutability of the different products, including their portability. As a result, these provisions affect both the life insurance and long-term savings portfolio of The Phoenix Group's companies, and their future sales. The Phoenix's insurance agencies are subject to regulatory directives, and changes in these directives may impact their operations and profitability. In addition to the regulation in the long-term savings and insurance sectors, The Phoenix is subject to the regulatory requirements of securities laws and Companies Law and noncompliance therewith is liable to generate various sanctions as well as damage to goodwill.

As The Phoenix is controlled by the Company, it may be affected by the Commissioner of Banks in Israel's Proper Conduct of Banking Business Directives. These include, inter alia, restrictions on the scope of loans that a bank in Israel may issue to a single borrower, to the six largest borrowers and to the group of largest borrowers in the banking corporation (as these terms are defined in the above directives)

The Phoenix Insurance is subject to equity adequacy requirements. Low equity levels (although conforming to equity adequacy requirements) may have a negative impact on the Company's operations and its ability to insure new businesses.

In 2009, the minimum equity requirements for insurance companies were increased, and the rules for recognition of tier-1 and tier-2 equity were made more stringent. As part of the implementation process for the Solvency II directive, insurance companies may be required to supplement their equity.

- H. **Legal precedents** – The Phoenix is exposed to legal decisions that might constitute binding legal precedents in reference to insurance activities, change the scope of The Phoenix liabilities and incur unexpected costs for insurance policy transactions or for estimates of insurance obligations given in the past.

- I. **Claims and class actions** – The Phoenix is exposed to numerous claims in the context of the Company's insurance activities (such as investments and extension of credit), and in particular is exposed to those lawsuits with the potential to become class actions, and The Phoenix might find itself obliged to pay very considerable sums. At the reporting date, The Phoenix Insurance is party to legal proceedings, including class actions, which may lead to its obligation to pay material amounts.
- J. **Competition** – Intensified competition in those fields in which The Phoenix is active might have a detrimental effect on The Phoenix's profits. Increased competition might arise from fiercer competition between existing competitors; the entry of new competitors, or the entry of new distribution channels. Competition has an effect in terms of market share, product tariffs and The Phoenix's costs.
- K. **Policy retention** – Activities in life insurance, provident funds and pension funds segments are vulnerable to policy cancellations and redemptions during the agreement period. The ability to retain the existing client portfolio depends, among other things, on the terms of the policy, fund or trust as appropriate, the terms offered by competitors, the policyholders' ability to transfer their money, market conditions, marketing activities and more. The Phoenix's ability to retain its existing life insurance portfolio depends, inter alia, on its ability to achieve favorable results compared with its competitors.
- L. **Operating risks** – During its business activities, The Phoenix is exposed to many operating risks, such as failure of internal systems, failure of computing and information systems including a lack of information security, human error (employees, agents and suppliers), fraud, computer crime and external damage to The Phoenix (such as earthquakes). Specifically, a significant proportion of The Phoenix activities (business activities, regulatory demands and operations) rely on computerized information systems. Therefore, a lack of sufficient infrastructure or alternatively, failures in The Phoenix's computing systems might cause significant damage. Actuarial errors have a significant effect on the adequacy of The Phoenix's rates and on estimates of the scope of the insurance obligations. Furthermore, possible errors in adapting reinsurance coverage to that given to policyholders, and in particular in large-scale insurance policies, expose The Phoenix to potential losses.
- M. **Insurance risks** – The Phoenix Insurance is exposed to risks associated with pricing and the assessment of insurance liabilities. The insurance policies sold by the Company cover a range of risks, such as death, life expectancy, disease, medical developments, natural disasters (such as earthquakes), and theft. The Phoenix is also exposed to catastrophes, where the principal catastrophe is an earthquake in Israel and war and terrorism in Israel. These events may lead to a large volume of aggregate losses in property, life and health insurance. Pricing of policies and the assessment of insurance liabilities are based on past experience, assessment of the legal situation, and assessment of existing risks and changes therein. Changes in risks, incident frequency and severity, and the legal situation may affect the results of The Phoenix's operations. Mistakes in the costing and estimation of liabilities could result from selection of the wrong pricing model (model risk), use of biased parameters in the pricing model (risk parameters) and an increased rate of cancellations of the existing policies.
- N. **Reinsurance** – The Phoenix Insurance buys reinsurance on international markets. The Phoenix ability to buy reinsurance on good terms is influenced by the company's performance and global reinsurance capacity (dependent upon among other things on reinsurers' stability and the incidence of catastrophic events around the world). Changes in the cost and scope of reinsurance offered in these markets have an influence on The Phoenix profits and its ability to expand the insurance volume and commit to certain insurance liabilities. Reinsurance does not absolve The Phoenix from its obligations towards its policyholders in accordance with the insurance policies and for that reason, reinsurers' financial stability and credit ratings influence the business results of insurance companies. Therefore, non-fulfillment of a reinsurer's commitments to The Phoenix might have a significant effect on the Company's ability to meet its obligations to its clients (for example, in the event of a catastrophe).
- O. **Damage to goodwill** – The Phoenix's goodwill and reputation constitute important factors in the scale of The Phoenix's operations and profitability, when The Phoenix conducts business with new clients and in the retention of existing clients. Embezzlement, legal proceedings against The Phoenix and irregular or illegal activities might damage the Company's good name.
- P. **Exposure to the financial integrity of The Phoenix, the value of its shares or its rating** – Harm to the financial integrity of The Phoenix, the value of its shares or a lowering of its credit

rating could make it difficult for it to operate and affect the future terms of its capital and debt raising insofar as needed which might be necessary in order to comply with capital adequacy requirements.

1.12.22 Risk factors table

The following table gives details of the principal risk factors to which The Phoenix is exposed and their potential degree of influence on its business:

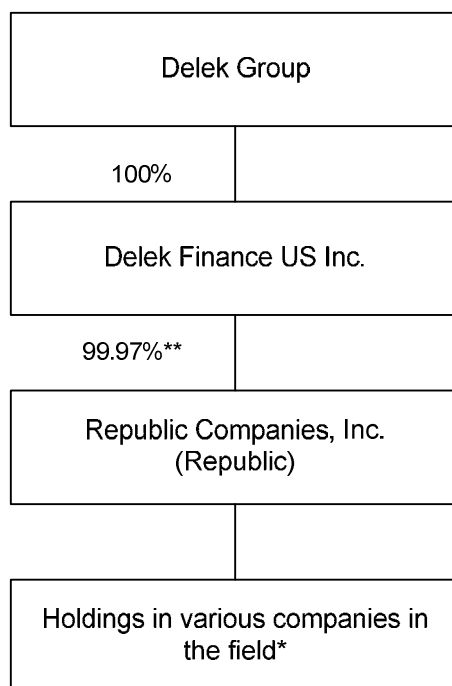
Risk factor	Effects of risk factors on The Phoenix's activities		
	Major	Moderate	Minor
Macro risks			
Economic situation	✓		
Employment levels		✓	
Market risks	✓		
Liquidity risks			✓
Credit risks	✓		
Industry risks			
Regulation	✓		
Legal precedents		✓	
Competition		✓	
Portfolio retention rates	✓		
Reinsurance	✓		
Insurance risks	✓		
Changes in public preferences		✓	
Risks specific to The Phoenix			
Damage to goodwill		✓	
Damage to The Phoenix's financial integrity, share value, and rating	✓		
Operating risks		✓	
Lawsuits and class actions	✓		

The degree to which the risk factors affect The Phoenix is based on the assessments made by The Phoenix's management, while taking into account the scope and nature of the Company's activities at the date of this statement. Changes in activity characteristics and/or market conditions might also change the degree of the effect.

1.13 The Insurance segment in the U.S.

Delek Group's operations in the insurance sector in the U.S. was acquired in December 2006 for a total consideration, including transaction expenses, of USD 298 million, which was paid upon closing the transaction.

The following is a chart of the primary holdings in the insurance sector in the United States:*



* All the held companies also controlled companies, and are consolidated in the financial statements

** The balance of Republic is owned by senior officers of the Company.

1.13.1 General information on the segment of operations

A. Structure of segment of operations

Republic Companies Inc. ("Republic"), an insurance holding company that was formed in Delaware, holds several subsidiaries and insurance agencies, mainly involved in property and general insurance. The company operates through a network of independent insurance agencies in the states of Texas, Louisiana, Oklahoma, Arkansas, Mississippi, California, and New Mexico. Altogether, Republic holds insurer licenses in 48 states. Such licenses allow Republic to collaborate with some of the largest insurers in the segment who wish to expand their activities to additional states, and therefore find it convenient to utilize the licenses held by the company (in other words, Republic operates as front for said companies). Every year, contracts are usually signed with no more than a few companies. Republic has been operating under that name in the US insurance segment, since the turn of the twentieth century.

Unless stated otherwise, in this chapter, the terms "the Republic Group" or the "Group" will be used to describe Republic and its subsidiaries and affiliates.

The Republic Group classifies its operations under four categories:

1. **Personal Lines** – Insurance agents and agencies selling Republic insurance policies for homeowners and vehicle owners ("**Personal Insurance Lines**").
2. **Commercial Lines** – Insurance agents and agencies selling Republic property insurance policies, motor liability insurance policies and workers' compensation policies to small and middle size businesses ("**Commercial Insurance Lines**").
3. **Program Management** – Managing General Agencies (underwriting agencies) ("MGAs") which offer, alongside the Republic Group's standard insurance products, additional insurance products intended to segments and entities with **special characteristics** that are incompatible with the usual risk profiles provided by standard insurance policies.

Unlike operations in the personal and commercial insurance lines, MGAs in the Program Management segment independently issue policies under the Republic name, or under the names of its subsidiaries and affiliates, exercising their discretion in respect of the terms and prices of the policies, wherein the reinsurance terms are established by mutual consent. Republic usually bears only a small part of the total liability (5% to 40%), although some smaller programs are 100% retained and it is agreed that the agencies will handle the insurance claims while Republic supervises current claim settlements.

4. **Insurance services** – Insurance services for insurance companies (“**Insurance Services**”), involve cooperation with insurance companies not affiliated with the Republic Group, by providing fronting services allowing these companies to use the Republic Groups licenses and rights in the areas in which it owns licenses, in return for fronting fees, and subject to signing reinsurance agreements with these companies. Republic assumes liability for settling policyholder claims, but it is fully backed by reinsurance with those insurance companies.

Property and liability insurance provides protection for **predefined** events such as property damage and third party claims. A distinction may be made between personal insurance lines (i.e. personal policies) and the sale of property and liability insurance in commercial insurance lines, i.e., (business policies). The Republic Group operates in both markets. Furthermore, a distinction may be made between the standard (admitted) market and the non-standard (non-admitted) market. In the admitted market, the policies and prices are usually supervised and the cover tends to be standard. In this market, the Republic Group focuses on the less competitive market segments, in which the large insurance companies are less involved due to factors such as type of business, location, nature of cover or size of policy premiums. Most of the Republic Group's operations, in all lines, are concentrated in the admitted market. The non-admitted market focuses on risks that are difficult to estimate and are covered by more flexible policies and prices. The cover in this market is usually unsupervised. The Republic Group is licensed to operate in the non-admitted market, primarily in vehicle insurance and liability insurance lines.

The reserves for insurance claims are also influenced by the type of operation. Insurance on property and vehicles are usually calculated on a short-tail basis, while for reserves calculated for some of the liability and workers compensation lines are naturally long-tailed. The Republic Group does not operate in the health insurance and life insurance segments.

For further particulars regarding the Republic Group's lines of operation, see section 1.13.2 below.

The table below presents financial information pertaining to the Republic Group's main lines of operation. The operating loss or profit relates to the total income less claims, acquisitions and operating expenses but does not include interest expenses on debts, the non-controlling interest and capital gains in companies which are not consolidated, (data are presented in accordance with US GAAP principles, in USD millions):

For the year ended December 31, 2011:

	Gross premiums	Insurance premiums earned	Investment results	Other	Total revenues	Operating profit (loss)²³⁰
Personal insurance	207.4	168.0	8.9	1.8	178.7	(13.1)
Commercial insurance	135.3	110.7	7.7	0.5	118.9	(36.6)
Program Management	149.1	74.9	5.9	1.4	82.2	(2.8)
Insurance services	240.0	0	1.7	11.1	12.8	3.8
Consolidated	731.8	353.6	24.2	14.8	392.6	(48.7)

²³⁰ Operating profit refers to the profit before finance expenses and tax and before one-time items including provisions for pension, impairment of value, goodwill, intangible assets and non-controlling interest.

For the year ended December 31, 2010:

	Gross premiums	Insurance premiums earned	Investment results	Other	Total revenues	Operating profit¹
Personal insurance	213.8	150.9	12.0	1.6	164.5	17.8
Commercial insurance	129.3	88.4	10.1	0.4	98.9	5.7
Program Management	223.3	75.7	7.3	1.7	84.7	6.6
Insurance services	241.9	0	2.46	9.6	12.2	2.6
Consolidated	808.3	315.0	32	13.3	360.3	32.7

For the Year ended December 31, 2009:

	Gross premiums	Insurance premiums earned	Investment results	Other	Total revenues	Operating profit¹
Personal insurance	221.3	173.3	13.5	2.5	189.3	(11.9)
Commercial insurance	132.0	97.6	11.6	0.4	109.6	(10.3)
Program Management	268.1	94.3	8.0	3.5	105.8	9.1
Insurance services	289.8	0	3.5	10.5	14.1	6.5
Consolidated	911.2	365.2	36.6	16.9	418.8	14.0

As shown in the table above, Republic's operating loss for the reporting year amounts to USD 47 million. The loss after revision of the provision for pension, USD 13 million, and amortization of goodwill, USD 61 million, and after the effects of tax and other adjustments (mainly a tax benefit), amounts to USD 111 million. For details about amortization of goodwill at Republic, see section 8B and Note 20 to the financial statements.

The loss can be attributed to three factors: unexpected adverse development as the result of increasing reserves for older vehicle and general liability and workers' compensation claims; record weather related losses from tornado, wind, hail and wildfire claims that were approximately double the expected weather catastrophe losses for a normal year; and the impairment of goodwill and intangible assets in the Company's Personal Lines and Program Management segments as the result of the large underwriting loss and reduced underwriting capacity due to lower statutory surplus.

Although Republic did not experienced any hurricane losses in 2011, record tornado, wind, hail and wildfire losses in Texas, Oklahoma, Arkansas, Louisiana and Mississippi resulted in approximately USD 64.5 million of losses (after reinsurance) compared to USD 23.2 million in 2010.

In addition to record weather-related losses, Republic experienced adverse loss and loss adjustment expense, primarily from a number of old claims for liabilities, workers' compensation and auto liability claims.

Total net adverse reserve development of USD 41.8 million was recognized in 2011, approximately USD 11.8 million of which was charged in the fourth quarter.

As mentioned, the goodwill impairment was largely the result of increased weather volatility and related underwriting losses and a decline in a large workers' compensation program, which have resulted in declining surplus in the Company's insurance

subsidiaries, thereby reducing the Company's underwriting leverage capacity and placing stress on future premium projections. These factors, combined with increases in the appropriate discount rate used in the valuation model, resulted in goodwill impairment.

Republic's gross premiums were USD 731.7 million for 2011 compared to USD 808.3 million in 2010 in general terms. The U.S. insurance market is slowing in most sectors as a result of the economic situation and the free capital in the markets that affect competition and the ability to grow. Republic continues to retain its traditional independent agency business, including modest growth in commercial sectors; however, Program Management and Insurance Services are seeing some decline as a result of terminated programs and declining premiums due to the competition mentioned above. The surplus capital of companies in the U.S. market will make premium growth difficult in the foreseeable future. The principal factors influencing premium turnover in 2011 include these:

- Commercial insurance business increased 4.7% in 2011 compared to 2010.
- Personal insurance business declined by 3.0%, with most of the decline coming from standard personal property and standard auto.
- Program Management business was down 33.2% in 2011 over 2010. The workers' compensation program that provided significant growth in 2010 was terminated by mutual agreement in the first quarter 2011, and in an attempt to help offset the loss of the program, Republic has entered into two new programs. The premium volume in the new programs was modest in 2011, but is projected to grow in the coming months.
- Insurance Services and premium underwriting business was essentially flat in 2011 compared to 2010. The modest increase was the result of two new programs outpacing the decline in several large private auto programs. The large auto programs experienced significant growth over the past several years; however, competition has resulted in a leveling and now slight decline for this business. All of the Insurance Services premium is 100% ceded to unaffiliated reinsurers in exchange for fees.

Net premiums after the cost of reinsurance were USD 334.4 million in 2011 compared to USD 333.6 million in 2010. Termination of the large workers compensation program in the Program Management sector resulted in a 9% reduction in total net premiums in 2011, since most of the premiums are ceded to reinsurers. Catastrophe reinsurance costs remain relatively high as the result of reinsurer losses from the hurricanes in 2008 and catastrophe model changes.

Republic's net insurance premiums earned (residual) were USD 353.6 million in 2011 compared to USD 315.0 million in 2010. The increase in earned premiums largely represents the residual impact of the run-off of the 20% quota share reinsurance treaty from 2010. In 2010 Republic's gross premiums amounted to USD 803.3 Millions, compared with USD 911.2 million in 2009 – a decrease of 11.3%. The Program Management and the insurance services sectors were the main source of the decrease., most of it stemming from the general slowdown in the US business section.

The private, vehicle and homeowners insurance lines have decreased by only 3%, and this too was a consequence of changes adopted in the underwriting policy, the results of which are seen clearly in the company's balance sheet for this sector. Fronting policies decreased by 16% during 2011, with the decrease resulting mainly from an overall decrease in the business operations of the companies that collaborated with Republic in marketing these types of policies. Gross premiums in the Program Management sector (underwriting agencies) also decreased by about 16.7% in 2010, mainly as a consequence of the decrease in premiums attributed to the workers compensation program in California. This decrease resulted from the economic slowdown in California, which caused many businesses to downsize their operations. In 2010, the gross premiums in the commercial insurance line decreased by about 2.1%. Considering the strong competition in the insurance market and the general slowdown, a decrease of 2.1% is a significant achievement for Republic when compared to its competitors. This sector continues to lose because of the intense competition and the decline in business activities. Republic is taking steps to optimize this portfolio.

Republic's Share premiums in 2010 net of reinsurance costs amounted to USD 333.6 million, compared to USD 326.6 million in 2009 – an increase of 2.2%. The increase in Share premiums while gross premiums decreased, is attributed to the Quota-Share reinsurance agreement that encompasses 20% of Republic's private and commercial insurances, which was in effect during the period June 2009 to May 2010.

Republic's 2010 results included an operating profit of USD 32.7 million, compared with USD 14 million in 2009. Net income amounted to USD 18.8 million as compared with USD 6.7 million in 2009.

The increase in operating profit and net profit in 2010 stems primarily from a significant improvement in the underwriting results of personal insurance, which combines more conservative underwriting with a decrease in the scope of claims arising from the 2009 weather damages.

Exposure to weather:

Republic's operation reflect a high risk profile for weather risks, owing to the composition of the insured portfolio (most of it property) and the geographic area in which the company operates. For this reason, the company's management has been working to decrease its exposure to weather risks, mainly through diversifying its marketing channels and products portfolio. The company is also considering expansion into geographic areas where the weather risks are lower.

2010 was the best year as regards the scope of claims arising from weather damages - about USD 50 million (before reinsurance). In 2009, by comparison, claims amounted to about USD 80 million, while in 2008 they were USD 241 million. And after reinsurance: 2010 – USD 23 million; 2009 – USD 57 million; 2008 – USD 79 million.

The assets allocated to the various insurance sectors at 31 December for the years 2011 and 2010 (in accordance with US GAAP,²³¹ in USD millions):

	2011	2010
Personal insurance	356.4	376.8
Commercial insurance	298.5	269.5
Program Management	447.2	498.9
Insurance services	330.5	361.9
Consolidated	1,432.6	1,507.1

B. Legal restrictions, standardization and special constraints

1. Regulations applicable to Republic Group due to its holdings in insurance companies and agencies: Republic Group is the parent of several insurance companies and agencies and is subject to the laws of the states in which these companies are registered, in particular, Texas, Oklahoma, Arizona, and California. In general, these laws require registration at the insurance departments of the states and reporting of the operations of the Group's companies. Furthermore, material transactions between the Group's companies including the reinsurance and insurance services agreements, are required to be fair and reasonable, and if there are material transactions or relating to specific categories, then they also require prior notice and approval from the local insurance department.
2. Change of control: Insurance companies are subject to provisions limiting the acquisition or transfer of control. A potential buyer interested in acquiring control of an insurance company or agency requires prior written approval from the insurance department of the state in which the insurance company or agency is registered. The approval takes into consideration factors such as the financial strength and plans of the applicant. In view of the aforesaid, the Republic Group is not free to sell and/or transfer control of the companies it controls without receiving the appropriate approvals, and even control changes within Republic itself cannot be made without the appropriate approvals.

²³¹ Total assets allocated to sectors according to US GAAP are not materially different from total assets according to IFRSs.

3. The National Association of Insurance Commissioners: The National Association of Insurance Commissioners ("NAIC") is an organization formed by insurance commissioners of the various states to discuss and formulate policy in respect of regulation, reporting and accounting for insurance companies. NAIC has no legislative authority, but it is influential in determining the insurance laws of the various states. The association published recommendations for laws and regulations presenting minimum standards for regulation of insurance. Most states have adopted these recommendations in state legislatures, including the NAIC rules for minimum capital in respect of their investments and operations. Pursuant to the Sarbanes-Oxley Act of 2002, the NAIC adopted additional standards starting in 2010 for insurance companies, such as corporate management transparency, auditor independence and especially the implementation of some of the provisions of Section 404 of the Sarbanes-Oxley Act regarding internal auditing of financial reporting. Additional risk-management rules and provisions for conforming to equity requirements are currently being implemented.
4. Legislative and regulatory changes: From time to time, legislative and regulatory changes have been proposed that could adversely affect the insurance industry. Among others, the proposal of a federal insurance law is under discussion, which will be added on top of the current state laws. Although the Texas legislature does not meet in 2012, other state legislatures will be in session. The legislative process is part of an overall trend accompanying the insurance industry – a trend of ever-increasing regulatory involvement in the business process.
5. Restrictions on policy terms: In 2002, the Terrorism Risk Insurance Act (TRIA) was enacted in response to the uncertainty that prevailed in the insurance and reinsurance markets following the terror attacks on the World Trade Center in New York. The act established a federal assistance program aimed to help the commercial insurance industry to cover claims relating to future terror-related losses and requires insurance companies to offer underwriting cover for damages and losses caused by certain terror acts. As a consequence of this law, the Republic Group is required to include damages caused by acts of terror in its insurance policies. In December 2007, TRIA was extended until the end of 2014, with certain modifications. Future federal and state legislation relating to insurance or reinsurance of terrorism could have an adverse effect on the revenue or financial position of the Republic Groups.
6. State regulation: The state insurance commissioners in the United States have broad powers to regulate the operations of insurance companies. The main purpose of these regulatory powers is to protect the policyholders. The extent of regulation varies from state to state, and could include, for example, business licensing, accreditation of reinsurers, supervision of business integrity and approval of policies and premium rates. Regulation also includes the obligation to file financial statements prepared in accordance with the accounting principles and requirements of state insurance departments, which will audit these statements. As part of the broad authority vested in them, state insurance commissioners may determine and establish regulations for local issues or events. For example, for a certain period after Hurricane Katrina in 2005, the state of Louisiana prohibited insurance companies from canceling insurance policies when the reason for such cancellation was nonpayment of premiums by the policyholders.
7. Periodic audits by state insurance departments: State insurance departments are entitled to conduct periodical audits for various purposes, such as review of an insurance company's financial position, operations and transactions with related parties. **Statutory Accounting Principles (SAP)** are accounting principles intended to help insurance inspectors supervise the solvency of insurance companies. Unlike the GAAP accounting principles, the **SAP principles focus on valuation** of the assets and liabilities of insurance companies in accordance with the relevant insurance laws. The SAP principles that were adopted in part by insurance commissioners in Texas, Oklahoma and Arizona, determine, inter alia, the retained earnings of the companies affiliated with the Republic Group, and therefore also have an effect on the dividends they are allowed to distribute.
8. Restrictions on dividend distribution: In Texas and Oklahoma, state insurance departments are required to approve the distribution of dividends if the dividend, together with all the dividends declared or distributed in the preceding 12 months, exceeds the greater of: (1) 10% of regulatory capital or policyholders' surplus (which is the SAP equivalent of GAAP equity) as at 31 December of the year preceding the distribution; or (2) 100% of the statutory earnings for the calendar year preceding the year in which the

scope of the dividends to be distributed was determined. The Arizona insurance department must approve the distribution of dividends if the dividend, together with all the dividends declared or distributed during the preceding 12 months, exceeds the lower of the following: (1) 10% of regulatory capital as at 31 December of the prior year; or (2) 100% of net investment profits for said calendar year deducting capital gains. Furthermore, all Group subsidiaries and affiliates may only distribute dividends out of their retained earnings. At December 31, 2011, Republic's lead insurance company, Republic Underwriters Insurance Company did not have sufficient earned surplus to pay dividends without Insurance Commissioner approval due to the large net loss in 2011. It should be noted that there are also contractual restrictions prohibiting Group companies from distributing dividends if they are in breach of terms of debentures or loan contracts. The minimal capital limitations must also be reviewed.

9. Guaranty associations: In Texas, Oklahoma, Arizona, and other states, property and loss insurers are required to be members of Guaranty Associations that are intended to cover the cost of payments to policyholders on account of liabilities incurred by defaulting insurance companies.
10. Participation in obligatory insurance plans: Similar to Guaranty Associations, the Republic Group is required to participate in obligatory insurance plans for individuals and entities which otherwise would be unable to afford insurance, and to set aside funds for these plans.
11. At the report date, to the best of Republic's knowledge, it is not in breach of any of the applicable laws.

C. Changes in the scope and profitability of operations in the industry

The property and liability insurance segment is given to cyclical fluctuations in the pricing and availability of insurance cover. Markets with surplus insurance capital may face fierce competition over prices. They may be forced to provide overly extensive insurance coverage, and suffer erosion of underwriting discipline and deteriorating operating results. Such market conditions would typically lead to a period of reduced coverage, after insurance companies leave fiercely competitive and unprofitable sectors or reduce their operations in them. Insurance companies then tend to implement more stringent underwriting discipline, increase their premiums and issue insurance policies with more restrictive terms. The insurance market in general does not necessarily operate in this or any other specific manner, and sometimes a certain segment may boom while another busts. The Republic Group endeavors to minimize the impact of such cyclical fluctuations by expanding its operations into geographic and demographic segments where competition is weaker and where there is a lower supply of insurance services and products.

One of the key factors that drives insurance cycles for the property insurance segment is the volatility associated with severe weather activity. In 2011, there were record worldwide losses from natural events such as earthquakes, flooding, windstorms, wildfires, etc., with economic and insured losses totaling an estimated \$380 billion and \$108 billion, respectively. While the largest events involved earthquakes and flooding in Asia and Australia and New Zealand, the U.S. saw unprecedented weather activity involving unusually severe tornadoes, hail and windstorms, early and late season winter storms, record wildfires, widespread flooding and hurricanes. Thunderstorm and tornado activity was the deadliest since 1975, exceeding \$25 billion in insured losses of the estimated \$40 billion in losses for the year. There were a total of 69 severe thunderstorm events claiming 617 lives in 2011, while tropical cyclone activity, that is usually the major driver of loss, saw three events that amounted to estimated insured losses of \$5.5 billion. It was a very extreme year in terms of catastrophe losses from climatic events in the United States and if taken as a whole, the spring 2011 tornado and severe storm season would be ranked as the fourth most costly disaster event in U.S. history. In addition, drought conditions also impacted large portions of the U.S., especially including the most severe drought on record for Texas. Republic experienced unusually high losses from the tornadoes, hail storms, winter storms and wildfires in 2011.

Weather losses for the U.S. as a whole and Republic in particular were more seasonal in 2010 and 2009. However, in 2008, four rare tropical weather events struck Texas and Louisiana, including three hurricanes, Ike, Gustav and Dolly, all in the third quarter of 2008, and this was after the unusually heavy spring wind and hail storms in Texas and Oklahoma. Weather damage in the U.S. was also moderate in 2007 and 2006 following significant hurricane experience in Louisiana and Texas with Hurricanes Katrina and Rita in 2005 which

significantly impacted the regions in which the Republic Group operates (for further information in this matter see Section 1.13.19 below).

Profitability in 2011 was negatively impacted by adverse development of loss and loss adjustment expenses, primarily from old auto, workers' compensation and mortality claims.

Many U.S. insurers have experienced adverse development for different reasons, some of which are symptomatic of a stressed economy. Republic believes that the causes of its adverse development include increasingly complex claims and higher litigation costs driving up the cost to settle; more difficult cases involving coverage disputes, construction defects and fatalities; more suspicious claims and late reported claims; escalating medical costs; demand surge on roofing claims; internal claims process focused more on bulk reserves than on adequate case reserves with infrequent follow-up; and aggressive plaintiff lawyers unwilling to reasonably settle cases.

As the result of underwriting losses, Republic has experienced stress on its underwriting leverage metrics and goodwill and intangible valuations. In 2011, Republic recorded impairment charges for goodwill and intangible assets as the result of weather volatility, declining premium projections, and increases in the discount rate used in valuation models. Future underwriting losses or declines in premiums could lead to further impairment.

Between 2003 and 2007 the Republic Group showed profits due to several initiatives including redesign of the personal products line, re-underwriting of the commercial insurance line, Program Management plans, and a focus on semi-urban, rural and small- to medium-sized town markets. Nevertheless, 2008 was an extremely fickle year, with record weather damages from hurricane losses, in combination with a global economic crisis that had a significant effect on the value of the investment portfolios, because of the underwriting and operating losses sustained by many insurers.

The worldwide economic downturn that began in 2008 continues to challenge insurance companies and other businesses. While certain financial market and economic measures improved in 2009, 2010 and 2011, unemployment, manufacturing output, housing values and foreclosures, low interest rates and international uncertainty about the euro zone debt crisis and unrest in the Middle East, all continue to generate uncertainty in the private and business marketplace. Uncertain economic times often result in property and liability insurance claims that are of suspicious nature or to some degree excessive compared to more stable economic times. Liability claims may be pursued against insurance companies over longer periods of time and involve more extensive litigation in efforts to secure or increase damage awards.

Republic is taking steps to change the mix of its operations in order to vary and spread its focus on property insurance to types of insurance that focus on liabilities, aiming to balance its insurance portfolio. This has included geographic dispersion of risks and improvement on the quality of insurance risks in 2011. These moves were evident in the significant increase in work compensation plans in the Program Management sector in 2009 and 2010, but the economic slump and poor performance led to a decrease in the work compensation plans in 2011.

As the economic crisis continues or worsens in 2012 or beyond, it may adversely affect the operations of insurance companies, including Republic. The implications of the economic crisis include higher unemployment, business and private bankruptcies, foreclosures on assets, reduced investment income, damage to the financial robustness of reinsurers and reinsurance capacity, and an increase in reinsurance premiums. All these could have negative implications for the scope and profitability of operations.

D. Market developments

There were no significant market developments in the course of 2011, except for continued economic uncertainty, which continues to negatively impact Republic's premiums and operations in all insurance lines. Despite the unusually high level of natural catastrophes in the U.S. and worldwide, insurance industry capital and surplus remains strong. Reinsurance rates remain high and surplus strength continues to make it difficult to raise premium rates, with the exception of certain coastal property risks.

Even though the financial markets allowed for positive returns in 2011, market volatility persists and insurance sector evaluations continue to be low. The U.S. Federal Reserve's efforts to suppress market interest rates are projected to continue until 2014. This situation continues to affect the insurance sector in terms of the value of investment portfolios, harm to investments, lower yields, less liquidity, harm to intangible assets and goodwill, and limited

access to capital markets. The unemployment and the many bankruptcies affect the premiums, and indirectly also the damages, as a result of the higher moral risk (i.e., the risk that a policyholder will fabricate a fraudulent or unlawful insurance claim).

Although only one large hurricane occurred in North America in 2011, and it did not impact Republic's area of operations, the substantial effects of the two large hurricanes, Ike and Gustav, and the smaller hurricane Dolly, which occurred in 2008, plus the impact of record spring tornadoes, wind and hail storms continue to impact the results of Republic's operations, as expressed in high reinsurance premiums.

Historically, after large weather catastrophes, reinsurers have been able to raise additional capital from public offers for sale. However today, in view of the crisis in capital markets worldwide, the only source of capital is from organic growth through higher reinsurance premiums.

Even though access to new capital is more limited, the insurance sector manages to maintain record high levels of capital. As a result, insurance premiums continue to be low, competition is fierce and the pressure on underwriting discipline is high. Most market analyses do not foresee changes in these market conditions until 2013 and beyond.

E. Key success strategies in the insurance operations sector, and the changes taking place in the industry

The highly competitive and intensely regulated insurance industry is divided into numerous insurance branches and different insurance populations. The Republic Group regards the following as critical success factors in its sector of operations:

1. Know-how and experience – Operating an insurance business requires, among others, extensive familiarity and ties with different entities operating in the area, including MGAs and independent insurance agents, a solid reputation with policyholders and a deep understanding of the market conditions. In view of the above, know-how and experience in the sector of operations are critical success factors and the Republic Group relies on its many years of experience and know-how in its areas of operation.
2. Focus on less-competitive insurance segments – In view of the competition in the insurance industry, including with major insurance companies with greater resources than the Republic Group, a focus on under-served insurance markets that have been neglected or ignored by larger companies and where Republic's local knowledge allows the Republic Group to compete more effectively against its larger competitors.
3. Reducing operations in competitive sectors – Reducing operations in sectors or products where other, stronger insurers are active (such as auto insurance), and expanding operations in sectors where the company has a competitive edge (such as homeowner insurance).
4. Given Republic's underwriting losses in 2011 and prior and given the weather volatility that Republic has experienced over the past seven years, a comprehensive review is underway concerning Republic's product mix and geographic concentration to evaluate appropriate ways to improve underwriting results and profitability.

F. Main entry and exit barriers of the insurance operations sector, and their changes

The key entry barriers to the industry are the various licensing requirements including greater equity requirements, the need to establish marketing systems or communication systems with agents, and goodwill. The main exit barriers are long-term commitments to policyholders, commitments to insurance agents and companies receiving insurance services from the company, approval of state insurance departments for transferring control in insurance companies and for withdrawal from certain product lines or geographic areas (state insurance departments may attempt to limit a company's decision to stop insuring damages in coastal areas exposed to wind damages).

G. Alternative products to those of Republic and changes therein

Alternative products to those the Republic Group are mainly similar products provided by other insurance companies. The main differences between insurance products provided by different companies generally involve the extent of coverage and the cost of premiums, as well as the level of service provided in the underwriting and claims processes.

H. Structure of competition in the sector of operations and changes therein

The Republic Group competes with many companies in its product lines. The personal insurance market in Texas is dominated by a few large insurance companies (including their subsidiaries and affiliates), including State Farm, Allstate Farmers, Liberty Mutual/Safeco, USAA, Central Mutual, Hannover Harford and Travelers. In the commercial market, the Republic Group competes, inter alia, with Allied, Cincinnati, America First, Hanover, Liberty Middle Market, Travelers, Union Standard, Hartford Central Mutual, CAN, Zurich and UBI. In general, the Republic Group's share of the Texas market is about 1%. The Republic Group has three direct competitors in the MGA market – Praetorian, Delos and Assurant. There are several competitors in the insurance services market, including State National Companies, Old American County Mutual Fire Insurance Company, Consumers County Mutual Insurance Company, and Home State County Mutual Insurance Company.

Competition is based on pricing, offered covers, customer service, agent relations (including ease of doing business for agents, service provided to agents and commissions paid to them), size and financial robustness. The Republic Group seeks to distinguish itself from its competitors by providing a broad product line and focusing on markets where competition is relatively weak. Moreover, the company deals with competition in its areas of operation by fostering good, long-term relations with insurance agents and MGAs, applying its know-how and experience in its areas of operation and fostering its reputation with policyholders. The Republic Group also offers operational flexibility thanks to its various licenses and concessions, which cover a wide range of insurance activities.

1.13.2 **Products and services**

Republic Group operates in four major insurance sectors:

A. Personal Insurance:

In this sector, Republic Group sells insurance policies to individuals through independent insurance agents and three affiliated insurance agencies. Insurance policies include homeowners, fire and low-value dwelling insurance, standard and nonstandard auto insurance and personal policies. Policyholders are located in Texas, Oklahoma, Louisiana, New Mexico, Mississippi and Arkansas, while unconventional vehicle policies are also marketed in Arizona, Oregon and Utah. Republic Group focuses on geographic and demographic areas where the competition is relatively low.

1. Personal property and building insurance: Insurance against various damages, including damage to the building, property inside home, garages and other buildings on the property; fire insurance covering damages caused by fire, lightning, wind and hail storms, collapse of buildings and damages caused by water-related or electricity-related accidents. The Republic Group's home insurance policies provide an average coverage of USD 210,000, while the coverage provided low-value housing is usually more limited and provides an average of USD 71,000 (not including coverage of home contents).
2. Personal auto insurance: Standard auto insurance policies insure against bodily injury and physical damage to the vehicle. Coverage is limited to USD 500,000 per policy, but the average overall coverage of the policy is less than USD 200,000. This insurance is primarily marketed to policyholders who purchase other insurance cover from the company, such as property and homeowners insurance.
3. Nonstandard auto insurance: Nonstandard auto insurance policies cover bodily injury and physical damage to vehicles whose owners have driving records making it difficult for them to purchase standard car insurance, and are therefore required to pay higher than average premiums. Most nonstandard risks amount to USD 50,000 or less. A nonstandard auto insurance policy is still marketed by a general insurance agency affiliated to the Republic Group.
4. Personal umbrella insurance: Umbrella insurance policies offer additional insurance cover beyond the limits of homeowner and vehicle insurance. Most umbrella policies are limited to USD 5 million, and 95% of the risks involved are ceded to reinsurers.

B. Commercial Insurance

In this sector, Republic sells insurance to small and medium-sized businesses through independent insurance agencies and an affiliated agency that insures farm and ranch businesses. The policies include, inter alia, auto, workers' compensation, property insurance (real estate), general liability and umbrella insurance, as well as farm and ranch insurance.

The Republic Group focuses on markets where competition between insurance companies is relatively limited, such as garages, family restaurants, light industry and small workshops.

1. Property insurance: Insured properties are limited to a maximum property value of USD 20 million and insurance is not available for properties where the risks involve residences, such as apartments and hotels. The average property insurance coverage is USD 730,000 and all risks over USD 1 million are reinsured.
2. Liability insurance: Commercial liability insurance provides third-party liability cover for businesses, including bodily injury, medical treatments and fire damages. This policy is limited (deducting reinsurance) to about USD 1 million per insurance event.
3. Commercial package: The commercial insurance package is a combination of property and liability policies.
4. Auto insurance: Commercial auto insurance policies insure against bodily injury and physical damage to vehicles, and may be extended to include medical payments, car rental and more. The policy is limited to USD 1 million per insurance event.
5. Workers' compensation insurance: The insurance provides employers with cover in order to meet statutory workers' compensation benefits for workers who are injured on the job.
6. Umbrella insurance: Commercial umbrella insurance policies provide additional liability insurance for businesses, beyond the limits of standard insurance coverage. Most umbrella policies are limited to a maximum of USD 5 million and the average coverage is USD 3.6 million. 95% of the risks involved are ceded to reinsurers.
7. Farm and ranch insurance: These policies are designed to meet the special needs of farm and ranch owners, providing coverage for dwellings, farm structures, equipment and liabilities. In addition to the Republic Group's regular areas of operation, these policies are marketed in additional areas, including the states of Arkansas, Kansas, Mississippi and Missouri. One large farm and ranch plan was terminated in 2009 due to low results.
8. Public Authorities insurance – property insurance policies for small local authorities and schools, marketed via an affiliated agency.

C. Program Management

Unlike insurance sectors marketed through independent agents, the Republic Group markets personal and commercial policies in the Program Management segment through contracts with unaffiliated MGAs. The MGAs have the capacity and authority to offer policies that they underwrite themselves, subject to specific guidelines set by the Group and these policies are binding for the Group. The Republic Group uses the term "program" to describe such an agreement with an MGA, wherein the Group provides the MGA with uniquely customized insurance products, some of which are directed at market segments that fail to meet the risk profile of standard insurers. The Republic Group requires MGAs to sell the policies according to its guidelines. MGAs provide policyholders with the services that any regular insurance company would provide them, including underwriting, billing and claims administration, yet they are prohibited by law from issuing their own policies.

1. Features of MGA agreements: MGAs issue insurance policies under Republic's name and therefore Republic is liable for the insurance risk. At times, Republic cedes part of this insurance risk to reinsurers. In both cases, Republic is directly liable to policyholders. In addition to bearing all or part of the insurance outcomes of each program, Republic may receive a fronting fee from the MGAs or from the related reinsurers. MGA commissions are based on program profitability. Relations with MGAs are based on years of experience and familiarity with products, markets and marketing of the programs. MGA agreements are generally for a one-year term and are automatically renewed annually, unless one of the parties chooses to terminate with 90 – 180 days prior notice. Republic operates various control mechanisms for overseeing MGA operations: It receives monthly reports from MGAs and conducts audits of each program at least twice a year, in order to evaluate MGA compliance with the guidelines provided.
2. Insurance products: Insurance policies sold through MGAs include workers' Compensation, commercial auto insurance, commercial liabilities (for small businesses), prize indemnity insurance (insurance covering nonpayment of prize money promised a participant in a contest or sporting event), insurance of loan collaterals and guarantees, and employer insurance.

3. Reinsurance: Reinsurers are all high ranking reinsurance companies and/or companies willing and able to provide letters of credit or trust account information to secure their reinsurance balances.

D. Insurance services and corporate

In this sector, Republic Group provides insurance services to national and regional insurers that wish to use the company's concessions and licenses to access insurance markets in Texas and other states. According to the agreements with the insurance companies, Republic underwrites risks that are entirely ceded to the carriers in exchange for a fee. In other words, Republic does not bear the risk involved in these policies as long as the insurers meet their obligations towards the company, and in effect it could be said that the company has full reinsurance. Nonetheless, the company is directly liable towards the policyholders. Most of the insurance policies sold under these agreements are personal and commercial auto policies. Republic limits such agreements to insurers rated A- or higher by A.M. Best rating company, or companies with a lower rating or even with no rating at all, but which provide sufficient collateral. The above limitations have managed to curtail credit losses in this segment. The Republic Group also includes the income from the general agencies it owns for its transactions with insurance companies which are not affiliated with it, in this segment. In the results for this segment, the Republic Group also includes other expenses that have not been allocated to other segments.

1.13.3 Customers

- A. Personal Insurance Segments: Policyholders are private individuals, and the policies are marketed via independent agents and general Republic-owned agencies.
- B. Commercial Insurance segments: Policyholders are small to medium-sized commercial enterprises and businesses, typically in service segments such as garages, family restaurants, light industry, workshops and owners of farms and ranches. Policies are marketed via independent agents and general Republic-owned agencies.
- C. Program management: Policies are marketed by unaffiliated insurance agencies (MGAs). Policyholders include private individuals and small businesses.
- D. Insurance services: These policies are marketed by unaffiliated insurers rated A- or higher by the A.M. Best rating company, or companies with a lower rating or with no rating at all, but which provide sufficient collateral. Policyholders include private individuals and businesses.
- E. About 63% of Republic's insurance policies are issued in Texas. Many customers reside in outlying areas, in relatively small towns with populations of no more than 100,000. At present, about 13% of premiums come from the state of California, through MGAs, as a result of the workers' compensation program.

1.13.4 Marketing and distribution

- A. Personal and commercial product lines: Republic's standard insurance products are marketed through a broad network of independent agents and MGAs. Independent agents do most of the marketing in the personal and commercial products. The agents have no discretion as to the policy terms and they offer the policies with which Republic provides them. Republic prefers to maintain long-term relationships with insurance agents and agencies and more than a third of its agents have worked with Republic for 10 years or more. The Republic Group has a network of over 700 independent agents in the personal and commercial segments. In 2011, the largest Republic independent agency or agency group was responsible for less than 2% of the company's gross premiums.
- B. Republic Group's marketing strategy focuses on segments where competition in the insurance market is relatively weak - mostly segments that cannot afford the premiums of other insurers, and segments located in rural or semi-urban areas, which larger insurance companies are not willing to develop and/or do not view as a strategic target. Furthermore, the company tries to market its range of products to policyholders who already own one or more of its products.
- C. Insurance services and Program Management: Underwriting is provided by six program managers, plus two in run-off. Insurance services are provided to eight unaffiliated insurers and additional earnings come from five affiliated MGAs.
- D. In 2011 and 2010 Republic's largest MGA was responsible for 10.4% and 22.6% of the total premiums, respectively. The agreement with the MGA was terminated in 2011.

- E. One program in the insurance services segment accounted for 23.2% and 22.9% of gross premiums for 2011 and 2010, respectively. However, since this program is completely covered by reinsurance, no net premium is produced in the net share.
- F. The Republic Group's product development and marketing strategy is based on dialogue and constant consultation with agents and agencies, MGAs and insurers marketing the company's products in different segments. This strategy allows the Group to learn from the agents about market needs and to issue policies that sometimes cover risks not covered by the competition.

1.13.5 Seasonality and Weather Damages

- A. The risks insured by the Group usually lead to a larger volume of claims during the second and third quarters of the year, due to a seasonal concentration of weather-related insurance events in the geographic region of operation. Although weather-related losses (including hail, windstorms, tornadoes and hurricanes) can occur during any quarter, historically the second quarter has the highest frequency of such weather events, causing losses that are not covered by reinsurance (hurricanes, by comparison, are more likely to occur in the third quarter, but the losses they cause are usually greater in scope so that they are often covered by reinsurance for large events).
- B. While the second quarter traditionally produces weak results due to seasonal spring storms, 2011 produced some of the most deadly tornadoes, in terms of loss of life and property, in 50 years and resulted in the worst spring storm season in the U.S. in recent history. Unusually severe and frequent tornado, wind and hail losses in Texas, Oklahoma, Arkansas, Louisiana and Mississippi resulted in Q2 2011 being Republic's worst non-hurricane impacted quarter ever. Although there were no significant weather events in Q3 or Q4 2011, the widespread and extensive nature of the loss activity allowed for continuing development from weather events from Q2 for the remainder of the year. Additionally, the unprecedented drought conditions in Texas also resulted in record wildfire losses in the state in Q2 and Q3.
- C. Weather related claims following windstorms and hail were lower than average in 2010 compared to 2009. This result stems from the fact that the average number of weather events during the year was high, but they did not take place in Republic's regions of operation.

In 2009, Republic's net loss caused by weather related damage (after reinsurance) was the second highest in the company's history, following the highest loss in 2008, when three hurricanes hit Republic's region of operation and caused record weather-related damage in Texas. Even though hurricanes are not common in Republic's region of operation, they can cause much damage. Hail storms do not usually affect such large areas as do hurricanes, but they can cause extensive damage, as occurred late in the season by non-typical storms in western Texas in September 2009, which caused damages amounting to USD 30.4 million, and USD 20 million after reinsurance.

The Group purchases reinsurance to protect itself against the high frequency and severity of insurance events related to the weather.

1.13.6 Reinsurance²³²

- A. Republic purchases reinsurance for its personal and commercial insurance operations, in order to reduce its exposure to insurance risks. The company also participates in material reinsurance agreements in the Program Management segment and the insurance services segment, based on its estimate of the potential risk and the premium leverage requirements.

²³² For information pertaining to types of reinsurance see footnotes in section 1.13.6 above: **Contractual reinsurance** between insurance companies and reinsurers is carried out under a reinsurance contract according to which the reinsurer accepts, under agreed conditions, all the risks / transactions sent to it by the direct insurer, without necessitating approval for each risk / transaction separately. Contractual reinsurance is divided into **relative reinsurance**, whereby the risk (claim cover) is split into equal premiums and **non-relative reinsurance** whereby the risk (claim cover) covered by the reinsurer is not directly proportional to the division of premiums. Relative reinsurance is divided into a **quota share**, whereby the reinsurer covers a fixed percentage of claims in a specific sector in return for an equal share of the premium, and **surplus contract**, whereby the reinsurer covers a variable percentage of each claim up to a fixed maximum in return for an equal share of the premium. Non-relative reinsurance is split into **excess of loss**, according to which insurance cover is provided for individual claims whereby the direct insurer covers aggregate damages up to a fixed residual amount and the reinsurer covers the excess amount; and a **stop loss** contract whereby the reinsurer compensates for a preset amount / percentage of the claimed amount. Other than contractual reinsurance, there is also facultative reinsurance which is split among several reinsurers.

Republic's personal and commercial insurance segments are protected by reinsurance against weather related damages and catastrophes.

- B. Republics weather damages and catastrophes reinsurance plan and its excess of loss type reinsurance in 2011 were similar to those of 2010, as regards both coverage and price. In 2011 Republic's said reinsurance contracts compensated for single-loss events up to an amount of USD 280 million, with a retention amount of USD 20 million per event, and included a separate USD 10 million retention for non-coastal weather events. Republic's personal and commercial segments are covered by excess of loss reinsurance contracts and facultative reinsurance, with Republic participating at USD 1 million for any event. The personal, commercial and program management (MGAs) insurance segments are also covered by relative contractual reinsurance. As noted above, the insurance services segment operates in a manner whereby insurance payments to policyholders are fully (100%) backed by reinsurance which is covered by the insurance companies providing the insurance services in return for the fronting fees that Republic receives.

Republic's reinsurers influence its insurance capacity, insurance terms and rates and its profitability. Reinsurance does not absolve Republic from its liability towards policyholders under the insurance policies, but only grants it the right to demand that its reinsurers reimburse it for its losses, and therefore the robustness of the reinsurers may impact the business results of insurance companies. See Section 1.13.19 for further information relating to the centrality of reinsurer influence on Republic's operations. Section 1.13.19 describes Republic's reliance on reinsurers in the context of hurricane damages sustained by the United States in 2008. Due to the global financial crisis, the number of reinsurers and their equity began to decline, leading to a decrease in volume as well as a drop in rating indicating damage to the robustness of reinsurers against the backdrop of heavy losses in assets portfolios and material equity write-offs. It should however be noted that Republic's reinsurance for 2011 has not changed materially, though reinsurance prices have remained high following the large scale weather catastrophes occurring in 2008 and before, and on account of reinsurer inability to raise new capital in the financial markets.

Republic's reinsurance program for weather related catastrophes and excess of loss contract for all risks in 2012 is similar to its program for 2011 as regards both coverage and price, with the exception that the USD 10 million non-coastal retention element was not renewed for 2012 due to excessive pricing.

In 2009, Republic entered a 20% quota share reinsurance program for its personal and commercial insurance segments. The objective of the quota share program is to provide underwriting flexibility and leverage resulting from continuous increase in other segments and in view of projected capital inadequacy in the event of losses following several large-scale catastrophes. This quota share program was not renewed in 2010.

Republic Group chooses its reinsurers according to their financial robustness, operating and payment history and overall reputation. The Group contracts with a large number of reinsurers in order to minimize the risk involved in the failure of any reinsurer to meet its obligations. The Group only contracts with reinsurers rated A- (Excellent) or higher by the A.M. Best rating company or with reinsurers rated lower, on condition that they provide additional collateral. If a reinsurer's rating drops below A, Republic will replace the reinsurer or require external collateral, such as a bank guarantee. At December 31, 2011, approximately 90.5% of Republic's reinsurance was covered by reinsurers rated A- (Excellent) or higher. Additionally, Republic has access to funds held or letters of credit of approximately USD 200 million at December 31, 2011.

The table below presents a summary of reinsurance data relating to the various segments (in USD millions):

Segment	Personal insurance		Commercial insurance		MGAs		Insurance services	
	2011	2010	2011	2010	2011	2010	2011	2010
Gross insurance premiums	207.4	213.8	135.3	129.3	149.1	223.3	240.0	241.9
Reinsurance premiums	39.9	52.9	24.1	33.0	93.4	146.8	240.0	241.9
Share (%) covered by reinsurance	19.2	24.7	17.8	25.5	62.6	65.7	100	100

The decrease in 2011 was mainly due to the runoff of the contractual program that covered 20% of the personal and commercial insurance segments and was not renewed in June 2010.

The scope of reinsurance in general for 2012 is not expected to be materially different from that purchased in 2011. For more about reinsurance, see Note 29 to the financial statements.

1.13.7 Actuary

The Republic Group's liabilities include liabilities for reported losses, liabilities for losses incurred but not reported (IBNR), and liabilities for loss adjustment expenses (LAE)²³³ which are intended to cover the final cost of claim settlement, including claim investigations and legal defense. The extent of liabilities for reported claims is based on estimates claim damages. The level of liabilities for IBNR and LAE is estimated on the basis of past damage costs, policy provisions and other factors. The process of estimating liabilities for IBNR and LAE is an imprecise science requiring discretion since these liabilities are influenced by factors that are subject to significant fluctuation.

The Group applies actuarial models to determine its liabilities. Republic Group employs six certified actuaries with an average of over 20 years of actuarial experience in the different insurance segments. The actuarial models are also used by the company to price premiums in the various segments, as well as to examine reserves for past claims.

1.13.8 Fixed Assets and Facilities

The Republic Group's main office is located in Dallas, Texas, where the Group leases a six-storey office building (covering a total area of 10,500 square meters). All of the Group's administration, finance, underwriting, IT, and other operations are conducted from there. Republic also leases a smaller area for its claim management operation, in an adjacent building. The lease period is until February 28, 2017, with an option to extend it for a further five years. Rent is not material. Furthermore, the Group also leases offices in Houston and San Antonio, Texas, in Phoenix, Arizona, and in Louisiana. These offices serve the Group's subsidiaries.

The Republic Group uses several information systems. Among other systems, the Group uses the RepubLink system designed for its agents, allowing them to file policies for the company's approval personal product lines. The system also provides information relating to policies, such as prices and other terms. The system allows the Group to collect and obtain data relating to policyholders, such as history of claims and premium payments. The investment in IT systems is a material expense and is expected to continue as such due to the Republic Group's efforts to use new technologies for its customer services and to remain competitive in its operations.

1.13.9 Intangible assets

Republic's intangible assets include the value of its connections with agencies, its trademarks, and the licenses and concessions to operate as an insurance company in the various states. As the result of the operating loss in 2011, an impairment loss of USD 52.9 million deemed to have occurred related to Republic's goodwill and intangible assets.

²³³ Loss adjustment expenses (LAEs) are the estimated expenses for covering losses for claims filed but not yet concluded; these expenses are adjusted from time to time according to estimates of anticipated losses.

1.13.10 Human capital

Organizational structure

- A. Republic's human resources – At December 31, 2011, Republic has 401 employees divided among the following departments:

Department	Number of employees
Commercial insurance	70
Claims	66
General agencies	62
IT Systems	56
Bookkeeping / Finance / Accounting	33
Personal insurance	27
Corporate services and billing	27
Underwriting and Actuary	23
Administration / Legal / Human resources	12
Marketing	17
Insurance programs / insurance services	8
Total	401

In 2010 and 2009, 410 and 424 employees were retained by the company, respectively. There are no employer-employee relationships between the Republic Group and the agents marketing its insurance products, other than the agents employed in the agencies owned by Republic.

- B. Senior management and officers – Republic employs about 30 officers, of which 14 are senior executives. The main compensation for company officers is a salary and periodic bonuses based on performance, as an occasional incentive.

Mr. Parker Rush, Republic's president since 2003, will resign from Republic in March 2012 and will be succeeded by Mr. Joseph Mattingly, who has more than 30 years' experience in insurance. . Mr. Uri Omid served as chairman of Delek Finance US Inc and of Republic through August 2011.

Republic has employment agreements with some of its executives. Its other employees are employees whose employment can be terminated at will. Republic provides employee health and life insurance as well as savings plans, profit sharing and other compensation plans.

In December 2006 and November 2007, several senior executive officers at Republic were granted options that are exercisable into Republic shares over a period of five years, in consideration of an additional variable exercise price over the vesting period as set forth in the terms and conditions of the options. Furthermore, a plan for the allocation of restricted stock (representing 0.5% of Republic's share capital) was also adopted. As at December 31, 2011, the fair value of the restricted stock was still zero. Since the projected performance for 2009 and 2010 did not lead to the vesting of these shares, they were cancelled. The fair value of the options as at December 31, 2011 was USD 0.96 million. In the event that all warrants are exercised, Republic's holding rate is expected to decline to about 98%.

1.13.11 Investments

As required under the regulations, in the investment plan and by the rating companies, Republic invests in low-risk investment channels such as government bonds, US state bonds, bonds issued by local government organizations, corporate bonds, mortgage bonds, and ordinary shares that pay dividends. Most of Republic's investment portfolio consists of fixed-income instruments, and in 2011 they were managed by Brookfield Investment Management Inc. (which has assets under management of more than USD 150 billion and specializes in the management of insurance company assets). Brookfield has the authority and discretion to acquire and sell securities on Republic's behalf, subject to instructions it receives from Republic's investment committee. Republic Group's total investment portfolio, including cash and short-term investments, at December 31 for the years 2009, 2010 and 2011, was USD 588.4 million, USD 597.5 million and USD 589.7 million respectively. The investment portfolio earned a positive yield in 2011, despite the volatility of the capital markets, and this in view of the relatively low-risk nature of the

investments. At December 31, 2011, the portfolio has a large balance of cash and short-term investments (USD 42.9 million) waiting for reinvestment, in the wake of the sale of a number of securities in 2011 that was designed to attain profit in view of improved market conditions. In view of the low interest rate environment and unlikely prospect for higher rates, reinvesting cash is not likely yield higher returns in the near term.

1.13.12 Finance

A. Republic has the following finance arrangements:

	Amount (USD millions)	Interest rate at Dec. 31, 2011
Debt to bank	30	3.25%
Subordinated loans	92.8	4.675%
Other	3.3	4.0%
Total	126.1	4.32%

USD 1.9 million is planned for payment during 2011, and the balance is long-term debt.

Following is a breakdown of the debt:

	Amount (USD million)	Effective interest rate at Dec. 31 2011	Basis for determining the interest rate	Maturity date
Senior debt to bank	30	3.25%	LIBOR for 1, 3 or 6 months + 2.5%, or Prime	Quarterly payments of USD 9 M, from beginning of 2013 with a balloon payment in 2015
Subordinated loans	10.3	4.37%	LIBOR for 3 months + 4%	September 2033
1 .Principal				
2 . Principal	20.6	4.28%	LIBOR for 3 months followed by + 3.85%	October 2033
3 . Principal	20.6	3.75%	LIBOR for 3 months + 3.2%	November 2036
4 . Principal	25.8	3.75%	LIBOR for 3 months + 3.2%	June 2037
5 .Principal	15.5	8.18%	Fixed interest up to September 2012, LIBOR for 3 months + 3.3% thereafter.	September 2037
Total	92.8			

Other debts:

Original issue discount note	2.6	4.0%	OID note with 4% interest, 10% charge rate	Annual payment of USD 1.5 M through 2013
Note payable acquired upon the consolidation of a partially owned subsidiary	.70	4.1%	LIBOR for one year + 3%	December 2012

B. Financial covenants

1. In connection with the senior debt to a bank, the details of which appear in sub-par. A above, several covenants were determined, including the following financial criteria:
2. Republic's consolidated equity according to US GAAP shall be more than USD 220 million.
3. The minimum statutory equity of Republic Underwriters Insurance Company (RUIC) (Republic's leading subsidiary) shall be more than USD 200 million.
4. The ratio of net premiums to required statutory equity shall not exceed 2.25:1.
5. RUIC's combined ratio for the last four quarters shall be no more than 110% (provision has been made to exclude USD 30 million of weather related losses for compliance purposes).
6. The loss rate from losses that are not weather related shall not exceed 65%.
7. The fixed charges coverage ratio shall be more than 1.25 : 1.

In addition to the foregoing, provisions were prescribed restricting the creation of certain classes of debt or liens, restrictions on the issue of shares and the merging of certain assets, distribution of dividends, business changes, etc.

With reference to a debt of USD 30 million to a bank and in light of the severe weather events and their implications for its profitability and equity at December 31, 2011, Republic was not in compliance with some of its financial covenants. In March 2012, the bank granted Republic a blanket waiver for covenant issues existing at December 31, 2011. Additionally, the bank amended the credit agreement and extended the period for compliance with certain financial covenants starting in 2012, without fees or additional cost. No changes were made to the payment schedule (principal and interest).

C. Credit facilities

Republic also has a \$20 million revolving note facility a bank. \There facility is not currently being utilized, and it expires May 2012

Republic does not generally accept credit facilities, and finances its operations through equity and bonds.

D. Credit rating

The A.M. Best financial strength and credit rating company gave Republic an A- (Excellent) rating in 2003, and in February 2012 it reaffirmed the rating. This is the fourth level on A.M. Best's scale of 15 rating categories. However, A.M. Best changed the outlook from "stable" to "negative" as the result of underwriting losses from 2007 through 2011. Among other things, the rating is for the use of insurance agencies and reinsurance companies engaged with Republic. The rating is reviewed every year, unless there has been a transfer of control or a significant insurance event.

E. Raising additional sources of finance

Republic is of the opinion that it is capable of meeting the cash flow requirements for its ordinary business in the foreseeable future. Raising additional sources of finance may be necessary should Republic decide to perform acquisitions in the future.

1.13.13 Taxation

For details concerning taxation, see Note 42 to the Company's financial statements.

1.13.14 Restrictions on and oversight of Republic's activity

See Section 1.13.1.(b) above.

1.13.15 Substantial agreements

The Republic Group has agreements with various entities, including agents, insurance agencies, MGAs, other insurers, reinsurers, credit providers and suppliers. Republic has no significant agreement that is not part of its normal course of business.

1.13.16 Legal proceedings

Several applications for class actions in connection with Hurricane Katrina were filed against Republic and other companies. Most of the claims have been settled. In 2011, previous applications for class actions filed against Republic and other companies unrelated to Republic in connection damage to property resulting from poor construction standards and allegations of fee overcharges were dismissed. Republic is of the opinion that the remaining claims do not contain exposure on a significant scale and that Republic is part to the action with a large number of other insurance companies. For details concerning legal proceedings, see Note 32 to the Company's financial statements.

1.13.17 Business strategy and objectives

- A. Focusing on short-tail insurance branches: Republic concentrates on short-tail insurance products²³⁴ (such property and auto insurance), in contrast with long-tail insurance products (such as product liability). This is due to the fact that Republic considers that it is easier to cost these products and their subsequent liabilities, thus reducing fluctuations in performance.
- B. Focus on markets that are less competitive: Republic provides agents and program managers with access to products and markets that large insurance companies usually avoid. As part of this strategy, Republic has begun to issue policies for low-value homes and has embarked on ranching business insurance.
- C. Focus on those areas in which Republic has proven capability: Republic prefers to exploit the experience and knowledge it has acquired over many years to focus on worthwhile products, areas, and marketing channels, rather than enter unfamiliar markets. Republic operates, inter alia, to develop ties with new agents and MGAs as a way of expanding its business in preferred markets. Republic has more than a hundred years of experience in Texas and more than 40 years experience in Louisiana, Oklahoma, and New Mexico, and it tries to utilize its competitive advantage stemming from its seniority and reputation in these areas for entering markets in other areas with similar characteristics.
- D. Correct pricing of insurance products taking into account the cyclical nature of the insurance market: Republic tries to correctly cost its business with the intention of generating underwriting profits, by applying a high level of selectivity for the risks it undertakes, and it uses the risk-adjusted return approach to allocate capital. Republic allocates capital and other resources to its product lines in response to varying market conditions. Republic intends to expand the range of products it offers in market segments that have low insurance capacity and the potential for profit is high, and to reduce the number of products it offers in those market segments where competition makes it impossible to achieve desired profit and underwriting levels. In view of the above, the market segments in which Republic operates may change from time to time.

1.13.18 Risk factors

A. Exposure to catastrophes and weather-related losses

As an insurance company, and particularly taking into account the geographical in which it operates, Republic Group is exposed to risk resulting from natural or man-made disasters, such as hurricanes, hail storms, tornados, and fires. In 2011, losses from tornadoes, hail and wind from spring storms were the highest in Republic's history as the U.S. experienced some of the most severe spring weather in decades. Other severe periods include the exceptional hail storm in El Paso, Texas in September 2009, and Hurricanes Ike and Gustav in September 2008, as well as Hurricanes Katrina and Rita that occurred in August and September 2005. Despite the fact that in 2010 weather-related damage was the lowest for the last three years, in 2008 damage from wind, hail and tornadoes was the highest in Republic's area of activity for decades. There was a slight improvement in weather-related damage in 2009, so that these years are indicative of the risk inherent in the exposure to catastrophes and weather-related damage. It is difficult to predict the occurrence of such events with statistical accuracy, or to estimate the scope of the loss that may be caused. Republic's losses resulting from these disasters depend on various factors, including the exposure of the policyholders in the affected area, the volume of reinsurance and the increase in prices, unexpected changes in the insurance cover resulting from legal or regulatory proceedings as a result of a catastrophe, etc.

²³⁴ Republic concentrates on short-tail insurance products (such property and auto insurance), in contrast with long-tail insurance products (such as product liability). This is due to the fact that Republic considers that it is easier to cost these products and their subsequent liabilities, thus reducing fluctuations in performance.

B. Statutory surplus/underwriting leverage issues/debt covenant compliance

Statutory surplus of Republic's lead insurance subsidiary could erode due to continued underwriting losses, investment losses or non-admission of deferred tax assets. Without an infusion of capital, the erosion of surplus would lead to concerns on the part of rating agencies, regulators and Republic's banks, and could cause significant and rapid reductions in premiums so as to retain the required underwriting leverage. Compliance with debt covenants would be difficult in such situations.

C. Incorrect pricing of premiums

The Republic Group's performance depends, inter alia, on its ability to correctly price the premiums for a broad range of risks. Underpricing on the part of Republic may affect profitability, while overpricing may adversely affect its competitive ability and the volume of its sales, in turn affecting profitability.

D. Incorrect assessment of liabilities in respect of losses and loss adjustment expenses (LAE)

Republic estimates its liabilities in an effort to cover all the losses and loss adjustment expenses caused in respect of its insurance policies. Republic Group must therefore prepare estimates for claims actually filed and for liabilities from IBNR claims. Estimating the liabilities naturally entails an element of uncertainty, and the actual losses and LAE in respect of these losses that Republic is required to pay may differ substantially from its estimates.

E. Collapse of reinsurers, change in the capacity and tariffs of reinsurers

Republic Group uses reinsurance to hedge against insurance risks or as a way of sharing the risks with the reinsurers. The collapse of reinsurers, a change in reinsurance capacity and in reinsurers' prices may affect the company's ability to pay policyholders or limit its ability to draw up insurance. In the insurance services branch, Republic Group issues policies in the name of insurance companies in return for brokerage fees. The risk in this branch is born by these insurance companies, however should they fail to meet their commitments towards Republic Group, Republic may be forced to bear payment of the loss without receiving indemnity.

After the heavy losses incurred in the wake of the hurricanes in 2008, and together with the general economic crisis in all markets, reinsurance tariffs for 2009 rose substantially and remained high for policy renewals in 2010, 2011 and 2012. The reinsurers must rely almost exclusively on higher tariffs in order to recoup the money they lost following the damage caused by the storms and investments. Traditional sources of capital that usually flow into the reinsurance market after major losses are currently not forthcoming due to changes in the global markets. Due to the higher cost of the reinsurance and the loss of capital, global capacity also declined. Accordingly, Republic's availability will lead to higher costs and less coverage on account of the higher attachment points (the maximum amounts of retention).

F. Dependence on independent insurance agents who market Republic Group's products

Republic Group's business depends on the success of independent insurance agents in marketing its insurance products. These insurance agents also market the products of competing companies, and at some stage may give them precedence in their marketing efforts, adversely affecting the volume of Republic's sales. In addition, customers may choose to purchase insurance through other marketing channels such as the internet, and not through the insurance agents who market Republic's products.

G. Dependence on MGAs

Republic Group is assisted by MGAs operating under its instructions. The MGAs are responsible for issuing insurance policies in Republic's name and for handling claims in respect of these policies. Republic Group is exposed to the risk that the MGAs will not act appropriately with the authority that was delegated to them by it, or that generally accepted contractual conditions were not within their reach. In addition, MGAs may move over to competing companies or curtail their activity for Republic for a variety of reasons such as a change in tariffs or a change in the ownership of the agencies. One unrelated MGA was responsible for USD 182.1 million and USD 76.4 million of gross premiums in 2010 and 2011, respectively. This MGA was acquired by a third party in the fourth quarter of 2010. At this time, the company has decided to terminate its relationship with the agency during 2011, and concurrently has signed contracts with new agencies that should offset any loss in future premiums.

H. Lowering of rating

Financial strength ratings are important for the competitive status of insurance companies. Republic's insurance companies have an A- (Excellent) rating from A.M. Best, and this rating is periodically tested by the rating company. Republic's rating was affirmed in February 2012, although the outlook was changed from "stable" to "negative" as the result of underwriting losses from 2007 through 2011. Continued underwriting losses, higher underwriting leverage, investment losses, non-admission of deferred tax assets under statutory accounting requirements and erosion of surplus would negatively influence Republic's rating. A lowering of the rating would adversely affect Republic's customer base and the willingness of independent insurance agents and MGAs to engage with it.

I. Introduction of more rigorous policy conditions by the courts or regulators

The Republic Group's insurance policies contain various exclusions aimed at limiting the scope of the risk and the potential liability for Republic. Rulings by the courts or the regulators to the effect that these exclusions are no longer valid may increase Republic Group's liability and affect its financial performance.

J. The insurance market in Texas

Given that most of the Republic Group's revenues from insurance premiums originate in Texas, Republic Group is exposed to events that may adversely affect the market in this state, such as economic recession, political instability, unemployment, more stringent regulations, stronger competition, war and terror-related events. It is worth noting that the economic crisis may, inter alia, lead to a decline in the volume of insurance drawn up, lower insurance tariffs, an increase in the number of insurance events on which policyholders file a claim.

K. Competition

The insurance industry is highly competitive. Republic Group competes with large insurance companies, including national companies that have much larger financial, marketing and management resources than Republic Group. The Group also competes with entities that insure themselves, particularly in the commercial insurance market. Another competitive risk to which Republic Group is exposed is the marketing of insurance products through the internet.

L. Poor performance by Republic Group's investments

Republic Group's investments are subject to a variety of investment risks such as economic conditions in the market, market volatility, fluctuating interest rates, liquidity risks, credit and insolvency. Republic Group is specifically exposed to losses that may be caused should an untimely need arise to exercise securities that it holds to cover insurance liabilities. The severe crisis in the capital markets increased the risk inherent in the Republic Group's investments.

M. Regulation

Republic Group is subject to comprehensive regulation and oversight in the states in which the Group's companies operate. The regulation addresses a variety of issues such as restrictions on the company's investments, accounting and reporting standards, and more. Regulatory changes or a failure by the companies that belong to the Republic Group to comply with permits and conditions, may adversely affect its business. In addition to existing regulation, from time to time legislative changes are put forward that may adversely affect the insurance industry. Among other things, a bill for federal insurance legislation is currently being discussed in addition to the existing state laws, as well as a bill to subordinate some of the state laws to laws that will be adopted by the National Association of Insurance Commissioners (NAIC). This process may create a situation in which the regulations are interpreted differently in each state, making it difficult for companies operating in several states, such as Republic, to implement the regulations.

N. Information systems

The Republic Group's activity is contingent upon the proper function of its information and communications systems. The company relies on these systems to recruit new customers, for customer service, the filing of claims, and billing. Should Republic Group's information systems malfunction or if it cannot unsuccessfully upgrade them from time to time, the Group's operations will be affected.

O. Impairment of Deferred Tax Assets

The Republic Group recorded a net deferred tax asset of \$24MM as of December 31, 2011. Republic was in a three-year cumulative net loss position at the end of 2011; accordingly, Republic evaluated the need for a valuation allowance related to recoverability of its deferred tax asset. Based upon all available evidence, the company decided no valuation allowance was necessary at year-end 2011. However, if Republic were to experience additional losses (from severe weather, from adverse reserve development, from investments or other sources) then the company may be required to record a valuation allowance against its deferred tax asset. Such an allowance would not only reduce equity, but would also impair the company's ability to write additional premiums in the near term.

P. Further impairment of goodwill

The Republic Group has goodwill and intangible assets that are subject to annual impairment tests. Significant impairment charges were recognized in 2011 and 2008. Additional impairment is possible based on market factors or Republic's performance. Depending on underwriting results, weather volatility, premium volume, retention of programs, valuation of deferred tax assets, discount rates, control premiums, etc., Republic could experience additional impairment charges in 2012 and beyond.

	Extent to which the risk factor influences Republic Group's business		
	Strong influence	Medium influence	Small influence
Macro risks	Negative events in the insurance market in Texas, including economic recession or political instability	Poor performance by Republic's investments, in part due to exchange rates, interest rates, and inflation	Unemployment Wars and terror
Sectoral risks	Catastrophes and weather-related losses Collapse of reinsurers, change in the capacity and tariffs of reinsurers	Regulation, including changes in regulatory capital requirements, accounting standards, or tax laws Competition	
Risks specific to Republic	Lowering of rating Compliance with debt covenants Maintenance of required underwriting leverage	Actuarial issues including Incorrect assessment of liabilities in respect of losses and LAE Incorrect costing of premiums Dependence on insurance agents Dependence on MGAs	Information systems

The extent to which the aforementioned risk factors affect Republic Group's activity is an estimate only, and in practice the degree of influence may be different.

1.13.19 Event or matter outside the normal course of the corporation's business

In 2009-2011 there were extraordinary events pertaining to exceptional weather-related losses and the economic crisis that affected the US economy and Republic's activity.

In 2011, the U.S. experienced extreme outbreaks of violent spring weather with numerous tornado, wind and hail events. Property damage and loss of life was the highest in decades. The average number of tornadoes in the U.S. in any given year is roughly 1,200, whereas in the second quarter of 2011 alone it is estimated that there were more than 1,400. The tornado outbreaks of April 22-28 and May 20-27 2011 were two of the strongest ever recorded. Taken as a single event, the spring 2011 tornado and severe storm season would be the fourth most costly event in U.S. insurance history, with estimated losses exceeding USD 14 billion and more than 500 lives lost. In addition to the violent spring storms, a record drought in Texas caused numerous wildfires, resulting in significant property damage throughout the state.

Although the 2011 hurricane season was active, only one storm impacted the U.S. mainland, although not in Republic's operating area. Altogether, Republic incurred weather-related losses

totalling USD 92.1 million before reinsurance and USD 64.5 million after reinsurance. This compares to USD 49.5 million and USD 23.2 million before and after reinsurance, respectively, for 2010. In general, 2010 weather related losses were on the low side of historical patterns.

2009 was a challenging year due to the prolonged economic slowdown that resulted in volatile (although somewhat improved) financial markets, rising unemployment, large-scale personal and business failures and bankruptcies, low premium prices, and the large scale property losses and doubtful liability. In addition, weather-related losses continued to be higher than average in the past. Although no hurricanes hit North America in 2009, an exceptional, unseasonal hail storm, hit a generally arid area of western Texas resulting in a loss of USD 20 million in September 2009.

In response to the financial markets, Republic chose to sell a large part of its securities for investment in 2009 and recorded investment profit. As a result, an increase in capital was created for its insurance company subsidiaries. Nevertheless, there will be fewer future opportunities for investment income until stability returns to the markets and interest rates being to rise again.

In 2011 and 2010, the US economy remained sluggish, reflected in high unemployment, more receivership, uncertainty regarding fiscal policy and regulation, and continuing volatility in the financial markets. In addition, the insurance market was weak with capital surpluses that requires a corresponding premium – pushing down rates of insurance premiums, intensifying competition, and forcing the insurers to carry losses stemming from competition over market share at the expense of underwriting profits. Despite its volatility, the capital market offered an opportunity to realize capital gains, generating revenues and increasing the amounts required according to regulation.

1.13.20 Forecast for developments in the coming year

In view of the company's major losses that are not weather related, additional premium rate increases were implemented in 2011 and will continue in 2012 in almost all lines of business. Unprofitable products or programs have been or will be terminated as appropriate. Republic's product mix and geographic concentrations are under review as part of an intensive effort to return to underwriting profitability.

Republic is also applying new underwriting tools and procedures to increase its discretion in underwriting with respect to defining the insured risks. Additional steps are being taken to further reduce property exposure to hurricanes in some coastal areas, and to reduce the concentration of risk in El Paso, Texas, where an increase in losses was recorded due to hail storms in 2007-2009, despite the fact that in the past losses resulting from hail were infrequent.

Owing to the decline in capital and in the statutory surplus, Republic is closely monitoring premium volume, policy retentions and underwriting results in order to allocate its capital as efficiently as possible. In order to maintain the net premium to statutory capital ratio (underwriting leverage) and attain the desirable leverage targets, premium volume in some businesses will have to be lowered.

The large underwriting losses from weather and non-weather related claims in 2011 have delayed expansion plans until underwriting profitability has been restored.

1.14 Automotive segment

1.14.1 General

The Group's automotive segment is based on the activities of Delek Automotive Systems Ltd. and its subsidiary companies and corporations (Delek Automotive Systems Ltd., its subsidiaries and corporations are referred to collectively as "**Delek Automotive**").

Until October 2010 the Company was the controlling shareholder in Delek Automotive with a holding (through Delek Investments) of approximately 55% of its shares. On October 20, 2010, Delek Investments sold 20,000,000 ordinary shares of NIS 1.0 par value each, which on the day of the transaction represented approximately 22% of the shares of Delek Automotive, to Mr. Gil Agmon, CEO of Delek Automotive, in consideration of NIS 1 billion. As a result of this transaction, control of Delek Automotive passed from Delek Investments to Mr. Gil Agmon who at the report publication date holds 37.45% of the issued paid-up share capital of Delek Automotive. Shortly before the reporting date, the Company held 32.13% of the shares in Delek Automotive.

In the sale agreement Gil Agmon undertook (unilaterally) toward Delek Investments that as long as he is the controlling shareholder in Delek Automotive and as long as Delek Investments holds more than 20% of the share capital of Delek Automotive, he will act to appoint two directors recommended by Delek Investments, and as long as Delek Investments holds more than 15% (but not more than 20%) of the share capital of Delek Automotive, he will act to appoint one director

recommended by Delek Investments. Pursuant to the Articles of Incorporation of Delek Automotive, up to ten directors can be appointed at Delek Automotive (including external directors). On the basis of an undertaking between the parties the Articles of Incorporation of Delek Automotive were amended so that a resolution on the following matters would be passed by a majority of 75% of the shareholders attending a general meeting of Delek Automotive: allotment of shares or securities convertible into shares; sale, transfer or disposal of most of the assets of Delek Automotive or a material change therein; voluntary liquidation of Delek Automotive. For details on the effect of the transaction on the Company's results and on the way in which its holding in Delek Automotive is presented in its financial statements, see Note 14 to the financial statements.

Delek Automotive has been operating in Israel since 1994 as importer, distributor and seller of Mazda vehicles and vehicle parts. In 1999, it started to import, distribute and sell Ford vehicles and vehicle parts in Israel. In addition, since December 2011, Delek Automotive has also been importing, distributing and selling BMW vehicles²³⁵²³⁶, accessories and spare parts in Israel through its wholly owned subsidiary, Kamor Motors Ltd. Delek Automotive also operates service centers (authorized garages) where it provides maintenance and repair services to its customers as well as support and guidance to its network of authorized garages ("**the Service Centers**") and Mazda, Ford, BMW and Mini dealers throughout the country (for details, see sections 1.14.2(A) and 1.14.2(B)). Delek Automotive also has a franchise to market, distribute and sell Lincoln vehicles and vehicle parts in Israel. At the reporting date, Delek Automotive does not sell these vehicles and vehicle parts.

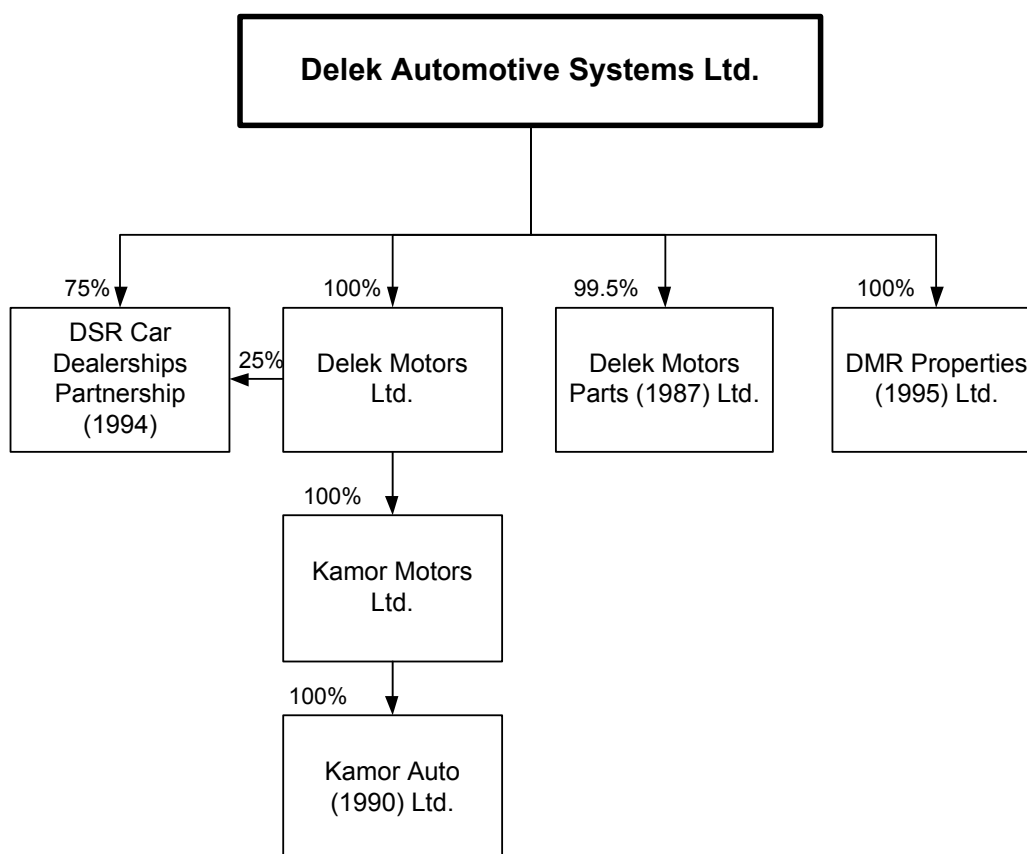
Under agreements from July 2011 (as amended in November 2011), on December 13, 2011, Delek Automotive acquired 84% of shares in Kamor Motors Ltd. ("**Kamor Motors**" and "**the transaction**") through Delek Motors Ltd., a wholly owned subsidiary, after it had previously acquired 16% of the shares in Kamor Motors which had been held by the public, in consideration of NIS 235,000,000. As part of the transaction, the holdings of Kamor Motors in subsidiaries in which its tire operation had been concentrated, its automobile operation in Bulgaria, as well as the vehicle marketing franchise of Chery Automobile Co. Ltd., were sold to third parties. After completion of the above transaction and tender offer, Delek Automotive holds 100% of the shares in Kamor Motors. At the report publication date, Kamor Motors imports, distributes and sells BMW and Mini vehicles (including motorcycles), accessories and spare parts through Kamor Auto (1990) Ltd. ("**Kamor Auto**"), a wholly owned subsidiary. Kamor Auto also provides garage services for BMW vehicles. For further details regarding the transaction, see section 1.14.17.

Delek Automotive is a public company whose securities are listed on the Tel-Aviv Stock Exchange Ltd. ("TASE").

²³⁵ In this report, the term "vehicles" also includes motorcycles.

²³⁶ In this report, BMW vehicles include Mini cars and Husqvarna motorcycles and their parts.

The following chart describes the structure of the main holdings of Delek Automotive:



1.14.2 General information about the segment of operations

A. Structure of segment and changes therein

The Israeli automotive market differs from most other automotive markets in the world because of its geographical isolation and high import vehicle duties. The motorization level in Israel is low compared to various Western countries, owing to a relatively low standard of living, relatively high vehicle prices caused by high import duties, inferior road infrastructure and high population density.

The automotive market comprises a number of vehicle importers that import vehicles manufactured in different parts of the world. Most importers import only two or three brands. The development of the automotive market in Israel is characterized by volatility stemming, *inter alia*, from changes in the macroeconomic environment.

Among the characteristics and trends affecting the operations of Delek Automotive and its competitors are these: (a) high dependence on suppliers - the business success of the vehicle importers depends on the financial and business positioning of the manufacturers and on new product strategies, global brand management, model and pricing policy and marketing support. (b) changes in consumer preference - preferences for certain models are based on technological advantages, environmental protection, price and marketability in the secondary market. (c) taxes - in Israel, purchase taxes and import duties on private cars – among the highest in the world – can amount to almost 100% of the price of the vehicle. These taxes affect the power to purchase new vehicles and consequently could affect Delek Automotive's sales. (d) fuel prices - these prices can affect consumer preferences, resulting in a long-term impact on the type of vehicles sold, based on fuel type (diesel, natural gas or gasoline).

B. Legal, regulatory, standardization and special constraints in the segment

The vehicle market is influenced by legislative and regulatory requirements which are a significant factor that could affect the supply of and demand for vehicles in Israel.

1. Zelekha Committee

On September 24, 2011, the Minister of Communications appointed a public committee headed by Prof Yaron Zelekha to examine ways of reducing the centralization in the automotive industry and formulate recommendations for the removal of barriers to increase competition and lower industry prices ("**the Zelekha Committee**"). The Zelekha Committee was tasked with proposing reform options which would improve competition in the industry. On February 12, 2012, the Zelekha Committee submitted its recommendations which focused on five key topics²³⁷:

- A) In order to increase competition, it was recommended that a direct vehicle importer holding a market share of 8% or more for longer than two consecutive years or two non-consecutive years in a four-year period be permitted to have an agreement to import vehicles into Israel with only one vehicle manufacturer, but if this manufacturer manufactures a number of models through wholly owned (100%) subsidiaries, the importer may import all its models with no limitations, irrespective of its market share. This recommendation would be granted a transitional period of one year. If and to the extent that this part of the report is adopted in its entirety, this would have a materially adverse impact on Delek Automotive. It was also recommended that a direct importer be prohibited from holding shares in a leasing and/or rental company and owning more than one service and training garage for the vehicles it imports. It was also recommended that the import of vehicles manufactured in accordance with American standards be permitted under certain conditions. Delek Automotive believes that adoption of this part of the Committee's report would not have an adverse impact on its businesses.
- B) With regard to the marketing and sale of vehicles and connection with the importer, it was recommended, inter alia, that the difference between the price of the vehicle sold by the importer in the most expensive transaction and its price in the cheapest transaction be limited (mainly between the price to the private consumer and the price paid by leasing companies and car fleets) to 5% of the price of the cheapest vehicle, including the value of various benefits granted to the customer during or after the transaction. It was also recommended to make the official importer responsible for various matters even if it is not the direct importer of the vehicles, and to cancel the obligation to repair the vehicle in the importer's garage as a condition of maintaining the warranty, subject to another garage's compliance with the requirements of the Ministry of Transport. Delek Automotive is unable to estimate the effect of this section of the report, if and to the extent that it is adopted in its entirety.
- C) In respect of the regulation of garages and parts, it was recommended, inter alia, that parts should be sold at a uniform price (except for a limited quantity discount), so that parts may also be sold to garages which are not authorized garages of the importer and that garages should be obligated to make repairs under warranty even if the part is not purchased from them. It was also recommended to obligate the importer to train and certify each garage authorized by the Ministry of Transport at a uniform supervised price, to prohibit an importer from supervising, controlling and obtaining information about the repairs and service carried out by garages, to prohibit them from advertising a recommended price for the consumer and to remove from the importer the power to cancel the "authorized" status of garages and to transfer that power to the Ministry of Transport. Delek Automotive believes that adoption of this part of the committee's report will not affect it adversely.
- D) With regard to taxation, it was recommended, inter alia, that the percentages of the value benefit for an employee receiving a company car from his employer be based on the actual vehicle purchase price (where the car is not new) and not on the list price of the car when it was new, and to update the purchase tax discount as part of green taxation so that it would apply not only to electric cars but also to hybrids. Delek Automotive believes that adoption of this part of the committee's report would not have a material effect on its operations.

²³⁷ The Committee also made recommendations relating to electric cars and motor vehicle appraisal and taxation. Its recommendations made no reference to trucks and motorcycles. For the complete recommendations, see <http://media.mot.gov.il/DOVER/zilha-doch.pdf>

- E) With regard to personal import and parallel import, the Committee recommended that a vehicle importer, whether a regular importer or whether a person assisting another with personal import, be required to obtain a valid license issued by the Ministry of Transport and that the law regulate the status of a “personal import adviser” who would be permitted to import up to 20 cars per year as inventory without being registered as an additional owner of the car in Israel. It was also recommended to relax the demands made by the Ministry of Transport on importers (regular or parallel) in the matter of guarantees and equity in order to reduce the entry barriers into the industry and also to permit the parallel import of a car as a “new car” (with no previous owner) if it was registered in the dealer’s name as a new car in the country of origin. It was also recommended that the main importer be made responsible for the servicing and parts of cars imported by parallel or personal import. Delek Automotive believes that adoption of this section of the committee’s report will not affect it because it already services the cars of personal import customers.

On February 22, 2012, the Minister of Transport decided to set up an inter-ministry team for implementation of the recommendations of the Zelekha Committee. The team will comprise senior representatives from the Ministry of Transport, the Budget Division of the Ministry of Finance, the Antitrust Authority and the Tax Authority. According to articles in the press, alongside the work of this committee, the Ministry of Transport has embarked on implementation of part of the Zelekha Committee recommendations by means of legislative amendments and directives to industry entities.

2. Parallel import

In 1999, the government introduced a reform in the Israeli automotive market. The Ministries of Finance and Transportation set up a committee to remove barriers and eliminate centralization in the automotive market and to open it up to competition. The committee recommended a series of steps which were implemented in legislation over the years. Their flagship reform was the Control of Commodities and Services Order (Import of Vehicles and Provision of Vehicle Services) (Amendment), 2010 which was published in the Official Gazette on March 7, 2010 and was designed to remove the principal barriers to the parallel import of vehicles (respectively, the “**Amendment to the Order**” and “**Parallel Import**”), and on April 6, 2010 most of the provisions of the Amendment to the order took effect. A Parallel Importer, as defined in the provisions of the Order, shall not import more than three vehicle models subject to the power of the Director of the Vehicle and Maintenance Services Department in the Ministry of Transport or a person authorized by the Minister of Transport for that purpose to change the number of vehicles in compliance with the terms of the Order. Delek Automotive believes that existing market conditions mean that it is not economically feasible to engage in parallel import because no parallel importer has been registered since the market was opened to parallel import. Delek Automotive’s assessment of the effect of parallel import on its operations is forward-looking information as defined in the Securities Law, and it is based, inter alia, on the fact that the pre-tax consumer prices of vehicles in Israel are among the lowest in the world. This assessment is not certain and might not be realized, inter alia, because of changes in the tax rates imposed on car imports and regulatory changes relating to parallel import. The recommendations of the Zelekha Committee were published in February 2012. For details of the recommendations pertaining to the parallel and personal import of vehicles and their effect on the businesses of Delek Automotive, see section 1.14.2(B)(1).

3. Licensing groups

Vehicles sold in Israel are divided into licensing groups based on their price as determined by the tax authority at the beginning of every calendar year. An annual licensing fee is paid on the basis of these licensing groups which until January 1, 2010 were also used to determine the use value of a vehicle purchased until this date. The use value of the car as defined in the Income Tax Order [New Version] is one of the benefits or allowances granted by employers to their employees (company cars), on which employees pay taxes calculated in accordance with the Income Tax Regulations (Value of Use of a Vehicle), 1987. The change in the price group affected prices of new vehicles because of the desire of vehicle importers to belong to a particular price group. In light of the fact that the method of calculating the use value of a company car was changed from

the price group method to the linear method (whereby the use value will be a rate determined by the price of the vehicle to the consumer) since January 1, 2010, a change in the price group no longer affects prices of new vehicles.

4. Vehicle use value

On December 31, 2007, the Income Tax (Value of Use of a Vehicle) (Amendment) Regulations, 2007 came into force. Under these regulations, the use value of a company car would be increased gradually in accordance with four brackets at the start of each calendar year, from January 1, 2008 to January 1, 2011. When these regulations were approved, the tax rates for middle level income earners were reduced, with the aim of partially offsetting the additional tax paid by the users of company cars. Delek Automotive believes that these regulations could have a long-term impact on the distribution of vehicle sales in Israel, and on the distribution of Delek Automotive sales between institutional customers (including leasing companies) and private customers.

5. Green taxation reform

On November 25, 2009, the Knesset Finance Committee approved the green taxation reform which was actually implemented on August 1, 2009 as part of a temporary order including the following changes to purchase tax and above-mentioned use value: (1) a "green index" was determined which grades vehicles in accordance with their pollution level and the purchase tax rate is set on the basis of this grade. Instead of a vehicle purchase tax of 72% - 75% (private or commercial, respectively), it was decided to levy purchase tax at the rate of 83% along with a tax reduction to be in the form of a shekel incentive whose amount derives from the vehicle's pollution level. This was in addition to cancellation of the tax incentive granted to vehicles equipped with electronic stabilization control systems. The combination of a higher tax rate and shekel incentive does not necessarily lead to an increase in the effective tax and in some cases it even reduces the tax burden. It also determined a reduced purchase tax rate of 30% for hybrid vehicles and 10% for zero-pollution vehicles (such as electric vehicles) for a limited number of years, subject to the pollution levels of these vehicles. (2) It was decided to change the method for calculating the use value of a company car from the price group method to the linear method whereby the use value is a fixed rate of the consumer price. This method is applied only to new vehicles registered after January 1, 2010, while the price group method will continue to be applied to existing vehicles and those registered up to January 1, 2010. The monthly use rates for 2010 were 2.04% for vehicles priced up to NIS 130,000 and 2.48% for vehicles priced over NIS 130,000. The use value from 2011 is 2.48% of the vehicle price. Moreover, since the 2010 tax year there has been a reduction in the monthly use value of hybrid vehicles irrespective of their purchase date and in 2011 this amounted to NIS 530 per month. In August 2010 the Tax Authority published its intention to update its pollution grading classification in a manner which would impose stricter conditions for the relatively lower pollution grades as of 2012. Delek Automotive believes that changes in recording income for the use of such vehicles could have a long-term effect on the ratio between sales to institutional customers (leasing and rental companies) and sales to private customers, as well as on all vehicle sales in Israel. Delek Automotive's estimate of the effect of these taxation changes on its operations is forward-looking information as defined in the Securities Law and it is based on its past experience. This forward-looking information might not be realized because this estimate is not certain and it could change, *inter alia*, because of regulatory changes, changes in market conditions, etc.

6. Prevention of restrictive arrangements

Pursuant to an order agreed by virtue of Article 50B of the Antitrust Law, 1998, which took effect on April 24, 2003, restrictions and prohibitions designed to prevent restrictive arrangements and to open the parts market to competition were imposed on vehicle importers. For further details, see section 1.14.16(D).

7. Import of generic spare parts

On October 15, 2010 a new procedure issued by the Ministry of Transport took effect. It regulates the import of generic spare parts for vehicles and it permits the import into Israel of any spare part sold in Europe or the United States.

On May 29, 2011 the Ministry of Transport published a "procedure for licensing personal import spare parts for personal use" designed to determine the requirements and

conditions for the licensing and release from customs of spare parts for personal import vehicles.

8. Prohibition on Repairing Vehicles in an Unauthorized Garage Bill, 2010

To the best of Delek Automotive's knowledge, the Knesset Economic Affairs Committee is reviewing a private bill placed on the Knesset table on June 28, 2010 which would prohibit vehicle repairs in garages not authorized by the Ministry of Transport. The bill was intended to eliminate repairs in unauthorized garages and increase the safety of vehicles on the roads for fear of repairs using unsafe and stolen parts. Under the bill any person repairing his car in an unauthorized garage or operating such a garage will be charged with criminal offences and sentenced to a fine or 18 months' imprisonment.

9. Standardization

Every year, the Standards Department of the Ministry of Transport's Motor Vehicle Division defines the changes in the mandatory requirements for various vehicle types for the next model year, citing the amendments to European standards and the specific requirements for Israel. Mandatory requirements in Israel are based on EEC directives and US federal standards. The standards focus on air pollution and safety of vehicles, passengers and pedestrians. Vehicles that are not in compliance with these standards are not permitted to be imported into Israel.

In August 2011 the Ministry of Transport published a procedure permitting the import from the USA of vehicles with headlamps complying with American standards provided that the headlights comply with its requirements. This procedure was intended to increase competition in the sector by removing barriers. It also cancels the need to import vehicles so that the headlamps can be tested in Israeli laboratories and it allows importers to send only the headlights for inspection in an authorized overseas laboratory before they are imported.

In December 2011 the Ministry of Transport permitted for the first time the import into Israel of vehicles complying with American standards and manufactured in the NAFTA countries (USA, Canada and Mexico) provided that the parent plant is in Japan, in order to increase competition in the sector and cause vehicle prices to fall as a result of the differentials between the euro and USD exchange rates. So far, it is only the import of vehicles complying with American standards which has been permitted.

In accordance with the recommendation of the Zelekha Committee, permission will be granted for the import of vehicles manufactured according to American standards, whether or not they have been manufactured in the USA, provided that the model is marketed in the USA and has been approved by a qualified American standards laboratory pursuant to the relevant provisions of European law. This measure is intended to expand the number of countries from which vehicles are imported without harming safety standards. For details of the recommendations of the Zelekha Committee, see section 1.14.2(B)(1).

10. Consumer Protection Regulations (Cancellation of Transaction), 2010 ("the Transaction Cancellation Regulations")

On December 14, 2010 the Transaction Cancellation Regulations entered into force. They provide, *inter alia*, that a consumer may cancel an agreement to purchase goods provided that he returns the goods to the dealer undamaged and unused. The consumer may cancel the agreement within 14 days of the transaction date provided that the item has not yet been registered in the consumer's name pursuant to the Traffic Ordinance [New Version].

The Transaction Cancellation Regulations are not expected to have an effect on Delek Automotive's business because it has for years permitted cancellation of transactions, as long as the vehicle has not been registered in the consumer's name, and because a vehicle is not delivered to the consumer before it has been registered in his name, pursuant to the Traffic Ordinance.

11. Additional restrictions

For further details of the environmental legal restrictions and arrangements applicable to the importation of vehicles and spare parts, see section 1.14.12.

C. Changes in the volume of segment operation and its profitability

In recent years, market conditions have improved for Israeli consumers owing to favorable currency exchange rates and tax reductions. After a period in which vehicle deliveries increased between 2005 and 2008, there was a slowdown which started in the fourth quarter of 2008 and continued until the first half of 2009. This caused a sharp decrease of 11% in total vehicle deliveries compared with 2008. In 2010, alongside the continuing recovery in the global economy and in the Israeli economy in particular, there was a continuation of the growth trend in the vehicle import market which began toward the end of 2009 and a significant increase in vehicle deliveries was recorded. Total vehicle deliveries in 2010 amounted to 221,010, an increase of approximately 25% compared with total deliveries in 2009. The growth trend in the vehicle market also continued in 2011 although this was slightly moderated by slower growth in the Israeli market, and vehicle deliveries totaled 230,758, an increase of 4% compared with total deliveries in 2010²³⁸.

Changes in the volume of activity in the automotive market were accompanied by changes in the mix of activity in this market, the most prominent of which was the increase in sales to institutional customers. These customers do not always service their vehicles at an authorized garage chain and some use non-original vehicle parts. Nevertheless, Delek has agreements for maintenance and supply of vehicle parts with a number of institutional organizations, such as leasing companies and the Ministry of Defense. Delek Automotive estimates that changes in the operational leasing sector, should they take place, will not have a material effect on its sales of vehicle parts.

Delek Automotive believes that the effect of the changes in the operational leasing sector on its sales of vehicle parts is forward-looking information as defined in the Securities Law and this belief is based, *inter alia*, on past experience. It is not certain and it might not be realized, *inter alia*, because of events contrary to the Company's expectations.

D. Technological changes which could have a material impact on the segment²³⁹

The declared policy of the Ministry of Transport is to encourage the use of alternative transport in order to reduce vehicle air pollution and fuel consumption. Recent years have seen the launch of hybrid vehicles combining gasoline engines with electric motors which consume less fuel. In December 2010 the Ministry of Transport approved for the first time the import of hybrid vehicles combining a diesel engine with an electric motor. They emit much less carbon dioxide and their fuel consumption is greatly reduced. Despite the significant tax benefits, prices of hybrid vehicles are higher than those of the vehicles sold by Delek Automotive in the equivalent categories. Consequently, these vehicles do not constitute significant competition for those sold by Delek Automotive. The market share of hybrid vehicles in Israel is similar to that in other Western markets such as Europe and the United States (approximately 2%). Data from the Ministry of Transport indicate that in 2010 10,743 hybrid vehicles took to the roads compared with 4,110 in 2011. Furthermore, there are now entities in the vehicle market as well as others which are engaged in the development of vehicles which will be powered by electricity only. Ministry of Transport data indicate that 49 electric vehicles took to the roads in 2011. Since at present the mileage between charges is low compared with that of gasoline vehicles, Delek Automotive does not expect these vehicles to constitute significant competition for its vehicles in the next few years until substantial technological advances are made.

E. Critical success factors in the segment and changes therein

Several significant factors contribute to the success of vehicle and vehicle parts importers in Israel: (a) new models and their branding among consumers; (b) trading conditions for the importer, and primarily the currency exchange rates applying to imports and the exchange rates of the currencies used by competitors; (c) marketing ability of the importer; (d) reputation and service level of the importer, vehicle parts supplier and garage; (e) good relations with the manufacturer; (f) commercial relations with leasing and rental companies; (g) high resale value of vehicles in the used car market; (h) price, quality and availability of vehicle parts,

²³⁸ This information is to the best of Delek Automotive's knowledge and is quoted from Vehicle Importers Association reports.

²³⁹ This information is to the best of Delek Automotive's knowledge and it is taken from the Public Committee Report on Increasing Competition in the Vehicle Sector, February 2012.

F. Principal entry barriers to the segment

In the opinion of Delek Automotive, the entry barriers to the vehicle import segment in Israel are relatively high for the following reasons: (a) strong ties between the importer and the manufacturer; (b) essential financial strength of the car importer; (c) great importance of the level of service provided by the importer and its past experience with its customers.

However, in the opinion of Delek Automotive, there are no significant entry barriers to the vehicle parts import market. Among the reasons for this are that trading in vehicle parts requires a license from the Ministry of Transport and obtaining such a license does not entail a large investment of resources and effort.

G. Alternative products and changes in the segment

The Ministry of Transport is progressing with its urban transport development plans. In January 2011 a fast lane project was launched at the entrance to Tel Aviv. The project is designed to increase the use of public transport and reduce traffic congestion at the entrance to Tel Aviv and inside the city. An exemption from payment for vehicles carrying a number of passengers encourages carpooling. In August 2011 the light railway project which is designed to solve Jerusalem's severe traffic congestion problems was inaugurated in the city. In addition, the Ministry's plans call for inauguration of the first line of the light railway in a few years and this will change the transport reality in the Tel Aviv metropolis after many years of delays and postponements.

H. Competitive environment and changes therein

Competition in the vehicle parts market is fierce. For details, see section 1.14.6.

1.14.3 Products and services

A. Mazda and Ford vehicles

Delek Automotive imports, distributes and sells a wide range of Mazda and Ford private and commercial vehicles under franchise agreements with the manufacturers. For a description of the franchise agreements, see sections 1.14.14(A) and 1.14.14(B).

Since it started operations through December 31, 2011, Delek Automotive delivered 526,000 vehicles to Israeli customers, of which 394,000 were Mazdas and 132,000 were Fords.

The following tables illustrate the breakdown of vehicle deliveries by Delek Automotive in units for 2011 and 2010, by quarter and by manufacturer:

2011

Manufacturer	Q1	Q2	Q3	Q4	Total
Mazda	7,611	5,644	4,960	3,019	21,234
Ford	2,684	2,388	2,468	4,070	11,610
Total	10,295	8,032	7,428	7,089	32,844

2010

Manufacturer	Q1	Q2	Q3	Q4	Total
Mazda	7,889	8,243	6,705	9,019	31,856
Ford	1,817	2,979	2,994	3,065	10,855
Total	9,706	11,222	9,699	12,084	42,711

Delek Automotive imports, markets and distributes vehicles for different market segments: family sedans (Mazda 3 and Ford Focus), executive cars (Mazda 6 and Ford Mondeo), 4x4s (Ford Explorer and Ford Edge), transport vehicles (Ford Transit), minivans (Mazda 5, Ford S-MAX and Ford Galaxy), commercial vehicles (Ford F-350 and Ford Connect) and mini cars (Mazda 2 and Ford Fiesta).

The market share of Delek Automotive in 2011 and 2010 was 25% and 19% respectively of all vehicle deliveries in Israel²⁴⁰.

²⁴⁰ Based on reports published from time to time by the Automobile Importers Association.

The decline in Delek Automotive's market share in 2011 stems primarily from the damage to its ability to compete caused by the strengthening of the Japanese yen together with the weakening of the import currencies of its competitors. Moreover, the fact that until the fourth quarter of 2011, Delek Automotive was selling the old model of the Ford Focus which had been launched more than six years earlier, while its competitors were benefitting from new models, harmed its ability to compete which in turn harmed its market share.

B. Importation of vehicle parts and provision of garage services

Delek Automotive markets and distributes all types of vehicle parts and accessories for the vehicles it imports.

Delek Automotive also provides maintenance and repair services for its customers, and support and training for its network of dealers and service centers for Mazda and Ford vehicles throughout the country and at its central service center (the central garage) at Nir Zvi (for a description of the real estate asset on which the central garage is located, see section 1.14.7). The price and the method of providing services at the central garage and the authorized garages are based on "manufacturer hour" (the maximum tariff for the work hours required to carry out any job as defined by the manufacturer). The service centers comply with the standards defined by Delek Automotive and set out in their agreements. The service centers are supported and supervised by regional service inspectors who visit these centers a few times a month, inspect compliance with the standards and solve professional problems.

1.14.4 Breakdown of revenues from products and services

- A. The following table shows data for Delek Automotive revenues from products and services in 2011 and 2010 (in NIS millions), as a percentage of the Group's net revenue and as a percentage of the automotive segment's revenue²⁴¹:

	2011			2010		
	NIS millions		% of segment revenue	NIS millions	% of Group revenue	% of segment revenue
Import and sale of vehicles	3,260		89%	4,191	9.4%	90.92%
Sale of parts and garage services	403		11%	418	0.9%	9.08%
Total	3,663		100%	4,609	10.3	100%

- B. Below are data for Delek Automotive gross earnings from products and services in 2011 and 2010 (in NIS millions), as a percentage of the Group's margin and as a percentage of automotive segment profit:²⁴²

	2011			2010		
	NIS millions		% of segment revenue	NIS millions	% of Group's margin	% of segment revenue
Import and sale of vehicles	322		75.2%	488	-	78.2%
Sale of parts and garage services	106		24.8%	136	-	21.8%
Total	428		100%	624	-	100%

²⁴¹ In light of the sale of Delek Automotive shares in October 2010, as described at the top of section 1.10 above, the Company ceased consolidating Delek Automotive in its statements. Owing to the sale, Delek Automotive's operating sales have been presented in the statement of income under the "Profit from discontinued operations" item, where the comparison figures have been reclassified.

²⁴² In light of the sale of Delek Automotive shares in October 2010, as described at the top of section 1.10 above, the Company ceased consolidating Delek Automotive in its statements. Delek Automotive's operating sales have been presented in the statement of income under the "Profit from discontinued operations" item, where the comparison figures have been reclassified.

- C. The gross profit of revenues in the segment in 2011 and 2010 were 11.7% and 13.53%, respectively.
- D. On October 20, with closure of the transaction for the transfer of control in Delek Automotive from Delek Investments to Delek Automotive, Delek Investments stopped consolidating the data of Delek Automotive in its financial statements.

1.14.5 Customers

- A. There are two main categories of Delek Automotive customers: private and institutional. Institutional customers include car leasing and rental companies and the government vehicle administration. Below is the breakdown of sales to private and institutional customers for 2011 and 2010:

	2011	2010
Private customers	38%	33%
Institutional customers	62%	67%

This breakdown of sales does not stem from Delek Automotive's policy but from the structure of the vehicle market in recent years. In view of the large numbers of vehicles purchased by institutional customers, these customers are granted bulk discounts and preferential credit terms.

At the beginning of 2012 Delek Automotive changed the credit terms for some of its institutional customers by providing a longer credit period and charging interest on the loan. To secure part of this credit, the Company has obtained a first fixed lien on the customers' rights in the sold vehicles. (See also sections 1.14.9(D) and 1.14.19(E). At the report publication date, the balance of the debt partially secured by these liens amounted to NIS 120 million.

- B. Delek Automotive customers purchasing parts and garage services are mainly the service centers, distributors, customers of the central garage, institutional customers and also insurance companies providing repair services for their customers under existing insurance arrangements.

1.14.6 Marketing and distribution

- A. Delek Automotive markets and distributes the Mazda and Ford cars it imports by means of its eight showrooms and by means of eight showrooms operated by six independent dealers. Delek Automotive sales are completed at its showrooms and it also sells directly by approaching institutional customers.
- B. Delek Automotive's showrooms are located around the country. They are rented from third parties, with the exception of the Mazda showroom in Tel-Aviv which is owned by Delek Automotive, and the Ford showroom in Tel Aviv which is leased from Delek Investments.
- C. Delek Automotive has agreements with six independent dealers that maintain and operate showrooms in major cities for displaying the cars it imports. These agreements do not grant the dealers exclusivity. However, there are specific areas in which Delek Automotive agrees there will be no more than one dealer (although Delek Automotive itself may operate in any area). The agreements with the dealers are for one-year periods from the date of signature and are renewed automatically for one additional year unless one of the parties gives three months' written notice of termination. Delek Automotive sets the commissions which it pays its dealers, and payments are made only after it receives full payment for the sale of the vehicle.
- D. Most Mazda and Ford vehicle parts are marketed by the company's central logistics center at Nir Zvi and sold to 58 garages nationwide which have been certified as service centers for Mazda and Ford vehicles. Delek Automotive also sells parts through various dealers and distributors of vehicle parts in Israel. In recent years Delek Automotive has been upgrading the service centers.

Under agreements between Delek Automotive and the service centers, the owner of a service center is required to operate, maintain and manage the center at its expense, in a manner and with an appearance and at a location to be determined by Delek Automotive in accordance with its instructions and subject to the provisions of any law. The owner is required to purchase and maintain permanent inventories of vehicle parts and accessories that comply with the quality and compatibility requirements and can satisfy the level of service required for Delek Automotive customers, as defined by Delek Automotive from time to time. The owner

undertakes to repair, without charging the customer for labor and/or parts, any vehicle covered by a manufacturer's warranty and/or Delek Automotive service agreement, provided the repair is included in the warranty and/or service agreement and Delek Automotive approves the repair in advance. Delek Automotive pays the service center owner for services rendered under the warranty or service agreement, in an amount that includes the price for parts less a discount decided upon from time to time by Delek Automotive, plus labor costs as determined in the agreement. The agreements are valid for one year from the date of signature, and are renewed automatically for additional one-year periods. Notwithstanding the aforesaid, each party may terminate the agreement at any time and it will expire three months from the date of the notice.

- E. Delek Automotive also supports the marketing of its products through advertisements in the various media, at the discretion of its management and in compliance with the manufacturer's standard rules.

1.14.7 Competition

In 2011 Delek Automotive's market share was approximately 14% of total vehicle deliveries in the sector and approximately 16% of total private vehicle deliveries (compared with 19% and 22% respectively in 2010). The Israeli automotive market is oligopolistic and includes a number of importers representing various manufacturers. Competition in the vehicle market is between the various importers and is reflected in the wide range of car models imported from different parts of the world: Europe, USA and the Far East, but it is not reflected in the representation of a particular manufacturer by more than one importer. (For details of the parallel import reform and its application as of June 2010, see section 1.14.1(B)1). Nevertheless, competition continues to be based mainly on brand, model, price, service quality, the vehicle's resale value in the used car market and payment terms. The factors influencing competition in the sector are external and include competition in the global automobile market, vehicle manufacturers, exchange rates of the currencies in which the vehicles are purchased. Internal influences include the activities of the other importers in the Israeli market such as potential parallel importers. To the best of Delek Automotive's knowledge,²⁴³ its main competitors are Union Motors (Toyota), Colmobil-Colmotor (Hyundai, Mitsubishi and Mercedes), Japanauto (Subaru), David Lubinski (Peugeot and Citroen), Moshe Carasso & Sons (Nissan and Renault), Champion Motors (VW, Audi and Seat) and UMI (Chevrolet, Saab and Isuzu), Mayer's Cars and Trucks Ltd. (Honda, Volvo), Automotive Equipment and Vehicles Ltd. (Suzuki, Chrysler), Talcar (Kia) and Shlomo Sixt (Opel).

There is intense competition in the vehicle parts and garage service markets. The competition to sell parts is waged on original parts imported by parallel import, generic parts, counterfeit parts, parts from scrapped cars, reconditioned parts and stolen parts. Authorized and unauthorized garages compete for business. Delek Automotive cannot estimate its market share in the service and vehicle parts market since there are no official data in this field, owing to the numerous service providers, distributors, and small- and medium-size dealers.

1.14.8 Property, plant and equipment, and facilities

Below is a summary of the main real estate and other material property, plant and equipment of Delek Automotive:

- A. The Mazda showroom in Tel Aviv is owned by Delek Automotive and the Ford showroom in Tel Aviv is leased from Delek Investments.
- B. Logistics Center

Delek Automotive has a new logistics center comprising warehouses and offices situated on an area of 64,000 sq. m. near Moshav Nir Zvi. According to the outline plan, the land is designated to serve as an industrial and storage area for a plant manufacturing pipes and fittings. Delek Automotive has leasing rights to this land through 2045 (with an option for a 49-year extension). The Logistics Center, which was completed in 2004, is one of the most advanced of its kind and it was built with an eye on the future of Israel's car market. Activities in the center include vehicle storage, preparation and delivery of vehicles to customers, and marketing and sales of vehicle parts. Delek Automotive's management and service staff are also located in this center. The Logistics Center currently has capacity to store up to 2,500 vehicles, and in future will have capacity for another 1,000 vehicles. At the date of publication of this report, Delek Automotive uses 100% of its current maximum storage space. Delek

²⁴³ Based upon the reports published from time to time by the Automobile Importers Association.

Automotive does not expect to make another such significant investment in this property. For details of the central garage located in the logistics center, see sub-section (C).

At the date of publication of this report, all the buildings in the Logistics Center have received a Form 4. For details of legal proceedings pertaining to construction at the Logistics Center, see sections 1.14.15(A) below.

On February 6, 2006, DMR Properties received an enhancement levy assessment from the local Regional Planning and Construction Committee ("**the Committee**") in respect of grant of a building permit for the Logistics Center, in the amount of NIS 21,600,000 million. DMR Properties paid half of the amount of the levy. On March 8, 2006, DMR Properties submitted a counter-assessment to the Committee, arguing that the principal charge under the assessment should be billed not to DMR Properties but to the Israel Lands Administration ("**ILA**") On February 17, 2008, a settlement agreement was signed between DMR Properties and the Committee, whereby the enhancement levy is NIS 10 million at its value on the date on which DMR Properties paid the Committee. Following this agreement, DMR Properties, through its legal advisers, approached ILA requesting reimbursement of part of the enhancement levy it had paid. ILA's response to the request from DMR Properties was that it was not prepared to agree to a settlement without going to court. DMR Properties now intends to complete preparation of the documents needed to apply to the court for reimbursement of part of the enhancement levy.

Delek Automotive also purchased 78,500 sq. m. (gross) of land adjacent to the above-mentioned land, as follows:

1. 71,000 sq. m. of which Delek Automotive purchased 58.5% (41,500 sq. m.) from Koor in accordance with an agreement from 2000. The leasing rights to this land expired on September 30, 2002 and since then legal proceedings have been taking place in order to extend their validity. They involve the conservation and agricultural cultivation of the land as well as regulation of the rights of the previous owner who is not active at present.

After the above road was paved, part of this land was also expropriated, leaving an area of 33,500 sq. m. leased by Delek Automotive. Moreover, another expropriation is expected and this would leave Delek Automotive with approximately 22,350 sq. m.

Delek Automotive believes that the expectation of another expropriation is forward-looking information as defined in the Securities Law, and it is based, *inter alia*, on a plan to upgrade the road in the area. This belief is not certain and it might not be realized, *inter alia*, because of changes in the above-mentioned plan.

2. 22,000 sq. m. of land to which Delek purchased the leasing rights from Koor pursuant to an agreement from 2000. After paving of a road, part of this area was expropriated leaving a leased area of approximately 12,000 sq. m.
3. 15,000 sq. m. of the aforesaid land to which Delek Automotive has leasing rights until September 18, 2042 with an option for a 49-year extension. This is the land where Delek Automotive's central service center (central garage) is located. Following the above-mentioned settlement agreement between Delek Automotive and the Committee, on February 17, 2008 a Form 4 was issued for the central garage. The central garage has a business license through December 31, 2012.
4. In addition to that stated in sub-sections B and C, Delek Automotive purchased 50% of the leasing rights (undivided interest) in a plot of land of approximately 5,000 sq. m. bordering on the plot on which Delek Automotive's new Logistics Center at Nir Zvi was constructed, in order to enable convenient access to the center. For further details, see section 1.14.12(A).

C. Showrooms

Under an agreement signed on January 28, 2008 between DMR Properties (1995) Ltd., a subsidiary of Delek Automotive ("**DMR Properties**") and Vitania Ltd. ("**Vitania**"), of the first part and a third party, DMR Properties and Vitania acquired title to a 5,000 sq. m. plot of land ("**the Plot**") in consideration of NIS 64 million, in equal parts and on the same conditions (50% for each party)²⁴⁴.

²⁴⁴ The total cost of the land amounted to NIS 66 million.

On February 6, 2008, DMR Properties and Vitania entered into an agreement, which was amended on November 28, 2011, regulating the joint construction of an income-generating property on the Plot and an adjacent plot, if acquired (**"the Cooperation Agreement"**). On the same date, a loan agreement was signed between DMR Properties and Vitania, in which DMR Properties undertook to grant Vitania a loan of NIS 32 million to finance the purchase of Vitania's share in the Plot (**"the Loan Agreement"**). The Cooperation Agreement and Loan Agreement were approved by the general meetings of Delek Automotive and Delek Real Estate. On November 28, 2011 the parties signed an amendment to the Loan Agreement so that between January 1, 2012 and December 31, 2013 the loan would bear annual interest of prime + 2%, and the interest from January 1, 2014 would be set by the parties, based on the costs of raising the funds for DMR Properties. In addition, the loan repayment date was set for November 15, 2015 and it was agreed that Vitania would have the right to make early repayment of the loan at any time without incurring ancillary costs. In order to secure repayment of the loan, a first lien was filed against all Vitania's contractual rights in the plot in favor of DMR Properties. Under the Cooperation Agreement DMR Properties and Vitania are constructing on the Plot an income-generating property containing a showroom which will be leased to Delek Automotive for its operations (the **"Project"**). In an amendment to the Cooperation Agreement from November 28, 2011, the parties agreed that the rent to be paid by DMR Properties would be 10% of all the investments in respect of the sections designated for its use.

The construction plan for the Project comprises two stages: (1) Stage A consists of the building of all the parking basements (which will also be used in Stage B), the showroom for Mazda and Ford vehicles on the basement floor as well as an innovative special-purpose display tower for Mazda and Ford vehicles in the eastern section of the Plot. The showroom and display tower will be leased to DMR Properties or another subsidiary of Delek Automotive for its operations. Delek Automotive believes that this stage will be completed in 2014; (2) Stage B consists of the construction of an office building in the western section of the Plot, part of which will serve as a showroom for BMW vehicles and the other part will be let.

As for the costs of the Project, Delek Automotive believes that Stage A will cost NIS 150 million (in addition to the cost of purchasing the above-mentioned land) and Stage B is expected to cost NIS 100 million.

Delek Automotive's estimates regarding continuation of the Project and its construction costs are forward-looking information as defined in the Securities Law and are based, *inter alia* on the estimates of the professionals providing services to Delek Automotive for the Project. These estimates are not certain and could change, *inter alia*, as a result of dependence on external factors which are not under the control of Delek Automotive, such as a delay in obtaining building permits and/or approvals from other authorities as required by law, difficulties with suppliers, etc.

In order to finance the construction of Stage A of the Project, in October 2010, DMR Properties and Vitania (jointly: the **"Borrowers"**) entered into a credit agreement with Israel Discount Bank (respectively: the **"Credit Agreement"** and the **"Bank"**), whereby the Bank would make a credit facility available to the Borrowers in a total aggregate amount of up to NIS 150 million (the **"Credit Facility"**). The Credit Agreement provides that the Credit Facility must be used by October 15, 2013 and the interest for the Credit Facility will be prime plus a margin of 0.45% per year²⁴⁵. It also provides that in order to guarantee repayment of the credit debts, the Borrowers undertook to provide the Bank with collateral which includes, *inter alia*, a first-grade mortgage in favor of the Bank on the land which is free of any encumbrance, except for as provided in the agreement²⁴⁶. The Borrowers undertook toward the Bank that they would comply with certain terms in the credit period to the satisfaction of the Bank. These include financial covenants, including a prohibition on any type of payments out of the Project's revenues to interested parties, if these payments endanger the repayment ability of the Borrowers, unless the Bank has given its prior consent thereto, and also a requirement for minimum equity capital of Delek Motors (for details of the financial covenants of Delek Automotive and calculation thereof, see section 1.10.13(B)). It was also agreed that the

²⁴⁵ This is subject to the Bank being entitled to increase the interest rate by 2% in the event of a breach by the Borrowers and subject to the Borrowers being entitled to reduce the interest by 0.2% if they deliver to the Bank a letter of guarantee as stipulated in the Credit Agreement. Moreover and subject to the terms governing the Credit Agreement, the Borrowers will be liable for a one-off payment and commission.

²⁴⁶ These liens have been registered in the Register of Companies and in the Land Registry.

Borrowers would be equally responsible vis-à-vis the Bank so that each party would be responsible for reimbursement of only half of the liabilities to the Bank. By the date of publication of this report, NIS 18 million had been withdrawn from the above Credit Facility and Delek Automotive had withdrawn half of this amount.

Intangible assets

Delek Automotive has franchises from Mazda, Ford, BMW and Mini for the import of vehicles and parts, as described in sections 1.14.14(A) and 1.14.14(B). Delek Automotive is materially dependent on these franchises.

Human resources

At December 31, 2011, Delek Automotive has employees (not including employees of Kamor Motors and its subsidiaries) divided into the following departments:

Department	No. of employees
Management	8
Finance, IT, administration	26
Mechanics	68
Service	33
Sales	41
Logistics	46
Vehicle parts	39
Total	261

As a result of the acquisition of Kamor Motors, the Delek Automotive currently has 123 employees in Kamor Motors and its subsidiaries.

Delek Automotive is dependent on Mr. Gil Agmon, the controlling shareholder in Delek Automotive and its CEO, *inter alia*, because any change in the active management of Delek Motors Ltd. ("**Delek Motors**") (a wholly-owned subsidiary of Delek Automotive) requires prior written consent from Ford. Furthermore, Mazda may notify Delek Motors of termination of the Mazda Agreement if there is a change in the management of Delek Motors. (For further details, see sections 1.14.14(A) and 1.14.14(B)).

D. Benefits and the nature of the employment agreements

Delek Automotive employees, including senior officers, are generally employed under employment agreements. According to Delek Automotive policy and the provisions of the Notice to an Employee (Terms of Employment) Law, 2002, new Delek Automotive employees receive a detailed written description of their employment terms when they start work. Employees receive all the rights to which they are entitled under Israel's labor laws. Most Delek Automotive employees have senior employee insurance policies that include provisions for compensation and Delek Automotive's obligation for severance pay, as part of the terms of employment. Delek Automotive pays all its employees a bonus every year.

In addition, since Delek Motors is a member of the Vehicle Importers Association, which is affiliated to the Chamber of Commerce Association, its employees are covered by a general collective agreement for import, export, service and trade sector employees from February, 21, 1977 (as amended on June 11, 1980 and October 27, 1983) ("**the Collective Agreement**"). In addition, extension orders applied some of the provisions of the Collective Agreement to all employees and employers in the import, export and wholesale trade sectors, and therefore, it appears that they apply to all Delek Automotive employees.

Officers and senior management employees at Delek Automotive are employed under agreed terms, which include, *inter alia*, a monthly salary, entitlement to a company car, provisions for senior employee insurance and in-service training fund. For details of the agreement with Rami Naor, a relative of the Group's controlling shareholder, which expired in the reporting year, as deputy chairman of the board of Delek Automotive, see details pursuant to Article 22 in Chapter D of the Periodic Report.

E. Training and instruction

Delek Automotive holds regular training sessions for its employees, according to its needs and the employee's function. Delek Automotive also sends its professional employees to trade fairs, seminars and workshops on various topics.

F. Employee compensation plans

Delek Automotive compensates its employees according to function and rank. The compensation is not part of the employment agreements and varies from year to year.

G. Allotment of securities to senior employees

In 2011 17,952 option warrants granted in 2006 to senior employees were exercised into shares, constituting 1.84% of the issued capital of Delek Automotive. In 2011 Delek Automotive recognized expenses totaling NIS 222,000 from the exercise of these option warrants (compared with NIS 1,083,000 in 2010).

1.14.9 Suppliers

Vehicles and vehicle parts are supplied to Delek Automotive by Mazda and Ford from their various factories around the world at the manufacturers' discretion. Mazda products generally come from Japan, while Ford products generally come from Europe. Delek Automotive is dependent on these suppliers. In 2011 approximately 56% of the import value of vehicles and 51% of the import value of parts were from Mazda, with the remainder from Ford (44% and 49% respectively). For a description of the agreements with Mazda and Ford, see sections 1.14.14(A) and 1.14.14(B).

Vehicles and vehicle parts are available within 90 days of the date of the order and in accordance with the business plan structured with each of the vehicle manufacturers.

1.14.10 Working capital

A. Vehicle inventory policy

Delek Automotive orders new vehicles from the car manufacturers about once a month, and the vehicles arrive in Israel two to three months later. Delek Automotive's policy is to hold stock sufficient for an estimated four months.

B. Vehicle parts inventory policy

The Commodities and Services Control (Vehicle Import and Servicing) Order, 1978, obligates the supplier to supply transportation products for any vehicle model imported by the importer within seven days from receipt of the order. However, the importer or its agent is protected if it proves that it complied with procedures for ordering the product from any possible source at the time, and that the delay was beyond its control, provided the product is supplied within 14 days.

The vehicle parts inventory at Delek Automotive's Logistics Center is based on the experience of Mazda, Ford and Delek Automotive regarding requirements for vehicle parts in the Israeli market. Vehicle parts are delivered about two to three months after being ordered. For immediate orders, when the part is not in stock, Delek Automotive orders the required parts from the central parts facilities of Mazda and Ford in Europe and ships them to Israel by air. Therefore, in order to maintain inventory at the levels required to provide its customers with appropriate service, Delek Automotive uses a computer system based on statistical models which takes relevant parameters into consideration. Delek Automotive maintains a five-month inventory of parts. The vehicle parts inventory totals 45,000 items which are valued at NIS 73 million in the financial statements at December 31, 2011.

C. Warranty policy

In addition to the Ford and Mazda vehicle warranties attached to the manufacturer agreements, the manufacturers provide warranties as detailed in the warranty manual in each new car. Mazda and Ford provide a three-year or 100,000 km warranty for all their models, whichever comes first. In the agreements with the manufacturers, Delek Automotive undertook to implement or ensure that the service centers implement the warranty services as described in the warranty manual. Under the manufacturer warranty, Delek Automotive grants this warranty for all the vehicles it sells. Delek Automotive is entitled to reimbursement from the manufacturers for expenses incurred by supplying warranty services under the franchise terms. Delek Automotive is under no independent obligation to provide a warranty for the vehicles, except for what is stated in the agreements with the manufacturers. The warranty is therefore a direct and exclusive warranty from the manufacturer who determines its terms for

the customer, while Delek Automotive acts as the manufacturer's agent in all matters pertaining to the provision of service to the customer in general and implementation of the vehicle warranty in particular. Therefore, and based on its experience, Delek Automotive does not foresee any expenses as a result of this warranty and therefore has not made any provisions for warranties on its books. The manufacturer agreements describe the terms for reimbursing Delek Automotive for warranty services, and *inter alia* that Delek Automotive is required to report within 90 days on every repair effected under the warranty, and to keep the parts for up to 30 days after payment. In addition, the manufacturers may request the return of the faulty parts that were replaced. In the reporting year, there were no material disputes with manufacturers in connection with these warranty services. For details of repairs carried out by the service centers under the warranty, see section 1.14.5(D).

Delek Automotive's trade license for transportation products specifies that it is required to provide the buyer, at the time of the sale, with a warranty for the proper operation of the vehicle part as specified in the license for at least three months or 6,000 km, whichever is earlier. The warranty manuals provided with the vehicles sold by Delek Automotive specify that the parts warranty is as follows: for vehicles delivered by October 2, 2011, the warranty is for the first six months or 10,000 km, whichever is earlier, from the date of its installation by a Delek Automotive service center. For vehicles delivered after October 2, 2011 Mazda provides a 12-month warranty for its parts, and Ford provides a warranty for its parts for the first 12 months or 20,000 km, whichever is earlier, from the date of installation in a Group service center.

D. Credit policy

In the reporting year supplier credit averaged 195 days (compared with 225 days in 2010). Given the fact that taxes on the import cycle are paid by Delek Automotive in cash, in the reporting year its effective credit period averaged 98 days (compared with 110 days in 2009). In the reporting year the credit granted by Delek Automotive to its customers averaged 75 days. The volume of credit to its customers in the reporting year averaged NIS 978 million in 2010 (compared with NIS 1,320 million in 2010), and credit from suppliers averaged NIS 980 million in the reporting year (compared with NIS 1,130 million in 2010).

Investments

On July 1, 2004, DMR Properties (50%), Delek Israel (25%) and Delek Real Estate (25%) established a partnership called Delek – Nir Zvi (**"the Nir Zvi Partnership"**). The Nir Zvi Partnership was established for the acquisition (undivided interest) of 50% of the leasing rights in a 5,000 sq. m. plot adjacent to the plot on which the Group's new Logistics Center at Nir Zvi is built, to allow convenient access to the Center. The leasing rights were acquired under an agreement made on September 29, 2003 between a partnership of DMR Properties, Delek Real Estate and Delek Israel (in establishment) and the Middle East Tube Company Ltd. (**"the Acquisition Agreement"**) (**"Tubes"**). The Nir Zvi Partnership has leasing rights in the Land through 2045, with an option for a 49-year extension²⁴⁷. According to the outline plan, part of the Land is defined as a private open area designated for expropriation for the widening of Road 44. To the best of Delek Automotive's knowledge, the Nir Zvi Partnership is initiating a change in the designation of the area for the establishment of a commercial center and gas station. The Nir Zvi Partnership is financed by a shareholder loan and by external sources such as banks. Under the agreement between the partners in the Nir Zvi Partnership, if by December 31, 2009, the permits referred to in the agreement for establishing a gas station and commercial areas on the Land are not obtained and/or there is no agreement for operating the gas station by the fuel company, Delek Real Estate and Delek Israel are entitled, during one year from that date, to leave the partnership and receive from DMR Properties all their investments plus linkage differentials and 6% annual interest. Consequently, after Delek Real Estate notified DMR Properties of its wish to leave the partnership and get back its investment as described above, in January 2010 DMR Properties bought back from Delek Real Estate its share in the partnership and paid it NIS 2,101,000 for leaving the partnership²⁴⁸. After transfer of Delek Real Estate's rights in the partnership to DMR Properties, the latter will 69++ hold 75% of the rights in the partnership. The agreement

²⁴⁷ These rights have not yet been registered in the partnership's name in the Land Registry Office. Upon completion of the handling of the plans for the joint venture which were submitted in the name of Tubes, it will be possible to deal with signature of the lease agreement with the Administration for the rights which were acquired.

²⁴⁸ The transfer of rights has not yet been registered in the records of the Register of Partnerships.

between the partners in the Nir Zvi Partnership was approved at the general meeting of Delek Automotive on November 4, 2003.

- E. In April 2002, August 2003, and December 2005, Delek Automotive purchased shares in Mobileye N.V., constituting 3.3% of its equity with full dilution, for USD 7.2 million. The fair value at December 31, 2011 is approximately NIS 94 million, based on investments made in this company. Mobileye N.V. is developing an advanced sensor technology system for the automotive industry.
- F. In 2006 Delek Automotive acquired 2,200,000 Ford Motor Co. shares in consideration of USD 15 million (the equivalent then of NIS 70 million). The fair value of the shares at December 31, 2010 is approximately NIS 90 million, based on their stock exchange price. Ford Motor Co. is a public company whose shares are traded on the New York Stock Exchange and is the manufacturer of Ford vehicles. At March 19, 2011, the Ford shares held by Delek Automotive were worth approximately NIS 104 million.

1.14.11 Financing

- A. Below is the average interest rate on loans from bank sources that were in effect in 2011 and are not intended for the exclusive use of Delek Automotive²⁴⁹:

	Average interest rate	
	Short-term loans	Long-term loans
NIS credit		Prime + 0.45%
Credit in yen/euro/sterling	Libor + 1.8%	-
Credit in USD	Libor + 1.2%	-

- B. Credit restrictions

Within the framework of the loans and credit facilities Delek Motors has obtained from the banks, it has undertaken to the banks that its equity in the consolidated balance sheet at the end of each calendar year would not drop below 20% of its total assets for said year. "Total assets" is defined as total assets in the balance sheet less short-term credit from bank corporations in an amount which does not exceed the balance of cash and cash equivalents in the banks. In light of the first-time consolidation of the balance sheet of Kamor Motors, the ratio of equity to total assets at December 31, 2011 and at the report publication date is 9%²⁵⁰. In March, waivers were obtained from the banks in respect of compliance with said financial covenant in which the banks agreed that in the consolidated balance sheet for 2011 the equity would drop below 20% of total assets for that year.

In respect of loans from a particular bank, the balance of which at December 31, 2011 amounted to NIS 99,836,000, Kamor Motors undertook to comply with particular financial covenants. At December 31, 2011, Kamor Motors was not in compliance with the required financial covenants. After the balance sheet date, Kamor Motors obtained a waiver in relation to a breach of the financial covenants at December 31, 2011. In addition, Delek Motors granted Kamor Motors a guarantee in favor of the bank up to the sum of the loans totaling NIS 130 million. The credit agreements

Moreover, the credit agreements with the banks contain an undertaking from Delek Motors not to create liens on its property and assets in favor of any another person or entity and not to sell or transfer its assets in any way (except by way of sales in the normal course of its business) to a third party without the prior written consent of the banks.

- C. Between the balance sheet date and the reporting date there was no significant change in the volume of credit from banking corporations and no new loans were obtained.
- D. Delek Automotive credit facilities and terms

At December 31, 2011 and at the date of the Periodic Report, Delek Automotive had unsigned credit facilities totaling NIS 1,500,000 million. At December 31, 2011 it had used NIS 860 million of this amount. At the report publication date there had been no material change in the volume of credit it had used. These credit facilities were granted for one year.

²⁴⁹ The average interest rate in the table is close to the effective interest rate.

²⁵⁰ This financial covenant is reviewed by the banks at the end of each calendar year.

The standard forms for opening an account which were signed by Delek Automotive many years ago stipulate that the bank will have precedence in calling in any loan granted to Delek Automotive, *inter alia*, in the event that any document signed by Delek Automotive gives another entity the right to demand immediate repayment of its debts and liabilities vis-à-vis said entity.

E. Variable interest credit

Below are details of variable interest credit used by Delek Automotive at the balance sheet date:

Change mechanism	Interest range in 2011	Basic interest rate before report publication date (March 15, 2011)
Bank of Israel interest +	0.95%	0.95%
JPY LIBOR +	1.2% – 3%	1.9%
EUR LIBOR +	2% – 1.2%	-
USD LIBOR +	1.2%	1.2%

1.14.12 Taxation

- A. For details of the Ministry of Finance's decision regarding the plan to increase the use value of company cars, see section 1.14.2(4)(B) above.
- B. For details of the green taxation reform, see section 1.14.2(5)(B).
- C. Vehicles sold by Delek Automotive in Israel are subject to VAT at the rate applicable on date of the sale (since January 1, 2010 it has been 16%).
- D. Vehicles imported from Japan are subject to 7% tax on the value of the vehicle.
- E. Delek Automotive pays the taxes listed in subsections A-D when the vehicles are released from customs. The sales prices of the vehicles take these taxes, *inter alia*, into account.

1.14.13 Environmental risks and their management

The provisions of law, regulations and various orders dealing with environmental protection ("Environmental Protection Laws") are applicable to a non-material part of Delek Automotive's operations. These issues relate to the garage and service operations provided by Delek Automotive and their consequences, including an internal gasoline station to fuel the new vehicles marketed by Delek Automotive; operation of a carwash station; removal of waste from the central service garage, including, *inter alia*, oils, filters and tires. Pursuant to the Tire Removal and Recycling Law, 2007, Delek Automotive is bound by an annual tire recycling quota and noncompliance is liable to result in the imposition of a fine. Delek Automotive takes care to comply with this quota every year.

Under section 3 of the Hazardous Substances Law, 1993, Delek Motors has received from the Ministry of the Environment a category C poisonous substances permit (for poisonous substances which are not dangerous) which is valid until April 4, 2014, to use a carwash substance in the preparation of vehicles for delivery to the Nir Zvi Logistics Center,.

Delek Automotive believes that the costs of compliance with environmental protection laws are not expected to have a material effect on its results. Its assessments regarding the potential implications of environmental quality laws for its business is forward-looking information as defined in Article 32A of the Securities Law, which is based on its familiarity with regulation in the sector and its past experience. Nevertheless these estimates might not be realized for many reasons, among them regulatory changes, changes in Delek Automotive's installations, discovery of significant pollution on its premises, etc.

1.14.14 Restrictions and supervision of Delek Automotive operations

Below are details of the legal restrictions and other legal arrangements relevant to a material part of Delek Automotive's basic operations and which could affect them:

A. Legislation in the vehicle import industry in Israel

The Control of Commodities and Services (Vehicle Import and Servicing) Order, 1978, states, *inter alia*, that no importer or agent may sell a new imported vehicle without a license from the competent authority. Delek Automotive has licenses as defined in the above Order, for importing vehicles, valid through December 31, 2012. The licenses are granted for one year

and are renewed every year. Delek Automotive also has special permits for importing original vehicle parts for Mazda, Ford and BMW vehicles (including Minis and Husqvarna motorcycles from BMW). These permits are valid through May 9, 2012, December 11, 2012 and January 30, 2013, respectively. The order also sets conditions for the awarding of a vehicle import license which include the obligation to provide maintenance services and define which service garages the importer shall operate, as well as the obligation to provide a warranty for at least two years and to market and supply transport products.

For details of a Ministry of Transport procedure regulating the import of generic vehicle parts, see section 1.14.2(7)(B).

B. Price control

There are no price controls for vehicles, spare parts and garage services.

C. Business licenses

Delek Automotive's operations require a business license under the Business Licensing Law, 1968. At the report publication date, Delek Automotive has licenses for all its operations.

Trade in vehicles and vehicle parts requires a permit from the Ministry of Transport pursuant to the Commodities and Services Control (Manufacture of and Trade in Transportation Products) Order, 1983. Delek Automotive has a valid license from the Ministry of Transport for trading in transport products, valid through December 31, 2013.

D. Antitrust

An order by virtue of section 50B of the Restrictive Trade Practices Law, 1988, which came into force on April 24, 2003, was designed to preserve freedom of competition in the vehicle sector. It prohibits, inter alia restrictions on service garages with regard to the purchase and use of transport products. It entitles consumers to purchase warranties in addition to the statutory warranty or the one determined by the manufacturer (based on the longer of the two periods). It prohibits the setting of warranty conditions which are contingent on the purchase of other products and services. It forbids service garages from demanding various items of information. It bans service garages from imposing price restrictions and determines criteria for the granting of authorized garage status. It also forbids the granting of exclusivity to service garage operators. This order was valid for five years until April 24, 2008. In any event, Delek Automotive operates in accordance with this order. For the recommendations of the Zelekha Committee in connection with the increase of competition and reduction of centralization in the automotive sector, see section 1.14.2(1)(B).

1.14.15 Material agreements

The material agreements to which Delek Automotive is a party are these:

A. Mazda agreement

Delek Automotive has imported and sold Mazda vehicles and vehicle parts since 1992. Under an agreement from April 1, 2005 (as amended and extended from time to time) between Mazda Motor Corporation ("**the Manufacturer**"), Delek Motors and the Itochu Corporation ("**the Exporter**"), the Manufacturer is committed to supply Delek Motors with specific Mazda models as detailed in the appendix to the above agreement,²⁵¹ for the purpose of marketing and sales in Israel. Replacement parts for these vehicles are also part of the Mazda Agreement ("**Mazda Vehicles and Parts**"). On September 21, 2011 Delek Motors signed a franchise agreement with the Manufacturer which replaces and supersedes the franchise agreement from April 1, 2011 which was signed by Delek Motors and the Manufacturer and the Exporter. This followed a letter which was received by the Vehicle and Maintenance Services Department in the Ministry of Transport whereby a franchise agreement between three parties to which the Exporter is party does not comply with the provisions of the Supervision of Commodities and Services Order (Import of Vehicles and Provision of Vehicle Services), 1978. The provisions of the new franchise agreement ("**the Mazda Agreement**") are similar in substance to the provisions of the previous franchise agreement except for the term of the agreement which is until September 30, 2014.

²⁵¹

The appendix to the agreement is not updated; rather, the quantities and models ordered are agreed upon from time to time between Delek Motors, the Manufacturer and the Exporter.

Below is a summary of the main terms of the Mazda Agreement:

The supply of Mazda Vehicles and Parts to Delek Motors pursuant to the Mazda Agreement will not prevent Delek Motors from purchasing vehicles and vehicle parts for sale in Israel from suppliers other than the Manufacturer, provided such sale does not have a significantly adverse effect on the sale of Mazda Vehicles and Parts. Mazda gave its consent to the acquisition of Kamor Motors. The Manufacturer has sole discretion to determine whether a sale has a significantly adverse effect on the sale of Mazda vehicles. Delek Motors is required to inform Mazda of its intent to sell other vehicles or vehicle parts at least 90 days in advance. In addition, the Manufacturer is not prevented from selling non-Mazda vehicles or parts to any other party in Israel.

Notwithstanding the aforesaid, the Manufacturer has the right to sell and export Mazda vehicles in Israel through other parties, as specified in the Mazda Agreement. These parties include government bodies, the diplomatic corps, international bodies such as the UN, Japanese companies that purchase more than ten vehicles per year, companies controlled by the Manufacturer and/or their employees and others. Delek Motors may not sell, directly or indirectly, vehicles and vehicle parts outside of Israel.

Vehicles and parts are ordered through specific agreements between Delek Motors and the Manufacturer. These agreements come into effect when the Manufacturer receives the order. The Manufacturer will make every effort to fill these orders, but it is not obligated to do so. Vehicles are delivered to the shipping port and after delivery Delek Motors is liable for any damage or loss. The Manufacturer retains its rights in the vehicles including the right to seize possession until receipt of full payment.

Delek Motors undertakes not to use parts for purposes other than servicing or equipping vehicles in Israel. The Mazda Agreement sets the legal and business conditions relating to the distribution of Mazda Vehicles and Parts, including the establishment of a marketing and distribution system, implementation of marketing and sales activities, establishment of a service center for vehicles and a customer service management system. It also requires the establishment of storage facilities suitable for vehicles, provision of customer warranties according to the Manufacturer's warranty, submission of regular reports to the Manufacturer, non-disclosure agreements, safekeeping of intellectual property, and an arbitration mechanism for resolving problems between the parties, all as set forth in the Mazda Agreement.

Each party is entitled to terminate the agreement at any time by written notice to the other parties if one or the other is in breach of the agreement and does not remedy that breach within two months after a written demand for remedy was sent to the party in breach.

Each party to the agreement is entitled to terminate the agreement by written notice to the other parties in one of the following events as set forth in the agreement: foreclosure, application for liquidation, receivership, request for reorganization, insolvency, delay in payment, transfer of all or most of the businesses, assets and liabilities of Delek Automotive, the freezing of Delek Automotive's business, merger, and so forth.

The Manufacturer is entitled to terminate the Mazda Agreement at any time by written notice to Delek Motors, if the Manufacturer decides that it is unable to continue business with Delek Motors as a result of death, incompetence, disregard, or any change in Delek Motors' management or as a result of a change in the legal or organizational structure of Delek Motors or in the case of a material change in the composition of the company's shareholders or investors²⁵².

If, as a result of *force majeure* (as defined in the agreement), any party to the Mazda Agreement is prevented from fulfilling its obligations for more than six months, any party to the agreement shall then have the right to terminate the agreement immediately by written notice to the other parties to the agreement.

Under the Mazda Agreement, the Exporter and Delek Motors may not transfer their obligations and rights, in whole or in part, to any third party without the prior written consent of the Manufacturer.

²⁵² The manufacturer has granted approval in advance to the transfer of control in Delek Automotive from Delek Investments and Properties to Mr. Gil Agmon and recognized Mr. Agmon as the largest shareholder in Delek Automotive and Delek Investments and Properties as the second largest shareholder in the company.

B. Ford Agreement

Delek Motors (in this sub-section 1.14.18(B), the “**Dealer**”) has been importing and selling Ford vehicles and vehicle parts since 1999, under an agreement signed on June 1, 1999 between Ford Motor Company (“**Ford**”) and Delek Motors (“**the Ford Agreement**”). Following are the main provisions of the Ford Agreement:

Ford appointed Delek Motors as a non-exclusive authorized dealer in Israel of vehicles and parts made by or for Ford and of other products as determined by Ford from time to time. Delek Motors agreed not to act directly or indirectly for any other business enterprise and shall act solely as a Ford dealer unless Ford agrees otherwise in writing.

Delek Motors undertook not to act in any way in the sale of new vehicles or parts which compete with Ford products without prior written consent from Ford. In the agreement, Ford agrees that Delek Automotive be a franchisee of Mazda products and defined rules for the integration of Mazda and Ford franchises in Israel. Ford agreed to the acquisition of Kamor Motors.

The Ford Agreement remains in effect from the date of its execution until it is terminated by one of the parties in accordance with its provisions.

The Ford Agreement stipulates the business and legal conditions for distribution of Ford products by Delek Motors in Israel, including marketing and distribution operations, establishment of a service system that complies with Ford standards, employment and training of suitable human resources, provision of warranties for Ford products, maintenance and repair services, the use of trade names and trademarks, and an arbitration mechanism for resolving disputes between the parties.

Section F of the Ford Agreement (“**section F**”) stipulates that Ford entered into the agreement on the basis of the representation and agreement that (1) only Gil Agmon (37.47%) and Delek Investments (32.13%)²⁵³ will be the principal owners of the Dealer, with holdings of 10% or more. It also stipulated that notwithstanding any statements to the contrary in the agreement, as long as no other person holds 10% or more of the shares of the Dealer, Gil Agmon is the largest shareholder and Delek Investments holds at least 10% of the shares in the Dealer, the Ford Agreement will remain valid and no prior consent will be required from Ford with regard to future changes in shareholdings in the Dealer; (2) only Gil Agmon will be fully authorized to engage in active management of the Dealer and he will devote his efforts to this purpose exclusively. The agreement also stipulates that the Dealer shall give Ford prior written notice of any proposed change in control (subject to that stated above) or in management authority, and immediate notice of the death or incapacity of any person as aforesaid. It also stipulated that any such change shall be valid only upon an amendment to the agreement to be signed in writing by Ford and the Dealer. In the event that its advance written approval (which it shall not unreasonably withhold) is not obtained Ford shall have the right to terminate the agreement as set forth hereunder.

Delek Motors has the right to terminate the Ford Agreement at any time by giving Ford 30 days' written notice.

Ford has the right to terminate the Ford Agreement without notice should any of the events listed in the agreement and which are under the control of Delek Motors, occur. These events include transfer by Delek Motors of the rights or obligations under the agreement; transfer of any material assets owned by Delek Motors that are required for running its business; any change without Ford's prior written consent (which it shall not unreasonably withhold) in the direct or indirect control of the active management of Delek Motors, as set forth in section F; discovery that Delek Motors or any other person whose name appears in section F made false representations when entering into the agreement or that Delek Motors made false representations in respect of any of the details listed in section F of the agreement; insolvency of Delek Motors; failure of Delek Motors to function as normal or to keep its Ford business open during regular business hours as set forth in the agreement; a court conviction of Delek

²⁵³ Until October 2010 the principal owners were Delek Automotive – direct holding of 100%, Yitzhak Sharon (Teshuva) – indirect holding of 72%. In a letter dated September 14, 2010 (the “Letter of Consent”) Ford stated that it recognizes as the owner of the Dealer prior to the transfer of control (Delek Automotive holds 100% of the Dealer and Delek Investments holds 54.9% of Delek Automotive) and that it gives its written consent to said change in control (Delek Automotive's 100% holding of the Dealer and Gil Agmon's 38% holding and Delek Investments' 33% holding of Delek Automotive) where Gil Agmon is the largest shareholder.

Motors or any of the entities listed in section F for violation of the law; or a disagreement between the parties which Ford believes could have an adverse effect on the business of Delek Motors, or the reputation or goodwill of Delek Motors or of Ford or other authorized agents of Ford, its associates or its products; or non-agreement between the above parties which Ford believes could have an adverse effect on the businesses of Delek Motors, its reputation or that of Ford or of its associates; a breach by Delek Motors of some of its undertakings under the agreement; late payment to Ford or a Ford company after prior notice was given and the breach was not corrected within 15 days; suspension or revocation of Delek Motor's operating license for any reason whatsoever. In addition, Ford has the right to terminate the Ford Agreement by giving 60 days' notice if Delek Motors fails to fulfill its undertakings in accordance with the agreement and does not remedy the breach within the 60-day notice period. Ford and Delek Motors both have the right to terminate the Ford Agreement by giving 15 days' written notice in the event of the death, physical or mental disability of the owners of Delek Motors listed in section F, provided that Ford suspends this right for a period of three months to one year if their successor or legal representative asks Ford to do so and Ford is convinced, to its satisfaction, that he or she is able to comply with the terms of the Ford Agreement. Ford has the right to terminate the Ford Agreement at any time by giving at least 120 days' written notice. Ford has the right to terminate the Ford Agreement at any time by giving at least 30 days' notice if Ford offers a new agreement or an amended version of the agreement to its authorized dealers.

In the event of a change in the control of Delek Motors or if most of the assets of Delek Motors are transferred to any other party, which requires Ford to negotiate a new distribution agreement with that party, Ford shall have the right of first refusal to purchase Delek Motors or the assets offered for sale on the same conditions as agreed with that party. Ford has the right to assign its right of first refusal to any third party. The right of first refusal can be enforced vis-à-vis any transferee of Delek Motors.

C. Expected agreements with BMW

In March 2012, Delek Automotive, through Delek Motors, will enter with BMW into a franchise agreement for the import into Israel of BMW cars, SUVs, and motorcycles as well as original accessories and parts ("**the BMW Agreement**") ("**the BMW Motorcycle Agreement**"), respectively. Under the agreement Delek Motors will be granted a franchise to sell BMW products, including cars, SUVs and motorcycles as well as original BMW accessories and parts, manufactured or which will be manufactured by BMW or supplied to BMW by third parties. In addition, in March 2012 Delek Motors will enter into another agreement with BMW under which it will receive a franchise to import and sell Mini cars as well as original accessories and parts for these cars, in Israel (in this section: "**the Mini Agreement**") (the three franchise agreements: "**the Franchises**"). In addition to the expected granting of the Franchises to Delek Motors in March 2012, Kamor Motors, the holder of the franchise for the import and sale of BMW products in Israel, is expected to terminate this franchise with BMW. Following is a summary of the principal terms of the Franchises at March 19, 2012:

1. The Franchises are franchises for the import, sale and provision of service in Israel for BMW and Mini products (in this section: "**the Territory**"). Delek Motors is prohibited from selling or marketing BMW and Mini products outside the Territory and it is also prohibited from selling the goods directly or indirectly to sellers which have not been approved by BMW. In order to guarantee these undertakings, Delek Motors has agreed to pay for any breach thereof punitive compensation amounting to 15% of the market price of vehicles sold in this manner, including the accompanying optional accessories. Delek Motors also agreed not to distribute products competing with BMWs and Minis (except for Mazda, Ford and Lincoln) and that it would not produce, distribute or marketing competing products or use competing products for repair and maintenance purposes, except in its operations as importer, except with prior written consent from BMW. Notwithstanding, under the agreements Delek Motors may enter into agreements with dealers approved by BMW for the distribution of BMW and Mini cars in Israel.
2. BMW has the right to sell BMW and Mini products and parts therefor in Israel, directly or indirectly, to a limited number of entities other than Delek Motors, as set forth below:

BMW is entitled to sell cars and parts in Israel, directly or indirectly and not via Delek Motors, to car fleets (defined in the agreement as entities purchasing more than 10 BMW's a year), public authorities or similar national or international bodies, persons defined as VIPs, journalists, customers ordering armored vehicles, as well as employees of BMW or its affiliates. BMW also has the right to sell or transfer Mini vehicles to end

customers in cases where the purchase is effected through distributor subsidiaries or online. If BMW exercises its right to sell BMW's and Minis to car fleets Delek Motors will be entitled to reasonable compensation to be determined by BMW, provided that Delek Motors works to develop the car fleet businesses. Delek Motors will also be entitled to this compensation if BMW makes an online sale of a Mini vehicle directly to an end customer, and if at the customer's request, the delivery is performed by Delek Motors.

BMW is entitled to sell BMW motorcycles and their parts in Israel, directly or indirectly and not via Delek Motors, to car fleets, public authorities or similar national or international bodies, representatives of foreign governments and members of foreign armies stationed in Israel, persons defined as VIPs, foreign journalists, racing car drivers recognized by BMW, employees of BMW or end customers if the purchase is effected through a subsidiary distributor or online. If BMW exercises its right and sells BMW motorcycles directly to an end customer via an online order, and if the customer requests that the delivery be made by Delek Motors, or if Delek Motors serves as an intermediary in the sale or delivery of a motorcycle to a car fleet, Delek Motors will be entitled to reasonable compensation to be determined by BMW. If BMW exercises its rights as described above, Delek Motors will not be entitled to any compensation.

3. BMW Bank GmbH of Germany has granted credit to Kamor Motors for the shipment of BMW products. In order to guarantee payment of the shipment costs by Kamor Motors, Delek Motors will provide BMW with a guarantee in the sum of up to 21 million euros.
4. The Franchises impose various obligations on Delek Motors, including, inter alia, setups for sales and marketing, display, demonstration, product publicity, customer service, management of the garage and parts warehouse, provision of customer service, inventory maintenance, technical training for employees, etc. Delek Motors is also committed to operating and ensuring the quality of service and customer centers in accordance with the number of vehicles in Israel.
5. The forecast of the annual number of products to be sold by Delek Motors in the Territory will be determined by the parties at the start of each sales year, and if the parties fail to agree, it will be determined by BMW. The sales forecast will be determined, inter alia, on the basis of a market analysis and on the performance required in respect of customer service (except for the BMW Motorcycle Agreement where there will be a review of the past sales of Kamor Motors and of the options for developing business opportunities in Israel).
6. BMW has the right to change product prices at any time. Naturally, Delek Motors has the right to set the sales prices for end customers.
7. BMW has undertaken to provide a two-year warranty for its products commencing on the date of delivery to Delek Motors, subject to compliance with the terms of the Franchises. BMW may, at its discretion, apply the warranty, whether by replacing a defective product or whether by repairing it. Delek Motors has undertaken to provide the customer with a warranty which is not inferior to that of the manufacturer.
8. The Franchises are not transferable by Delek Motors to a third party unless with advance consent from BMW. Pursuant to the Franchise Agreements, a change in the identity of the owner of Delek Motors or in the composition of its shareholders requires advance written approval from BMW, except in the following instances: acquisition or sale of more than 10% of the holdings of Delek Automotive in Delek Motors, sale of shares as a result of which Mr. Gil Agmon is no longer the controlling shareholder in the Company, or any sale of shares as a result of which the holdings of Delek Investments and Properties Ltd. in the Company drop below 10%.
9. The Franchises are valid until February 28, 2015 (except for the Motorcycle Franchise which has no time limit), but the parties may terminate them in the event of a fundamental breach by one of the parties, as defined in the Franchises (e.g. insolvency of Delek Motors, or its application for a declaration of bankruptcy, Delek Motors engaged in activities requiring the prior consent of BMW without having obtained such consent, deliberate forgery of documents sent to BMW under the agreement, resale to suppliers which are not authorized under the agreement, liquidation, change in the ownership of Delek Motors and/or its senior management in a manner which does not allow for execution of the Agreement, etc.) immediately (subject to the exclusions listed in the Franchises). In the event of another breach BMW may terminate the Franchise by giving three months' notice (in the Motorcycle Agreement – six months) after it gave an

opportunity to remedy the breach in a period of up to six months. Moreover, each of the parties has the right to terminate the BMW Motorcycle Agreement by giving the other party one year's notice. BMW may within 60 days from the termination of the Agreement buy back from Delek Motors all or part of its products, subject to the terms set forth in the Agreement.

10. Moreover, Delek Motors has undertaken to be liable, jointly and severally with Kamor Motors, for any claim and liability arising from the franchise agreements preceding these agreements, between Kamor Motors and BMW, for the import and sale of BMW and Mini products. In particular, Delek Motors and Kamor Motors will be jointly liable for the supply of warranty services for all BMW and Mini vehicles and products sold by Kamor Motors. It was also agreed that the liquidation of Kamor Motors will not derogate from this liability of Delek Motors.

D. Husqvarna Motorcycle Agreement

On January 30, 2008, Kamor Motors, a wholly owned subsidiary of Delek Automotive, entered into a non-exclusive franchise agreement for the import into Israel of motorcycles with Husqvarna, a subsidiary of BMW ("**the Husqvarna Motorcycle Agreement**"). Husqvarna motorcycles, manufactured in Italy, are prestigious motocross motorcycles. This agreement is valid until March 31, 2012 and it is the intention of Delek Automotive to enter into a new franchise agreement in respect of these motorcycles. At the reporting date Delek Automotive's import of these motorcycles is not material.

1.14.16 Legal proceedings

- A. On September 4, 2007, Israel Police questioned Gil Agmon, CEO of Delek Automotive and Delek Motors, and Yoram Mizrachi, deputy CEO of Delek Motors, on suspicion, together with DMR Properties and one of its former officers, of bribing an engineer on the Lodim Local Planning and Construction Committee and making a false record in a corporation's documents, in connection with the construction of the Logistics Center at Nir Zvi. The CEO and deputy CEO were detained for two days and released on bail which expired at the end of the year. On December 12, 2010 the pair were notified by Israel Police that the Prosecutor's Office of the Central District had decided to close the investigation file. On December 11, 2011 the Prosecutor of the Central District announced that the file had been closed owing to insufficient evidence.
- B. On July 13, 2010 a motion was filed in the Tel Aviv District Court for certification of a class action against the subsidiaries Delek Motors and Delek Motors Parts (1987) Ltd. ("**the Defendants**"). The plaintiff argues that the Defendants dictate "standard hours" to their service centers for various services on cars at their service centers and require them to charge the customer for work according to the standard hours even though actual work hours amount to less than that. According to the claim, this type of agreement between the Defendants and the centers is a restrictive practice in contravention of the law, it undermines consumer rights and provides grounds to file a claim for damages against the Defendants.

The plaintiff is asking to represent all the owners of vehicles imported by one or more of the Defendants, who had their cars serviced at the Defendants' service centers and who were charged for labor at the centers according to the standard time (a predefined repair time for each job).

The amount of the plaintiff's personal claim is NIS 1,161 and the amount of the class action is estimated at NIS 168 million. The Defendants submitted their responses to the motion for certification as a class action on November 14, 2010, stating that they do not dictate labor time to their service centers, and in any event this is not a restrictive practice.

On February 21, 2010 a first pre-trial hearing was held in the case as a result of which and following an application from the plaintiff, the court ordered that the pleadings be sent to the Antitrust Commissioner and the Attorney General. In their response on March 16, 2011 the attorney of the Antitrust Authority announced that the Authority was precluded from expressing its opinion on the application and requested that the representatives of the Attorney-General be exempted from attending the hearings.

On July 5, 2011 the parties filed an agreed application for termination of the lawsuit by way of dismissal. According to the arrangement between the parties which was presented in the application in which the defendants declared that they do not dictate "standard hours" to the garages as actual labor hours. Furthermore, the defendants undertook that 30 days after approval of the arrangement they would send a circular to all the garages in order to clarify

once again that payment of labor costs would be charged on the basis of actual hours worked which are not to exceed the maximum stipulated by the manufacturer. The defendants also undertook, in accordance with the arrangement, not to bill the garages for the above-mentioned "standard hours". It was further agreed that the claimant would meet with the CEO of Delek Motors and present his position with regard to the relations between the customer and the respondents, in all matters pertaining to the subject of the claim and that the claimant would be awarded NIS 80,000 and his lawyers – NIS 118,000. The court reviewed the application and found that it contained certain elements of a settlement agreement and so he ordered publication of the application, in accordance with the law and the regulations, and that it be referred to the Attorney-General and court administrator. 45 days after publication of this application, the parties filed a court motion for validation of the judgment in favor of the settlement arrangement. On November 17, 2011 it was decided to approve the motion and grant the settlement arrangement the force of a judgment.

1.14.17 Objectives and business strategy

The primary goal of Delek Automotive is to increase the scope of its operations and profits. In this regard, on December 13, 2011 Delek Automotive completed the acquisition of Kamor Motors, importer and dealer of BMW vehicles in Israel. Since this date Delek Automotive has been focusing on the market segment of luxury cars and motorcycles. In addition to its goals of increasing its operations and profits, the Group is dedicated to making constant improvements in its service. In recent years Delek Automotive has implemented a number of measures to achieve these goals, among them centralizing its facilities at the Nir Zvi Logistics Center and upgrading its service centers (see section 1.14.6D)). In the next three years Delek Automotive is planning to upgrade its BMW facilities and merge the operations of Kamor Motors and its subsidiaries into the Delek Automotive Group.

1.14.18 An event or matter deviating from the Corporation's businesses

- A. On June 26, 2011 Delek Motors, a fully owned subsidiary of Delek Automotive, entered into two conditional agreements with Kamor and with Messrs. Joel and Ron Weiss and companies under their control ("the Weiss Group") for the acquisition of all their holdings in Kamor Motors (the agreements jointly: "the Acquisition Agreements"). The Acquisition Agreements were conditional, inter alia, on the receipt of approval from the Antitrust Commission of the transaction and the successful completion of a full tender offer for the acquisition of Kamor Motors shares which are not held by Kamor and the Weiss Group.
- B. The Acquisition Agreements also stipulated that upon completion of the transaction, the following agreements would be signed by Kamor Motors and the Weiss Group: A) an agreement under which all the holdings of Kamor Motors in Kamor – Rio Tnua Ltd. (through which Kamor Motors runs its tire operation) would be sold by Kamor Motors to the Weiss Group; B) an agreement under which all the holdings of Kamor Motors in Kamor Auto Ltd. (through which Kamor Motors runs its vehicle operation in Bulgaria) would be sold to the Weiss Group; C) an agreement under which the management services provided by the Weiss Group to Kamor Motors would be terminated. In addition, as part of the transaction, shares in Kamor Motors held by Toro Global (2001) Ltd. (the indirect controlling shareholder in Kamor) would be transferred, at no consideration, to Kamor Motors, so that Kamor Motors would hold 100% of the issued paid-up capital of Kamor Auto.
- C. On October 30, 2011 the Antitrust Commissioner approved the transaction provided that within one year from the date of the merger, all the holdings of Kamor Motors in subsidiaries holding a franchise to market vehicles manufactured by Chery Automobile Co. Ltd. are sold. As a result, Kamor Motors entered into an agreement with a third party to sell all its holdings in subsidiaries holding a franchise to market vehicles manufactured by Chery Automobile Co. Ltd. and the sale was completed on December 19, 2011.
- D. On November 8, 2011 the conditions precedent for implementation of the transaction were fulfilled, except for the successful completion of the full tender offer for the shares of Kamor Motors. In accordance with the provisions of the Acquisition Agreements, on November 13, 2011 Delek Motors published, together with Kamor and the Weiss Group, a specification for a full tender offer. On November 30, 2011 Kamor Motors reported receipt of the full tender offer and on December 5, 2011 it implemented a forced acquisition of the balance of Kamor Motors shares for which acceptance notices were not given, pursuant to article 337 of the Companies Law. On December 8, 2011 the shares of Kamor Motors were delisted and it became a private company.
- E. With the success of the full tender offer all the conditions precedent for implementation of the transaction were fulfilled and on December 13, 2011, Kamor and the Weiss Group transferred

all their holdings in Kamor Motors to Delek Motors and as of this date, Delek Motors holds 100% of the issued and paid-up share capital of Kamor Motors.

- F. On February 19, 2012 Kamor Motors Ltd. carried out a complete early redemption of its debentures (Series A) which were held by the public, after a meeting of the debenture holders held on January 31, 2012, approved an amendment to the deed of trust in such a way as to enable this early redemption. The early redemption totaled NIS 52,100,000. Upon its completion the debentures of Kamor Motors were delisted and Kamor Motors ceased to be a "reporting corporation", as this term is defined in the Securities Law, 1968.

G. Kamor Motors

At the report publication date, Kamor Motors, through its fully owned subsidiary Kamor Auto, imports and sells BMW vehicles and parts, including Minis and BMW and Husqvarna motorcycles manufactured in Italy (all in the BMW Group). All BMW products are luxury models in the premium vehicle market. Kamor Motors used to engage in other operations through subsidiaries which it sold shortly before or after the date of its acquisition by Delek Motors.

The vehicle market in Israel is characterized by a large number of importers which import numerous brands from around the world. In 2011, deliveries of luxury²⁵⁴ vehicles totaled 8,174, representing an increase of 7.2% compared with 2010. These figures are indicative of a steady rise in the luxury vehicle sector over the past few years. In recent years the numbers of vehicles imported into Israel by personal import have also been increasing, and in this category the overwhelming majority are luxury vehicles²⁵⁵. In 2011 the number of vehicles imported by personal import increased by 7.7% from 2,600 in 2010, to 2,800 (according to non-official figures published in the press). One of the conclusions of the Zelekha Committee was to recommend an expansion in the numbers of vehicles imported by personal import. Kamor Motors believes that full adoption of the conclusions regarding personal import and garages could have an adverse effect on the results of its operations.

BMW cars compete in the luxury car segment where each series competes with similar models of other manufacturers. In this entire segment BMW cars are in direct competition mainly with Lexus, Audi, Mercedes, Volvo, Jaguar, Hummer, Infiniti, Rover, Buick, Cadillac and luxury Volkswagen models. The Mini is a distinctive two-door niche car with a unique design and racing capabilities. Kamor Motors believes that the Mini, because of its high price in relation to its size, competes with other small cars with special design features and/or racing capabilities such as the Volkswagen Beetle and the Volkswagen Golf.

In 2011 the market share of BMWs, including the Mini and luxury SUVs, totaled 15.1% of the luxury car market compared with 15.42% in 2010. In 2011 the market share of BMW's totaled 19.7% of the market of its direct competitors which consisted of the corresponding models of Audi, Mercedes, Volvo, Lexus and luxury Volkswagens, compared with a market share of 18.4% in 2010. Kamor Motors handles the competition in this segment by increasing its sales promotion and marketing activities and bolstering the trade-in service offered to its customer. As a rule, there is no seasonality in the car industry. However, in the last quarter of every year, there is a non-material slump in sales owing to the fact that customers wait for the next year's models.

Kamor Motors is dependent on BMW, the manufacturer of the vehicles it imports into Israel. Through Kamor Auto it entered with BMW into franchise agreements for the import into Israel and sale of its vehicles, original accessories and parts. In addition to the franchises Delek Automotive is expected to receive for the import and sale of BMW's and Minis and BMW motorcycles, as described above in section 1.14.14(C). In March 2012, Kamor Motors is expected to enter with BMW into agreements for the termination of the franchises under the franchise agreements of Kamor Auto.

In 2011 and in 2010 the revenues of Kamor Motors totaled NIS 500 million and NIS 482 million, respectively. In 2011 and in 2010 the gross profit of Kamor Motors totaled NIS 30 million and NIS 55 million, respectively. In 2011 and in 2010 the assets and liabilities of Kamor Motors totaled NIS 278 million and NIS 506 million, respectively.

1.14.18 Expected developments in the coming year

²⁵⁴ A luxury vehicle is defined by Kamor Motors on the basis of its price and category. The following brands are usually referred to as luxury vehicles: Porsche, Mercedes, Jaguar, Hummer, Infiniti, Rover, Volvo, Audi, BMW, Lexus, Buick, Cadillac.

²⁵⁵ These data are to the best of the knowledge of Delek Automotive and they are taken from a report of the Zelekha Committee published at: <http://media.mot.gov.il/DOVER/zilha-doch.pdf>

In the last quarter of 2011 Delek Automotive launched the new model of the Ford Focus to great acclaim. In 2012 it is expected to launch the new Ford Transit. Mazda is also about to launch its SKYACTIV Technology automobiles. The enormous benefit of this unique innovative technology is that these vehicles consume less fuel and emit fewer pollutants. The first car from this range to reach Israel will be the CX-5 SUV which is expected to launch in April 2012. Delek Automotive has announced its strategic plan in cooperation with BMW whereby supply of its models will be substantially expanded and aggressive pricing is expected to change sales customs in Israel's luxury car segment.

Furthermore, after completing the acquisition of Kamor Motors, the Delek Automotive Group began importing, marketing and selling BMW motorcycles and scooters. The Company recently announced its strategic plan in cooperation with BMW. It will carry out a significant expansion of the models it sells and its introduction of aggressive pricing is expected to change sales practices in the luxury car segment.

1.14.19 Risk factors

A number of risk factors could threaten the operations of Delek Automotive:

A. Dependence on manufacturers

Delek Automotive is completely dependent upon the manufacturers of the cars it imports. Under its agreements with the manufacturers, Delek Automotive is required to comply with certain conditions. The Ford agreement is unlimited in time and may be terminated as described in section 1.14.14(B). The Mazda agreement is valid for three years as noted in section 1.14.14(A). The BMW agreement, the BMW motorcycle agreement and the Mini agreement will be valid for three years and the BMW motorcycle agreement is unlimited in time as described in section 1.14.14(C). The Husqvarna agreement is valid until March 31, 2012 and the Company is expected to enter into a new franchise agreement with Husqvarna which will be unlimited in time, as described in section 1.14.14(D). In addition, the parties may terminate these agreements as provided therein. Non-renewal or termination of the agreements will have a material impact on the operations of Delek Automotive. In addition, Delek Automotive is dependent on the manufacturers' models and pricing structure. If the manufacturer produces more expensive models, this could affect the financial results of Delek Automotive. Furthermore, given the global economic crisis which is affecting the car manufacturing industry, if one of the manufacturers whose vehicles are imported by Delek Automotive were to halt its operations either completely or for a lengthy period (including as a result of force majeure), this could have a material effect on the business of Delek Automotive.

B. Changes in the exchange rates of the importing countries

Most of Delek Automotive's expenses are in foreign currency, while its revenues are in shekels and therefore it is exposed to fluctuations in the currency exchange rates. Revaluation of these currencies against the shekel could result in a decline in the profitability of Delek Automotive.

C. Changes in foreign currency rates relevant to competitors

The exchange rate component in the price of Delek Automotive products is 85-90% of the selling price of those products. Therefore, if foreign currency exchange rates relevant to the competitors remain unchanged or depreciate while currencies relevant to Delek Automotive appreciate, the competitive ability of Delek Automotive will be impaired.

D. Changes in bank interest rates in Israel and abroad

A large part of Delek Automotive's bank credit is at variable interest, which is a function of bank interest in Israel and abroad. Therefore, Delek Automotive is exposed to changes in the bank interest in Israel and abroad.

E. Customer credit

Delek Automotive's sales to institutional customers are partially accomplished using credit, as is common in the automotive industry. The credit is not fully secured and is concentrated among a few customers with a large volume of sales. Therefore, failure by one such customer to repay the credit can specifically affect Delek Automotive's cash flow and business results. At December 31, 2011, NIS 518 million of the total customer debt (amounting to NIS 669 million) is concentrated among five customers of which two are controlled by the same entity. At December 31, 2011 approximately NIS 40 million of total customer debt is partly secured

and NIS 629 million is not secured at all (see section 1.14.4(A)). At the report publication date, the Company has customer debts totaling NIS 120 million secured by liens.

F. Reducing centralization in the vehicle market

As described in section 1.14.2(B), in recent years the Ministries of Finance and Transport have been taking steps to reduce centralization in the vehicle market in Israel and to remove market barriers by means of tax reforms, standardization and regulation of vehicle imports. After implementation of its new strategy, Delek Automotive estimates that in the short term, these changes will not have a significant effect on the Group's operations, since parallel and personal import of cars imported by the Company are not economically viable.

G. Competition in the sector of operations of Delek Automotive

As described in section 1.14.6, Delek Automotive faces competition in the segments of its operations. If new competitors selling vehicles in Delek Automotive's market segments enter the market and/or new models are introduced into these segments and compete with the models sold by Delek Automotive, or if these models are sold at competitive prices, this competition could affect the results of Delek Automotive and its market share. In addition, there is intense competition in the vehicle parts market which could affect the results of Delek Automotive in this segment. Furthermore, in recent years, electric cars and hybrid vehicles combining an internal combustion engine with an electric motor have been introduced into the market and this leads to reduced gasoline consumption. Delek Automotive does not believe that these vehicles constitute significant competition for its vehicles in the family category. However, as explained in section 1.14.2(B) above, these vehicles are receiving encouragement and support from government authorities and this is likely to increase demand. Furthermore, automobile and other entities have recently been developing electric cars. Delek Automotive does not anticipate material expansion in this segment in the near future. For the recommendations of the Zelekha Committee with regard to increasing competition and reducing centralization in the automobile segment, see section 1.14.2(1)(B).

H. Economic slowdown in the Israeli and/or global market

The volume of economic activity in Israel is affected by political, security and macroeconomic factors. An economic slowdown in the Israeli economy could affect the volume of vehicle sales in Israel and have a negative impact on the business results of Delek Automotive. However, in recent years, despite the economic slowdown in the Israeli market, Delek Automotive has successfully established its position as one of Israel's leading car importers, although in 2011 its competitive ability was moderately harmed by changes in its import currencies compared with the import currencies of its competitors. Since the last quarter of 2008 the economic slowdown in the Israeli economy caused by the global economic crisis has been of a severity not witnessed for decades. This slowdown, combined with forecasts of falling prices (see section 1.14.2(C)), resulted in a significant decrease in vehicle deliveries in the last quarter of 2008, a trend which continued in the first half of 2009 and was halted in the second half of the year. In 2010 the growth trend continued and there was a noticeable improvement in economic activity in the market. The growth trend slowed in 2011. The slowdown could also raise customer credit risk levels and thus have an adverse effect on the profitability of Delek Automotive, caused both by a decline in sales and larger price reductions.

I. Regulatory changes

Changes in regulatory arrangements that apply to the vehicle industry, such as changes in the government taxation policy, changes in policy for classifying vehicles as private or commercial for tax purposes, or changes in the policy for the use value of a leased vehicle for employee use, could lead to a change in the demand for various types of vehicles and affect the results of Delek Automotive's operations. For details of these changes, see section 1.14.2(B).

J. Changes in the management or control of Delek Motors

Under the Ford agreement, any change in the direct or indirect control or active management of Delek Motors as set forth in the Ford Agreement gives Ford the right to terminate the agreement, (see section 1.14.14(B)). Furthermore, Ford has the right to terminate the agreement, *inter alia*, if the court convicts Delek Motors, Delek Automotive, Yitzhak Sharon (Teshuva) or Gil Agmon of violation of the law or any other action unbecoming for reputable business executives. Furthermore, under the Mazda agreement, the Manufacturer is entitled to terminate the agreement at any time by written notice to Delek Motors, if the Manufacturer decides that it is unable to continue business with Delek Motors because of death, incapacity, disregard or any change in the management of Delek Motors or as a result of a change in the

legal or organizational structure of Delek Motors or in the case of a material change in the composition of the company's shareholders or investors.

Below is a summary of risk factors by type (macro risks, industry-wide risks and risks specific to Delek Automotive), rated according to the estimates of Delek Automotive's management by the degree of impact on Delek Automotive's business: major, medium or minor impact.

	Impact of risk factors on company operations		
	Major effect	Moderate effect	Minor effect
Macro risks	Changes in the exchange rates of the currencies of the importer countries	Economic slowdown in the Israeli and/or global market	Changes in bank interest rates in Israel and abroad
Industry-wide risks	Changes in rates of currencies used by competing importers Reduction of market centralization Regulatory changes	Customer credit Competition in Delek Automotive's areas of operation	-
Risks specific to Delek Automotive	Dependence on manufacturers	Changes in the management or control of Delek Automotive	-

The above analysis of the risk factors is based solely on estimates, and the actual effect on Delek Automotive's operations might differ.

1.15 **Additional Information**

1.15.1 **Biochemicals**

The Group holds 76.37% of the shares in Gadot Biochemical Industries Ltd. ("Gadot"), a public company whose debentures are traded on the Tel Aviv Stock Exchange^{256 257}. Gadot is engaged in

²⁵⁶ On July 25, 2004, an agreement was signed between the Company and ORL, which at the date of the report holds 23.07% of Gadot's issued and paid-up share capital (the Company and ORL are to be referred to jointly in this footnote as the "Parties") ("Voting Agreement") (as amended on May 16, 2005). The Voting Agreement stipulates that as part of the cooperation between the Parties as shareholders of Gadot, the Parties will do their utmost to solidify and agree upon positions ahead of time regarding any matter related to Gadot and brought for a vote to its general meeting, guided by the best interest of Gadot and subject to the unconditional provisions of any law. Several issues were defined to require the unanimous agreement of the Parties. Should they not reach such agreement, they will vote at the general meeting such that they comply with the provisions of the Voting Agreement. It was agreed that as long as the Voting Agreement is in effect, neither of the Parties will enter into a voting agreement and/or hold custody of and/or coordinate permanently with a Gadot shareholder that is not a party to the Voting Agreement, unless agreed to by the other Party. Provisions were drafted regarding the appointment of directors (ORL is entitled to recommend the appointment of two directors and Delek Investments is entitled to recommend the appointment of five directors. The Parties undertook to support the appointment of the directors recommended by the other Party. One director recommended by ORL will serve on each committee of the Board of Directors). Additionally, the Agreement sets out provisions regarding the right of first refusal and tag along right in cases of the transfer of shares to a third party and that in the event of the appointment of a liquidator/receiver/trustee for any of the Parties, the provisions of the Voting Agreement will apply to the Gadot shares transferred to his possession. It was further agreed that if the holdings of any of the Parties are lower than 15% of Gadot's share capital, the other Party will have the right to provide written notice of cancellation of the Voting Agreement, which will enter into effect 48 hours from the date of receipt of the notice.

²⁵⁷ In accordance with a full tender offer from August 30, 2011, Delek Investments acquired 1,891,003 ordinary shares of NIS 0.1 par value each in Gadot, which represent 10.27% of its issued and paid-up capital. This tender offer contains conditions for implementation of a forced sale pursuant to Article 337(A) of the Companies Law. After this tender offer, Delek Investments holds 76.37% of Gadot's issued and paid-up capital and ORL holds 23.63% of Gadot's issued and paid-up capital. In view of the above, on September 15, 2011 the shares of Gadot were delisted from the stock exchange and on September 21, 2011 Gadot ceased to be a public corporation and became a private company as these terms are defined in the Companies Law. When Amendment 17 to the Companies Law took effect on February 17, 2012, it became a debentures company. Following an ordinary tender offer from August 30, 2011, Delek Investments acquired 72,575 option warrants of Gadot which are exercisable into Gadot ordinary shares of NIS 0.1 par value each (in this footnote: "the Option Warrants"), and following a tender offer from September 25, 2011, Delek

the manufacture, marketing and sale of crystalline fructose for the food industry, as well as of citric acid, salts and other products, primarily for the food, pharmaceuticals and detergent industries and also in the manufacture, marketing and sale of ingredients for nutritional supplements.

A. Gadot has four principal areas of operation:

1. Fructose - The manufacture, marketing and sale of crystalline fructose and of tri-sodium citrate which is a byproduct of the fructose production process. Most of Gadot's fructose sales are to Europe, for the food industry. Fructose (fruit sugar) is a monosaccharide (derived by separating sugar into its two components: fructose and glucose), and which undergoes various processes until it becomes crystalline fructose. The company produces crystalline fructose for the food and beverage industry as a premium sweetener – fructose has properties that make it preferable to sugar, such as a more concentrated sweetness, slower decomposition in the digestive system, high solubility and enhancement of fruit flavors. It is therefore used in the food industry, especially for sweets, jams, baked goods, ice creams and more. In addition, Gadot produces a citric acid known as trisodium citrate (TSC) from the glucose solution byproduct of the fructose manufacturing process, which is primarily used in the food and beverage and detergent industries.
2. Citric acid and salts produced in Israel - The production of citric acid and salts (citric acid salts and phosphoric acid salts). Citric acid is produced in the West by a small number of large manufacturers and in China by several large and a few smaller manufacturers, who together produce a quantity larger than that produced by the large manufacturers in the West. Gadot produces citric acid which is used in the food industry (primarily in soft drinks) and as a raw material in the detergent and pharmaceuticals industries and for other applications. Gadot also produces citric acid salts for the food industry (soft drinks, calcium supplements, food enhancement, food supplement extracts sold “over the counter” in health food shops and for other uses) and for the paper industry. Gadot's citric acid and citric acid salts, manufactured at the facility in Israel, are marketed by Gadot in the United States, Europe, Israel, Asia and South America.
3. Citric acid produced in China - In March 2007, Gadot began constructing and operating a facility for the production of citric acid in China through a Chinese subsidiary (99%). Unlike the fermentation technology used by Gadot in Israel, which requires the use of a clean processed raw material such as sugar or starch, the fermentation technology in the Chinese plant is based on cassava which is a cheaper and “rawer” raw material and undergoes a biochemical process of fermentation and purification until the final citric acid product is obtained. Through the date of the report, Gadot had invested USD 70.6 million in the cost of constructing this facility. In the first quarter of 2010, the test run of the facility was completed and the facility began commercial production in the second quarter of 2010. The product of the Chinese plant is sold to Gadot's customers in Israel and the rest of the world, except for the US. Since the start of its operations, the Chinese plant has sustained continuing losses caused mainly by a significant rise in the price of its raw materials (primarily cassava), levies imposed on citric acid producers in China who export to Europe, the US and Canada, and difficulties in raising funds to finance the ongoing operation. Gadot stepped up its efforts in an attempt to bring the Chinese plant to profitability and it also provided significant financial resources, management support and assistance in planning and operating its facilities. Nevertheless, the Chinese plant continues to make losses. This is due principally to an ongoing substantial rise in the prices of raw materials (mainly cassava) and energy, compared with the forecast made in the first business plan, failure to find alternative sources of production, the levies imposed on the Chinese producers of citric acid after the start of the plant's construction and difficulties in raising funds to finance current operations. In addition, at the end of 2011, there was a substantial fall in the selling prices of citric acid. As a result, and owing to the substantial financing needed to continue the Chinese operation despite the limited financial resources available to Gadot and the difficulties in obtaining credit in China to finance the operation, on March 29, 2012, Gadot's board of directors decided to make meaningful reductions in the plant's activities and consider how to proceed with the

Investments acquired 249,480 Option Warrants. The remaining 37,945 Option Warrants, whose owners failed to respond to this tender offer, expired on November 7, 2011.

Chinese operation. Consequently, in its statement of income, Gadot has made impairment provisions in the amount of USD 61.1 million which is the value of most of the assets of the Chinese subsidiary. For further details, see note 17 to the Company's financial statements.

4. Ingredients of nutritional supplements - The manufacture, marketing and sale of nutritional supplements and the processing of ingredients for the dietary supplements market. Gadot commenced operation in this segment in June 2007, with the acquisition of 85% of the US company Pharmline Inc. ("Pharmline") in consideration of USD 11.3 million (total acquisition cost – USD 12.2 million)²⁵⁸. The dietary supplements market includes over-the-counter nutritional supplements sold in health food stores and pharmacies. Pharmline manufactures and processes ingredients used in the manufacture of dietary supplements, and most of its sales are in North America. Most of its revenues stem from the supply of processing services on a subcontracting basis and the manufacture and marketing of products, and the remainder from the sale of products manufactured by other manufacturers (finished products which are not self-produced) The products and services it sells include minerals, vitamins, vitamin and mineral blends for the enriched food industry, arthritis products, natural extract products, oils, nutritional supplements and processing services.
- B. Gadot's plant in Israel stands on land it owns in Haifa Bay, near the Kishon River. All of Gadot's production facilities are at this location, including the fructose production facility and facilities for the production of citric acid, salts and other products as well as a facility for refining raw sugar, which was constructed in cooperation with Tate & Lyle ("T&L"). Construction was completed in 2008. Since the second quarter of 2011 and at the reporting date, the sugar refining facility has not been operational because of a strategic decision by T&L to quit the sugar sector. T&L has stopped supplying raw materials to the plant. At the reporting date, Gadot is negotiating with T&L to preserve the facility so that its operation may be resumed at a future date. Since the third quarter of 2009 through mid-2011, the facility supplied most of Gadot's sugar requirements for its operation and owing to the stoppage Gadot has had to purchase sugar at much higher prices. Pharmline's operations are conducted in Orange County, in New York, which is the location of its offices, laboratories, production area, pharmacy and storage, reception and delivery areas. The citric acid production activity in China is carried out at a facility located in an industrial park in the Yancheng District, in a less developed northern area of the Jiangsu province, and was built on an area of 266,000 sq. m. for which Gadot has a 50-year lease. The plant in China has manufacturing facilities, control equipment and devices, IT systems, furniture and vehicles. At December 31, 2011, Gadot employs 183 people at its facility in Israel, 82 people work at Pharmline and a team of 248 are employed at the citric acid plant in China.
- C. Gadot's financial position
1. In 2010 and 2011 Gadot's revenues totaled USD 139 million and USD 148 million, respectively. In 2010 and 2011 its gross profit totaled USD 17 million and USD 3 million, respectively, and its net profit (loss) totaled USD (17) million and USD (103) million, respectively.
 2. At December 31, 2011 Gadot had a working capital deficit of USD 45.7 million stemming primarily from long-term and short-term liabilities undertaken to finance long-term investments which will be repayable next year. Gadot is looking into a number of options for raising financing (including taking loans from Delek Investments and ORL), and Gadot's management believes it has the option of disposing of assets if necessary. In November 2009, Delek Capital and ORL informed Gadot that should it lack financial resources to meet its obligations, they would provide it with financing in a maximum amount of USD 20 million (relative to the ratio of their holdings) ("the Original Support Amount"). In April 2010, Delek Investments and ORL injected USD 6.6 million and USD 2.3 million, respectively, and in May 2011 Delek Investments and ORL injected USD 3.5 million and 1.3 million through an equity investment in Gadot as part of its rights issue.

²⁵⁸ On January 2, 2009 Gadot's holdings in Pharmline increased to 90% as a result of exercise by a minority shareholder in Pharmline of a put option in consideration of USD 665,000; on December 30, 2010 the remaining shares in Pharmline were purchased in consideration of USD 3.2 million, following exercise of a put option by the CEO and founder of Pharmline.

3. ORL notified the company that its undertakings to exercise rights as part of the company's rights issue based on its shelf prospectus report from April 2010 and April 2011 are part of its actions to assist Gadot by providing this financing. On August 25, 2011, Delek Investments announced that it was updating the sum of the Original Support Agreement to USD 28 million ("the Updated Support Amount"). After the sum of the updated amount had been used in its entirety, on November 28, 2011, Delek Investments sent Gadot a new letter of support valid until December 31, 2012, stating that if Gadot does not have the financial resources to meet its obligations, Delek Investments will provide financing in a maximum amount of USD 19 million ("the Additional Letter"). On March 29, 2012, Delek Investments sent Gadot a new letter of support which replaces the previous one, stating that if Gadot does not have additional resources to meet its obligations in the next two years (from January 1, 2012), Delek Investments will provide it with financing in the sum of USD 48 million ("the New Support Amount"). Since 2011 and up to the reporting date, Gadot has obtained loans totaling USD 47 million from Delek Investments. Of these loans, the sum of USD 5.6 million was granted on account of the New Support Amount. Each of these loans was granted without collateral and each of them bears annual interest of Libor + 3.5% and is repayable (principal and interest) on January 1, 2014. At the report publication date, the balance of the additional amount which has not yet been used by Gadot amounts to USD 42.4 million. The specific terms relating to the receipt of the remaining funds from Delek Investments under the New Support Amount have not yet been formulated and Gadot intends to enter into a framework agreement with Delek Investments in order to regulate the financing terms.
4. After approval of Gadot's financial statements on March 29, 2012, it became clear that Gadot is not in compliance with the financial covenants which are part of its USD 15 million loan agreement between it and a number of financial entities from the Harel Insurance Investments and Financial Services Ltd. Group ("Harel") from June 2010. As a result and in accordance with the terms of the agreement, Harel has the right to call in the loan (which at the reporting date stands at USD 15 million). As a result, in its financial statements at December 31, 2011, Gadot presented this loan as part of its current liabilities (current maturities). At the reporting date, Gadot believes, based on conversations it has had with Harel regarding its noncompliance with the above financial covenants, that at this stage Harel will not call in the loan. However, Gadot's noncompliance with these covenants constitutes grounds to call in other loans taken by Gadot and/or its subsidiaries owing to the cross-default clauses in the loan agreements to which Gadot and/or its subsidiaries are party. At the reporting date, the other loans which might be called in as a result of Gadot's noncompliance with the financial covenants total USD 36 million.

1.15.2 Water desalination

The Group's desalination operations in Israel and other countries are carried out through IDE Technologies Ltd. ("IDE"), a private company held by the Group (49.8%), Company CEO Asaf Bartfeld (0.2%) and Israel Chemicals Ltd. ("ICL") (50%). The Group and ICL entered into an agreement that sets out their relationship as shareholders in IDE and includes provisions regarding the appointment of directors at IDE. The agreement further stipulates that decisions on specific issues (such as a change in IDE's areas of activity, its merger or liquidation, appointment or laying off of a CEO and distribution of dividends over and above 50% of IDE's net profit) will require a special majority on the Board of Directors and at the IDE general meeting. Additionally, the agreement sets out provisions regarding instances where IDE requires additional funds to finance its activity, also including investments of the parties in IDE, if necessary. It also sets out provisions regarding the resolution of disputes between the parties (a dispute resolution mechanism was stipulated and should the parties fail to resolve the dispute, each party will be able to invoke the BMBY clause), as well as provisions regarding the right of first offer and tag-along right.²⁵⁹ In addition, IDE has a management agreement with Delek Infrastructure and ICL, pursuant to which management and consulting services are provided to IDE in return for a management fee.

IDE is engaged in the design, construction and sale of sea water desalination facilities, construction of turnkey and EPC desalination plants, operation of desalination facilities and development, construction and operation of sea water desalination facilities and projects using the BOT (Build,

²⁵⁹ It should be noted that these provisions are also set out in the IDE Articles, and in any event, in case of a discrepancy, the provisions of the shareholder agreement shall prevail.

Operate, Transfer)²⁶⁰ and BOO (Build, Operate, Own)²⁶¹ methods. IDE also engages in activities on a much lower scale than its desalination operations. These are in areas related to desalination and they include the design and supply of industrial evaporators, industrial cooling systems and snow and ice-making machines.

In addition to the foregoing, one of IDE's activities is the provision of services and sale of equipment and chemicals to various desalination facilities.

General

Desalination is the process of removing salts and minerals from brackish water and sea water to produce high-quality water for industrial use and potable water. Desalination can also be used in the treatment of industrial and municipal wastewater.

There are two main desalination methods: (1) Thermal desalination - conducted through an evaporation process, in which the water gradually evaporates through a passage between a number of cells, each time at a lower temperature and pressure. In each cell, a certain amount of water is evaporated, while the salts remain in the water that does not evaporate and are removed as brine or concentrate. The water vapor undergoes a condensation process which in the end yields desalinated water. This is the oldest method of desalinating water but it consumes a great deal of energy; (2) Membrane desalination (reverse osmosis) - is mainly performed through a process of reverse osmosis using membranes. In this process, the water is forced under high pressure through membranes that allow only the water to pass through them. The salts that are concentrated on the other side of the membrane are discharged as brine or concentrate. At present, membrane desalination is the most common, being significantly less expensive than thermal desalination owing to lower energy consumption. However, the water is not as pure, and the desalination is conditional upon treatment of the water prior to desalination.

The desalination activity is subject to regulation that includes standards and procedures, most of which are related to water health, safety and environmental protection. The laws and regulations differ depending on the location of the activity and include the following: (1) guidelines for the prevention of water pollution and protection of the environment; (2) regulation of emissions into the air, water and soil, including the discharge of brine; (3) production, import, sale, storage, transport and use of certain materials and products; (4) generation, storage and disposal of waste; (5) tort law, including with respect to property damage and bodily harm, and the health and safety of employees and third parties; (6) guidelines regarding the quality of desalinated water. (7) monitoring and setting quotas for water production and use by the authorities. Additionally, since most project agreements are the result of winning a government or other tender, the activity is subject to the rules of the relevant tender.

Desalination in Israel and around the world

The use of desalinated water is designed as an alternative to natural fresh water and, therefore, the extent of desalination activity around the globe depends, to a large extent, on the supply of and demand for drinking water. Among other things, these are influenced by factors such as the severity of the shortage of fresh water; population growth rate; increase in the standard of living and industrialization, regulation of industrial waste and disposal of wastewater; natural phenomena that cause irregularities in the supply of water, costs of desalination, economic conditions and ability to invest in desalination plants.

According to Global Water Intelligence (GWI)²⁶² data, the amount of desalinated water around the world grew from 40 million m³/d in 2005 to 65 million m³/d in 2010. GWI estimates that in 2015, the amount of desalinated water will rise to 100 m³/d, and the global market for desalinated water will reach USD 10 billion annually within the next five years. However, not all of the global desalination markets are accessible to IDE, as a significant portion are located in Arab countries in the Middle

²⁶⁰ Under this method, IDE enters into an agreement with a customer. It constructs a desalination plant, operates it and sells the product or its services to the customer at a price agreed in advance in the contractual period and this price also includes the operational costs. At the end of the contractual period the plant becomes the property of the customer.

²⁶¹ Under this method, IDE enters into an agreement with a customer. It constructs a desalination plant, operates it and sells the product or its services to the customer at a price agreed in advance in the contractual period. During this period the plant is the property of IDE and it bears all the operational costs. At the end of the contractual period the plant becomes the property of the customer.

²⁶² A private entity which analyzes desalination market data and provides consulting services to the Company. For details, see <http://www.globalwaterintel.com>.

East (approximately 50% of the desalinated water in 2010). The desalination markets accessible to IDE will be referred to as the "accessible markets."

Desalination began in Israel at the beginning of the 1960s, with the construction of the desalination facility in Eilat. Over the years, the field has developed significantly in terms of technology, and total activity has grown, with the major desalination facilities so far built in Israel being the ones in Ashkelon, Palmachim and Hadera. In accordance with the targets and quotas set by the government, additional desalination plants are slated for construction in Israel. The two that are supposed to begin operations in the coming years are the desalination plant in Ashdod, scheduled to begin operation in 2013, with an annual capacity of 100 million m³, and the Sorek desalination plant that will be the largest in Israel, providing 150 million m³ a year, as of 2013. Mekorot is in charge of construction of the plant in Ashdod, and Sorek Desalination Ltd. (SDL), jointly owned by IDE (51%) and Hutchison Water International Holdings Pte (49%), was awarded the tender for construction of the Sorek plant. According to data from the Israel Water Authority²⁶³, total desalination activity in Israel in 2005 was 36 million m³ and in each of 2010 and 2011 it was 300 million m³ a year. According to decisions made by the Israeli government, the annual quantity of desalinated water is expected to reach 590 million m³ and 750 million m³ in 2013 and 2020, respectively. According to data from the Israel Water Authority, IDE (through subsidiaries) currently operates desalination plants (in Ashkelon and Hadera), which produce 83% of all desalinated water in Israel.

Competitive standing

A global pioneer and leader in water desalination, IDE has been active in the field for the past 45 years. IDE has executed close to 400 projects in over 40 countries, including Israel, India, China, Australia, various countries in Europe, North America, Latin America and the Caribbean. In the field of thermal desalination, IDE is a leading company, with rich experience in the design and construction of over 320 desalination plants of this type. Based on analysis of GWI data, IDE believes that its share of the thermal desalination market in the accessible markets and worldwide is 75%. IDE's primary markets in this field today are China and India because of the high level of pollution in the seawater and high availability of surplus heat from industrial sources. The membrane desalination field is characterized by long-term BOT projects, and IDE has built and is currently operating (through subsidiaries) two of the world's largest membrane desalination plants, in Ashkelon and Hadera. To the best of IDE's knowledge, its main competitor in the thermal desalination market is Veolia. To the best of IDE's knowledge, its main competitors in the membrane desalination market are Veolia and Degremont.

Human capital, property plant and equipment, marketing

IDE's headquarters are located in Kadima, Israel, where IDE leases 5,500 m² in office space. Additionally, IDE purchased 20,000 m² in the Haifa Bay area, where it is building a logistics center that includes warehouses, open storage areas and areas for assembly and operation of the facilities. Additionally, IDE has several small offices in the USA, China, India and in other places as well.

As of December 31, 2011, IDE had 400 employees (including in wholly owned subsidiaries), a large number of whom are university graduates with knowledge and experience in the water industry. Marketing of services and products is done through the physical presence of IDE employees in main markets and through a global system of agents. As part of its marketing activity, IDE visits potential customers, consultants and contractors and prepares budgetary quotes and plans for the execution of projects by identifying customer needs and presenting efficient solutions that meet their needs.

Technological developments and work methods

IDE's main work methods in desalination projects are as follows:

EPC (Engineering Procurement and Construction) projects: IDE specializes in the design and construction of desalination facilities. As part of this activity, in which the customers are generally industrial factories, IDE turns the plant over to the customer immediately after completion, and the customer then operates it. To date, IDE has designed, built and handed over 400 plants around the world, including one in Sardinia, Italy. This plant was handed over in 2000 and is the largest thermal desalination plant using the mechanical vapor compression distillation method. It produces 17,280 m³/d. IDE also constructed the desalination plant in Jamnagar, India which is the largest in

²⁶³ As stated on the website of the Israel Water Authority: www.water.gov.il/hebrew/Pages/home.aspx.

India. In 1998, 2005 and 2008 nine desalination units with a daily capacity of 160,000 m³/d were constructed there. IDE also constructed the desalination plant in Las Palmas, Spain which was handed over in 2000 and has an output of 35,000 m³/d. There is also the plant in Tianjin, China which was handed over in 2010 and is the largest in China. At the reporting date it has four thermal desalination units whose total output is 100,000 m³/d. As described below, in 2010 IDE started construction of an additional four desalination units which are scheduled to become operational in 2012.

BOT (Build, Operate, Transfer) projects: Under long-term agreements, IDE builds and operates the plants and sells the water produced at a fixed price per cubic meter for the term of the agreement. IDE currently operates and sells desalinated water from three plants it built in this manner - in Hadera, Ashkelon and Larnaca (Cyprus).

The average EPC project lasts between one and three years, while a typical BOT project, which lasts between 10-25 years, changes the project financing and imposes a large portion of the risk on the company performing the construction and operation.

Most of IDE's revenues are attributable to construction - in other words, EPC projects and the construction phase of BOT projects, which constituted 86%, 58% and 72% of its total revenues in 2009, 2010 and 2011, respectively. The balance of its revenues is attributable to the sale of water and provision of operation and maintenance services

IDE's main projects

As mentioned above, over the years, IDE has designed and handed over 400 plants of varying sizes and capacities. At the reporting date, IDE is currently the operator of four plants and has contracts for the construction of six projects, slated for completion in the coming three years²⁶⁴.

Major BOT projects completed by IDE, in which IDE continues to provide operating and maintenance services:

- A. Desalination plant in Larnaca, Cyprus - This plant was built by a partnership controlled by IDE (IDE has a direct holding of 95% and the remaining 5% is held by a wholly owned subsidiary of IDE), which was awarded a tender by the Cyprus Water Authority. Construction of the project was completed in July 2001 at a cost of NIS 181 million. In 2008, an agreement was executed with the Cyprus Water Authority to expand the facility and therefore, its capacity is now 65,000 m³/d per day (approximately 21.5 million m³ annually). The original agreement was for the partnership to operate the plant for 10 years, through July 2011 and it was later extended until June 2012 with an extension option until September 2012.
- B. The desalination plant in Ashkelon, Israel - VID Desalination Ltd. in which IDE holds 50% of the shares, and Veolia Water 50%. In November 2001, VID was awarded the tender issued by the State of Israel for construction of the plant through a BOT scheme, and the plant was completed in 2005, at a cost of NIS 1.1 billion. The concession period is for 25 years, and it is to be transferred to the State of Israel, without consideration, in June 2027. The plant is operated and maintained by ADOM (Ashkelon Desalination) Ltd., a company in which IDE holds 40.5%. It is one of the largest reverse osmosis desalination plants in the world, and its desalination capacity was recently increased to 120 million m³ annually. Revenues of IDE subsidiaries engaged in the operation of this plant are from the sale of desalinated water and the provision of operation and maintenance services. IDE benefits from the distribution of dividends by VID and ADOM.
- C. The desalination plant in Hadera, Israel - In September 2006, H2ID Ltd., a company 50% owned by IDE and 50% owned by Shikun & Binui Ltd., was awarded a tender issued by the State of Israel to design, finance, construct, operate and maintain a desalination plant in Hadera, with a total annual capacity (after expansion) of 127 million m³. It is currently the largest reverse osmosis desalination plant in the world. The concession term is 25 years (consisting of 2.5 years of construction and 22.5 years of operation and maintenance), at the end of which the plant will be handed over to the State of Israel free of charge. The facility is operated and maintained by OMIS Water Limited, a company in which IDE holds 60%. The plant began operations in 2010. Revenues of IDE subsidiaries established for the project are from the sale of desalinated water and provision of operation and maintenance services. IDE benefits from the distribution of dividends by H2ID and OMIS.

²⁶⁴ In 2011, IDE entered into agreements for two additional projects for construction of an ice plant and a thermal plant in sums which are not material to IDE.

Projects under constructions as of December 31, 2011:

Location and date of contract	Brief description of the project	Estimated capacity (m ³ /d)	Rate of holding in the project	Target date for completion
Tianjin, China June 2007 (initial contract); May 2010 (second contract)	The original contract - construction of four thermal desalination plants. The second contract - construction of another four thermal units.	Total 200,000 (at the reporting date the output of the existing 4 units is 100,000)	100%	2012 The first four units were completed in 2010
India, May 2008	Delivery of two thermal desalination plants	50,000	100%	2011 (at the reporting date project construction had not been completed; by the end of 2011 95% had been completed)
Western Australia, July 2008	Design and delivery of a reverse osmosis desalination plant	140,000	100%	2012
Sorek, Israel; September 2009	Construction and operation of a desalination plant by Sorek Desalination Ltd. ("SDL") for 26 years under a BOT agreement with the State of Israel. Desalination operation at full capacity is expected to start in the second half of 2013 (partial capacity operation is expected sooner). Expected to be the largest plant in the world using membrane technology (planned annual contractual output of 150 million m ³).	500,000 contractual output; its actual production capacity is 620,000 m ³).	IDE holds 51% in SDL and the rest is held by Hutchison Water International Holdings Pte.	2013
Vasilikos, Cyprus; October 2009 and amended in February 2010	Provision of a reverse osmosis desalination facility to the Electricity Authority of Cyprus. Construction began in 2010.	60,000	100%	Work was halted because of an explosion at a navy base close to the facility. Completion date, which was planned for 2011, was deferred. New completion date not yet set.
Chennai, India; December 2009	Construction and operation of a reverse osmosis desalination plant for seven years. Construction began in 2010.	100,000	IDE holds 30% of the project (Vatech Wabag holds the remaining 70%)	2012

In addition to the aforementioned projects, IDE regularly participates in tenders and enters into negotiations on future desalination projects.

Activity related to desalination

Given its understanding and expertise in issues related to water biology and chemistry, hydraulic systems, development of industrial compressors and more, IDE also offers solutions for regular treatment of industrial waste, handling brine, cooling systems for mines, systems for storage of thermal energy and snowmaking machinery.

IDE is also attempting to enter the smaller desalination markets and at the end of 2011 it started marketing an easy-to-install-and-operate compact modular system (IDE PROGREEN™), which desalinates water using reverse osmosis. This system reduces the impact of desalination on the environment by eliminating the need for chemicals in the preliminary treatment processes. This system was designed, inter alia, for use in isolated areas, such as military bases and holiday resorts.

Risk factors

IDE's activity involves various risk factors: general market conditions; scope and timing of desalination projects; competition; changes in technology; changes in the abilities required of the company resulting from the number of projects; financing needs; dependence on the counterparties in the BOT transactions; quality, price and availability of materials or subcontractors for performance of the projects; timetable delays and budget deviations; legal proceedings and disputes; lack of protection for intellectual property; limited accessible markets; regulation in various countries; and changes in exchange rates.

Financial information

In 2009, 2010 and 2011, IDE's total revenues amounted to NIS 1,481,898 thousand, NIS 728,875 thousand and NIS 1,261,765 thousand, respectively, according to the following breakdown - revenues from construction contracts (EPC and the first stage of BOT) were NIS 1,269,558 thousand, NIS 419,959 thousand and NIS 907,152 thousand, respectively, and revenues from sales of water and operation and maintenance services were NIS 212,340 thousand, NIS 308,916 thousand and 354,614 thousand, respectively. In 2009, 2010 and 2011, IDE's gross profit amounted to NIS 375,775 thousand, NIS 198,657 thousand and NIS 293,594 thousand, respectively. In 2009, 2010 and 2011, IDE's net profit amounted to NIS 279,147 thousand, NIS 120,576 thousand and NIS 139,810 thousand, respectively.

The guarantees provided by the Company to IDE in connection with finance agreements for its various projects, totaled, at December 31, 2011, NIS 86 million. The Group's investment in IDE is handled in accordance with the equity method. For additional financial information regarding IDE's operations, see note 14 to the financial statements.

1.15.3 Power plants

Delek Infrastructure Ltd, a company wholly owned by Delek Investments, is engaged in the building and operation of power plants in Israel and abroad. As part of its activity, Delek Infrastructure, through subsidiaries, has built and currently operates two power plants in Israel and Brazil, and is working to build four additional power plants in Israel, which are currently in the development and design phases, and it is in the process of obtaining the various statutory approvals, as outlined below.

A. Active power plants

1. Ashkelon power plant

I.P.P. Delek Ashkelon ("Delek Ashkelon"), a company wholly owned by Delek Investments (a tiered subsidiary of Delek Investments) built a power plant on the premises of the desalination facility in Ashkelon, to generate 87 MW of electricity. Most of the power plant's capacity is provided to the desalination plant of VID in Ashkelon, and the rest is sold to private customers and/or Israel Electric Corporation. The period for supply of power to the desalination plant was set as 22.5 years. This period ends in June 2027.

On February 28, 2008, the Public Services Authority – Electricity ("Electricity Authority") approved the issue of temporary licenses for the generation and supply of electricity to the power plant, and on February 16, 2009, the Minister of National Infrastructures approved the issue of permanent licenses for the generation and supply of electricity by the plant. The plant began operations on January 10, 2008.

On April 13, 2008, Delek Ashkelon entered into an agreement for the provision of up to 22.5 MW of electricity to Nilit Ltd. ("Nilit"). The agreement is for a period through December 31, 2011, with an option to extend for another six years. The provision of electricity to Nilit began in April 2008.

On September 29, 2011, the Yam Tethys Partnership announced the cancelation of the Spot agreements and as a result a reduction in the gas supply to all of its customers, and in November and December, 2011 the Yam Tethys Partnership announced a reduction in

the gas supply from the quantity in the original agreement. In January 2012, Noble, which is the operator in the Yam Tethys Partnership, announced that the drop in the quantities supplied is the result of "force majeure". Due to the decrease in quantities of gas supplied Delek Ashkelon had to reduce the amounts of electricity produced by it and operate at reduced capacity, and as a result Delek Ashkelon ceased providing electricity to customers other than the desalination plant, and even that is only on a partial basis. Delek Ashkelon is currently examining the effect of an additional decrease in the gas quantities on the Company's activities and on its results.

Delek Ashkelon expects that when the gas supply starts from the Tamar reserve the Yam Tethys Partnership will start to provide gas again in quantities that will enable it to operate the power plant at full capacity and to provide gas to its other customers.

Delek Ashkelon's total revenues in 2009, 2010 and 2011 were NIS 185 million, NIS 172 million and NIS 163 million, respectively.

2. Power plant in Goiânia, Brazil

Delek Infrastructure holds shares (51%) in Enegen Participacoes S.A., a company incorporated in Brazil ("Enegen"). Enegen holds 70% of the rights in a project for the construction of a 140 MW power plant in Goiânia, Brazil. The cost of the construction of the power plant amounted to USD 50 million ("the Project"). Delek Infrastructure's share in the project is 35%. The construction of the power plant was completed in January 2009. The plant began operations in March 2009, under a 15-year agreement for the sale of the availability of the plant and sale of energy to the administration of the electricity system in its region of operation in Brazil.

B. Power plants in the development and design phases and in proceedings for various statutory approvals.

1. Power plant in Ramat Gabriel

IPP Delek Ramat Gabriel Ltd. ("Delek Ramat Gabriel") is a subsidiary of Delek Infrastructure which owns 57% of its share capital and voting rights. The other shareholders are Sigma Epsilon Power Engineering "Gabriel Tavor" Ltd. (28%) and Adi Energy Ltd. (15%). On January 10, 2008, Delek Ramat Gabriel signed a Memorandum of Understanding with Nilit regarding the construction of an independent power plant on Nilit's premises in the Ramat Gabriel industrial zone in Migdal Haemek. It is planned to be a cogeneration plant (production of electricity and steam), with a capacity of 60 MW. In accordance with the construction plans, the plant will provide all of Nilit's electricity and steam requirements, and the surplus electricity will be sold to private consumers. As of the date of the report, the estimated cost of construction of the power plant is USD 90 million. On November 13, 2008, an agreement was signed between Delek Ramat Gabriel and Nilit. The term of the agreement was set for 27 years, commencing when financing for construction of the plant is closed. Pursuant to the agreement, Delek Ramat Gabriel will supply electricity and steam to Nilit during the term of the agreement, with an estimated value of NIS 60 million per year. On June 6, 2011, Delek Ramat Gabriel received a conditional license for the production of electricity from the Electricity Authority to build the power plant in Ramat Gabriel, with a capacity of 60 MW. Delek Ramat Gabriel is in negotiations with a banking entity for financing of the construction of the power station.

2. Power plant in Alon Tavor

IPP Delek Alon Tavor Ltd. ("Delek Alon Tavor") is a subsidiary of Delek Infrastructure, with a holding structure identical to that of Delek Ramat Gabriel. On October 28, 2008, Delek Alon Tavor signed a Memorandum of Understanding with Tnuva Central Cooperative for the Marketing of Agricultural Produce in Israel, Ltd. ("Tnuva"), concerning the construction of a cogeneration plant (for electricity and steam) operating on natural gas, on the grounds of the Tnuva factory in Alon Tavor, with a capacity of 55 MW. As of the date of the report, the estimated cost of construction of the power plant is USD 90 million. In July 2009, the agreement was signed with Tnuva for the planning, financing, licensing, construction, operation and maintenance of the power plant. The term of the agreement was set for 27 years, commencing on the date on which financing is closed for the construction of the power plant. During the term of the agreement, the land on which the power plant will be built will be leased through a sublease to Delek Alon Tavor. The plant is slated to provide electricity and steam to the Tnuva factory and will be entitled to

provide surplus energy and steam to other factories in the Alon Tavor Industrial Zone. On December 30, 2010, Delek Alon Tavor received a conditional license for the production of electricity from the Electricity Authority. The Company is in negotiations with a banking entity for financing of the construction of the power station.

3. Power plant at Sorek

On September 29, 2009, IDE and Hutchison signed a memorandum of understanding with Delek Infrastructure, prior to the submission of their bid in the BOT tender for the construction of a desalination plant at Sorek, pursuant to which Delek Infrastructure, through a project company it will establish when it builds the power plant, will supply all of the electricity needs of the desalination plant. The provisions of the tender allow Delek Infrastructure to construct a power plant, on the area designated for the desalination plant, subject to receipt of the statutory approvals. Delek Infrastructure plans to exercise this right and to build a power plant that will serve the desalination plan as well as additional customers. As of the date of the report, the estimated cost of construction of the power plant is USD 160 million. IPP Delek Sorek ("Delek Sorek") is a wholly owned subsidiary of Delek Infrastructure which was established in August 2010 for the purpose of the construction of the power plant in Sorek. After the success of IDE and Hutchison in the tender and the receipt of a permit to build a BOT sea-water desalination plant in Sorek, on May 26, 2011 Delek Sorek signed a detailed engagement agreement with Sorek Desalination Ltd. (a joint company of IDE and Hutchison hereinafter "SDL") for the supply of electricity to the desalination plant for a period of 22 years. On December 30, 2010, Delek Sorek received a conditional license for the production of electricity for the power plant at Sorek from the Electricity Authority for up to 140 MW.

4. Power plant in Kiryat Gat

On January 6, 2010, Delek Infrastructure entered into an agreement with private developers, according to which it would be allocated holdings of no less than 84% (after allocation) in Eshkol Gat Ltd., which changed its name to IPP Delek Eshkol Gat Ltd. ("Delek Eshkol Gat"), a company that is promoting the project for construction of a power plant for the production of electricity using natural gas, with an installed capacity of 240 MW, in the Kiryat Gat Industrial Zone and has an option to purchase the property on which the power plant is supposed to be built. The balance of the holdings (up to 16%) will remain with the developers. Additionally, the developers were granted an option to increase their holdings by an additional 10% from the project company (up to a total of 26%), subject to that stated in the agreement. On May 5, 2010, the transaction was completed after performance of the conditions precedent. On August 16, 2010, Delek Eshkol Gat filed an application for a conditional license with the Electricity Authority for the conventional method, but this license was not granted to it. On December 19, 2010 Delek again filed an application for a conditional license and again this license was not granted.

On November 14, 2011, the Electricity Authority informed Delek Eshkol Gat that following a discussion concerning Delek Eshkol Gat's application for a conditional license for the production of electricity using conventional technology, and in light of the special circumstances of Delek Infrastructure, which is an interested party in the gas provider which is applying to be an interested party in conventional electricity production, Delek Eshkol Gat will be granted a license with the following terms: a conditional license for a capacity not exceeding 146 MW, and which will not include an obligation to purchase available capability and energy, on condition that Delek Infrastructure will notify in writing that it is prepared not to exercise its merger transaction with Etgal Energy Ltd as detailed below, and on condition that Delek Eshkol Gat will file a new application for a conditional license according to the capacity and terms agreed by the Electricity Authority. Since this is a matter of damage to the potential of the power plant which was designed for 240 MW, Delek Infrastructure decided that, for the good of the project, it should be built by another party so that it will not be bound to the decision of the Electricity Authority. In February 2012, Delek Infrastructure signed a Memorandum of Understanding with a third party for the sale of its holdings in the project, and the parties are currently working towards completing the sale agreement.

C. Engagement with Shikun & Binui in the Etgal Transaction

On June 15, 2011, Delek Infrastructure signed agreements with the shareholders of Etgal Energy Ltd, Shikun & Binui and Etgal Holdings ("Etgal Energy"), according to which it will

purchase Etgal Holdings' shares in Etgal Energy and will allocate to it additional shares in Etgal Energy such that its total holdings in Etgal Energy will be 50%, equal to Shikun & Binui's holdings in Etgal Energy. Etgal Energy owns the conventional power plant in Ashdod which is fired by fuel oil with a capacity of 27.5 MW, and it also holds a conditional license for the construction of an additional power plant on the land in Ashdod, which will be fired by natural gas with a capacity of 120 MW.

Delek Infrastructure filed an application with the Restrictive Trade Practices Controller to approve the transaction, whose decision, further to that stated regarding the power plant in Kiryat Gat, was to approve the merger transaction with Shikun & Binui if Delek submits the merger transaction of Eshkol Gat again for the examination of the Controller, after it has received his approval.

As of the date of the report, Delek Infrastructure is considering its actions regarding Project Etgal, in light of the Restrictive Trade Practices Controller's decision regarding the Eshkol Gat and Etgal power plants and in light of changes in the electricity industry, and Delek Infrastructure's signature on the Memorandum of Understanding for the sale of its share of Delek Eshkol Gat as stated above.

D. Activity in the power plant industry

As of the date of the report, the Israel Electric Corporation generates, transmits and distributes virtually all of the electricity used in Israel. However the trend in the industry in recent years, which can also be seen in the declared objectives of the State of Israel, is to increase electricity production capacity in the future through private producers. The development, design and construction processes of power plants are lengthy and take several years. Among other things, they require compliance with numerous regulatory requirements, financial abilities, professional know-how and experience. The process is characterized by a large degree of uncertainty, as it is in part in the control of third parties (particularly state authorities), which regulate issues such as deployment of gas infrastructures to the location of the plant, licensing proceedings and regulation, and rates. Even after completion of the design processes and receipt of the permits, which may be very lengthy, the activity is characterized by large investments during the construction and test run, while the revenues from the projects are only received after completion of construction, over a very long period. In light of the above, plans regarding costs, timetables, etc., are based solely on estimates, which may not materialize.

In 2010, at the request of the Knesset Finance Committee, the Minister of National Infrastructures convened an informal interministerial committee to put together recommendations regarding the question of the continued operation of a gas provider in general (and in this regard the indirect holdings of the group in an Israel gas provider) in the IPP market in Israel. The imposition of restrictions on the activity of the group in the Israeli power plant industry is a risk factor with respect to the activity described in this section, and the Company is working with the appropriate authorities to fully exercise its right by law to operate in the Israel electricity generation sector. However, in light of the changes in the electricity industry, the Company is considering the continuation and scope of its activities in this area.

1.15.4 Delek Real Estate

At the reporting date, the Company holds 5% of the shares in Delek Real Estate²⁶⁵. The Company provided Delek with guarantees which were granted when Delek Real Estate was a subsidiary of the Company and it also provided loans after Delek Real Estate shares were distributed as a dividend in the Roadchef transaction. For details of the loans and guarantees, see Regulation 22 in Chapter D of the Periodic Report. Below are details of the loans and guarantees granted by the Company and its subsidiaries to Delek Real Estate, which are in effect at the reporting date (it is clarified that what is presented in the Securities section is the book value of the assets used as securities in Delek Real Estate's financial statements at December 31, 2011):

²⁶⁵ Until May 2009, when Delek Real Estate shares held by the Company were distributed as a dividend in kind, Delek Real Estate was a subsidiary of the Company. For details of a statement of claim and motion for certification as a class action where were filed in the District Court against the Company, its controlling shareholder, a number of officers in the Company and in Delek Real Estate, both past and present, for damages caused to the shareholders of Delek Real Estate as a result of errors of omission and commission allegedly carried out in Delek Real Estate, see Note 14 to the financial statements.

The Company	The loan / guarantee	Section detailed under Regulation 22 in Chapter D of the Periodic Report	Main terms	Securities
Delek Group	Total debt of NIS 227 million attributable to the Company's acquisition of Delek Real Estate's debts from a banking corporation during the Roadchef transaction and loans used by Delek Real Estate to repay the debt to the banking corporation (for details, including impairment provisions for loan balance, see Note 14 to the financial statements)	5A	Total of NIS 150 million bearing interest of prime - 0.25%. The interest is due for repayment in quarterly payments and the principal is due for payment in one installment in January 2018. NIS 77 million linked to the CPI plus 1% annual interest over the average cost (interest rate and associated costs) of raising CPI-linked debentures of the Company of similar average duration. This loan bears annual interest of 6.35%. The principal due for repayment in one installment on January 31, 2018. In the reporting period Delek Real Estate did not make any interest payments.	A second-ranking charge on the Carmel Coast project in the amount of the bank debt acquired by the Company. There is a commitment to grant the charge but the charge has not been registered.
The Phoenix	The balance of loans from 2004 and 2008 is NIS 66.5 million, of which 52% is from profit-sharing policies and 48% is from proprietary trading funds.	6H	In August 2011 Delek Real Estate was supposed to make two payments of NIS 43 million (including interest). These payments were not made. On September 21, 2011 Delek Real Estate transferred NIS 4.6 million on account of the debt.	30% of Delek Real Estate Income Producing Properties Ltd. The book value of the shares in Delek Real Estate's books – NIS 108 million. 100% of the shares in Elad Israel Residences Ltd. The book value of the shares in Delek Real Estate's books – NIS 140 million. Delek Real Estate's rights in the plot in Kfar Silver. The book value of the plot in Kfar Silver in Delek Real Estate's books is not material. At the balance sheet date, The Phoenix has a valuation according to which the value of the securities for the loan is higher than the balance of the loan recorded in the books.
Delek Group	Guarantees for the liabilities of Delek Real Estate and its subsidiaries to banks, totaling NIS 60 million.	5B	Under an agreement from 2005 there is a commitment to pay an annual commission of 1.5%. The commission was not paid in the reporting period.	--
Excellence	Holding of Delek Real Estate debentures: Trust funds and ETFs – NIS 16 million.	9	Linked interest 4.8%, dates for repayment of the principal through 2019. Shekel interest of 7.3%, dates for repayment of the principal through August 2012.	--
Excellence	Holding of Delek Real Estate shares: ETFs – NIS 0.3 million.	9	--	--

For details of the various agreements between Delek Real Estate and the Company and its subsidiaries, see Regulation 22 in Chapter D of the Periodic Report.

In July 2011 various macroeconomic and microeconomic developments and developments specifically relating to Delek Real Estate's portfolio of parking lots leased to NCP ("the Parking Lot Asset") led Delek Real Estate's board of directors to conclude that it was doubtful whether it would be able to meet its long-term obligations and so it was necessary to formulate current guidelines regarding the servicing of its debt. Furthermore, the Board took the view that these developments were also impacting on its plans to find resources to meet its short-term obligations. Its conclusion was that by law it was precluded from repaying its long-term as well as its short-term debts (i.e. its current debts) for fear that this would result in preferential treatment for creditors which is prohibited by law, and violate the principle of equality among creditors²⁶⁶.

These were the circumstances in which at the end of July 2011 Delek Real Estate sent a request to the financial creditors and holders of debentures Series Y (where the payment date of half of its principal was in the second half of September 2011) for deferral of the principal payments which were scheduled for payment in the period until January 31, 2012 ("the Interim Period"). This would allow it to enter into negotiations with its creditors in order to find a comprehensive solution for the repayment of all its obligations.

Delek Real Estate announced that subject to consent of the holders of the debentures Series Y to deferral of payment of the principal, it would continue to meet its current obligations in the Interim Period as part of the normal course of its business, including interest payments to its various creditors²⁶⁷. It would also repay the principal of the loans to its secured creditors from the consideration received from disposal of its assets which were pledged to these creditors, insofar as they were disposed of.

Since August 2011, meetings of the holders of debentures (Series D, E, F and Y) ("the Debenture Series") have been convened and representatives for holders of the Debenture Series have been appointed, and various notices have been sent to the Company by the trustees for the Debenture Series and by other creditors, including The Phoenix Insurance Company Ltd. ("The Phoenix").

On February 28, 2011, further to the failure at a meeting of the holders of the debentures (Series Y) to pass a resolution with the required majority to defer by three weeks payment of the principal scheduled for September 3, 2011, the board of directors of Delek Real Estate decided, after receiving legal advice, that until another resolution was passed, Delek Real Estate would not make payments of principal and interest to any of its creditors (including bank corporations and affiliates). This would exclude payment of principal and interest to secured creditors, from the considerations received from assets pledged to these creditors, and Delek Real Estate would continue to pay the current expenses required for its operations.

Further to the above-mentioned, payments of principal and interest were not made to the holders of Delek Real Estate debentures on their payment dates.

At the beginning of October 2011 a consensus was reached for the Interim Period in which the parties would conduct negotiations in an attempt to formulate new guidelines for payment of Delek Real Estate's obligations. Furthermore, on November 23, 2011, Delek Real Estate made payments of the interest which had been scheduled for August 28, 2011 and September 3, 2011 to the holders of debentures (Series E and Y).

On January 31, 2012, a document of principles for an arrangement was signed by Delek Real Estate, representatives of the debentures Series D and E and the controlling shareholder private companies. In addition, an application to convene meetings of creditors and shareholders to approve an arrangement under Article 350(A) of the Companies Law²⁶⁸, which would be based on the document of principles signed with the representatives of Series D and E ("Document of Principles" and "Application to Convene Meetings", respectively) was filed in the Tel Aviv Jaffa District Court. Under the Document of Principles, the debentures (Series D, E and Y) would be replaced by two series of debentures, cash and shares in Delek Real Estate, so that upon implementation of the arrangement, 46% of the shares would be held by debenture holders, 50.09% by the controlling shareholder, and 3.99% by existing shareholders of Delek Real Estate.

²⁶⁶ A description of Delek Real Estate's position which is presented below is based on its reports.

²⁶⁷ Except for the controlling shareholder which notified the Company that in the Interim Period it waives the interest payments owed to it for its holdings of Delek Real Estate's debentures (Series B).

²⁶⁸ The Company is party to the application since it is a creditor of Delek Real Estate.

On March 12, 2012, a judgment was handed down in the Application to Convene Meetings of creditors ("the Judgment") in which the court ordered that the vote on the detailed arrangement would be held in one meeting of all the debenture series, but the trustee of each series would hold a preliminary meeting in which they would discuss the position of the series and the manner of vote (in other words, whether the trustee should distribute his vote based on a breakdown of the voting or whether to cast one vote in accordance with the position of the majority of the holders. This is subject to the right of each objector to exclude itself from the consensus.

At the reporting date, Delek Real Estate is in a position of insolvency and its continuation as a "living enterprise" depends on formulation of a detailed arrangement between Delek Real Estate, its financial creditors and the Company's controlling shareholder. At the reporting date, the negotiations with regard to formulation and completion of the detailed arrangement are ongoing and it is impossible to know if and when it will materialize.

The Company's management is conducting regular reviews of Delek Real Estate's debts and repayment ability, based on public information and discussions with its management. For details of the impairment provisions made by the Company in its financial statements for the balance of the above-mentioned loans, see note 14 to the financial statements.

Class action

On November 28, 2011 a statement of claim and motion for its certification as a class action were filed in the Tel Aviv Jaffa District Court (Economic Department) ("the Motion"), against the Company's controlling shareholder, the Company and officers of Delek Real Estate, both past and present, among them the chairman of the Company's board of directors, the Company's CEO and Legal Counsel ("the Respondents"). Delek Real Estate is not a defendant in the statement of claim.

In the application the applicant argues that the shareholders of Delek Real Estate incurred damages as a result of the acts of omission and commission allegedly carried out in the Company by the respondents.

The damages in the statement of claim amounts to NIS 720 million.

1.15.5 Barak Capital

The Company holds (through Delek Investments) 47% of shares in Barak Capital Ltd. ("Barak Capital") whose controlling shareholder is Mr. Eyal Bakshi ("Bakshi") who holds 48% of its shares. Barak Capital is a private holding and investment company which holds companies, directly and through investees, in various areas of the capital market, including trading in financial derivatives, financial transactions, underwriting and consulting on public offerings.

The agreement from February 2007 between the Company and Bakshi and Barak Capital's Articles of Association, regulates among other things, the following topics: Barak Capital shareholders have the right to appoint directors of whom the Company may recommend two out of five directors; the majority required to pass resolutions on the Board of Directors and in general meetings so that resolutions are passed by an ordinary majority except for resolutions pertaining to the allotment of shares or negotiable securities, a material change in the Company's businesses; transfer, sale or liquidation of most of the assets or a material change therein; liquidation, merger, split or a restructuring which require a special majority; right of first refusal mechanism and tag-along right; financing the operations of Barak Capital; non-competition, conflicts of interests; confidentiality, etc.

At the reporting date Barak Capital engages in three areas of operation:

- A. Proprietary trading - Most of Barak Capital's revenues are from its proprietary trading activity. This activity is conducted by scores of traders in Israel and globally who handle the group's proprietary trading accounts and trade in international markets, with each trader acting independently, under the supervision of and subject to the policies of Barak Capital. Trading activities include activity in shares, bonds, options, futures contracts, commodities and currencies. Activities are based on the use of long/short strategies and sophisticated and unique trading strategies, taking advantage of market mispricing.
- B. Underwriting and investment banking - This activity is performed by the subsidiary, Barak Capital Underwriting Ltd. ("Barak Underwriting"). Barak Underwriting operates in the following areas: A. Underwriting and distribution of public offerings; B. Raising capital and debt for companies in private issues to institutional and private investors; C. Distribution and advisory services for corporations regarding mergers and acquisitions; D. Investment banking activity and advisory services to corporations regarding mergers and acquisitions

- C. Academy of Trade – Established in 2011, Barak Capital's Academy of Trade offers professional and practical training in capital market trading to persons wishing to work in the field. This training is provided by a professional team of experienced lecturers.

Until April 2011 Barak Capital was also active in the area of ETFs through Index Teudot Sal Ltd. ("Index"). On February 10, 2011 Barak Capital entered into an agreement to sell all its holdings in Index (45.1% at full dilution) to DS Apex Holdings Ltd. ("DS Apex") in consideration of NIS 35 million. Pursuant to the conditions of the agreement for the sale of the shares, on the transaction completion date (April 3, 2011), Index repaid all the shareholder loans and credit balances of Barak Capital to Index and DS Apex replaced Barak in all the financing granted by Barak Capital to Index and purchased the capital note issued by Barak Capital to Index. Following the sale of its holdings in Index, Barak Capital's profit (before tax) amounts to NIS 34 million (the Company's share in this profit amounts to NIS 16 million).

At the reporting date, Barak Capital has more than 100 traders and employees.

In the Company's financial statements Barak Capital is presented in accordance with the equity method. [For details, see note --- to the financial statements]. Barak Capital's activity involves various risks attributable to the complexity of its operations, large volume of trading and significant regulation in the financial sector. These risks include market risks (index changes and market volatility which can destabilize the positions managed by Barak Capital), lack of market liquidity, interest rate changes which can affect the value of Barak Capital's assets and financial and security crises (both global and local).

1.15.6 Investments in Securities

The Company and Delek Investments hold cash and short-term investments, including investments in financial assets available for sale, which at December 31, 2011 amounted to NIS 1,020 million. In light of the low yields in the debt instruments markets recently, and the desire to diversify the Company's investment channels, during the first half of 2010 an Investment Committee was established comprising three Board members, and headed by an external director of the Company, Professor Ben-Zion Zilberfarb. The Investment Committee defines the Company's investment policy and meets at least once every quarter to monitor the implementation of this policy. In addition, there is a team of management members that meets frequently (at least once a week) to discuss the composition of the portfolio, and to make decisions, in accordance with the procedures and policy outlined by the Committee, regarding the purchase or sale of securities in the investment portfolio.

In accordance with the policy set by the Committee, the Company's investment in foreign negotiable securities is concentrated in shares of companies with a market value exceeding USD 20 billion, and with a rating above BBB+. In addition, guidelines were determined for the total amount of the portfolio, its diversity and the level of negotiability and periodic fluctuation of the purchased shares. The guidelines related to the total amount of the portfolio and its diversity are updated from time to time in accordance with the decisions of the Committee, and per the Company's liquidity needs and long-term yield requirements, subject to market conditions.

Below is the composition of the liquid balances of the Company and Delek Investments as of December 31, 2011 (in NIS millions)²⁶⁹:

	Balance at December 31, 2011
Cash and deposits (1)	270
Portfolio of foreign securities (2)	31
Shares in Noble Energy Inc, net (3)	43
Shares traded on the TASE (4)	328
Corporate bonds and debenture funds	154
Others – mainly government bonds	194
Total	1,020

(1) The cash and deposits are with banking corporations in Israel and abroad.

²⁶⁹ It is noted that during 2011 sharp downturns were recorded in the financial markets in Israel and around the world, inter alia, against a backdrop of a reduction in the United States' credit rating and the continued crisis in the EU. As a result of these downturns there was a decrease in the market value of the Group's financial assets.

- (2) The value of the portfolio close to the date of approval of the financial statements was USD 8.1 million (approximately NIS 31 million).

A. Investment in Noble shares

	Balance at December 31, 2011
Investment in Noble shares	64
Less specific loan	21
Total	43

In accordance with the decisions of the Company's board of directors in August 2009, July 2010 and August 2010 an investment framework was approved of up to 4% of the share capital of Noble, a company traded on the New York Stock Exchange.

The investment in Noble shares is presented as a financial investment, classified as an available-for-sale financial asset and is measured according to its fair value.

In 2009, 2010 and 2011 the Group both bought and sold Noble shares. As a result of the sale of Noble shares, in those years the Group earned total profit before tax of NIS 46 million, NIS 38 million and NIS 397 million, respectively.

On December 31, 2011, the investment in Noble came to NIS 64 million, constituting 0.1% of Noble's share capital. The profit inherent in this holding amounts to NIS 12 million.

Subsequent to the balance sheet date, the Group sold Noble shares for consideration of NIS 29 million, for total profit (before tax effect) of NIS 10 million. The balance of the investment and the positive capital fund as of the date of approval of the financial statements is NIS 38 million and NIS 4 million, respectively.

In 2009 and 2010, the Company engaged in an agreement with a foreign bank, pursuant to which it provided the Company with a non-recourse credit facility according to which the Group would be able to purchase up to 5,244,000 Noble shares, constituting approximately 3% of its total share capital, for a total not to exceed USD 230 million, for repayment by November 2013. As collateral for the credit the Group pledged the Noble shares purchased by it in favor of the foreign bank. The Group undertook during the credit term to maintain a ratio of 55% between the value of the debt balance and the value of the collateral (in other words, the value of all the holdings in Noble shares). Should the ratio between the debt balance and the value of the collateral exceed 66% (subject to changes under certain circumstances), the Group will be required to take immediate action to comply with a ratio of 55% between the debt balance and value of the collateral. Calculation of the debt balance and value of the collateral, and the ratio between the two, is done by the Group every day after closing of the trade of the shares. The Group will be entitled to withdraw dividends to be distributed in respect of the pledged shares, subject to compliance with the ratio between the collateral and said debt. Additionally, the agreement includes provisions regarding forced immediate repayment events, including cases of extreme change in the volume of Noble trade, suspension of trading or extreme declines in the prices of Noble shares. The interest in respect of the credit used from the facility is annual interest of Libor + 1.57%, for repayment on an annual basis. As of December 31, 2011 and close to the date of publication of the report, a total of NIS 21 million and NIS 8 million of the credit facility was used, respectively. The value of Noble shares held by the Company as of December 31, 2011 and close to the date of publication of the report was NIS 64 million and NIS 38 million, respectively.

The following is a summary of information on Noble (the information below is based on Noble's reports in the US):

Noble is an energy company that has been registered for trade on the New York Stock Exchange (NYSE) since 1980, and is engaged in the acquisition, exploration, development, production and marketing of crude oil, natural gas and natural gas liquids (NGL) around the world. These operations include performance of geophysical and geological estimates and drilling. Aside from rights in the developed and undeveloped fields of crude oil and natural gas, Noble owns facilities for the processing of natural gas, storage of natural gas and a system of pipelines for the processing and transport of crude oil, natural gas and NGL.

Noble has activities both within and outside the US. Outside the US, Noble is primarily active off the coasts of Israel and Cyprus, in the North Sea and in West Africa. Noble operates in Israel through its subsidiary, Noble Energy Mediterranean Ltd. Noble has rights to three main

projects in Israel: the Yam Tethys project (which includes the Mari and Noa gas reserves); the Tamar project (which includes the Tamar and Dalit natural gas reserves); and the Leviathan project (which includes the Leviathan gas reserve). In addition Noble is engaged in oil and gas exploration pursuant to other licenses. As of the date of the report, Noble holds four holdings and 15 licenses in Israel, for which it also serves as operator. Some of its partners in the projects and licenses stated above are Delek Drilling, Avner and Delek Investments, corporations which are controlled by the Company (for further details, see the Energy Segment above).

Noble also holds rights in a production-sharing contract and the “Block 12” exploration license located off the coast of Cyprus, where the Aphrodite natural gas discovery was made, in which it also serves as operator (for further details, see the Energy Segment above).

As part of its activities Noble is exposed to various risk factors, including, inter alia, changes in the economic status of countries around the world and financial crises; changes in regulation which relate to the different laws that apply to Noble in the framework of its activities, to fiscal policy, and to environmental laws in the countries in which Noble operates; fluctuations in natural gas prices; difficulty in executing projects; financial, technical and logistical challenges which relate to the development of discoveries and projects; imprecision of estimates of crude oil and natural gas reserves; uncertainty that drilling and exploration activities will lead to the discovery of commercial wells; causing of damage and harm to the environment and exposure to lawsuits; terror activities; social and political protests, and the like.

Noble's financial statements are prepared in accordance with US Generally Accepted Accounting Principles (GAAP), and the financial data is presented in US dollars. For additional information about Noble, and to view its reports to the US Securities and Exchange Commission, see Noble's website: <http://www.nobleenergyinc.com>.

- B. The holdings in any public company that is traded on the TASE do not exceed 5% of the issued and paid up capital of that company.
- C. Mostly debentures traded on the TASE, which are mainly rated A- and above.

1.15.7 Other holdings and investments

The Group has other holdings and investments which are not part of the Group's areas of activity. These holdings include, inter alia, holdings in hi-tech companies and financial investments.

Part Four – Matters Pertaining to the Group as a Whole

1.16 Property, plant and equipment

The corporate headquarters are located in an office building on Giborey Israel Street in Netanya, covering a total area of 3,360 sq.m. plus parking space. The offices are leased to the Company and its subsidiaries and other companies owned by the controlling shareholder, whereby each company pays rent pro rata to the area it uses. The lease contract is part of the regular course of business and at market conditions. Rent paid is not material.

1.17 Human resources

1.17.1 Organizational structure

The Company is a holdings company which controls, directly and indirectly, numerous companies most of which conduct their operations independently. The Company's investments during the reporting period were made mainly through two subsidiaries directly held by the Company, Delek Investments (100%) and Delek Petroleum (100%).

Financing of the investments or guarantees for financing are often provided by the Company or by Delek Investments or Delek Petroleum, the headquarters companies (together - "the Headquarters Companies"). The procedure is that material transactions made by these subsidiaries are not only approved within the companies, but are also submitted for approval by the Company's board of directors. The description in the sections concerning the Company's entire operations refers to the Company and the headquarters companies as a single entity.

On December 30, 2010 the Company's board of directors decided in principle to merge the Company with Delek Investments. Subsequent to the balance sheet date, on March 1, 2011, the Company's board of directors decided that all the assets, rights, liabilities and debits of Delek Investments (the target company) will be transferred to the Company and assimilated by it (the receiving company). On February 16, 2012 the Company's merger plan with Delek Investments was approved by the tax authority's mergers and splits division. The merger was set as of Friday, December 31, 2010. Upon completion of the merger, Delek Investments will be eliminated without liquidation. The merger proceedings are expected to be completed, based on the dates set in section 323 of the Companies Law, by June 2012.

For further information pertaining to the merger between the Company and Delek Investments, see the immediate reports issued by the Company on March 1, 2011, March 6, 2011 and February 19, 2012 (Ref No. 2011-01-066840, 2011-01-070119 and 2012-01-044916, respectively), whereby the information appearing therein are presented here by way of reference.

1.17.2 Employee headcount

The Company and its headquarters companies employ a staff of 28, of whom eight are officers and senior management, and the rest are head office and administration employees. These employees also serve as managers of the headquarter companies and their employees.

1.17.3 Officers and senior management employees in the Group

The officers and senior managers are employed under personal contracts which include various forms of pension coverage. Some of the officers and senior management employees are entitled to acclimatization bonuses for periods of up to 6 months, based on the personal employment contracts signed with each of them. Some of the Group's company managers and directors (including the Company's CEO and Chairman, who serve as directors of Group Companies) have been granted, for their positions in such companies, shares and stock options, and usually constitute up to 3% of the issued and paid-up share capital of those companies. The terms for exercising the options include an extended period for their exercise as well as additional terms. In certain cases, loans have been provided to officers in the Group (including the CEO) for purchasing securities in the Group's companies. In addition, the Group usually awards incentives (bonus) to managers in amounts which are based on the following parameters: managerial rank, the Group's business results and the personal achievements of the manager in the Group. The officers are eligible for insurance, waiver and indemnification in respect of activities performed in their official capacity. Furthermore, most of the Group's officers and senior managers received phantom options in June 2009. For further information pertaining to the adoptions of the phantom option plan for employees and senior officers, under which, inter alia, phantom options were awarded to the Company's CEO and other officers, see Chapter D to the periodic report.

Based on the plan, the options will vest in three equal annual tranches, while the first tranche and the second tranche vested in June 2010 and in June 2011, respectively. The third tranche vests in June 2012. All options will expire in June 2014. The total number of options approved under the plan is 46,895 options, of which, as of reporting date, 31,567 options were allotted. As of December 31, 2011, the financial value of the foregoing remaining options amounts to NIS 13 million. The expense recognized for this plan during 2010 amounted to NIS 10 million, while in 2011 the amount recognized for this plan was NIS 2 million (in view of the impairment of the options due to the decrease in the value of Delek Group's shares this year).

For further information pertaining to remuneration of senior officers in the Group (including the CEO and Chairman of the Group) pursuant to Regulation 21 in the Securities Regulations (Periodic and Immediate Reports), 1970, see Chapter D to the periodic report.

1.18 Financing

This section does not refer to the credit received by the subsidiaries operating in the segments of operation, unless explicitly stated otherwise.

1.18.1 During the reporting period the Company reached agreement with a bank to receive credit as follows:

- A. A loan in the amount of NIS 150 million, repayable in a lump sum in January 2018 at interest rate of prime minus 0.25%.
- B. A loan in the amount of NIS 80 million, repayable in a lump sum in January 2018 at 7.85% interest.
- C. A loan in the amount of NIS 100 million, whereby the final repayment date (principal and interest) will be in June 2016 at fixed interest of 6.3%.

To secure the foregoing credit limit the Company pledged in favor of the bank all its rights in RoadChef, including its rights under the shareholders loan, as set forth in section 1.18.9 above.

1.18.2 Below is a breakdown of the average interest rate on loans from bank and non-bank sources effective during the reporting period and which are not designated for specific use:

		Short-term loans		Long-term loans	
		Average interest rate	Effective Interest rate	Average interest rate	Effective Interest rate
Banking sources	Unlinked NIS credit	---	---	7.0%	7.2%
	Unlinked NIS credit at variable interest	---	---	4.2%	4.3%
	Linked NIS credit	---	---	5.5%	5.6%
	USD linked credit	1.9%	2.0%	---	---
	Euro linked credit	---	---	---	---
Non-banking sources	Unlinked NIS credit	---	---	8.1%	8.3%
	Linked NIS credit	---	---	5.0%	5.1%

1.18.3 Credit received between the date of the financial statements and their publication

On March 2012, credit was received from a bank in the amount of NIS 150 million for a period of two years.

1.18.4 Credit facilities

Unless specifically stated otherwise, everywhere that credit facilities are noted in this report, it refers to the lines of credit for which commissions are paid and for the use of which is guaranteed, subject to compliance with their terms.

As of reporting date the Company does not have any credit for which commissions are paid and the use of which is guaranteed, subject to compliance with their terms.

1.18.5 Variable interest credit

Breakdown of variable interest credit received by the Company in 2011:

Variance mechanism	Interest range in 2011	Interest rates prior to publication of the periodic report
Bank of Israel Interest +	4.0% - 4.5%	4.0%
USD LIBOR +	1.7% - 2.1%	1.9%

1.18.6 Credit rating

Debentures Series F-S, V-W, DD are rated by Midroog with credit rating A1 Negative, of which Series N, P and R were expanded during 2011.

On July 18, 2011 Midroog announced confirmation of the A1 rating for the series it rated and updating of the rating outlook to negative. Furthermore, an A1 rating was awarded for the expansion of the existing series to raise an amount of NIS 701 million. . Debenture series J-M and V-W are rated by S&P Maalot. On December 26, 2011 S&P Maalot updated the Company's rating outlook from negative to stable, and at the same time confirmed the rating of iIA.

1.18.7 Material agreements with banking corporations

A. Agreement with a bank in Israel with respect to the purchase of Delek Real Estate's debt

In order to receive the Bank's consent to the lifting of the lien on 51% of the shares in RoadChef for the purchase transaction of RoadChef shares that was completed in January 2011, it was agreed that the Company would purchase, in addition to the debt in the amount of NIS 150 million as aforesaid, Delek Real Estate's debt to the Bank in the amount of NIS 64 million (together - "**the Purchased Bank Debt**"). For further information see sections 1.5, 2.2 and 2.3 of the Company's transaction report of January 5, 2011 (Reference No. 2011-01-006375), (indicated herein by way of reference).

The terms of Delek Real Estate's debt to the Company following the bank debt purchase is as follows:

1. an amount of NIS 150 million at interest of prime minus 0.25%, which will be repaid in quarterly installments.
2. An amount of NIS 76 million is at 6.40% interest.

Both the foregoing amounts are repayable on January 30, 2018 and a second tier lien will be registered in favor of the Company on the Hof Hacarmel project to secure them.

- B. Delek Real Estate undertook to sign documents regulating the endorsement of part of the Bank's rights in the lien on the Hof Hacarmel project in favor of the Company, so as to grant the Company limited rights in the amount of the Bank debt it purchased. In accordance with the foregoing and the aforesaid limits, Delek Real Estate will register a second tier lien in favor of the Company on the Hof Hacarmel project. Subsequent to the purchase of the debt from the Bank, the senior lien on the Hof Hacarmel project will guarantee Delek Real Estate's debt to the Bank in the amount of NIS 244 million. The value of the Hof Hacarmel project in Delek Real Estate's financial statements at Friday, December 31, 2011, amounted to NIS 299 million.
- C. Delek Real Estate gave an undertaking that the loans guaranteed by senior lien on the Hof Hacarmel project will not exceed NIS 320 million, and this all the while that the debt to the Company is unpaid. As of reporting date, no such lien has yet been registered in favor of the Company.

1.18.8 Financial covenants

Wherever financial covenants are mentioned in this report and the actual ratios are close to them, there are quantitative references, other than the operating segment of Delek USA, for which there are qualitative references.

The Company and Delek Investments undertook financial covenants in connection with long term bank loans, which at Saturday, December 31, 2011 amounted to approximately NIS 320 million, as follows:

- A. The value of MSA Acquisition Co. Ltd. ("MSA"), a foreign subsidiary held by RoadChef Ltd. and whose shares are pledged in favor of the bank by Delek Motorway Services ("DMS") with the addition of the unpaid balance of the loans provided to MSA by some of the foregoing companies and which is pledged in favor of the bank and divided into the unpaid balance of the credit, will not at any time fall below 1.5 (the value of collateral to debt ratio).

- B. The total cumulative amount of guarantees for securing the liabilities of the Company's subsidiaries shall not exceed NIS 1.5 billion (one and a half billion shekel)
- C. The ratio of assets to liabilities as defined between the Company and the bank will not be less than 1.2. With respect to this ratio:
 - 1. The value of the assets will include the share of the Company and of the headquarters companies (as defined in the agreement) in the equity of investees (public companies - at market value; private companies - as presented in the financial statements) plus loans granted to the investees and plus cash and/or unencumbered cash equivalents and other financial assets in the Company and the headquarter companies (as defined in the agreement).
 - 2. The liabilities will include the balance of short-term and long-term credit from banks and from others with the addition of loans from shareholders and interested parties which were extended to the Company and the headquarters companies (as defined in the agreement) in accordance with the financial statements.
- D. Delek Group is required to obtain prior approval for distribution of a dividend to the Company's shareholders, at a rate that exceeds 60% of its net annual income.
- E. In addition, under the foregoing agreement, the Company and Delek Investments are subject to the following causes for immediate repayment of the credit extended by the bank:
 - 1. If there will be a change in the control of the Company and/or of Delek Investments
 - 2. If a change takes place in the Company's control of Delek Investments or Delek Petroleum.
 - 3. If, during the period during which the bank extended credit for the buyback of the Company's debentures and/or early payment is made to the Company's debenture holders in a total accumulated amount exceeding NIS 300 million. It is hereby clarified that refinancing will not be considered as early repayment.

As at the reporting and shortly prior to the date of publication of the report, these companies are in compliance with the foregoing financial criteria.

1.18.9 Credit limits

The Group is subject to the Proper Banking Management Directives issued by the Supervisor of Banks in Israel, which include, inter alia, restrictions on the volume of loans which the Israeli banks may extend to a single borrower and to the six largest borrowers and largest borrower group in the bank (as these terms are defined in the aforementioned directives).

1.19 Taxation

For the a description of the tax laws applicable to the Company see Note 42 of the Group's financial statements.

1.20 Company liens, loans and guarantees

1.20.1 Liens

Below are particulars pertaining to the Group's liens as of December 31, 2011, which are not attributed to any of the foregoing operating segments:

A. Liens on Company assets:

As of December 31, 2011, there was a lien in favor of a bank on the Company's full rights in RoadChef, including its rights under the shareholders loan as aforesaid.

B. Delek Investments liens:

As of December 31, 2011, there was a lien in favor of a bank on 159,000 shares of Delek Energy Systems, which constitute 3.6% of Delek Investments' holdings in Delek Energy Systems, as of December 31, 2011. Delek Investments holds approximately 86.7% of the share capital of Delek Energy Systems. Furthermore, as at December 31, 2011 Delek Investments pledged in favor of the Sellers in the Cohen Development and Industrial Buildings Ltd. transaction, 8,000,000 participating units of Delek Drilling - Limited Partnership.

- C. For details of guarantees and liens of the Group's companies in the various operating segments, see the discussion in each segment of operation.
- D. Other than the foregoing, all the investments of the Company and its subsidiaries, Delek Petroleum and Delek Investments, in investees are free of liens.

1.20.2 Loans and guarantees to investees

Breakdown of material loans to the Company's subsidiaries and related companies, as at Saturday, December 31, 2011 (in NIS millions):

Lender	Borrower	Loan amount as at December 31, 2011
Delek Investments	Delek Capital	73
Delek Investments	Delek Energy	256
Delek Petroleum	Delek Luxembourg Holdings	73
Delek Petroleum	Delek USA	254
Delek Investments	IPP	77
Delek Petroleum	Delek Europe BV	452
Delek Group	Delek Yam Maagan	51
Total		1,236

Breakdown of material loans to the Company's subsidiaries and related companies, as at Saturday, December 31, 2011 (in NIS millions):

Guarantor	Guaranteed	Guarantee amount As at December 31, 2011
Guarantee for liabilities of subsidiaries and related companies²⁷⁰		
Delek Group ²⁷¹	Delek France BV	256
Delek Investments	Delek Ashkelon	87
Delek Petroleum ²⁷²	Delek France BV	316
Delek Group	RoadChef	59
Delek Group	IDE	46
Delek Investments	Delek Yam Maagan	31
Delek Investments	IDE	40
Delek Investments	Delek Capital	41
Delek Investments	Others	7
Interim total		883
Guarantees for the liabilities of third parties		
Delek Group	Israel Electric Corp.	61
Interim total		61
Total		944

The above information does not include guarantees to Delek Real Estate, which are specified in section 1.15.5 above.

²⁷⁰ Guarantees provided by the Company and headquarters companies (Delek Investments and Delek Petroleum) to the operational subsidiaries.

²⁷¹ Subsequent to the balance sheet date guarantees in the amount of EUR 30 million were canceled.

²⁷² Subsequent to the balance sheet date Delek Petroleum provided guarantees in favor of Delek Benelux, amounting to NIS 134 million.

1.21 **Restrictions and Supervision of the Corporation's Operations**

With the exception of the restrictions and supervision applicable to the Company and its subsidiaries under the various operating segments, as a public holdings company, the Company is subject to applicable restrictions under the Company's Law, 1999, Securities Law, 1968, their regulations, and the Antitrust laws. In addition, the Company is affected by the various directives concerning capital and debt raising on the financial market in Israel or for non-banking finance. In October 2010 the Prime Minister appointed a committee to deal with increasing competitiveness in the economy ("**The Committee**") with the aim of examining the affects of the current structure on the Israeli economy and in view of the examination, to recommend desired policy measures, including regulatory amendments and operative measures. In October 2011 the Committee published its draft recommendations. After receiving comments from the public and hearing public representatives and various other entities in the economy and academia, the Committee published its final recommendations in February 2012. The Committee's recommendations focus on three topics: Conditions for allocation of public assets, real and financial holdings, and control through pyramid holdings structure. The Committee's recommendations include, inter alia, the following: (1) entities in charge of the allocation of rights and assets of the State or on its behalf will be required to weigh considerations of competitiveness and centralization as part of the allocation process, and for this purpose, it will be required to consult with the Antitrust Commissioner whenever the financial value of the allocated asset or right is in excess of NIS 150 million or in lower values wherever the economic value of the asset does not reflect its significance to the public, and it will be required to relate to the implications of the overall centralization in the allocation of essential infrastructure rights, centralization considerations will be subject to principles for preventing significant consumer harm and the recommendations will also apply to the reallocation to existing concession holders with required amendments; (2) prohibiting control or holding in a significant financial entity by a significant real entity or by the controlling shareholder in a significant real entity, beyond a rate that will be set by the certified regulators in this matter, and provided that such rate will not exceed 10% of any type of control means (other than an entity that does not have a controlling core where the rate of holding will not exceed 5%). A significant financial entity is defined as a financial entity that manages assets in excess of NIS 40 billion. A significant real entity means a corporation that is not a financial entity: (a) that has a sales turnover of more than NIS 6 billion; and (b) whose fixed credit does not exceed NIS 6 billion. Relief was prescribed concerning an entity that was a significant real entity prior to the date of the law coming into force (if it will be legislated), or that became a significant real entity after receiving control or holding permit in a significant financial entity. Restrictions were set concerning tenure of directors in such entities and their control; it was determined that the control in pyramid structured companies that include more than two layers will be prohibited, and applicable recommendations were prescribed for companies with existing pyramid structures of three or more layers. Recommendations were also prescribed concerning the competitiveness in approval of transactions with interested parties and expanding the powers of the audit committee in a public company, encouragement of institutional investor activism, and recommendations for limiting exposure of institutional investors to a single entity and group of entities.

Adoption and implementation of the Committee's recommendations, particularly those prohibiting control or holdings by a significant real entity in a financial institution at a rate higher than the rate that will be set, and the recommendations pertaining to companies incorporated in a pyramid structure, may have material effect on the Company, taking into account the restrictions on its holdings structure, and particularly on its control in financial institutions, its ability to acquire and dispose of holdings in public companies and on the value of its holdings in such companies, the feasibility of distributing dividends from its investees, including due to tax aspects on the industries in which they operate, etc.

In September 2011, the Committee for Economic and Social Change headed by Prof. Trajtenberg submitted its recommendations to the government. These recommendations include, inter alia: Stopping the previously set declining path for the corporate tax rate and raising the corporate tax rate to 25% as of 2012 and recommending examination of raising this rate to 26% in 2013; raising capital gains tax (including tax on interest and dividends) as of 2012; cancellation and lowering of customs; empowering regulatory authorities dealing with supervision of monopolies and powerful entities in certain branches of the economy. In October 2011 the government adopted the main recommendations in the Committee's report, decided to begin their implementation and approved part of the recommendations dealing with taxation, including raising the corporate tax rate to 25% and raising the capital gains tax, as of 2012. In November 2011, a proposed bill was published, implementing the main recommendations, as aforesaid, regarding taxation.

As of reporting date, it is uncertain which of the other recommendations of the Committee will be adopted and the manner and time schedules for the implementation of the Committee's recommendations that will be adopted, and therefore it is not possible to assess the impact of the

foregoing on the Company's businesses. Nevertheless, implementation of the recommendations, if they will be implemented, may significantly affect the Company.

For further information, see sections 1.26.5, 1.26.7, 1.26.8, 1.26.15, and 1.26.16 below.

1.22 Material Agreements

For further information concerning material agreements under the various operating segments, see above sections 1.7.20, 1.8.20, 1.9.28, 1.10.18, 1.11, 1.12.18, 1.13.5 and 1.14.15. Other than the foregoing, other material agreements of the Company are with the key shareholders in several companies: IDE (see section 1.15.2 above), Barak Capital (see section 1.15.6 above), Delek Automotive (see section 1.14.1 above), Phoenix (see section 1.12.1 above) and Gadot (see section 1.15.1 above).

Significant financing agreements by headquarters companies is specified in sections 1.15.7 (3) and 1.18 above.

From time to time, the Company engages in material purchase agreements such as the agreement to acquire the controlling shares in Cohen Development, the fuel operations in France, the agreement to acquire RoadChef, etc. Other than their business terms, these agreements include various provisions concerning presentations, indemnification and transfer of information, which may become significant in problems arise subsequent to closing of the transactions.

Subsequent to the reporting period, a material contract was signed for selling natural gas to the Israel Electric Corp. For further information pertaining to the foregoing material contract, see section 1.11.12 (D) above.

1.23 Legal proceedings and insurance

For a description of the material legal proceedings to which the Group's companies are party, see Note 32 to the financial statements.

The various companies belonging to Delek Group carry a wide variety of insurances covering various events. By the nature of things, and in the Company's assessment, these insurances do not constitute protection against all the risks in the business operations of Delek Group, as specified, inter alia, in the chapter on risk factors in this report.

1.24 Business strategy and objectives

The Company customarily reviews its strategic plans from time to time and revises its goals in accordance with developments in its segments of operation and business opportunities which present themselves.

1.24.1 General:

Following the discovery of natural gas in the Mediterranean waters and regulatory changes that came into force in 2011, including the final recommendations of the Committee for Increasing Competitiveness in the Economy, the Company's general strategy is to focus on developing its core assets in the upstream energy sector and active management of its asset balance with the aim of increasing the value of the assets and maximizing their profitability. At the same time, the Group constantly examines its investments, which are not invested in its core segments and adjusting them to the Company's goals.

1.24.2 Continuous growth, development and trade in gas exploration and gas transmission infrastructures

In the short term the Group, together with its partners, is making every effort to complete the development of the Tamar gas field in order to enable supply of natural gas to the Israeli market during 2013. In addition, after signing gas sales agreements with Israel Electric Corp and other customers, the Group will continue increasing its customer base in Israel and abroad.

In the long term the Group, together with its partners, will prepare for developing the Leviathan field, which requires significant investment and infrastructure expansion. For this purpose, the Group is examining options to collaborate with strategic players in gas exploration and gas infrastructure, and in everything connected to the development of the field and marketing of natural gas in Israel and abroad.

The Group will act to achieve long-term project financing for various projects and in particular the Tamar and Leviathan projects.

The Group will continue investing in seismic surveys and developing other licenses it holds in order to locate new oil and gas discoveries.

1.24.3 The expansion of the fuel and refining operations in Europe and the United States by selective acquisitions and generating size advantage in the markets in which it operates.

The Group assumes that opportunities exist for expanding the fuel and refining operations in Europe and in the USA by acquisitions at attractive value in the short and mid terms. In this regard, the Group believes that its existing operations, together with targeted acquisitions and integrating them, will provide it with a platform for becoming a significant player in the gas station and convenience store operations in Europe. In view of the foregoing, the Group intends continuing to examine the acquisition of assets in the retail, wholesale, refining and logistics markets in the relevant downstream energy markets in Europe and the USA.

Furthermore, the Group intends continuing to manage its operations in Europe and in the USA according to operating models aiming at improving customer relations and increasing the retail operating margins. For this purpose, the Group intends closing weak performance sites, to introduce changes at sites operating under models such as CORO and RORO so that they will operate according to more profitable models such as COCO, to increase the number of convenience stores and to maximize their profitability by redesigning and rebranding, to introduce new brands and higher profit products.

For further information pertaining to the goals and strategy in the fuel and refining operations in the USA and Europe see sections 1.7.22 and 1.9.30 above.

1.24.4 Finance sector

The Group operates in the finance sector in Israel, mainly through Phoenix, *inter alia*, in elementary, health and life insurance and in long term savings, and through Excellence, which operates mainly in investment management for its clients and self-trading in securities.

As set forth in sections 1.22 and 1.25.1 above, assuming that the Centralization Committee's recommendations will be adopted and implemented, the Group may be forced to sell its controlling means in its financial entities in Israel, within four years.

1.24.5 Active management and positioning of the Group's businesses for increasing cash flows from them and maximizing the business value

The Group acts to actively manage its remaining businesses in order to maximize value and enable cash flows that will support, *inter alia*, the Company's dividend strategy and energy business growth. The Group provides its administrative capacities to the subsidiaries (by representation on the boards of directors of these companies) and often supports them in order to develop or exploit their potential value.

As a rule, the Group's expanded business portfolio, including businesses designated as yield generating by way of dividend or increased value, are meant to enable it business flexibility and the ability to support capital intensive oil and gas operations.

1.24.6 Wise management of financial operations for ensuring flexibility and maximizing shareholder's return

The Company's approach is to manage its businesses with the aim of ensuring financial flexibility for short and mid term financing needs and to maximize shareholders' return by distributing dividends.

In view of its significant holdings in public subsidiaries, the Group tries to maintain financial flexibility by increasing or decreasing its holdings. The Group actively manages its holdings and increases its share, *inter alia*, based on its assessment of the value of the shares or reduces its share, *inter alia*, based on its financing needs.

The Group's strategy is to maintain its financial strength and adequate solvency. Risk is reduced, *inter alia*, by a comprehensive business portfolio that balances between exposure and capital intensive businesses and cash yielding businesses. The Company's subsidiaries, some of which are public companies, are financially managed independently and the Company focuses on overseeing its businesses while examining its current and future financing needs.

1.24.7 Expanding and varying financing sources

In view of its financing needs and existing liabilities, the Company tries to maintain its ability to raise capital on the capital market and constantly examines expanding and varying its sources of finance.

1.24.8 Contribution to the community in Israel

Together with its efforts to achieve profits for its shareholders, the Company aims to contribute and assist the community in Israel where a major part of the Group's businesses are located. The Group acts through the Delek Foundation for Education, Culture and Science to administer all activities and contributions for the benefit of the society and the community by Delek Group and its subsidiaries under one roof. Each year the Group's companies donate to the Foundation the funds required by the Foundation for carrying out its community work. The Delek Foundation's main efforts focus on contributions to education, health and the food distribution societies.

1.25 Financial information concerning geographic regions

Below is a breakdown of the geographic regions in which the Group operates and its principal operations in them:

Israel - the Group operates in Israel in the automotive, fuel products, energy, insurance and finance, desalination, infrastructure and biochemical sectors.

USA - the Group operates in the USA in fuel products, refining, energy, biochemical and insurance sectors.

Western Europe - the Group operates in Western Europe in the fuel products, roadside service station and biochemical sectors.

Other - the Group operates worldwide in the desalination and biochemical sectors.

For further information concerning the geographic regions see Note 44 to the financial statements

1.26 Discussion of Risk Factors

The Company is primarily a holdings company and therefore its principal risk factors stem from the specific risk factors of each of the Group's various operating segments. The risk factors of each operating segment is described separately under the description of each separate operating segment. Aside from the risks described for those segments, below are details of additional key Group-wide risks to which the Group is exposed in Israel and abroad.

- 1.26.1** Changes in foreign currency exchange rates The Company and its investees have foreign-currency loans and therefore the Company is exposed to changes in the exchange rates of these currencies (mainly USD, Euro and GBP). The exchange rates may affect the business results of the Company and its investees since a significant part of their acquisitions and revenues are denominated in foreign currency. For example, a devaluation of the NIS against the USD, Euro or Yen will generate increased NIS costs for liabilities denominated in those currencies, and on the other hand, appreciation of the NIS against the USD, Euro or GBP will generate a decrease in revenues and as a result in profitability. Furthermore, the Company is exposed to exchange rate translation risks so long as the currencies in which its subsidiaries operate, and according to which their financial statements are drafted, are foreign currencies. The Company is specifically exposed to exchange rate changes of the USD, Euro and GBP, which impact the values in the Company's financial statements, also if there is no change in the original currency.

Though the Group tries, from time to time, to neutralize such currency risks by using various financial instruments, it is uncertain that it will succeed, and it may even undertake under such transactions to make various payments for hedging.

- 1.26.2** Change in interest rate: The Group has NIS loans at variable interest rates and therefore it is exposed to changes in interest rates in Israeli banks. Some of the Group companies took loans at variable interest at foreign interest rates, therefore they are exposed to changes in interest rates in those countries. In addition, changes in interest rates can impact the business results of the Company and the investees. Changes in interest rates in Israel and the US can have an adverse effect on the yields of the marketable debenture portfolios of the insurance companies held by the Company, which provide collateral for insurance liabilities.

- 1.26.3** Economic slowdown and changes in the Group's markets: The Group has substantial operations in various countries around the globe. Changes that occur in the markets in which the Group

operates, particularly an economic slowdown in those markets (including in Israel, the Benelux countries, France, Britain and the US), could have an adverse effect on the operations of the Company and its investees, as well as on the value and liquidity of their assets, the demand for their products and their revenues. The global economic crisis that began in 2008 led to global recession and adversely affected economies worldwide, including in the Benelux countries, France, Britain and the US. Since 2009 there has been a trend of stabilization and recovery, but some of the countries in which the Company operates are still steeped in recession.

- 1.26.4** Capital markets: Deterioration in the global capital markets, and particularly in the Tel Aviv stock exchange, could adversely effect the Group's operations. Changes in the prices of marketable securities held by the Group expose it to risks deriving, *inter alia*, from capital market volatility and will affect its ability to generate capital gains from the realization of its investments. Deterioration of the capital market in Israel and the continuing global crisis could have material impact on the operations of the Company and its overseas investees, also with regard to their capital and debt raising abilities.
- 1.26.5** Financing: The Group has substantial obligations and continuous need for refinancing its operations when such existing liabilities reach repayment date. Some of these liabilities include financial criteria and others are liable to limit the Group's operations (such as restrictions on distribution of dividends, issuing of shares, providing collateral, mergers and disposal of assets), and non-compliance with these criteria could lead to a demand for immediate repayment of the liabilities and exercise of collateral. The Group's inability to obtain financing in the future by receiving loans or debt and capital raising, under good terms, may prevent the expansion of its operations, harm its current operations and lead to non-payment of dividends and even non-compliance with obligations towards third parties, including debenture holders. The availability and terms of financing sources are dependent on various factors, including the operating status, financial position, capital market conditions and the ability and limitations of key financing bodies. In this regard it is noted that in July 2010, the recommendations of the Hodek Committee were adopted by the Commissioner of Capital Markets and they are applicable to the large institutional investors in Israel (insurance companies, pension funds and provident funds). The Commissioner's directives impose, with certain exceptions, conditions and restrictions on the investment in corporate debentures, such as receiving a greater amount of information from the issuers prior to deciding on the investment, and including financial criteria in the debenture terms and conditions. The manner in which these directives will be applied may vary from case to case. In recent years the Group raised a large part of its financing through issuing debentures in Israel, a major part of which were purchased by institutional investors which are affected by the adoption of the Hodek Committee recommendations. The adoption of the Hodek Committee recommendations and other restrictions that may be applied in the future, may limit the Company's ability to raise additional debt, under favorable terms, or restrict its operations.
- 1.26.6** Security and political situation: Deterioration in the security and political situation (domestic and international) in Israel could adversely affect the Group's operations. Since a major part of the Group's operations are in Israel, it is exposed to the implications of armed conflicts, terror acts and instability in Israel. Such conflicts or acts are liable to harm the Group's operations in several ways, including cause an Israeli economic slowdown which could adversely impact the scope of its operations and results; declines in the Israeli capital market which could adversely impact the Group's capital and debt raising ability, realization of its holdings and the value of its marketable holdings; harm the Group's employees in Israel and cause direct damage to the Group's installations, including its gas exploration, production and conveyance facilities (Yam Tethys, Tamar, Leviathan, Ashkelon) and its seawater desalination and electric power plants, which are situated relatively close to the Israeli border with the Gaza Strip and may serve as a specific target for their purposes; and a decline in the presence of foreign investors and international companies will to invest in and engage with Israeli companies. Furthermore, the Group's ability to operate in various countries around the globe, particularly in Middle East countries, which do not recognize Israel is already, by nature, restrictive. Calls and actions to boycott Israeli companies (in enemy countries as well as in friendly countries) may also adversely affect the Group's operations in Israel and abroad. Similar to the foregoing, the Group is exposed to armed conflict, hostile acts and political instability in all the countries in which it operates.
- 1.26.7** Changes in legislation and standards: Special laws apply to significant parts of the Group's operations. The Group's financial results could be affected by changes in legislation and standards in various areas, including antitrust laws, laws governing the obligation to issue tenders, laws regulating areas such as fuel, gas, telecommunications, supervision of insurance business, control on prices of products and services, excise rates, consumer protection, etc. Furthermore, changes in the policy of the authorities operating under these laws is liable to affect the Group. Similarly,

some of the Group's companies operate abroad and they are liable to be affected by changes in legislation, excise, regulatory proceedings and policy in the countries in which they operate.

In this matter attention is drawn to section 1.11.10 above, concerning the recommendations of the Sheshinski Committee which have material adverse impact on the Group's operations in the energy segment. Also see section 1.26.15 below.

A change in accounting regulations could affect the business results of the Group and its investees, and the ability of those investees to distribute dividends.

- 1.26.8** Supervision of banks: The Group and some of its investees are subject to the Proper Banking Practice directives issued by the Supervisor of Banks in Israel, which include, *inter alia*, restrictions on the volume of loans that Israeli banks may extend to a single borrower and largest borrower groups in the bank (as these terms are defined in the aforementioned directives). In view of the foregoing restrictions, the scope of the loans granted to the Group and its controlling shareholder may, under certain circumstances, impact the Group's ability to borrow additional sums from Israeli banks, and on its ability to make investments which require bank credit, or investments in companies which have taken large volumes of credit from certain Israeli banks.
- 1.26.9** Licenses and concessions: Some of the companies held by the Company operate on the basis of approvals, permits, licenses or concessions granted to them in Israel and abroad, in accordance with the law, by various authorities, *inter alia* the Ministry of National Infrastructures, Ministry of Telecommunications and Ministry of Transport. Failure to comply with the terms of these approvals, permits, licenses or concessions could lead to the imposition of sanctions, fines and even cancellation of the relevant approvals by the competent authorities. Such cancellation is liable to cause substantial harm to investees whose operations depend on these approvals. Some of these licenses and concessions have time limits and are renewable from time to time, all in accordance with the conditions and provision of the law and there is no certainty that these licenses or concessions will be renewed in the future. Non-renewal of such a license or concession may adversely impact the profitability of the company holding such a license or concession and consequently also on the Company's profitability.
- 1.26.10** Environmental protection: Some of the Company's investees, particularly in the fuel segment in Israel, the USA and Europe, and in the refining and biochemical segments, are exposed to various requirements laid down by the authorities in the matter of environmental protection in Israel and abroad. The other costs and resources necessary for complying with the environmental requirements are large. A change in legislation in this area or a change in the policy of the supervisory authorities may impact the profitability of these companies, and consequently also the Company's profitability and failure to comply with them may expose the Company to various sanctions, legal proceedings and loss of licenses.
- 1.26.11** Raw materials, equipment and infrastructure: Some of the Company's investees are exposed to changes in the prices of raw materials, such as the refining sector which is exposed to changes in fuel prices (which affect the refining margin) or biochemical operations which are exposed to changes in the global price of sugar. Changes in the prices of raw materials are liable to impact the profitability of investees and consequently also the Company's profitability. Moreover, the companies are dependent upon the proper conveyance and storage of the various raw materials (for example, proper operation of fuel pipelines and terminals) and access to various infrastructures. These may be affected as a result of various factors, such as labor strikes, security events, transport breakdowns, limited access to ports (particularly the two main ports in Israel) natural disasters, extreme climatic conditions, etc.
- 1.26.12** Development of the Group's gas operations: Over the past two years the significance of the Group's gas business activities has increased due to the Tamar and Leviathan discoveries and other discoveries made during the past year, through to reporting date. The increase and success of the Group's gas operations depend on a series of factors such as the successful development of the Tamar and Leviathan reserves, increased demand for gas in Israel, development of the infrastructures required for supplying gas, obtaining financing at favorable terms for developing the gas operations, continued good relationship between the Group and Noble, agreements for selling gas under favorable terms and the ability to export gas. Failure of any of these factors to materialize could have material adverse impact on the Group's operations. Also see risk factors in the energy segment - section 1.11 above.
- 1.26.13** Legal proceedings: Lawsuits have been filed against the Company and some of its investees, including class actions, in substantial amounts. If these companies are found liable in these legal proceedings or in any possible future legal action brought against the Company or its investees,

this could adversely impact the Company's business results. Also see Note 32 to the financial statements pertaining to contingent liabilities.

1.26.14 Salary and labor relations: Material changes in the minimum wage or other material changes in the labor laws are liable to affect the results of the Company's investees and consequently also the Group's business results. Furthermore, strikes and labor disputes in the investees are liable to adversely affect the business results of the Group.

1.26.15 Antitrust and increased competitiveness: The Group is subject to antitrust restrictions that deal with, inter alia, restrictions on the scope of operations, prohibited practices and manner of pricing products and services. Under certain circumstances, the Group's companies are liable to be restricted in their operations because of the provisions of the Antitrust laws in various countries, in a way that may restrict the expansion of their operations or even require them to downsize and change their operations. Furthermore, in certain cases, the Group and its investees may be subject to approval of transactions by the Antitrust Commissioner in Israel, which is liable to restrict and even prevent such transactions being carried out, or to require acting in accordance with the terms and conditions contained in merger permits which are granted or may be granted by him. Failure to comply with antitrust laws or claims of failure to comply with these laws, could lead to civil and criminal sanctions and the imposition of various restrictions on the Group's operations. Antitrust laws are, from time to time, subject to changes and interpretation, including being made more stringent.

In October 2010 the Prime Minister appointed a committee on increasing competitiveness in the economy with the aim of examining the effects of the current structure of the Israeli economy.. In February 2012, the committee submitted its final recommendations which focus on three issues: Conditions for the allocation of public assets, real and financial holdings, and control through pyramid holdings structure. In the matter of this section 1.25.1 above and section on Phoenix above. As one of Israel's largest holding companies, which operates in a variety of operating segments, measures that may be taken to limit the expansion of the Group's operations or obligating it to dispose of holdings, including holdings in the insurance and financial sectors in Israel, may adversely affect the Group's operations and results.

1.26.16 Restrictions on disposal of holdings: The Company and some of its investees are bound by legal and contractual restrictions which could inhibit the ability of the Company and its investees to dispose of these holdings. There are liens in favor of banks on a minor part of the shares of the public investees.

1.26.17 Dependence on the results of investees and their cash flows: As a holdings company, the results of the Company's operations are, *inter alia*, dependent on the results of its investees, which manage the majority of its operations and which hold the majority of its assets. A majority of the investees are public companies trading on the TASE (or the NYSE with regard to Delek USA) and operate independently, and their interests are not necessarily the same as the interests of the Company. The Company's sources of capital include profits distributed as dividends and repayments of loans by the investees. Changes in the profit distribution policy of the Company's investees, changes in profitability (including those brought about by changes in accounting principles) and in the cash flows of these companies, and restrictions on the distribution of profits are liable to affect the Company's cash flows and its business operations, and therefore it is not at all certain that they will be able to make such payments in time when it is in need of the cash flows. Furthermore, the Company's ability to raise foreign finance relies, inter alia, on the value of its holdings in the Group's companies.

1.26.18 Loans and guarantees to investees and related companies: As part of its operations the Company extended its investees (such as Delek Energy, Delek Europe and Delek USA) loans in material amounts as well as guarantees and collateral for various purposes such as guaranteeing finance they received, projects they carried out, etc. A decline in the profitability and cash flow of these investees or liquidity difficulties is liable to have an adverse effect on their ability to comply with the terms of the loans, or alternatively, to bring about the exercise of the guarantees provided by the Company and thereby adversely affect its financial position. In this context, it is noted that the Company and its subsidiaries have extended loans and guarantees in material amounts to Delek Real Estate.

1.26.19 Insurance: Notwithstanding the fact that various risks involved in their business operations are insured by the investees, they are unable to protect against the realization of all risks, including the risks specified above, and existing insurances are limited in aspects such as scope of insurance, insurance exceptions, timing of insurance payments, and the ability of the insurance companies to meet their liabilities. Accordingly, it is possible that there will be no insurance cover, full or partial, for the realization of various risks, including risks to the Group's employees and its plants.

- 1.26.20** Goodwill: The goodwill of the Group and of part of its brands were acquired over the years. The Group's success depends to a certain extent on its goodwill. Negative publicity of the Group and its brands is liable to harm its goodwill and the willingness of customers, suppliers, investors and others to engage with it. The Group's goodwill is liable to be adversely affected, inter alia, by negative events connected with environmental and health issues, legal proceedings and claims pertaining to unethical and illegal conduct.
- 1.26.21** Expansion and integration of new business segments: Previous and future acquisitions and investments expose the Group to several risks, including unexpected risks such as obligations or restrictions that were unknown at the time of the acquisition (for example, concerning environmental and antitrust issues); difficulties in achieving sales and profits that retroactively justify the acquisition; acquiring and managing additional liabilities; difficulties in integrating human resources and in making business, operating, financial and technological changes in acquired operations; difficulties opposite shareholders or other business partners in acquired operations; loss of key employees, suppliers or customers following acquisition; insufficient indemnification from the sellers for future liabilities; undertakings dependent on future payments; and difficulty in managing extensive and varied operations. Realization of these risks and other are may adversely affect the Company's operations and its financial results.
- 1.26.22** Information systems: The Group relies on information systems for its various activities. Information system failures (including as a result of natural disasters, power cuts, hackers penetrating the information systems, etc) and inability to repair them quickly is liable to harm the Group's businesses. Such failures could, inter alia, cause loss of business information, loss of customers and suppliers, harm to goodwill and significant costs for restoring the information systems.
- 1.26.23** Failure to comply with the undertakings of the parties engaged with the Group: Failure to comply with undertakings of parties with which the Group is engaged or their failure to pay can expose the Group to losses. Material exposure as aforesaid exists, inter alia, with regard to the exposure of reinsurance companies, and parties managing funds for the Group in the insurance and finance segments.

Breakdown of the Company's assessment of the types of risk factors and the degree of their impact on the Company's foregoing risk factors:

Risk factors	Scope of impact		
	Major Impact	Moderate Impact	Minor Impact
Macro risks	• Interest rate fluctuations • Changes in legislation and standards	• Foreign currency exchange rate changes • Capital market status • Economic recession • Supervision of banks	• Security and political situation
Industry-specific Risks	• Financing	• Environment • Raw materials, equipment and infrastructure	
Company-specific risks	• Development of the Group's gas operations:	• Licenses and concessions • Loans and guarantees to investees and related companies • Reliance on its investees and their cash flows:	• Restrictions on realization of holdings • Salary and labor relations • Antitrust and increased centralization • Legal proceedings • Goodwill • Insurance • Expansion and integration of new business segments: • Information Systems • Failure to comply with the undertakings of the parties engaged with the Group:

Also see reference to additional risk factors applicable to the Group's material investees set forth in sections 1.7 and 1.14 of the report.

March 23, 2012

Delek Investments and Properties Ltd.
7 Giborei Israel Street
Netanya 42504
Israel

Ladies and Gentlemen:

In accordance with your request, we have estimated the proved undeveloped reserves and future revenue, as of December 31, 2011, to the Delek Investments and Properties Ltd. (DI) interest in certain gas properties located in Noa Field, offshore Israel. Also as requested, we have estimated the gross (100 percent) contingent gas resources, as of December 31, 2011, for these properties. It is our understanding that DI owns a direct interest in these properties and a 6.53 percent interest in Delek Drilling Limited Partnership (Delek Drilling), a 9.11 percent interest in Avner Oil Exploration Limited Partnership (Avner), an 86.71 percent interest in Delek Energy Systems Ltd., and a 51.76 percent interest in Cohen Development & Industrial Buildings Ltd. Delek Drilling and Avner also own direct interests in these properties. We completed our evaluation on or about the date of this letter. This report has been prepared using price and cost parameters specified by DI, as discussed in subsequent paragraphs of this letter.

The estimates in this report have been prepared in accordance with internationally recognized standards, as stipulated by the Israel Securities Authority (ISA). The estimates in this report have been prepared in accordance with the definitions and guidelines set forth in the 2007 Petroleum Resources Management System (PRMS) approved by the Society of Petroleum Engineers (SPE). As presented in the 2007 PRMS, petroleum accumulations can be classified, in decreasing order of likelihood of commerciality, as reserves, contingent resources, or prospective resources. Different classifications of petroleum accumulations have varying degrees of technical and commercial risk that are difficult to quantify; thus reserves, contingent resources, and prospective resources should not be aggregated without extensive consideration of these factors. Definitions are presented immediately following this letter. This report has been prepared for use by DI in filing with the ISA; in our opinion the assumptions, data, methods, and procedures used in the preparation of this report are appropriate for such purpose.

RESERVES

Reserves are those quantities of petroleum anticipated to be commercially recoverable from known accumulations by application of development projects from a given date forward under defined conditions. Reserves must be discovered, recoverable, commercial, and remaining as of the evaluation date based on the planned development projects to be applied. Proved reserves are those quantities of oil and gas which, by analysis of engineering and geoscience data, can be estimated with reasonable certainty to be commercially recoverable; probable and possible reserves are those additional reserves which are sequentially less certain to be recovered than proved reserves.

We estimate the gas reserves and future net revenue, discounted at 0, 5, 10, 15, and 20 percent, to the DI interest in these properties, as of December 31, 2011, to be:

Category	Gas Reserves (BCF)		Future Net Revenue After Levy and Corporate Income Taxes (M\$)				
	Gross (100 Percent)	Working Interest	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
Proved Undeveloped	35.3	11.2	6,007.3	4,751.4	3,624.1	2,612.4	1,703.6

Gas volumes are expressed in billions of cubic feet (BCF) at standard temperature and pressure bases. These properties are not expected to produce commercial volumes of oil. Monetary values shown in this report are expressed in United States dollars (\$) or thousands of United States dollars (M\$). For your reference, the March 23, 2012, exchange rate was 3.74 Israeli New Shekels (NIS) per United States dollar.

The estimates of reserves shown in this report are for proved undeveloped reserves. Because production in excess of 35.3 BCF of gas will require partner approval and additional government coordination, no probable or possible reserves exist for these properties; additional volumes have been further classified as contingent resources. Reserves categorization conveys the relative degree of certainty; reserves subcategorization is based on development and production status. The estimates of reserves and future revenue included herein have not been adjusted for risk.

Working interest revenue for the reserves shown in this report is DI's share of the gross (100 percent) revenue from the properties prior to any deductions. Future net revenue is after deductions for royalties, capital costs, abandonment costs, operating expenses, an oil and gas profits levy, and DI corporate income taxes. The future net revenue has been discounted at annual rates of 0, 5, 10, 15, and 20 percent to determine its present worth, which is shown to indicate the effect of time on the value of money. Future net revenue presented in this report, whether discounted or undiscounted, should not be construed as being the fair market value of the properties. Table I presents revenue, costs, and taxes for the proved undeveloped reserves. Because Noa Field is currently under development and has no historical production, cost, or revenue data, we have not included a table showing DI's historical net production, operating costs, royalties, or net revenue per production unit.

We have made no investigation of potential gas volume and value imbalances resulting from overdelivery or underdelivery to the DI interest. Therefore, our estimates of reserves and future revenue do not include adjustments for the settlement of any such imbalances; our projections are based on DI receiving its net revenue interest share of estimated future gross gas production.

As requested, this report has been prepared using gas prices specified by DI. The initial gas price of \$5.91 per MCF is held constant through December 31, 2012, and then decreased to \$5.63 per MCF and held constant throughout the remaining lives of the properties.

Operating costs used in this report were provided by DI and appear reasonable based on our knowledge of similar operations. These costs are intended to include only direct project-level costs and DI's estimate of the portion of its headquarters general and administrative overhead expenses that can be directly attributed to this project. As requested, operating costs are held constant throughout the lives of the properties.

Capital costs used in this report were provided by DI. Capital costs are included as required for workovers, new development wells, and production equipment. Based on our understanding of DI's future development plans, a review of the records provided to us, and our knowledge of similar properties, we regard these estimated capital costs to be reasonable. Abandonment costs used in this report are DI's estimates of the costs to abandon the wells, platforms, and production facilities; these estimates do not include any salvage value for the lease and well equipment. As requested, capital costs and abandonment costs are held constant to the date of expenditure.

CONTINGENT RESOURCES

Contingent resources are those quantities of petroleum which are estimated, as of a given date, to be potentially recoverable from known accumulations, but for which the applied project or projects are not yet considered mature enough for commercial development because of one or more contingencies. These resources are subclassified as development pending and are contingent upon (1) finalization of the terms of the future partner agreements, (2) removal of the production limitation imposed by the State of Israel, and (3) future development drilling. If these contingencies are successfully addressed, some portion of the contingent resources estimated in this report may be reclassified as reserves; our estimates have not been risked to account for the possibility that the contingencies are not successfully addressed. This report does not include economic analysis for these contingent resources. Based on analogous field developments, it appears that the best estimate contingent resources in this report have a reasonable chance of being commercial.

We estimate the gross (100 percent) contingent gas resources for the properties located in Noa Field, as of December 31, 2011, to be:

Category	Gross (100 Percent) Contingent Gas Resources (BCF)
Low Estimate (1C)	21.5
Best Estimate (2C)	42.6
High Estimate (3C)	68.9

The contingent resources shown in this report have been estimated using deterministic methods. Once all contingencies have been successfully addressed, the approximate probability that the quantities of contingent resources actually recovered will equal or exceed the estimated amounts is generally inferred to be 90 percent for the low estimate, 50 percent for the best estimate, and 10 percent for the high estimate. For the purposes of this report, the volumes and parameters associated with the low, best, and high estimate scenarios of contingent resources are referred to as 1C, 2C, and 3C, respectively. The estimates of contingent resources included herein have not been adjusted for development risk.

GENERAL INFORMATION

This report does not include any value that could be attributed to interests in undeveloped acreage beyond those tracts for which undeveloped reserves and contingent resources have been estimated. For the purposes of this report, we did not perform any field inspection of the properties, nor did we examine the mechanical operation or condition of the wells and facilities. We have not investigated possible environmental liability related to the properties; however, we are not currently aware of any possible environmental liability that would have any material effect on the reserves and resources quantities estimated in this report or the commerciality of such estimates. Therefore, our estimates do not include any costs due to such possible liability.

The reserves and contingent resources shown in this report are estimates only and should not be construed as exact quantities. Estimates may increase or decrease as a result of market conditions, future operations, changes in regulations, or actual reservoir performance. In addition to the primary economic assumptions discussed herein, our estimates of reserves are based on certain assumptions including, but not limited to, that the properties will be developed consistent with current development plans, that the properties will be operated in a prudent manner, that no governmental regulations or controls will be put in place that would impact the ability of the interest owner to recover the reserves, and that our projections of future production will prove consistent with actual performance. If these volumes are recovered, the revenues therefrom and the costs related thereto could be more or less than the estimated amounts. Because of governmental policies and uncertainties of supply and demand, the sales rates, prices received, and costs incurred may vary from assumptions made while preparing this report. It should be noted that the actual production profile for each category may be lower or higher than the production profile used to calculate the estimates of future net revenue used in this report, and no sensitivity analysis was performed with respect to the production profile of the wells. This sensitivity analysis could lead to the conclusion that the reserves or contingent resources are not economic.

For the purposes of this report, we used technical and economic data including, but not limited to, well logs, geologic maps, seismic data, well test data, and property ownership interests. We were provided with all the necessary data to prepare the estimates for these properties, and we were not limited from access to any material we believe may be relevant. The reserves and contingent resources in this report have been estimated using deterministic methods; these estimates have been prepared in accordance with generally accepted petroleum engineering and evaluation principles set forth in the Standards Pertaining to the Estimating and Auditing of Oil and Gas Reserves Information promulgated by the SPE (SPE Standards). We used standard engineering and geoscience methods, or a combination of methods, including performance analysis, volumetric analysis, analogy, and reservoir modeling, that we considered to be appropriate and necessary to classify, categorize, and estimate volumes in accordance with the 2007 PRMS definitions and guidelines. Certain parameters used in our volumetric analysis are summarized in Table II. The reserves and contingent resources shown in this report are

for undeveloped locations; such volumes are based on estimates of reservoir volumes and recovery efficiencies along with analogy to properties with similar geologic and reservoir characteristics. As in all aspects of oil and gas evaluation, there are uncertainties inherent in the interpretation of engineering and geoscience data; therefore, our conclusions necessarily represent only informed professional judgment. There is no certainty that it will be commercially feasible to produce any percentage of the contingent resources.

Netherlands, Sewell & Associates, Inc. (NSAI) was engaged on January 16, 2012, by Mr. Gideon Tadmor, Chairman of DI, to perform this assessment. The data used in our estimates were obtained from DI, public data sources, and the nonconfidential files of NSAI and were accepted as accurate. Supporting geoscience, performance, and work data are on file in our office. The contractual rights to the properties have not been examined by NSAI, nor has the actual degree or type of interest owned been independently confirmed. We are independent petroleum engineers, geologists, geophysicists, and petrophysicists; we do not own an interest in these properties nor are we employed on a contingent basis. Furthermore, no limitations or restrictions were placed upon NSAI by officials of DI.

QUALIFICATIONS

NSAI performs consulting petroleum engineering services under Texas Board of Professional Engineers Registration No. F-2699. We provide a complete range of geological, geophysical, petrophysical, and engineering services, and we have the technical expertise and ability to perform these services in any oil and gas producing area in the world. The staff are familiar with the recognized industry reserves and resources definitions, specifically those promulgated by the U.S. Securities and Exchange Commission, by the Alberta Securities Commission, and by the SPE, Society of Petroleum Evaluation Engineers, World Petroleum Council, and American Association of Petroleum Geologists. The technical persons responsible for preparing the estimates presented herein meet the requirements regarding qualifications, independence, objectivity, and confidentiality set forth in the SPE Standards.

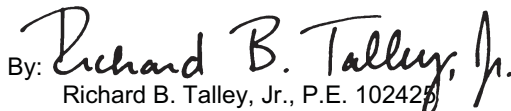
This assessment has been led by Mr. Richard B. Talley, Jr. and Mr. David E. Nice. Mr. Talley and Mr. Nice are Vice Presidents in the firm's Houston office at 1221 Lamar Street, Suite 1200, Houston, Texas 77010, USA. Mr. Talley maintains a valid Professional Engineer License (Texas Registration No. 102425). He has been practicing petroleum engineering consulting at NSAI since 2004 and has over 5 years prior industry experience. Mr. Nice maintains a valid Professional Geoscientist License (Texas Registration No. 346). He has been practicing petroleum geoscience consulting at NSAI since 1998 and has over 13 years prior industry experience.

Sincerely,

NETHERLAND, SEWELL & ASSOCIATES, INC.
Texas Registered Engineering Firm F-2699

By: 

C.H. (Scott) Rees III, P.E.
Chairman and Chief Executive Officer

By: 
Richard B. Talley, Jr., P.E. 102425
Vice President

Date Signed: March 23, 2012

RBT:DEG

By: 
David E. Nice, P.G. 346
Vice President

Date Signed: March 23, 2012

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

This document contains information excerpted from definitions and guidelines prepared by the Oil and Gas Reserves Committee of the Society of Petroleum Engineers (SPE) and reviewed and jointly sponsored by the World Petroleum Council (WPC), the American Association of Petroleum Geologists (AAPG), and the Society of Petroleum Evaluation Engineers (SPEE).

Preamble

Petroleum resources are the estimated quantities of hydrocarbons naturally occurring on or within the Earth's crust. Resource assessments estimate total quantities in known and yet-to-be-discovered accumulations; resources evaluations are focused on those quantities that can potentially be recovered and marketed by commercial projects. A petroleum resources management system provides a consistent approach to estimating petroleum quantities, evaluating development projects, and presenting results within a comprehensive classification framework.

These definitions and guidelines are designed to provide a common reference for the international petroleum industry, including national reporting and regulatory disclosure agencies, and to support petroleum project and portfolio management requirements. They are intended to improve clarity in global communications regarding petroleum resources. It is expected that this document will be supplemented with industry education programs and application guides addressing their implementation in a wide spectrum of technical and/or commercial settings.

It is understood that these definitions and guidelines allow flexibility for users and agencies to tailor application for their particular needs; however, any modifications to the guidance contained herein should be clearly identified. The definitions and guidelines contained in this document must not be construed as modifying the interpretation or application of any existing regulatory reporting requirements.

1.0 Basic Principles and Definitions

The estimation of petroleum resource quantities involves the interpretation of volumes and values that have an inherent degree of uncertainty. These quantities are associated with development projects at various stages of design and implementation. Use of a consistent classification system enhances comparisons between projects, groups of projects, and total company portfolios according to forecast production profiles and recoveries. Such a system must consider both technical and commercial factors that impact the project's economic feasibility, its productive life, and its related cash flows.

1.1 Petroleum Resources Classification Framework

Petroleum is defined as a naturally occurring mixture consisting of hydrocarbons in the gaseous, liquid, or solid phase. Petroleum may also contain non-hydrocarbons, common examples of which are carbon dioxide, nitrogen, hydrogen sulfide and sulfur. In rare cases, non-hydrocarbon content could be greater than 50%.

The term "resources" as used herein is intended to encompass all quantities of petroleum naturally occurring on or within the Earth's crust, discovered and undiscovered (recoverable and unrecoverable), plus those quantities already produced. Further, it includes all types of petroleum whether currently considered "conventional" or "unconventional."

Figure 1-1 is a graphical representation of the SPE/WPC/AAPG/SPEE resources classification system. The system defines the major recoverable resources classes: Production, Reserves, Contingent Resources, and Prospective Resources, as well as Unrecoverable petroleum.

The "Range of Uncertainty" reflects a range of estimated quantities potentially recoverable from an accumulation by a project, while the vertical axis represents the "Chance of

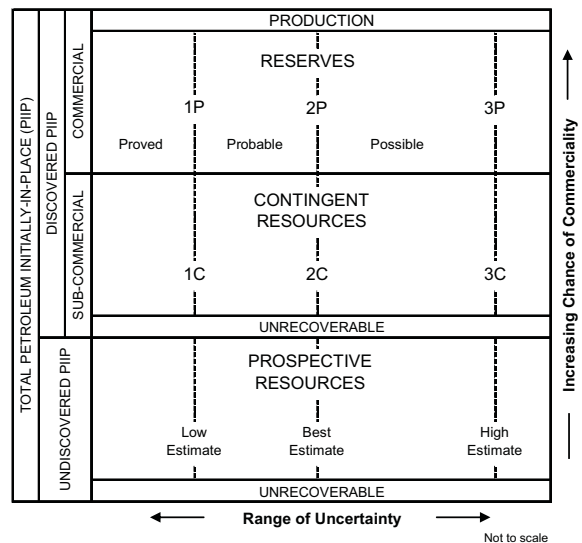


Figure 1-1: Resources Classification Framework.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Commerciality", that is, the chance that the project that will be developed and reach commercial producing status. The following definitions apply to the major subdivisions within the resources classification:

TOTAL PETROLEUM INITIALLY-IN-PLACE is that quantity of petroleum that is estimated to exist originally in naturally occurring accumulations. It includes that quantity of petroleum that is estimated, as of a given date, to be contained in known accumulations prior to production plus those estimated quantities in accumulations yet to be discovered (equivalent to "total resources").

DISCOVERED PETROLEUM INITIALLY-IN-PLACE is that quantity of petroleum that is estimated, as of a given date, to be contained in known accumulations prior to production.

PRODUCTION is the cumulative quantity of petroleum that has been recovered at a given date. While all recoverable resources are estimated and production is measured in terms of the sales product specifications, raw production (sales plus non-sales) quantities are also measured and required to support engineering analyses based on reservoir voidage (see Production Measurement, section 3.2).

Multiple development projects may be applied to each known accumulation, and each project will recover an estimated portion of the initially-in-place quantities. The projects shall be subdivided into Commercial and Sub-Commercial, with the estimated recoverable quantities being classified as Reserves and Contingent Resources respectively, as defined below.

RESERVES are those quantities of petroleum anticipated to be commercially recoverable by application of development projects to known accumulations from a given date forward under defined conditions. Reserves must further satisfy four criteria: they must be discovered, recoverable, commercial, and remaining (as of the evaluation date) based on the development project(s) applied. Reserves are further categorized in accordance with the level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterized by development and production status.

CONTINGENT RESOURCES are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from known accumulations, but the applied project(s) are not yet considered mature enough for commercial development due to one or more contingencies. Contingent Resources may include, for example, projects for which there are currently no viable markets, or where commercial recovery is dependent on technology under development, or where evaluation of the accumulation is insufficient to clearly assess commerciality. Contingent Resources are further categorized in accordance with the level of certainty associated with the estimates and may be subclassified based on project maturity and/or characterized by their economic status.

UNDISCOVERED PETROLEUM INITIALLY-IN-PLACE is that quantity of petroleum estimated, as of a given date, to be contained within accumulations yet to be discovered.

PROSPECTIVE RESOURCES are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from undiscovered accumulations by application of future development projects. Prospective Resources have both an associated chance of discovery and a chance of development. Prospective Resources are further subdivided in accordance with the level of certainty associated with recoverable estimates assuming their discovery and development and may be sub-classified based on project maturity.

UNRECOVERABLE is that portion of Discovered or Undiscovered Petroleum Initially-in-Place quantities which is estimated, as of a given date, not to be recoverable by future development projects. A portion of these quantities may become recoverable in the future as commercial circumstances change or technological developments occur; the remaining portion may never be recovered due to physical/chemical constraints represented by subsurface interaction of fluids and reservoir rocks.

Estimated Ultimate Recovery (EUR) is not a resources category, but a term that may be applied to any accumulation or group of accumulations (discovered or undiscovered) to define those quantities of petroleum estimated, as of a given date, to be potentially recoverable under defined technical and commercial conditions plus those quantities already produced (total of recoverable resources).

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

1.2 Project-Based Resources Evaluations

The resources evaluation process consists of identifying a recovery project, or projects, associated with a petroleum accumulation(s), estimating the quantities of Petroleum Initially-in-Place, estimating that portion of those in-place quantities that can be recovered by each project, and classifying the project(s) based on its maturity status or chance of commerciality.

This concept of a project-based classification system is further clarified by examining the primary data sources contributing to an evaluation of net recoverable resources (see Figure 1-2) that may be described as follows:

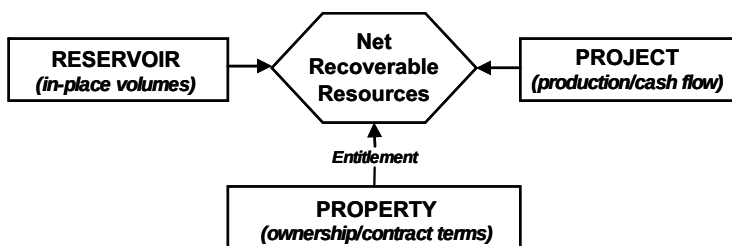


Figure 1-2: Resources Evaluation Data Sources.

- The Reservoir (accumulation): Key attributes include the types and quantities of Petroleum Initially-in-Place and the fluid and rock properties that affect petroleum recovery.
- The Project: Each project applied to a specific reservoir development generates a unique production and cash flow schedule. The time integration of these schedules taken to the project's technical, economic, or contractual limit defines the estimated recoverable resources and associated future net cash flow projections for each project. The ratio of EUR to Total Initially-in-Place quantities defines the ultimate recovery efficiency for the development project(s). A project may be defined at various levels and stages of maturity; it may include one or many wells and associated production and processing facilities. One project may develop many reservoirs, or many projects may be applied to one reservoir.
- The Property (lease or license area): Each property may have unique associated contractual rights and obligations including the fiscal terms. Such information allows definition of each participant's share of produced quantities (entitlement) and share of investments, expenses, and revenues for each recovery project and the reservoir to which it is applied. One property may encompass many reservoirs, or one reservoir may span several different properties. A property may contain both discovered and undiscovered accumulations.

In context of this data relationship, "project" is the primary element considered in this resources classification, and net recoverable resources are the incremental quantities derived from each project. Project represents the link between the petroleum accumulation and the decision-making process. A project may, for example, constitute the development of a single reservoir or field, or an incremental development for a producing field, or the integrated development of several fields and associated facilities with a common ownership. In general, an individual project will represent the level at which a decision is made whether or not to proceed (i.e., spend more money) and there should be an associated range of estimated recoverable quantities for that project.

An accumulation or potential accumulation of petroleum may be subject to several separate and distinct projects that are at different stages of exploration or development. Thus, an accumulation may have recoverable quantities in several resource classes simultaneously.

In order to assign recoverable resources of any class, a development plan needs to be defined consisting of one or more projects. Even for Prospective Resources, the estimates of recoverable quantities must be stated in terms of the sales products derived from a development program assuming successful discovery and commercial development. Given the major uncertainties involved at this early stage, the development program will not be of the detail expected in later stages of maturity. In most cases, recovery efficiency may be largely based on analogous projects. In-place quantities for which a feasible project cannot be defined using current, or reasonably forecast improvements in, technology are classified as Unrecoverable.

Not all technically feasible development plans will be commercial. The commercial viability of a development project is dependent on a forecast of the conditions that will exist during the time period encompassed by the project's activities (see

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Commercial Evaluations, section 3.1). "Conditions" include technological, economic, legal, environmental, social, and governmental factors. While economic factors can be summarized as forecast costs and product prices, the underlying influences include, but are not limited to, market conditions, transportation and processing infrastructure, fiscal terms, and taxes.

The resource quantities being estimated are those volumes producible from a project as measured according to delivery specifications at the point of sale or custody transfer (see Reference Point, section 3.2.1). The cumulative production from the evaluation date forward to cessation of production is the remaining recoverable quantity. The sum of the associated annual net cash flows yields the estimated future net revenue. When the cash flows are discounted according to a defined discount rate and time period, the summation of the discounted cash flows is termed net present value (NPV) of the project (see Evaluation and Reporting Guidelines, section 3.0).

The supporting data, analytical processes, and assumptions used in an evaluation should be documented in sufficient detail to allow an independent evaluator or auditor to clearly understand the basis for estimation and categorization of recoverable quantities and their classification.

2.0 Classification and Categorization Guidelines

2.1 Resources Classification

The basic classification requires establishment of criteria for a petroleum discovery and thereafter the distinction between commercial and sub-commercial projects in known accumulations (and hence between Reserves and Contingent Resources).

2.1.1 Determination of Discovery Status

A discovery is one petroleum accumulation, or several petroleum accumulations collectively, for which one or several exploratory wells have established through testing, sampling, and/or logging the existence of a significant quantity of potentially moveable hydrocarbons.

In this context, "significant" implies that there is evidence of a sufficient quantity of petroleum to justify estimating the in-place volume demonstrated by the well(s) and for evaluating the potential for economic recovery. Estimated recoverable quantities within such a discovered (known) accumulation(s) shall initially be classified as Contingent Resources pending definition of projects with sufficient chance of commercial development to reclassify all, or a portion, as Reserves. Where in-place hydrocarbons are identified but are not considered currently recoverable, such quantities may be classified as Discovered Unrecoverable, if considered appropriate for resource management purposes; a portion of these quantities may become recoverable resources in the future as commercial circumstances change or technological developments occur.

2.1.2 Determination of Commerciality

Discovered recoverable volumes (Contingent Resources) may be considered commercially producible, and thus Reserves, if the entity claiming commerciality has demonstrated firm intention to proceed with development and such intention is based upon all of the following criteria:

- Evidence to support a reasonable timetable for development.
- A reasonable assessment of the future economics of such development projects meeting defined investment and operating criteria.
- A reasonable expectation that there will be a market for all or at least the expected sales quantities of production required to justify development.
- Evidence that the necessary production and transportation facilities are available or can be made available.
- Evidence that legal, contractual, environmental and other social and economic concerns will allow for the actual implementation of the recovery project being evaluated.

To be included in the Reserves class, a project must be sufficiently defined to establish its commercial viability. There must be a reasonable expectation that all required internal and external approvals will be forthcoming, and there is evidence of firm intention to proceed with development within a reasonable time frame. A reasonable time frame for the initiation of development depends on the specific circumstances and varies according to the scope of the project. While 5 years is recommended as a benchmark, a longer time frame could be applied where, for example, development of economic projects are deferred at the option of the producer for, among other things, market-related reasons, or to meet contractual or strategic objectives. In all cases, the justification for classification as Reserves should be clearly documented.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

To be included in the Reserves class, there must be a high confidence in the commercial producibility of the reservoir as supported by actual production or formation tests. In certain cases, Reserves may be assigned on the basis of well logs and/or core analysis that indicate that the subject reservoir is hydrocarbon-bearing and is analogous to reservoirs in the same area that are producing or have demonstrated the ability to produce on formation tests.

2.2 Resources Categorization

The horizontal axis in the Resources Classification (Figure 1.1) defines the range of uncertainty in estimates of the quantities of recoverable, or potentially recoverable, petroleum associated with a project. These estimates include both technical and commercial uncertainty components as follows:

- The total petroleum remaining within the accumulation (in-place resources).
- That portion of the in-place petroleum that can be recovered by applying a defined development project or projects.
- Variations in the commercial conditions that may impact the quantities recovered and sold (e.g., market availability, contractual changes).

Where commercial uncertainties are such that there is significant risk that the complete project (as initially defined) will not proceed, it is advised to create a separate project classified as Contingent Resources with an appropriate chance of commerciality.

2.2.1 Range of Uncertainty

The range of uncertainty of the recoverable and/or potentially recoverable volumes may be represented by either deterministic scenarios or by a probability distribution (see Deterministic and Probabilistic Methods, section 4.2).

When the range of uncertainty is represented by a probability distribution, a low, best, and high estimate shall be provided such that:

- There should be at least a 90% probability (P90) that the quantities actually recovered will equal or exceed the low estimate.
- There should be at least a 50% probability (P50) that the quantities actually recovered will equal or exceed the best estimate.
- There should be at least a 10% probability (P10) that the quantities actually recovered will equal or exceed the high estimate.

When using the deterministic scenario method, typically there should also be low, best, and high estimates, where such estimates are based on qualitative assessments of relative uncertainty using consistent interpretation guidelines. Under the deterministic incremental (risk-based) approach, quantities at each level of uncertainty are estimated discretely and separately (see Category Definitions and Guidelines, section 2.2.2).

These same approaches to describing uncertainty may be applied to Reserves, Contingent Resources, and Prospective Resources. While there may be significant risk that sub-commercial and undiscovered accumulations will not achieve commercial production, it is useful to consider the range of potentially recoverable quantities independently of such a risk or consideration of the resource class to which the quantities will be assigned.

2.2.2 Category Definitions and Guidelines

Evaluators may assess recoverable quantities and categorize results by uncertainty using the deterministic incremental (risk-based) approach, the deterministic scenario (cumulative) approach, or probabilistic methods (see "2001 Supplemental Guidelines," Chapter 2.5). In many cases, a combination of approaches is used.

Use of consistent terminology (Figure 1.1) promotes clarity in communication of evaluation results. For Reserves, the general cumulative terms low/best/high estimates are denoted as 1P/2P/3P, respectively. The associated incremental quantities are termed Proved, Probable and Possible. Reserves are a subset of, and must be viewed within context of, the complete resources classification system. While the categorization criteria are proposed specifically for Reserves, in most cases, they can be equally applied to Contingent and Prospective Resources conditional upon their satisfying the criteria for discovery and/or development.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

For Contingent Resources, the general cumulative terms low/best/high estimates are denoted as 1C/2C/3C respectively. For Prospective Resources, the general cumulative terms low/best/high estimates still apply. No specific terms are defined for incremental quantities within Contingent and Prospective Resources.

Without new technical information, there should be no change in the distribution of technically recoverable volumes and their categorization boundaries when conditions are satisfied sufficiently to reclassify a project from Contingent Resources to Reserves. All evaluations require application of a consistent set of forecast conditions, including assumed future costs and prices, for both classification of projects and categorization of estimated quantities recovered by each project (see Commercial Evaluations, section 3.1).

Based on additional data and updated interpretations that indicate increased certainty, portions of Possible and Probable Reserves may be re-categorized as Probable and Proved Reserves.

Uncertainty in resource estimates is best communicated by reporting a range of potential results. However, if it is required to report a single representative result, the "best estimate" is considered the most realistic assessment of recoverable quantities. It is generally considered to represent the sum of Proved and Probable estimates (2P) when using the deterministic scenario or the probabilistic assessment methods. It should be noted that under the deterministic incremental (risk-based) approach, discrete estimates are made for each category, and they should not be aggregated without due consideration of their associated risk (see "2001 Supplemental Guidelines," Chapter 2.5).

Table 1: Recoverable Resources Classes and Sub-Classes

Class/Sub-Class	Definition	Guidelines
Reserves	Reserves are those quantities of petroleum anticipated to be commercially recoverable by application of development projects to known accumulations from a given date forward under defined conditions.	Reserves must satisfy four criteria: they must be discovered, recoverable, commercial, and remaining based on the development project(s) applied. Reserves are further subdivided in accordance with the level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterized by their development and production status. To be included in the Reserves class, a project must be sufficiently defined to establish its commercial viability. There must be a reasonable expectation that all required internal and external approvals will be forthcoming, and there is evidence of firm intention to proceed with development within a reasonable time frame. A reasonable time frame for the initiation of development depends on the specific circumstances and varies according to the scope of the project. While 5 years is recommended as a benchmark, a longer time frame could be applied where, for example, development of economic projects are deferred at the option of the producer for, among other things, market-related reasons, or to meet contractual or strategic objectives. In all cases, the justification for classification as Reserves should be clearly documented. To be included in the Reserves class, there must be a high confidence in the commercial producibility of the reservoir as supported by actual production or formation tests. In certain cases, Reserves may be assigned on the basis of well logs and/or core analysis that indicate that the subject reservoir is hydrocarbon-bearing and is analogous to reservoirs in the same area that are producing or have demonstrated the ability to produce on formation tests.
On Production	The development project is currently producing and selling petroleum to market.	The key criterion is that the project is receiving income from sales, rather than the approved development project necessarily being complete. This is the point at which the project "chance of commerciality" can be said to be 100%. The project "decision gate" is the decision to initiate commercial production from the project.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Class/Sub-Class	Definition	Guidelines
Approved for Development	All necessary approvals have been obtained, capital funds have been committed, and implementation of the development project is under way.	At this point, it must be certain that the development project is going ahead. The project must not be subject to any contingencies such as outstanding regulatory approvals or sales contracts. Forecast capital expenditures should be included in the reporting entity's current or following year's approved budget. The project "decision gate" is the decision to start investing capital in the construction of production facilities and/or drilling development wells.
Justified for Development	Implementation of the development project is justified on the basis of reasonable forecast commercial conditions at the time of reporting, and there are reasonable expectations that all necessary approvals/contracts will be obtained.	In order to move to this level of project maturity, and hence have reserves associated with it, the development project must be commercially viable at the time of reporting, based on the reporting entity's assumptions of future prices, costs, etc. ("forecast case") and the specific circumstances of the project. Evidence of a firm intention to proceed with development within a reasonable time frame will be sufficient to demonstrate commerciality. There should be a development plan in sufficient detail to support the assessment of commerciality and a reasonable expectation that any regulatory approvals or sales contracts required prior to project implementation will be forthcoming. Other than such approvals/contracts, there should be no known contingencies that could preclude the development from proceeding within a reasonable timeframe (see Reserves class). The project "decision gate" is the decision by the reporting entity and its partners, if any, that the project has reached a level of technical and commercial maturity sufficient to justify proceeding with development at that point in time.
Contingent Resources	Those quantities of petroleum estimated, as of a given date, to be potentially recoverable from known accumulations by application of development projects, but which are not currently considered to be commercially recoverable due to one or more contingencies.	Contingent Resources may include, for example, projects for which there are currently no viable markets, or where commercial recovery is dependent on technology under development, or where evaluation of the accumulation is insufficient to clearly assess commerciality. Contingent Resources are further categorized in accordance with the level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterized by their economic status.
Development Pending	A discovered accumulation where project activities are ongoing to justify commercial development in the foreseeable future.	The project is seen to have reasonable potential for eventual commercial development, to the extent that further data acquisition (e.g. drilling, seismic data) and/or evaluations are currently ongoing with a view to confirming that the project is commercially viable and providing the basis for selection of an appropriate development plan. The critical contingencies have been identified and are reasonably expected to be resolved within a reasonable time frame. Note that disappointing appraisal/evaluation results could lead to a re-classification of the project to "On Hold" or "Not Viable" status. The project "decision gate" is the decision to undertake further data acquisition and/or studies designed to move the project to a level of technical and commercial maturity at which a decision can be made to proceed with development and production.
Development Unclassified or on Hold	A discovered accumulation where project activities are on hold and/or where justification as a commercial development may be subject to significant delay.	The project is seen to have potential for eventual commercial development, but further appraisal/evaluation activities are on hold pending the removal of significant contingencies external to the project, or substantial further appraisal/evaluation activities are required to clarify the potential for eventual commercial development. Development may be subject to a significant time delay. Note that a change in circumstances, such that there is no longer a reasonable expectation that a critical contingency can be removed in the foreseeable future, for example, could lead to a reclassification of the project to "Not Viable" status. The project "decision gate" is the decision to either proceed with additional evaluation designed to clarify the potential for eventual commercial development or to temporarily suspend or delay further activities pending resolution of external contingencies.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Class/Sub-Class	Definition	Guidelines
Development Not Viable	A discovered accumulation for which there are no current plans to develop or to acquire additional data at the time due to limited production potential.	The project is not seen to have potential for eventual commercial development at the time of reporting, but the theoretically recoverable quantities are recorded so that the potential opportunity will be recognized in the event of a major change in technology or commercial conditions. The project "decision gate" is the decision not to undertake any further data acquisition or studies on the project for the foreseeable future.
Prospective Resources	Those quantities of petroleum which are estimated, as of a given date, to be potentially recoverable from undiscovered accumulations.	Potential accumulations are evaluated according to their chance of discovery and, assuming a discovery, the estimated quantities that would be recoverable under defined development projects. It is recognized that the development programs will be of significantly less detail and depend more heavily on analog developments in the earlier phases of exploration.
Prospect	A project associated with a potential accumulation that is sufficiently well defined to represent a viable drilling target.	Project activities are focused on assessing the chance of discovery and, assuming discovery, the range of potential recoverable quantities under a commercial development program.
Lead	A project associated with a potential accumulation that is currently poorly defined and requires more data acquisition and/or evaluation in order to be classified as a prospect.	Project activities are focused on acquiring additional data and/or undertaking further evaluation designed to confirm whether or not the lead can be matured into a prospect. Such evaluation includes the assessment of the chance of discovery and, assuming discovery, the range of potential recovery under feasible development scenarios.
Play	A project associated with a prospective trend of potential prospects, but which requires more data acquisition and/or evaluation in order to define specific leads or prospects.	Project activities are focused on acquiring additional data and/or undertaking further evaluation designed to define specific leads or prospects for more detailed analysis of their chance of discovery and, assuming discovery, the range of potential recovery under hypothetical development scenarios.

Table 2: Reserves Status Definitions and Guidelines

Status	Definition	Guidelines
Developed Reserves	Developed Reserves are expected quantities to be recovered from existing wells and facilities.	Reserves are considered developed only after the necessary equipment has been installed, or when the costs to do so are relatively minor compared to the cost of a well. Where required facilities become unavailable, it may be necessary to reclassify Developed Reserves as Undeveloped. Developed Reserves may be further sub-classified as Producing or Non-Producing.
Developed Producing Reserves	Developed Producing Reserves are expected to be recovered from completion intervals that are open and producing at the time of the estimate.	Improved recovery reserves are considered producing only after the improved recovery project is in operation.
Developed Non-Producing Reserves	Developed Non-Producing Reserves include shut-in and behind-pipe Reserves.	Shut-in Reserves are expected to be recovered from (1) completion intervals which are open at the time of the estimate but which have not yet started producing, (2) wells which were shut-in for market conditions or pipeline connections, or (3) wells not capable of production for mechanical reasons. Behind-pipe Reserves are expected to be recovered from zones in existing wells which will require additional completion work or future re-completion prior to start of production. In all cases, production can be initiated or restored with relatively low expenditure compared to the cost of drilling a new well.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Status	Definition	Guidelines
Undeveloped Reserves	Undeveloped Reserves are quantities expected to be recovered through future investments:	(1) from new wells on undrilled acreage in known accumulations, (2) from deepening existing wells to a different (but known) reservoir, (3) from infill wells that will increase recovery, or (4) where a relatively large expenditure (e.g. when compared to the cost of drilling a new well) is required to (a) recomplete an existing well or (b) install production or transportation facilities for primary or improved recovery projects.

Table 3: Reserves Category Definitions and Guidelines

Category	Definition	Guidelines
Proved Reserves	Proved Reserves are those quantities of petroleum, which by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under defined economic conditions, operating methods, and government regulations.	If deterministic methods are used, the term reasonable certainty is intended to express a high degree of confidence that the quantities will be recovered. If probabilistic methods are used, there should be at least a 90% probability that the quantities actually recovered will equal or exceed the estimate. The area of the reservoir considered as Proved includes (1) the area delineated by drilling and defined by fluid contacts, if any, and (2) adjacent undrilled portions of the reservoir that can reasonably be judged as continuous with it and commercially productive on the basis of available geoscience and engineering data. In the absence of data on fluid contacts, Proved quantities in a reservoir are limited by the lowest known hydrocarbon (LKH) as seen in a well penetration unless otherwise indicated by definitive geoscience, engineering, or performance data. Such definitive information may include pressure gradient analysis and seismic indicators. Seismic data alone may not be sufficient to define fluid contacts for Proved reserves (see "2001 Supplemental Guidelines," Chapter 8). Reserves in undeveloped locations may be classified as Proved provided that: • The locations are in undrilled areas of the reservoir that can be judged with reasonable certainty to be commercially productive. • Interpretations of available geoscience and engineering data indicate with reasonable certainty that the objective formation is laterally continuous with drilled Proved locations. For Proved Reserves, the recovery efficiency applied to these reservoirs should be defined based on a range of possibilities supported by analogs and sound engineering judgment considering the characteristics of the Proved area and the applied development program.
Probable Reserves	Probable Reserves are those additional Reserves which analysis of geoscience and engineering data indicate are less likely to be recovered than Proved Reserves but more certain to be recovered than Possible Reserves.	It is equally likely that actual remaining quantities recovered will be greater than or less than the sum of the estimated Proved plus Probable Reserves (2P). In this context, when probabilistic methods are used, there should be at least a 50% probability that the actual quantities recovered will equal or exceed the 2P estimate. Probable Reserves may be assigned to areas of a reservoir adjacent to Proved where data control or interpretations of available data are less certain. The interpreted reservoir continuity may not meet the reasonable certainty criteria. Probable estimates also include incremental recoveries associated with project recovery efficiencies beyond that assumed for Proved.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Category	Definition	Guidelines
Possible Reserves	Possible Reserves are those additional reserves which analysis of geoscience and engineering data indicate are less likely to be recoverable than Probable Reserves.	The total quantities ultimately recovered from the project have a low probability to exceed the sum of Proved plus Probable plus Possible (3P), which is equivalent to the high estimate scenario. When probabilistic methods are used, there should be at least a 10% probability that the actual quantities recovered will equal or exceed the 3P estimate. Possible Reserves may be assigned to areas of a reservoir adjacent to Probable where data control and interpretations of available data are progressively less certain. Frequently, this may be in areas where geoscience and engineering data are unable to clearly define the area and vertical reservoir limits of commercial production from the reservoir by a defined project. Possible estimates also include incremental quantities associated with project recovery efficiencies beyond that assumed for Probable.
Probable and Possible Reserves	(See above for separate criteria for Probable Reserves and Possible Reserves.)	The 2P and 3P estimates may be based on reasonable alternative technical and commercial interpretations within the reservoir and/or subject project that are clearly documented, including comparisons to results in successful similar projects. In conventional accumulations, Probable and/or Possible Reserves may be assigned where geoscience and engineering data identify directly adjacent portions of a reservoir within the same accumulation that may be separated from Proved areas by minor faulting or other geological discontinuities and have not been penetrated by a wellbore but are interpreted to be in communication with the known (Proved) reservoir. Probable or Possible Reserves may be assigned to areas that are structurally higher than the Proved area. Possible (and in some cases, Probable) Reserves may be assigned to areas that are structurally lower than the adjacent Proved or 2P area. Caution should be exercised in assigning Reserves to adjacent reservoirs isolated by major, potentially sealing, faults until this reservoir is penetrated and evaluated as commercially productive. Justification for assigning Reserves in such cases should be clearly documented. Reserves should not be assigned to areas that are clearly separated from a known accumulation by non-productive reservoir (i.e., absence of reservoir, structurally low reservoir, or negative test results); such areas may contain Prospective Resources. In conventional accumulations, where drilling has defined a highest known oil (HKO) elevation and there exists the potential for an associated gas cap, Proved oil Reserves should only be assigned in the structurally higher portions of the reservoir if there is reasonable certainty that such portions are initially above bubble point pressure based on documented engineering analyses. Reservoir portions that do not meet this certainty may be assigned as Probable and Possible oil and/or gas based on reservoir fluid properties and pressure gradient interpretations.

The 2007 Petroleum Resources Management System can be viewed in its entirety at
<http://www.spe.org/spe-app/spe/industry/reserves/prms.htm>.

REVENUE, COSTS, AND TAXES
PROVED UNDEVELOPED RESERVES
DELEK INVESTMENTS AND PROPERTIES LTD.
NOA FIELD, OFFSHORE ISRAEL
AS OF DECEMBER 31, 2011

Period Ending	Working Interest Revenue ⁽¹⁾ (M\$)	Royalties			Net Capital Costs (M\$)	Abandonment Costs (M\$)	Operating Expenses ⁽²⁾ (M\$)	Net Revenue Before Levy and Corporate Income Taxes		Levy Rate (%)	Net Revenue After Levy and Corporate Income Taxes		Income Tax Rate ⁽³⁾ (%)	Corporate Income Tax ⁽³⁾ (M\$)	Future Net Revenue After Levy and Corporate Income Taxes					
		State (M\$)	Interested Party (M\$)	Third Party (M\$)				Total (M\$)	Income Taxes Discounted at 0% (M\$)		Levy Rate (%)	Income Taxes Discounted at 0% (M\$)			Levy Rate (%)	Income Taxes Discounted at 0% (M\$)	Discounted at 5% (M\$)	Discounted at 10% (M\$)	Discounted at 15% (M\$)	Discounted at 20% (M\$)
12-31-2012	28,242.3	1,553.4	309.7	148.7	2,011.8	47,407.3	0.0	1,260.6	(22,037.2)	0.0	0.0	(22,037.2)	25.0	0.0	(21,011.6)	(20,549.8)	(20,117.1)			
12-31-2013	36,944.0	2,032.0	405.6	193.3	2,630.8	0.0	4,427.9	845.9	29,562.7	0.0	0.0	29,562.7	25.0	0.0	25,624.5	23,971.7	22,489.1			
12-31-2014	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0			
12-31-2015	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0			
12-31-2016	0.0	0.0	0.0	0.0	0.0	0.0	1,518.3	0.0	(1,518.3)	0.0	0.0	(1,518.3)	25.0	0.0	(988.7)	(809.5)	(668.4)			
Total	65,186.4	3,585.4	715.2	342.0	4,642.6	47,407.3	5,946.1	2,106.5	6,007.3	0.0	0.0	6,007.3	25.0	0.0	3,624.1	4,751.4	2,612.4	1,703.6		

Totals may not add because of rounding.

⁽¹⁾ For the purposes of the model, we have not attributed any part of the revenues to services.

⁽²⁾ Operating expenses are intended to include only direct project-level costs and Delek Investments and Properties Ltd.'s estimate of the portion of its headquarters general and administrative overhead expenses that can be directly attributed to this project.

⁽³⁾ Corporate income tax rates and estimates of corporate income taxes are provided by Delek Investments and Properties Ltd. and are its expected corporate income taxes per year.

MONTE CARLO INPUT DISTRIBUTION SUMMARY
DELEK INVESTMENTS AND PROPERTIES LTD.
NOA FIELD, OFFSHORE ISRAEL
AS OF DECEMBER 31, 2011

Parameter (Units)	Proved + 1C	Proved + 3C
Gross Rock Volume (Acre-feet)	109,591	140,800
Area (Acres)	3,115	3,961
Average Gross Thickness ⁽¹⁾ (Feet)	35	36
Net-to-Gross Ratio (Decimal)	0.471	0.511
Porosity (Decimal)	0.282	0.302
Water Saturation (Decimal)	0.382	0.342
Gas Formation Volume Factor (standard cubic feet per reservoir cubic feet)	223	223
Gas Recovery Factor (Decimal)	0.650	0.750

Note: For the purposes of this report, we used technical data including, but not limited to, well logs, geologic maps, seismic data, well test data, and property ownership interests.

⁽¹⁾ Average gross thickness is calculated by dividing the gross rock volume by the area.

Table II

All estimates and exhibits herein are part of this NSAI report and are subject to its parameters and conditions.

March 22, 2012

Delek Investments and Properties Ltd.
7 Giborei Israel Street
Netanya 42504
Israel

Ladies and Gentlemen:

In accordance with your request, we have estimated the proved developed, probable, and possible reserves and future revenue, as of December 31, 2011, to the Delek Investments and Properties Ltd. (DI) interest in certain gas properties located in Mari B Field, offshore Israel. It is our understanding that DI owns a direct interest in these properties and a 6.53 percent interest in Delek Drilling Limited Partnership (Delek Drilling), a 9.11 percent interest in Avner Oil Exploration Limited Partnership (Avner), an 86.71 percent interest in Delek Energy Systems Ltd., and a 51.76 percent interest in Cohen Development & Industrial Buildings Ltd. Delek Drilling and Avner own direct interests in these properties. We completed our evaluation on or about the date of this letter. This report has been prepared using price and cost parameters specified by DI, as discussed in subsequent paragraphs of this letter. These estimates have been prepared in accordance with internationally recognized standards, as stipulated by the Israel Securities Authority (ISA). The estimates in this report have been prepared in accordance with the definitions and guidelines set forth in the 2007 Petroleum Resources Management System (PRMS) approved by the Society of Petroleum Engineers (SPE); definitions are presented immediately following this letter. The 2007 PRMS project maturity sub-class for these reserves is "on production". This report has been prepared for DI's use in filing with the ISA; in our opinion the assumptions, data, methods, and procedures used in the preparation of this report are appropriate for such purpose.

We estimate the gas reserves and future net revenue, discounted at 0, 5, 10, 15, and 20 percent, to the DI interest in these properties, as of December 31, 2011, to be:

Category	Gas Reserves (BCF)		Future Net Revenue After Levy and Corporate Income Taxes (M\$)				
	Gross	Working Interest	Discounted at 0%	Discounted at 5%	Discounted at 10%	Discounted at 15%	Discounted at 20%
Proved Developed	206.3	65.2	87,662.6	78,601.5	69,999.4	63,640.9	59,046.3
Probable	22.0	6.9	6,670.5	4,829.4	3,672.6	2,892.1	2,337.3
Proved + Probable	228.2	72.2	94,333.0	83,430.9	73,672.0	66,533.0	61,383.5
Possible	22.0	7.0	6,991.8	4,957.1	3,726.7	2,919.3	2,355.1
Proved + Probable + Possible	250.3	79.2	101,324.8	88,388.0	77,398.7	69,452.3	63,738.6

Totals may not add because of rounding.

Gas volumes are expressed in billions of cubic feet (BCF) at standard temperature and pressure bases. These properties have never produced commercial volumes of condensate. Monetary values shown in this report are

expressed in United States dollars (\$) or thousands of United States dollars (M\$). For your reference, the March 22, 2012, exchange rate was 3.73 Israeli New Shekels (NIS) per United States dollar.

The estimates in this report are for proved developed, probable, and possible reserves. Our study indicates that there are no proved undeveloped reserves for these properties at this time. This report does not include any value that could be attributed to interests in undeveloped acreage. Reserves categorization conveys the relative degree of certainty; reserves subcategorization is based on development and production status. The estimates of reserves included herein have not been adjusted for risk.

Working interest revenue shown in this report is DI's share of the gross (100 percent) revenue from the properties prior to any deductions. Future net revenue is after deductions for royalties, capital costs, abandonment costs, operating expenses, an oil and gas profits levy, and DI's corporate income taxes. The future net revenue has been discounted at annual rates of 0, 5, 10, 15, and 20 percent to determine its present worth, which is shown to indicate the effect of time on the value of money. Future net revenue presented in this report, whether discounted or undiscounted, should not be construed as being the fair market value of the properties. Tables I through III present revenue, costs, and taxes by reserves category. Table IV presents DI's historical net production and operating costs, royalties, and net revenue per production unit.

As requested, this report has been prepared using gas price parameters specified by DI. The initial gas price of \$4.404 per MMBTU is held constant through December 31, 2012, decreased to \$3.15 per MMBTU and held constant through December 31, 2015, and then decreased to \$2.50 per MMBTU and held constant throughout the remaining lives of the properties.

Operating costs used in this report are based on operating expense records provided by DI. As requested, these costs include direct project-level costs and DI's portion of its headquarters general and administrative overhead expenses that can be directly attributed to this project. As requested, operating costs are held constant throughout the lives of the properties.

Capital costs used in this report were provided by DI and are based on authorizations for expenditure and actual costs from recent activity. Capital costs are included as required for platform upgrades. Based on our understanding of DI's future development plans, a review of the records provided to us, and our knowledge of similar properties, we regard these estimated capital costs to be reasonable. Abandonment costs used in this report are DI's estimates of the costs to abandon the wells, platforms, and production facilities; these estimates do not include any salvage value for the lease and well equipment. As requested, capital costs and abandonment costs are held constant to the date of expenditure.

For the purposes of this report, we did not perform any field inspection of the properties, nor did we examine the mechanical operation or condition of the wells and facilities. We have not investigated possible environmental liability related to the properties; however, we are not currently aware of any possible environmental liability that would have any material effect on the reserves estimated in this report or the commerciality of such reserves estimates. Therefore, our estimates do not include any costs due to such possible liability.

We have made no investigation of potential gas volume and value imbalances resulting from overdelivery or underdelivery to the DI interest. Therefore, our estimates of reserves and future revenue do not include adjustments for the settlement of any such imbalances; our projections are based on DI receiving its net revenue interest share of estimated future gross gas production.

The reserves shown in this report are estimates only and should not be construed as exact quantities. Proved reserves are those quantities of oil and gas which, by analysis of engineering and geoscience data, can be

estimated with reasonable certainty to be commercially recoverable; probable and possible reserves are those additional reserves which are sequentially less certain to be recovered than proved reserves. There is a 10 percent chance that the quantities produced will be equal to, or greater than, the quantities of the proved plus probable plus possible reserves. Estimates of reserves may increase or decrease as a result of market conditions, future operations, changes in regulations, or actual reservoir performance. In addition to the primary economic assumptions discussed herein, our estimates are based on certain assumptions including, but not limited to, that the properties will be developed consistent with current development plans, that the properties will be operated in a prudent manner, that no governmental regulations or controls will be put in place that would impact the ability of interest owner to recover the reserves, and that our projections of future production will prove consistent with actual performance. If the reserves are recovered, the revenues therefrom and the costs related thereto could be more or less than the estimated amounts. Because of governmental policies and uncertainties of supply and demand, the sales rates, prices received for the reserves, and costs incurred in recovering such reserves may vary from assumptions made while preparing this report. It should be noted that the actual production profile for each category may be lower or higher than the production profile used to calculate the estimates of future net revenue used in this report, and no sensitivity analysis was performed by Netherland, Sewell & Associates, Inc. (NSAI) with respect to the production profile of the wells. This sensitivity analysis could lead to the conclusion that the reserves are not economic.

For the purposes of this report, we used technical and economic data including, but not limited to, well logs, geologic maps, seismic data, well test data, production data, historical price and cost information, and property ownership interests. We were provided with all the necessary data to prepare the reserves estimates for this property, and we were not limited from access to any material we believe may be relevant. The reserves in this report have been estimated using deterministic methods; these estimates have been prepared in accordance with generally accepted petroleum engineering and evaluation principles set forth in the Standards Pertaining to the Estimating and Auditing of Oil and Gas Reserves Information promulgated by the Society of Petroleum Engineers (SPE Standards). We used standard engineering and geoscience methods, or a combination of methods, including performance analysis, volumetric analysis, and analogy, that we considered to be appropriate and necessary to classify, categorize, and estimate reserves in accordance with PRMS definitions and guidelines. As in all aspects of oil and gas evaluation, there are uncertainties inherent in the interpretation of engineering and geoscience data; therefore, our conclusions necessarily represent only informed professional judgment.

NSAI was engaged on February 1, 2012, by Mr. Gideon Tadmor, Chairman of DI, to perform this assessment. The data used in our estimates were obtained from Noble Energy, Inc.; Noble Energy Mediterranean, Ltd.; Avner; Delek Drilling; DI; public data sources; and the nonconfidential files of NSAI and were accepted as accurate. Supporting geoscience, performance, and work data are on file in our office. The contractual rights to the properties have not been examined by NSAI, nor has the actual degree or type of interest owned been independently confirmed. We are independent petroleum engineers, geologists, geophysicists, and petrophysicists; we do not own an interest in these properties nor are we employed on a contingent basis. Furthermore, no limitations or restrictions were placed upon NSAI by officials of DI.

QUALIFICATIONS

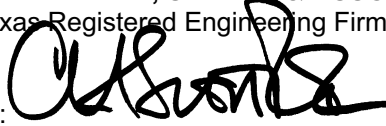
NSAI performs consulting petroleum engineering services under Texas Board of Professional Engineers Registration No. F-2699. We provide a complete range of geological, geophysical, petrophysical, and engineering services, and we have the technical expertise and ability to perform these services in any oil and gas producing area in the world. The staff is familiar with the recognized industry reserves and resources definitions, specifically those promulgated by the U.S. Securities and Exchange Commission, by the Alberta Securities Commission, and by the SPE, Society of Petroleum Evaluation Engineers, World Petroleum Council, and

American Association of Petroleum Geologists. The technical persons responsible for preparing the estimates presented herein meet the requirements regarding qualifications, independence, objectivity, and confidentiality set forth in the SPE Standards.

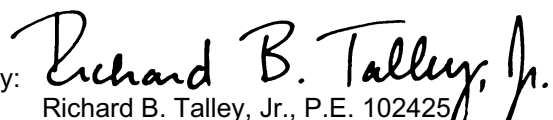
This assessment has been led by Mr. Richard B. Talley, Jr. and Mr. David E. Nice. Mr. Talley and Mr. Nice are Vice Presidents in the firm's Houston office at 1221 Lamar Street, Suite 1200, Houston, Texas 77010, USA. Mr. Talley maintains a valid Professional Engineer License (Texas Registration No. 102425). He has been practicing consulting petroleum engineering at NSAI since 2004 and has over 5 years prior industry experience. Mr. Nice maintains a valid Professional Geoscientist License (Texas Registration No. 346). He has been practicing consulting petroleum geoscience at NSAI since 1998 and has over 13 years prior industry experience.

Sincerely,

NETHERLAND, SEWELL & ASSOCIATES, INC.
Texas Registered Engineering Firm F-2699

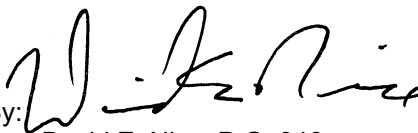
By: 

C.H. (Scott) Rees III, P.E.
Chairman and Chief Executive Officer

By: 
Richard B. Talley, Jr., P.E. 102425
Vice President

Date Signed: March 22, 2012

RBT:DEG

By: 
David E. Nice, P.G. 346
Vice President

Date Signed: March 22, 2012

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

This document contains information excerpted from definitions and guidelines prepared by the Oil and Gas Reserves Committee of the Society of Petroleum Engineers (SPE) and reviewed and jointly sponsored by the World Petroleum Council (WPC), the American Association of Petroleum Geologists (AAPG), and the Society of Petroleum Evaluation Engineers (SPEE).

Preamble

Petroleum resources are the estimated quantities of hydrocarbons naturally occurring on or within the Earth's crust. Resource assessments estimate total quantities in known and yet-to-be-discovered accumulations; resources evaluations are focused on those quantities that can potentially be recovered and marketed by commercial projects. A petroleum resources management system provides a consistent approach to estimating petroleum quantities, evaluating development projects, and presenting results within a comprehensive classification framework.

These definitions and guidelines are designed to provide a common reference for the international petroleum industry, including national reporting and regulatory disclosure agencies, and to support petroleum project and portfolio management requirements. They are intended to improve clarity in global communications regarding petroleum resources. It is expected that this document will be supplemented with industry education programs and application guides addressing their implementation in a wide spectrum of technical and/or commercial settings.

It is understood that these definitions and guidelines allow flexibility for users and agencies to tailor application for their particular needs; however, any modifications to the guidance contained herein should be clearly identified. The definitions and guidelines contained in this document must not be construed as modifying the interpretation or application of any existing regulatory reporting requirements.

1.0 Basic Principles and Definitions

The estimation of petroleum resource quantities involves the interpretation of volumes and values that have an inherent degree of uncertainty. These quantities are associated with development projects at various stages of design and implementation. Use of a consistent classification system enhances comparisons between projects, groups of projects, and total company portfolios according to forecast production profiles and recoveries. Such a system must consider both technical and commercial factors that impact the project's economic feasibility, its productive life, and its related cash flows.

1.1 Petroleum Resources Classification Framework

Petroleum is defined as a naturally occurring mixture consisting of hydrocarbons in the gaseous, liquid, or solid phase. Petroleum may also contain non-hydrocarbons, common examples of which are carbon dioxide, nitrogen, hydrogen sulfide and sulfur. In rare cases, non-hydrocarbon content could be greater than 50%.

The term "resources" as used herein is intended to encompass all quantities of petroleum naturally occurring on or within the Earth's crust, discovered and undiscovered (recoverable and unrecoverable), plus those quantities already produced. Further, it includes all types of petroleum whether currently considered "conventional" or "unconventional."

Figure 1-1 is a graphical representation of the SPE/WPC/AAPG/SPEE resources classification system. The system defines the major recoverable resources classes: Production, Reserves, Contingent Resources, and Prospective Resources, as well as Unrecoverable petroleum.

The "Range of Uncertainty" reflects a range of estimated quantities potentially recoverable from an accumulation by a project, while the vertical axis represents the "Chance of

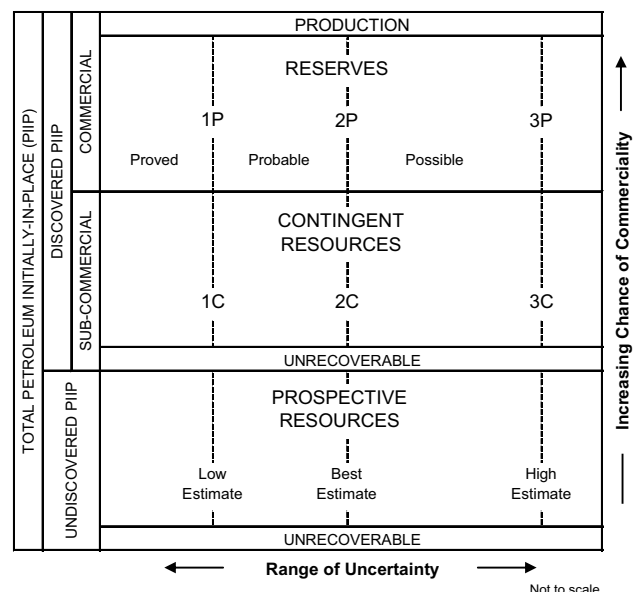


Figure 1-1: Resources Classification Framework.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Commerciality", that is, the chance that the project that will be developed and reach commercial producing status. The following definitions apply to the major subdivisions within the resources classification:

TOTAL PETROLEUM INITIALLY-IN-PLACE is that quantity of petroleum that is estimated to exist originally in naturally occurring accumulations. It includes that quantity of petroleum that is estimated, as of a given date, to be contained in known accumulations prior to production plus those estimated quantities in accumulations yet to be discovered (equivalent to "total resources").

DISCOVERED PETROLEUM INITIALLY-IN-PLACE is that quantity of petroleum that is estimated, as of a given date, to be contained in known accumulations prior to production.

PRODUCTION is the cumulative quantity of petroleum that has been recovered at a given date. While all recoverable resources are estimated and production is measured in terms of the sales product specifications, raw production (sales plus non-sales) quantities are also measured and required to support engineering analyses based on reservoir voidage (see Production Measurement, section 3.2).

Multiple development projects may be applied to each known accumulation, and each project will recover an estimated portion of the initially-in-place quantities. The projects shall be subdivided into Commercial and Sub-Commercial, with the estimated recoverable quantities being classified as Reserves and Contingent Resources respectively, as defined below.

RESERVES are those quantities of petroleum anticipated to be commercially recoverable by application of development projects to known accumulations from a given date forward under defined conditions. Reserves must further satisfy four criteria: they must be discovered, recoverable, commercial, and remaining (as of the evaluation date) based on the development project(s) applied. Reserves are further categorized in accordance with the level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterized by development and production status.

CONTINGENT RESOURCES are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from known accumulations, but the applied project(s) are not yet considered mature enough for commercial development due to one or more contingencies. Contingent Resources may include, for example, projects for which there are currently no viable markets, or where commercial recovery is dependent on technology under development, or where evaluation of the accumulation is insufficient to clearly assess commerciality. Contingent Resources are further categorized in accordance with the level of certainty associated with the estimates and may be subclassified based on project maturity and/or characterized by their economic status.

UNDISCOVERED PETROLEUM INITIALLY-IN-PLACE is that quantity of petroleum estimated, as of a given date, to be contained within accumulations yet to be discovered.

PROSPECTIVE RESOURCES are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from undiscovered accumulations by application of future development projects. Prospective Resources have both an associated chance of discovery and a chance of development. Prospective Resources are further subdivided in accordance with the level of certainty associated with recoverable estimates assuming their discovery and development and may be sub-classified based on project maturity.

UNRECOVERABLE is that portion of Discovered or Undiscovered Petroleum Initially-in-Place quantities which is estimated, as of a given date, not to be recoverable by future development projects. A portion of these quantities may become recoverable in the future as commercial circumstances change or technological developments occur; the remaining portion may never be recovered due to physical/chemical constraints represented by subsurface interaction of fluids and reservoir rocks.

Estimated Ultimate Recovery (EUR) is not a resources category, but a term that may be applied to any accumulation or group of accumulations (discovered or undiscovered) to define those quantities of petroleum estimated, as of a given date, to be potentially recoverable under defined technical and commercial conditions plus those quantities already produced (total of recoverable resources).

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

1.2 Project-Based Resources Evaluations

The resources evaluation process consists of identifying a recovery project, or projects, associated with a petroleum accumulation(s), estimating the quantities of Petroleum Initially-in-Place, estimating that portion of those in-place quantities that can be recovered by each project, and classifying the project(s) based on its maturity status or chance of commerciality.

This concept of a project-based classification system is further clarified by examining the primary data sources contributing to an evaluation of net recoverable resources (see Figure 1-2) that may be described as follows:

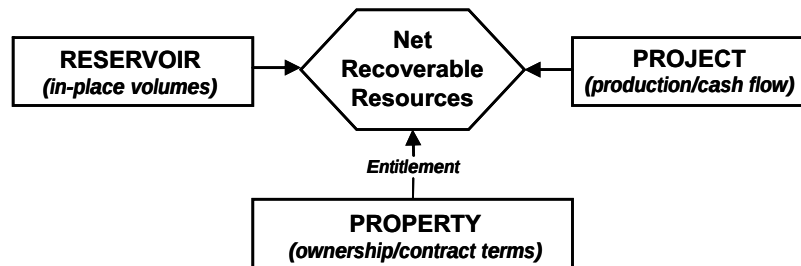


Figure 1-2: Resources Evaluation Data Sources.

- The Reservoir (accumulation): Key attributes include the types and quantities of Petroleum Initially-in-Place and the fluid and rock properties that affect petroleum recovery.
- The Project: Each project applied to a specific reservoir development generates a unique production and cash flow schedule. The time integration of these schedules taken to the project's technical, economic, or contractual limit defines the estimated recoverable resources and associated future net cash flow projections for each project. The ratio of EUR to Total Initially-in-Place quantities defines the ultimate recovery efficiency for the development project(s). A project may be defined at various levels and stages of maturity; it may include one or many wells and associated production and processing facilities. One project may develop many reservoirs, or many projects may be applied to one reservoir.
- The Property (lease or license area): Each property may have unique associated contractual rights and obligations including the fiscal terms. Such information allows definition of each participant's share of produced quantities (entitlement) and share of investments, expenses, and revenues for each recovery project and the reservoir to which it is applied. One property may encompass many reservoirs, or one reservoir may span several different properties. A property may contain both discovered and undiscovered accumulations.

In context of this data relationship, "project" is the primary element considered in this resources classification, and net recoverable resources are the incremental quantities derived from each project. Project represents the link between the petroleum accumulation and the decision-making process. A project may, for example, constitute the development of a single reservoir or field, or an incremental development for a producing field, or the integrated development of several fields and associated facilities with a common ownership. In general, an individual project will represent the level at which a decision is made whether or not to proceed (i.e., spend more money) and there should be an associated range of estimated recoverable quantities for that project.

An accumulation or potential accumulation of petroleum may be subject to several separate and distinct projects that are at different stages of exploration or development. Thus, an accumulation may have recoverable quantities in several resource classes simultaneously.

In order to assign recoverable resources of any class, a development plan needs to be defined consisting of one or more projects. Even for Prospective Resources, the estimates of recoverable quantities must be stated in terms of the sales products derived from a development program assuming successful discovery and commercial development. Given the major uncertainties involved at this early stage, the development program will not be of the detail expected in later stages of maturity. In most cases, recovery efficiency may be largely based on analogous projects. In-place quantities for which a feasible project cannot be defined using current, or reasonably forecast improvements in, technology are classified as Unrecoverable.

Not all technically feasible development plans will be commercial. The commercial viability of a development project is dependent on a forecast of the conditions that will exist during the time period encompassed by the project's activities (see

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Commercial Evaluations, section 3.1). "Conditions" include technological, economic, legal, environmental, social, and governmental factors. While economic factors can be summarized as forecast costs and product prices, the underlying influences include, but are not limited to, market conditions, transportation and processing infrastructure, fiscal terms, and taxes.

The resource quantities being estimated are those volumes producible from a project as measured according to delivery specifications at the point of sale or custody transfer (see Reference Point, section 3.2.1). The cumulative production from the evaluation date forward to cessation of production is the remaining recoverable quantity. The sum of the associated annual net cash flows yields the estimated future net revenue. When the cash flows are discounted according to a defined discount rate and time period, the summation of the discounted cash flows is termed net present value (NPV) of the project (see Evaluation and Reporting Guidelines, section 3.0).

The supporting data, analytical processes, and assumptions used in an evaluation should be documented in sufficient detail to allow an independent evaluator or auditor to clearly understand the basis for estimation and categorization of recoverable quantities and their classification.

2.0 Classification and Categorization Guidelines

2.1 Resources Classification

The basic classification requires establishment of criteria for a petroleum discovery and thereafter the distinction between commercial and sub-commercial projects in known accumulations (and hence between Reserves and Contingent Resources).

2.1.1 Determination of Discovery Status

A discovery is one petroleum accumulation, or several petroleum accumulations collectively, for which one or several exploratory wells have established through testing, sampling, and/or logging the existence of a significant quantity of potentially moveable hydrocarbons.

In this context, "significant" implies that there is evidence of a sufficient quantity of petroleum to justify estimating the in-place volume demonstrated by the well(s) and for evaluating the potential for economic recovery. Estimated recoverable quantities within such a discovered (known) accumulation(s) shall initially be classified as Contingent Resources pending definition of projects with sufficient chance of commercial development to reclassify all, or a portion, as Reserves. Where in-place hydrocarbons are identified but are not considered currently recoverable, such quantities may be classified as Discovered Unrecoverable, if considered appropriate for resource management purposes; a portion of these quantities may become recoverable resources in the future as commercial circumstances change or technological developments occur.

2.1.2 Determination of Commerciality

Discovered recoverable volumes (Contingent Resources) may be considered commercially producible, and thus Reserves, if the entity claiming commerciality has demonstrated firm intention to proceed with development and such intention is based upon all of the following criteria:

- Evidence to support a reasonable timetable for development.
- A reasonable assessment of the future economics of such development projects meeting defined investment and operating criteria.
- A reasonable expectation that there will be a market for all or at least the expected sales quantities of production required to justify development.
- Evidence that the necessary production and transportation facilities are available or can be made available.
- Evidence that legal, contractual, environmental and other social and economic concerns will allow for the actual implementation of the recovery project being evaluated.

To be included in the Reserves class, a project must be sufficiently defined to establish its commercial viability. There must be a reasonable expectation that all required internal and external approvals will be forthcoming, and there is evidence of firm intention to proceed with development within a reasonable time frame. A reasonable time frame for the initiation of development depends on the specific circumstances and varies according to the scope of the project. While 5 years is recommended as a benchmark, a longer time frame could be applied where, for example, development of economic projects are deferred at the option of the producer for, among other things, market-related reasons, or to meet contractual or strategic objectives. In all cases, the justification for classification as Reserves should be clearly documented.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

To be included in the Reserves class, there must be a high confidence in the commercial producibility of the reservoir as supported by actual production or formation tests. In certain cases, Reserves may be assigned on the basis of well logs and/or core analysis that indicate that the subject reservoir is hydrocarbon-bearing and is analogous to reservoirs in the same area that are producing or have demonstrated the ability to produce on formation tests.

2.2 Resources Categorization

The horizontal axis in the Resources Classification (Figure 1.1) defines the range of uncertainty in estimates of the quantities of recoverable, or potentially recoverable, petroleum associated with a project. These estimates include both technical and commercial uncertainty components as follows:

- The total petroleum remaining within the accumulation (in-place resources).
- That portion of the in-place petroleum that can be recovered by applying a defined development project or projects.
- Variations in the commercial conditions that may impact the quantities recovered and sold (e.g., market availability, contractual changes).

Where commercial uncertainties are such that there is significant risk that the complete project (as initially defined) will not proceed, it is advised to create a separate project classified as Contingent Resources with an appropriate chance of commerciality.

2.2.1 Range of Uncertainty

The range of uncertainty of the recoverable and/or potentially recoverable volumes may be represented by either deterministic scenarios or by a probability distribution (see Deterministic and Probabilistic Methods, section 4.2).

When the range of uncertainty is represented by a probability distribution, a low, best, and high estimate shall be provided such that:

- There should be at least a 90% probability (P90) that the quantities actually recovered will equal or exceed the low estimate.
- There should be at least a 50% probability (P50) that the quantities actually recovered will equal or exceed the best estimate.
- There should be at least a 10% probability (P10) that the quantities actually recovered will equal or exceed the high estimate.

When using the deterministic scenario method, typically there should also be low, best, and high estimates, where such estimates are based on qualitative assessments of relative uncertainty using consistent interpretation guidelines. Under the deterministic incremental (risk-based) approach, quantities at each level of uncertainty are estimated discretely and separately (see Category Definitions and Guidelines, section 2.2.2).

These same approaches to describing uncertainty may be applied to Reserves, Contingent Resources, and Prospective Resources. While there may be significant risk that sub-commercial and undiscovered accumulations will not achieve commercial production, it is useful to consider the range of potentially recoverable quantities independently of such a risk or consideration of the resource class to which the quantities will be assigned.

2.2.2 Category Definitions and Guidelines

Evaluators may assess recoverable quantities and categorize results by uncertainty using the deterministic incremental (risk-based) approach, the deterministic scenario (cumulative) approach, or probabilistic methods (see "2001 Supplemental Guidelines," Chapter 2.5). In many cases, a combination of approaches is used.

Use of consistent terminology (Figure 1.1) promotes clarity in communication of evaluation results. For Reserves, the general cumulative terms low/best/high estimates are denoted as 1P/2P/3P, respectively. The associated incremental quantities are termed Proved, Probable and Possible. Reserves are a subset of, and must be viewed within context of, the complete resources classification system. While the categorization criteria are proposed specifically for Reserves, in most cases, they can be equally applied to Contingent and Prospective Resources conditional upon their satisfying the criteria for discovery and/or development.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

For Contingent Resources, the general cumulative terms low/best/high estimates are denoted as 1C/2C/3C respectively. For Prospective Resources, the general cumulative terms low/best/high estimates still apply. No specific terms are defined for incremental quantities within Contingent and Prospective Resources.

Without new technical information, there should be no change in the distribution of technically recoverable volumes and their categorization boundaries when conditions are satisfied sufficiently to reclassify a project from Contingent Resources to Reserves. All evaluations require application of a consistent set of forecast conditions, including assumed future costs and prices, for both classification of projects and categorization of estimated quantities recovered by each project (see Commercial Evaluations, section 3.1).

Based on additional data and updated interpretations that indicate increased certainty, portions of Possible and Probable Reserves may be re-categorized as Probable and Proved Reserves.

Uncertainty in resource estimates is best communicated by reporting a range of potential results. However, if it is required to report a single representative result, the "best estimate" is considered the most realistic assessment of recoverable quantities. It is generally considered to represent the sum of Proved and Probable estimates (2P) when using the deterministic scenario or the probabilistic assessment methods. It should be noted that under the deterministic incremental (risk-based) approach, discrete estimates are made for each category, and they should not be aggregated without due consideration of their associated risk (see "2001 Supplemental Guidelines," Chapter 2.5).

Table 1: Recoverable Resources Classes and Sub-Classes

Class/Sub-Class	Definition	Guidelines
Reserves	Reserves are those quantities of petroleum anticipated to be commercially recoverable by application of development projects to known accumulations from a given date forward under defined conditions.	Reserves must satisfy four criteria: they must be discovered, recoverable, commercial, and remaining based on the development project(s) applied. Reserves are further subdivided in accordance with the level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterized by their development and production status. To be included in the Reserves class, a project must be sufficiently defined to establish its commercial viability. There must be a reasonable expectation that all required internal and external approvals will be forthcoming, and there is evidence of firm intention to proceed with development within a reasonable time frame. A reasonable time frame for the initiation of development depends on the specific circumstances and varies according to the scope of the project. While 5 years is recommended as a benchmark, a longer time frame could be applied where, for example, development of economic projects are deferred at the option of the producer for, among other things, market-related reasons, or to meet contractual or strategic objectives. In all cases, the justification for classification as Reserves should be clearly documented. To be included in the Reserves class, there must be a high confidence in the commercial producibility of the reservoir as supported by actual production or formation tests. In certain cases, Reserves may be assigned on the basis of well logs and/or core analysis that indicate that the subject reservoir is hydrocarbon-bearing and is analogous to reservoirs in the same area that are producing or have demonstrated the ability to produce on formation tests.
On Production	The development project is currently producing and selling petroleum to market.	The key criterion is that the project is receiving income from sales, rather than the approved development project necessarily being complete. This is the point at which the project "chance of commerciality" can be said to be 100%. The project "decision gate" is the decision to initiate commercial production from the project.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Class/Sub-Class	Definition	Guidelines
Approved for Development	All necessary approvals have been obtained, capital funds have been committed, and implementation of the development project is under way.	At this point, it must be certain that the development project is going ahead. The project must not be subject to any contingencies such as outstanding regulatory approvals or sales contracts. Forecast capital expenditures should be included in the reporting entity's current or following year's approved budget. The project "decision gate" is the decision to start investing capital in the construction of production facilities and/or drilling development wells.
Justified for Development	Implementation of the development project is justified on the basis of reasonable forecast commercial conditions at the time of reporting, and there are reasonable expectations that all necessary approvals/contracts will be obtained.	In order to move to this level of project maturity, and hence have reserves associated with it, the development project must be commercially viable at the time of reporting, based on the reporting entity's assumptions of future prices, costs, etc. ("forecast case") and the specific circumstances of the project. Evidence of a firm intention to proceed with development within a reasonable time frame will be sufficient to demonstrate commerciality. There should be a development plan in sufficient detail to support the assessment of commerciality and a reasonable expectation that any regulatory approvals or sales contracts required prior to project implementation will be forthcoming. Other than such approvals/contracts, there should be no known contingencies that could preclude the development from proceeding within a reasonable timeframe (see Reserves class). The project "decision gate" is the decision by the reporting entity and its partners, if any, that the project has reached a level of technical and commercial maturity sufficient to justify proceeding with development at that point in time.
Contingent Resources	Those quantities of petroleum estimated, as of a given date, to be potentially recoverable from known accumulations by application of development projects, but which are not currently considered to be commercially recoverable due to one or more contingencies.	Contingent Resources may include, for example, projects for which there are currently no viable markets, or where commercial recovery is dependent on technology under development, or where evaluation of the accumulation is insufficient to clearly assess commerciality. Contingent Resources are further categorized in accordance with the level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterized by their economic status.
Development Pending	A discovered accumulation where project activities are ongoing to justify commercial development in the foreseeable future.	The project is seen to have reasonable potential for eventual commercial development, to the extent that further data acquisition (e.g. drilling, seismic data) and/or evaluations are currently ongoing with a view to confirming that the project is commercially viable and providing the basis for selection of an appropriate development plan. The critical contingencies have been identified and are reasonably expected to be resolved within a reasonable time frame. Note that disappointing appraisal/evaluation results could lead to a re-classification of the project to "On Hold" or "Not Viable" status. The project "decision gate" is the decision to undertake further data acquisition and/or studies designed to move the project to a level of technical and commercial maturity at which a decision can be made to proceed with development and production.
Development Unclarified or on Hold	A discovered accumulation where project activities are on hold and/or where justification as a commercial development may be subject to significant delay.	The project is seen to have potential for eventual commercial development, but further appraisal/evaluation activities are on hold pending the removal of significant contingencies external to the project, or substantial further appraisal/evaluation activities are required to clarify the potential for eventual commercial development. Development may be subject to a significant time delay. Note that a change in circumstances, such that there is no longer a reasonable expectation that a critical contingency can be removed in the foreseeable future, for example, could lead to a reclassification of the project to "Not Viable" status. The project "decision gate" is the decision to either proceed with additional evaluation designed to clarify the potential for eventual commercial development or to temporarily suspend or delay further activities pending resolution of external contingencies.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Class/Sub-Class	Definition	Guidelines
Development Not Viable	A discovered accumulation for which there are no current plans to develop or to acquire additional data at the time due to limited production potential.	The project is not seen to have potential for eventual commercial development at the time of reporting, but the theoretically recoverable quantities are recorded so that the potential opportunity will be recognized in the event of a major change in technology or commercial conditions. The project "decision gate" is the decision not to undertake any further data acquisition or studies on the project for the foreseeable future.
Prospective Resources	Those quantities of petroleum which are estimated, as of a given date, to be potentially recoverable from undiscovered accumulations.	Potential accumulations are evaluated according to their chance of discovery and, assuming a discovery, the estimated quantities that would be recoverable under defined development projects. It is recognized that the development programs will be of significantly less detail and depend more heavily on analog developments in the earlier phases of exploration.
Prospect	A project associated with a potential accumulation that is sufficiently well defined to represent a viable drilling target.	Project activities are focused on assessing the chance of discovery and, assuming discovery, the range of potential recoverable quantities under a commercial development program.
Lead	A project associated with a potential accumulation that is currently poorly defined and requires more data acquisition and/or evaluation in order to be classified as a prospect.	Project activities are focused on acquiring additional data and/or undertaking further evaluation designed to confirm whether or not the lead can be matured into a prospect. Such evaluation includes the assessment of the chance of discovery and, assuming discovery, the range of potential recovery under feasible development scenarios.
Play	A project associated with a prospective trend of potential prospects, but which requires more data acquisition and/or evaluation in order to define specific leads or prospects.	Project activities are focused on acquiring additional data and/or undertaking further evaluation designed to define specific leads or prospects for more detailed analysis of their chance of discovery and, assuming discovery, the range of potential recovery under hypothetical development scenarios.

Table 2: Reserves Status Definitions and Guidelines

Status	Definition	Guidelines
Developed Reserves	Developed Reserves are expected quantities to be recovered from existing wells and facilities.	Reserves are considered developed only after the necessary equipment has been installed, or when the costs to do so are relatively minor compared to the cost of a well. Where required facilities become unavailable, it may be necessary to reclassify Developed Reserves as Undeveloped. Developed Reserves may be further sub-classified as Producing or Non-Producing.
Developed Producing Reserves	Developed Producing Reserves are expected to be recovered from completion intervals that are open and producing at the time of the estimate.	Improved recovery reserves are considered producing only after the improved recovery project is in operation.
Developed Non-Producing Reserves	Developed Non-Producing Reserves include shut-in and behind-pipe Reserves.	Shut-in Reserves are expected to be recovered from (1) completion intervals which are open at the time of the estimate but which have not yet started producing, (2) wells which were shut-in for market conditions or pipeline connections, or (3) wells not capable of production for mechanical reasons. Behind-pipe Reserves are expected to be recovered from zones in existing wells which will require additional completion work or future re-completion prior to start of production. In all cases, production can be initiated or restored with relatively low expenditure compared to the cost of drilling a new well.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Status	Definition	Guidelines
Undeveloped Reserves	Undeveloped Reserves are quantities expected to be recovered through future investments:	(1) from new wells on undrilled acreage in known accumulations, (2) from deepening existing wells to a different (but known) reservoir, (3) from infill wells that will increase recovery, or (4) where a relatively large expenditure (e.g. when compared to the cost of drilling a new well) is required to (a) recomplete an existing well or (b) install production or transportation facilities for primary or improved recovery projects.

Table 3: Reserves Category Definitions and Guidelines

Category	Definition	Guidelines
Proved Reserves	Proved Reserves are those quantities of petroleum, which by analysis of geoscience and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under defined economic conditions, operating methods, and government regulations.	If deterministic methods are used, the term reasonable certainty is intended to express a high degree of confidence that the quantities will be recovered. If probabilistic methods are used, there should be at least a 90% probability that the quantities actually recovered will equal or exceed the estimate. The area of the reservoir considered as Proved includes (1) the area delineated by drilling and defined by fluid contacts, if any, and (2) adjacent undrilled portions of the reservoir that can reasonably be judged as continuous with it and commercially productive on the basis of available geoscience and engineering data. In the absence of data on fluid contacts, Proved quantities in a reservoir are limited by the lowest known hydrocarbon (LKH) as seen in a well penetration unless otherwise indicated by definitive geoscience, engineering, or performance data. Such definitive information may include pressure gradient analysis and seismic indicators. Seismic data alone may not be sufficient to define fluid contacts for Proved reserves (see "2001 Supplemental Guidelines," Chapter 8). Reserves in undeveloped locations may be classified as Proved provided that: • The locations are in undrilled areas of the reservoir that can be judged with reasonable certainty to be commercially productive. • Interpretations of available geoscience and engineering data indicate with reasonable certainty that the objective formation is laterally continuous with drilled Proved locations. For Proved Reserves, the recovery efficiency applied to these reservoirs should be defined based on a range of possibilities supported by analogs and sound engineering judgment considering the characteristics of the Proved area and the applied development program.
Probable Reserves	Probable Reserves are those additional Reserves which analysis of geoscience and engineering data indicate are less likely to be recovered than Proved Reserves but more certain to be recovered than Possible Reserves.	It is equally likely that actual remaining quantities recovered will be greater than or less than the sum of the estimated Proved plus Probable Reserves (2P). In this context, when probabilistic methods are used, there should be at least a 50% probability that the actual quantities recovered will equal or exceed the 2P estimate. Probable Reserves may be assigned to areas of a reservoir adjacent to Proved where data control or interpretations of available data are less certain. The interpreted reservoir continuity may not meet the reasonable certainty criteria. Probable estimates also include incremental recoveries associated with project recovery efficiencies beyond that assumed for Proved.

PETROLEUM RESERVES AND RESOURCES CLASSIFICATION AND DEFINITIONS

Excerpted from the Petroleum Resources Management System Approved by
the Society of Petroleum Engineers (SPE) Board of Directors, March 2007

Category	Definition	Guidelines
Possible Reserves	Possible Reserves are those additional reserves which analysis of geoscience and engineering data indicate are less likely to be recoverable than Probable Reserves.	The total quantities ultimately recovered from the project have a low probability to exceed the sum of Proved plus Probable plus Possible (3P), which is equivalent to the high estimate scenario. When probabilistic methods are used, there should be at least a 10% probability that the actual quantities recovered will equal or exceed the 3P estimate. Possible Reserves may be assigned to areas of a reservoir adjacent to Probable where data control and interpretations of available data are progressively less certain. Frequently, this may be in areas where geoscience and engineering data are unable to clearly define the area and vertical reservoir limits of commercial production from the reservoir by a defined project. Possible estimates also include incremental quantities associated with project recovery efficiencies beyond that assumed for Probable.
Probable and Possible Reserves	(See above for separate criteria for Probable Reserves and Possible Reserves.)	The 2P and 3P estimates may be based on reasonable alternative technical and commercial interpretations within the reservoir and/or subject project that are clearly documented, including comparisons to results in successful similar projects. In conventional accumulations, Probable and/or Possible Reserves may be assigned where geoscience and engineering data identify directly adjacent portions of a reservoir within the same accumulation that may be separated from Proved areas by minor faulting or other geological discontinuities and have not been penetrated by a wellbore but are interpreted to be in communication with the known (Proved) reservoir. Probable or Possible Reserves may be assigned to areas that are structurally higher than the Proved area. Possible (and in some cases, Probable) Reserves may be assigned to areas that are structurally lower than the adjacent Proved or 2P area. Caution should be exercised in assigning Reserves to adjacent reservoirs isolated by major, potentially sealing, faults until this reservoir is penetrated and evaluated as commercially productive. Justification for assigning Reserves in such cases should be clearly documented. Reserves should not be assigned to areas that are clearly separated from a known accumulation by non-productive reservoir (i.e., absence of reservoir, structurally low reservoir, or negative test results); such areas may contain Prospective Resources. In conventional accumulations, where drilling has defined a highest known oil (HKO) elevation and there exists the potential for an associated gas cap, Proved oil Reserves should only be assigned in the structurally higher portions of the reservoir if there is reasonable certainty that such portions are initially above bubble point pressure based on documented engineering analyses. Reservoir portions that do not meet this certainty may be assigned as Probable and Possible oil and/or gas based on reservoir fluid properties and pressure gradient interpretations.

The 2007 Petroleum Resources Management System can be viewed in its entirety at
<http://www.spe.org/spe-app/spe/industry/reserves/prms.htm>.

REVENUE, COSTS AND TAXES
PROVED UNDEVELOPED RESERVES
DELEK INVESTMENTS AND PROPERTIES LTD.
MARI B FIELD, OFFSHORE ISRAEL
AS OF DECEMBER 31, 2011

Period Ending	Working Interest Revenue ⁽¹⁾	Royalties				Net Capital Costs (M\$)	Abandonment Costs (M\$)	Operating Expenses ⁽²⁾ (M\$)	Net Revenue Before Levy and Corporate Income Taxes Discounted at 0%		Levy Rate (%)	Net Revenue After Levy and Corporate Income Taxes Discounted at 0%		Income Tax Rate ⁽³⁾ (%)	Corporate Income Tax ⁽³⁾ (M\$)	Future Net Revenue After Levy and Corporate Income Taxes				
		State (M\$)	Interested Party (M\$)	Third Party (M\$)	Total (M\$)				Discounted at 0% (M\$)	Levy (M\$)		Discounted at 0% (M\$)	Discounted at 5% (M\$)			Discounted at 10% (M\$)	Discounted at 15% (M\$)	Discounted at 20% (M\$)		
12-31-2012	84,746.5	9,613.6	5,805.0	802.6	16,221.2	0.0	5,231.3	71,469.8	22.8	16,270.8	55,199.0	25.0	8,465.0	46,733.9	45,607.7	44,559.1	43,579.6	42,662.1		
12-31-2013	17,828.1	2,022.4	1,202.3	187.7	3,412.5	1,581.4	7,354.4	13,799.6	25.0	3,449.9	10,349.7	25.0	24.4	10,325.3	9,596.6	8,949.8	8,372.5	7,854.7		
12-31-2014	3,395.8	385.2	227.8	37.0	650.0	0.0	62.6	3,005.9	25.0	751.5	2,254.4	25.0	0.0	2,254.4	1,995.6	1,776.5	1,589.6	1,429.2		
12-31-2015	3,395.8	385.2	227.8	37.0	650.0	0.0	62.6	3,005.9	25.0	751.5	2,254.4	25.0	0.0	2,254.4	1,995.6	1,776.5	1,589.6	1,429.2		
12-31-2016	3,395.8	385.2	227.8	37.0	650.0	0.0	62.6	3,005.9	45.5	1,368.3	1,637.6	25.0	0.0	1,637.6	1,314.8	1,066.5	873.1	720.9		
12-31-2017	3,395.8	385.2	227.8	37.0	650.0	0.0	62.6	3,005.9	45.5	1,368.3	1,637.6	25.0	0.0	1,637.6	1,252.2	969.5	759.2	600.8		
12-31-2018	3,395.8	385.2	227.8	37.0	650.0	0.0	62.6	3,005.9	45.5	1,368.3	1,637.6	25.0	0.0	1,637.6	1,192.6	881.4	660.2	500.7		
12-31-2019	3,395.8	385.2	227.8	37.0	650.0	0.0	62.6	3,005.9	45.5	1,368.3	1,637.6	25.0	0.0	1,637.6	1,135.8	801.3	574.1	417.2		
12-31-2020	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	0.0	3,646.7	2,408.7	1,622.0	1,111.6	774.2		
12-31-2021	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	0.0	3,646.7	2,294.0	1,474.6	966.6	645.2		
12-31-2022	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	0.0	3,646.7	2,184.8	1,340.5	840.6	537.6		
12-31-2023	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	0.0	3,646.7	2,080.8	1,218.7	730.9	448.0		
12-31-2024	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	0.0	3,646.7	1,981.7	1,107.9	635.6	373.4		
12-31-2025	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	0.0	3,646.7	1,887.3	1,007.2	552.7	311.1		
12-31-2026	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	752.9	2,893.8	1,426.3	726.6	381.4	205.7		
12-31-2027	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	911.7	2,735.0	1,283.9	624.3	313.4	162.1		
12-31-2028	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	911.7	2,735.0	1,222.7	567.5	272.5	135.0		
12-31-2029	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	911.7	2,735.0	1,164.5	515.9	237.0	112.5		
12-31-2030	7,563.5	868.0	507.4	82.3	1,447.7	0.0	140.9	6,693.6	45.5	3,046.9	3,646.7	25.0	911.7	2,735.0	1,109.1	469.0	206.1	93.8		
12-31-2031	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
12-31-2032	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
12-31-2033	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
12-31-2034	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
12-31-2035	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
12-31-2036	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
12-31-2037	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
12-31-2038	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0		
Total	206,147.6	23,385.4	13,955.3	2,117.7	39,458.4	1,581.4	7,892.2	160,764.7	0.0	60,213.1	100,551.6	25.0	12,889.0	87,662.6	78,601.5	69,999.4	63,640.9	59,046.3		

Total may not add because of rounding.

⁽¹⁾ For the purposes of the model, we have not attributed any part of the revenues to services.

⁽²⁾ Operating expenses are intended to include only direct project-level costs and Delek Investments and Properties Ltd.'s estimate of the portion of its headquarters general and administrative overhead expenses that can be directly attributed to this project.

⁽³⁾ Corporate income tax rates and estimates of corporate income taxes are provided by Delek Investments and Properties Ltd. and are its expected corporate income taxes per year.

All estimates and exhibits herein are part of this NSAI report and are subject to its parameters and conditions.

REVENUE, COSTS, AND TAXES
PROBABLE RESERVES
DELEK INVESTMENTS AND PROPERTIES LTD.
MARI B FIELD, OFFSHORE ISRAEL
AS OF DECEMBER 31, 2011

Period Ending	Working Interest Revenue ⁽¹⁾ (M\$)	Royalties			Net Capital Costs (M\$)	Abandonment Costs (M\$)	Operating Expenses ⁽²⁾ (M\$)	Net Revenue Before Levy and Corporate Income Taxes Discounted at 0% (M\$)		Levy Rate (%)	Net Revenue After Levy and Before Corporate Income Taxes Discounted at 0% (M\$)		Corporate Income Tax ⁽³⁾ (M\$)	Future Net Revenue After Levy and Corporate Income Taxes Discounted (M\$)				
		State (M\$)	Interested Party (M\$)	Third Party (M\$)				Total (M\$)	Levy Rate (%)		Discounted at 0% (M\$)	Income Tax Rate ⁽⁴⁾ (%)		at 0% Discounted (M\$)	at 5% Discounted (M\$)	at 10% Discounted (M\$)	at 15% Discounted (M\$)	at 20% Discounted (M\$)
12-31-2012	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	22.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2013	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2014	1,443.2	163.7	96.8	15.7	0.0	0.0	0.0	1,304.1	0.0	25.0	326.0	0.0	0.0	978.1	865.8	770.7	689.7	620.1
12-31-2015	1,443.2	163.7	96.8	15.7	0.0	0.0	0.0	1,304.1	0.0	25.0	326.0	0.0	0.0	978.1	824.6	700.7	599.7	516.7
12-31-2016	1,443.2	163.7	96.8	15.7	0.0	0.0	0.0	1,304.1	0.0	25.0	326.0	0.0	0.0	710.5	570.4	462.7	378.6	312.6
12-31-2017	1,443.2	163.7	96.8	15.7	0.0	0.0	0.0	1,304.1	0.0	49.5	593.6	0.0	0.0	710.5	543.3	420.6	329.4	260.7
12-31-2018	1,443.2	163.7	96.8	15.7	0.0	0.0	0.0	1,304.1	0.0	49.5	593.6	0.0	0.0	710.5	517.4	382.4	288.4	217.2
12-31-2019	1,443.2	163.7	96.8	15.7	0.0	0.0	0.0	1,304.1	0.0	49.5	593.6	0.0	0.0	710.5	492.8	346.6	249.5	190.0
12-31-2020	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	323.9	156.6	108.7	65.0
12-31-2021	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	223.4	136.9	85.8	45.7
12-31-2022	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	212.5	124.4	74.6	45.7
12-31-2023	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	(22.2)	(120.7)	(67.5)	(22.7)
12-31-2024	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	(63.2)	(327.3)	(174.7)	(54.0)
12-31-2025	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	120.5	59.4	30.3	15.9
12-31-2026	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	279.3	131.1	63.7	32.0
12-31-2027	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	324.8	124.8	57.9	27.8
12-31-2028	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	279.3	118.9	52.7	24.2
12-31-2029	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	279.3	113.2	47.9	21.0
12-31-2030	756.3	85.8	50.7	8.2	0.0	0.0	0.0	683.5	0.0	45.5	311.1	0.0	0.0	372.3	0.0	0.0	0.0	0.0
12-31-2031	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2032	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2033	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2034	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2035	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2036	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2037	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2038	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	16,979.2	1,926.1	1,139.0	184.8	0.0	0.0	0.0	15,342.8	0.0	45.5	6,448.8	8,894.0	2,223.5	6,670.5	4,829.4	3,672.6	2,892.1	2,337.3

Totals may not add because of rounding.

⁽¹⁾ For the purposes of the model, we have not attributed any part of the revenues to services.

⁽²⁾ Operating expenses are intended to include only direct project-level costs and Delek Drilling Limited Partnership's estimate of the portion of its headquarters general and administrative overhead expenses that can be directly attributed to this project.

⁽³⁾ Corporate income tax rates and estimates of corporate income taxes are provided by Delek Investments and Properties Ltd. and are its expected corporate income taxes per year.

All estimates and exhibits herein are part of this NSAI report and are subject to its parameters and conditions.

REVENUE, COSTS, AND TAXES
POSSIBLE RESERVES
DELEK INVESTMENTS AND PROPERTIES LTD.
MARI B FIELD, OFFSHORE ISRAEL
AS OF DECEMBER 31, 2011

Period Ending	Working Interest Revenue ⁽¹⁾ (M\$)	Royalties			Net Capital Costs (M\$)	Abandonment Costs (M\$)	Operating Expenses ⁽²⁾ (M\$)	Net Revenue Before Levy and Corporate Income Taxes		Levy Rate (%)	Levy (M\$)	Net Revenue After Levy and Before Corporate Income Taxes		Income Tax Rate ⁽³⁾ (%)	Corporate Income Tax ⁽³⁾ (M\$)	Future Net Revenue After Levy and Corporate Income Taxes				
		State (M\$)	Interested Party (M\$)	Third Party (M\$)				Total (M\$)	Discounted at 0% (M\$)			Levy (M\$)	Discounted at 0% (M\$)			Discounted at 5% (M\$)	Discounted at 10% (M\$)	Discounted at 15% (M\$)	Discounted at 20% (M\$)	
12-31-2012	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	22.8	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2013	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2014	1,471.5	166.9	98.7	16.0	281.7	0.0	0.0	1,329.7	997.3	25.0	332.4	997.3	882.8	25.0	0.0	997.3	882.8	785.8	703.2	632.2
12-31-2015	1,471.5	166.9	98.7	16.0	281.7	0.0	0.0	1,329.7	997.3	25.0	332.4	997.3	882.8	25.0	0.0	997.3	882.8	714.4	611.5	526.8
12-31-2016	1,471.5	166.9	98.7	16.0	281.7	0.0	0.0	1,329.7	997.3	25.0	332.4	997.3	882.8	25.0	0.0	997.3	882.8	471.8	386.2	318.9
12-31-2017	1,471.5	166.9	98.7	16.0	281.7	0.0	0.0	1,329.7	997.3	25.0	332.4	997.3	882.8	25.0	0.0	997.3	882.8	428.9	335.9	265.8
12-31-2018	1,471.5	166.9	98.7	16.0	281.7	0.0	0.0	1,329.7	997.3	25.0	332.4	997.3	882.8	25.0	0.0	997.3	882.8	389.9	292.0	221.5
12-31-2019	1,471.5	166.9	98.7	16.0	281.7	0.0	0.0	1,329.7	997.3	25.0	332.4	997.3	882.8	25.0	0.0	997.3	882.8	354.4	254.0	184.6
12-31-2020	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	179.1	122.8	85.5
12-31-2021	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	162.9	106.8	71.3
12-31-2022	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	175.3	107.6	67.4
12-31-2023	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	(401.0)	(234.8)	(86.3)
12-31-2024	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	(59.8)	(32.9)	(18.9)
12-31-2025	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	83.4	45.8	25.8
12-31-2026	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	148.9	78.8	39.8
12-31-2027	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	141.8	69.9	34.6
12-31-2028	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	135.0	62.7	30.1
12-31-2029	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	128.6	57.0	26.2
12-31-2030	818.1	92.8	54.9	8.9	156.6	0.0	0.0	739.2	402.7	45.5	338.5	402.7	266.0	25.0	0.0	402.7	266.0	122.5	51.8	22.8
12-31-2031	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2032	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2033	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2034	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2035	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2036	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2037	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2038	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2039	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2040	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2041	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2042	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2043	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2044	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2045	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
12-31-2046	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.5	0.0	0.0	0.0	25.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	17,828.1	2,022.4	1,196.0	194.1	3,412.5	0.0	0.0	16,109.9	9,322.4	0.0	6,787.5	9,322.4	0.0	25.0	0.0	6,991.8	4,957.1	3,726.7	2,919.3	2,355.1

Totals may not add because of rounding.

⁽¹⁾ For the purposes of the model, we have not attributed any part of the revenues to services.

⁽²⁾ Operating expenses are intended to include only direct project-level costs and Delek Drilling Limited Partnership's estimate of the portion of its headquarters general and administrative overhead expenses that can be directly attributed to this project.

⁽³⁾ Corporate income tax rates and estimates of corporate income taxes are provided by Delek Investments and Properties Ltd. and are its expected corporate income taxes per year.

All estimates and exhibits herein are part of this NSAI report and are subject to its parameters and conditions.

HISTORICAL PRODUCTION AND OPERATING EXPENSE DATA
DELEK INVESTMENTS AND PROPERTIES LTD.
MARI B FIELD, OFFSHORE ISRAEL
AS OF DECEMBER 31, 2011

Year	DI Net Production (BCF)	Average Price Received Per Production Unit (\$/MCF)	Average Royalties Paid Per Production Unit (\$/MCF)	Average Production Costs Per Production Unit (\$/MCF)	Average Net Revenue Per Production Unit (\$/MCF)	Reserves Depletion Rate ⁽¹⁾ (Percent)
2011	48.1	4.71	0.90	0.22	4.00	39.8
2010	29.0	4.03	0.94	0.33	2.76	23.0
2009	25.3	3.47	0.82	0.30	2.35	16.7

⁽¹⁾ The reserves depletion rate is the percentage of yearly gas produced to the estimated proved plus probable reserves at the beginning of that year.

March 23, 2012

Mr. Gideon Tadmor
Delek Investments and Properties Ltd.
7 Giborei Israel Street
Netanya 42504
Israel

Dear Mr. Tadmor:

As independent consultants, Netherland, Sewell & Associates, Inc. hereby grants permission to Delek Investments and Properties Ltd. (DI) to use our 2012 reports dated March 19, March 20, March 22, and March 23 to be filed with the Israel Securities Authority.

- The report dated March 19, 2012, sets forth our estimates of the unrisked contingent and prospective gas resources, as of December 31, 2011, to the DI working interest in a discovery and prospects located in the Dalit Discovery area, offshore Israel.
- The report dated March 20, 2012 sets forth our estimates of proved undeveloped, probable, and possible gas reserves and future revenue, as of December 31, 2011, to the Delek Drilling Limited Partnership (Delek Drilling) interest in Tamar Field, located in the Tamar Lease I/12, offshore Israel.
- The report dated March 23, 2012, sets forth our estimates of the proved developed, probable, and possible reserves and future revenue as of December 31, 2011, to the DI interest in certain gas properties located in Mari B Field, offshore Israel.
- The report dated March 23, 2012 sets forth our estimates of proved undeveloped reserves and future revenue, as of December 31, 2011, to the DI interest in certain gas properties located in Noa Field, offshore Israel.

Sincerely,

NETHERLAND, SEWELL & ASSOCIATES, INC.

By:



Danny D. Simmons, P.E.
President and Chief Operating Officer

RBT:MGH

Chapter B



Board of Directors Report

on the State of the
Company's Affairs



Delek Group



March 29, 2012

Delek Group Ltd.

Directors' report on the state of the Company's affairs for the year ended December 31, 2011

The Board of Directors of the Delek Group Ltd. ("the Company") hereby presents the Company's Directors' Report for the year ended December 31, 2011.

A. The Board's explanations for the state of the Company's affairs

1. Description of the Company and its business environment

The Group is a holdings and management company which controls a number of corporations (the Company and the companies under its control are hereinafter referred to as "the Group" or "the Delek Group") with a range of investments in Israel and overseas in the fields of energy and infrastructures, finance and insurance, automobiles, and others.

The Company's financial data and its operating results are affected by the financial data and operating results of its investee companies, and by its sale or acquisition of holdings. The Company's cash flow is affected, inter alia, by dividends and management fees received from its investees, by inflows originating from the disposal of its holdings therein, by its ability to raise foreign financing which depends, inter alia, on the value of its holdings, by financial market conditions in Israel and abroad, and by investments made by the Group and the dividends it distributes to its shareholders.

2. Principal operations

- A) In the reporting period, the Group sold its shares in Noble in consideration for NIS 1,925 million.¹ The Company's pre-tax profit on this sale amounted to NIS 397 million.
- B) On January 24, 2011, the Group completed the acquisition of Delek Belron International Ltd.'s (a wholly-owned subsidiary of Delek Real Estate) ("Delek Belron") holdings in the companies holding Roadchef. It is noted that Delek Belron held a 75% interest in Roadchef, while Delek Petroleum held a 25% interest in Roadchef. Upon the transaction's completion, the Group (through Delek Petroleum), holds 100% of Roadchef. The consideration for the transaction totaled GBP 86.25 million (approximately NIS 497 million), which reflects a value of GBP 115 million (approximately NIS 663 million) for Roadchef. Payment of the consideration was offset against part of Delek Real Estate's debt to the Company, and paid in cash. For more information, see Note 14 to the financial statements.
- C) On April 29, 2011, the Group completed a transaction whereby Delek US acquired 53.7% of the share capital of Lion Oil Company ("Lion"). After completion of this transaction, Delek US held 88.3% of Lion's share capital. In October 2011, Delek US acquired the remaining minority shares in consideration for USD 13 million in cash. For more information, see Note 14 to the financial statements.
- D) In July 2011, Delek Petroleum issued a complete purchase offer to acquire all shares held by Delek Israel's other shareholders at a price of NIS 101 per share.

On August 4, 2011, Delek Petroleum announced the results of this purchase offer, whereby Delek Petroleum acquired from those offerrees who notified of their acceptance of the offer, a total of

¹ In this translation of the Board of Directors' Report, all amounts should be understood by the reader to be rounded to the nearest million or thousand, as the case may be.

1,099,699 ordinary shares in Delek Israel. These shares constitute 9.69% of Delek Israel's issued and paid-up capital and voting rights. Following this purchase, Delek Petroleum's interests total 9,861,473 ordinary shares, constituting a total of 86.90% of Delek Israel's issued and paid-up capital and voting rights. Consideration for the purchase totaled NIS 111 million.

- E) On August 2, 2011, the Company issued a shelf registration report effected by way of a complete exchange purchase offer and a purchase offer specification (updated on August 25, 2011) for the purchase of 1,009,910 ordinary shares of NIS 1 par value each in Delek Energy ("the Purchase Offer"). Under the purchase offer, the Group offered to buy from the offerees their shares, in consideration for 1,009,910 units, each comprised of (a) 36 participation units of NIS 1 par value in Delek Drilling, and (b) 472 participation units of NIS 0.01 par value in Avner.

On September 11, 2011, an acceptance notice was issued, whereby the Group purchased 353,988 shares in Delek Energy in consideration for 12,743,568 participation units of NIS 1 par value in Delek Drilling, and 167,082,336 participation units of NIS 0.01 par value in Avner. Following this transaction, the Company and Delek Investment's holdings in Delek Energy, Delek Drilling and Avner total 86.92%, 6.7%, and 9.4%, respectively. Due to its decreased effective interest in Avner, in Q3/2011 the Group recorded pre-tax gains of NIS 62 million. These gains are included under the 'Gains (losses) from disposal of investments in investees, net' item.

- F) In December 2011, the Company completed the acquisition of 51.76% of the share capital in Cohen Development and Industrial Buildings Ltd. ("Cohen Development"), which engages, inter alia, in oil and gas exploration and production management, in consideration for NIS 274.1 million. Cohen Development's oil and gas exploration and production management operations are carried out through a company under its joint control, in which Cohen Development holds a 50% interest - Avner Oil and Gas Ltd. ("Avner"), which serves as the general partner in the limited partnership Avner Oil Exploration ("the Avner Partnership"). Cohen Development holds half of the share capital in Avner, with the remaining shares held by DES. Following completion of this transaction for acquiring control in Cohen Development, the Company is now the controlling shareholder in Avner (by virtue of DES's holdings in Avner and Cohen Development's holdings in Avner). Obtaining control in the general partner enables the Company to manage and control the Avner Partnership. It is noted, that prior to the above transaction, the Company maintained indirect holdings of 50.3% in the Avner Partnership's participation units, and accounted for this investment in its financial statements as per the equity method due to its joint control prior to the transaction in Avner. After initially obtaining control in Avner, and as a result obtaining indirect control of the Avner Partnership, the Company consolidates the Avner Partnership in its financial statements despite accounting for this investment as per the equity method. Having acquired control, the Company recognized a gain of NIS 3,282 million in its income statements for 2011, which it classified under 'Gains (losses) from disposal of investments in partnerships and associates, net'.
- G) In May 2011, the Company declared a dividend of NIS 105 million for its results in the first quarter of 2011. This dividend was distributed in June 2011. In August 2011, the Company declared a dividend of NIS 100 million for its results in the second quarter of 2011. This dividend was distributed in September 2011. In November 2011, the Company declared a dividend of NIS 100 million for its results in the third quarter of 2011. This dividend was distributed in December 2011. Post balance sheet, the Company declared a dividend of NIS 120 million for its results in the fourth quarter of 2011.

3. Results of operations

A) Contribution to net profit (attributable to owners of the parent) from principal operations (NIS millions):

In 2011, the Company recorded net profits of NIS 2.6 billion, as compared to a net profit of NIS 1.7 billion in 2010. In Q4/2011, the Company recorded a profit of NIS 2.1 billion, as compared to NIS 1.4 billion in the same quarter last year.

The results of the Delek Group's operations are comprised of the results of the Group's ongoing operations and one-time events which affect the Group's financial results.

Analysis of the Company's results indicates that operating profit in 2011 amounted to NIS 500 million, as compared to NIS 400 million in 2010.

The operating segments which contributed most to the Group's net profit were refining and fuel operations in the US, which contributed NIS 378 million, and natural gas production and sales operations, which contributed NIS 199 million.

As detailed below in the analysis of the Company's results for 2011, one-time contribution to net profit, net of one-time expenses amounted to NIS 2.1 billion, as compared to NIS 1.3 billion in 2010.

One-time income in 2011 was affected mainly by NIS 3.3 billion in income recorded after assuming control in the Avner Oil and Gas Limited Partnership, while one-time expenses were mainly due to a NIS 299 million writedown of goodwill in finance operations in Israel and abroad, impairment of the Company's holdings in Delek Automotive to the amount of NIS 250 million, impairment of property, plant and equipment in Gadot (mainly in its facility in China) of NIS 230 million, and equity losses and impairment of Delek Automotive's debt balance to the amount of NIS 104 million.

The following table details the contribution of the various operating segments to the Group's net profit, the write-offs recorded in the various segments, and the gains recorded on Avner's revaluation (in NIS millions):

	2011	2010	10-12/11	10-12/10
Fuel operations in the US	378	(213)	(30)	(180)
Oil and gas exploration and production operations	199	64	34	(31)
Fuel operations in Europe	12	69	(7)	(13)
Fuel operations in Israel	9	48	(7)	(2)
Motorway service area operations in the UK	(23)	-	(10)	-
Insurance and finance operations ⁽²⁾	(48)	275	(50)	94
Automotive operations	19	195	10	10
Capital gains and others ⁽¹⁾	2,064	1,263	2,219	1,539
Profit attributable to equity holders of the parent	2,610	1,701	2,159	1,417

(1) Composition of capital and other gains:

	2011	2010
Writedown of goodwill in insurance and finance operations	(299)	(87)
Gains on revaluation (impairment) of an investment in Delek Automotive	(250)	1,824
Impairment of assets in Gadot (mainly in China)	(230)	-
Gains on the revaluation of an investment in the Avner Partnership (gains following assumption of control)	3,282	-
Equity and impairment losses on loans to Delek Real Estate	(104)	(41)
Other (including financing and tax expenses in headquarters companies and other adjustments)	(335)	(433)
Total others	2,064	1,263

(2) The results of insurance and finance operations in 2011 and 2010 are presented net of a writedown in goodwill.

B) Revenues from continuing operations

The Group's revenues in the reporting period amounted to NIS 59 billion, compared with NIS 43 billion in the corresponding period of 2010, an increase of NIS 16 billion, as detailed in the following table (in NIS millions):

	2011	2010	10-12/2011	10-12/2010
Fuel operations in the US	25,755	14,019	7,453	3,582
Fuel operations in Europe	16,285	11,367 *)	4,355	3,944
Fuel operations in Israel	6,259	5,136	1,523	1,325
Automotive operations ***)	-	3,363	-	-
Oil and gas exploration and production operations	722	558	150	140
Insurance and finance operations in Israel **)	6,825	9,717	2,556	2,918
Overseas insurance operations **)	1,409	1,364	351	352
Other segments including adjustments ***)	1,904	(2,720)	409	158
Total revenues	59,159	42,804	16,797	12,419

*) Re-stated

**) Represents insurance premiums on self-retention in life insurance and general insurance.

***) Adjustments include, inter alia, automotive segment revenues, classified as discontinued operations in the income statements.

Revenues were up mainly due to contributions of new operations: Delek France, which commenced operations in Q4/2010, contributed revenues of NIS 4,937 million in the reporting period; and Lion, which commenced operations in Q2/2011, contributed revenues of NIS 7,732 million in the reporting period. The increase in revenues was also due to an increase in the number of barrels sold by the refinery in Tyler, Texas and rising fuel prices, which affected the refinery's revenues and gas station operations in the US, Europe, and Israel. See also Note 44 to the financial statements - Information Regarding Operating Segments.

C) Operating profit

	2011	2010	10-12/2011	10-12/2010
Fuel operations in the US	1,036	62	(13)	13
Fuel operations in Europe	184	190	20	45
Fuel operations in Israel	140	189	20	35
Automotive operations ⁽¹⁾	89	480	19	323
Oil and gas exploration and production operations	601	268	109	(12)
Insurance and finance operations in Israel	471	647	24	107
Overseas insurance operations	(451)	65	(341)	(25)
Other segments including adjustments	(457)	(676)	(327)	(346)
Operating profit	1,613	1,225	(466)	139

(1) Starting Q4/2010, when the Group lost control of Delek Automotive, the Group presents its share in Delek Automotive's operating profit - see also Note 14 to the financial statements.

For analysis of operating profit for the various segments, see below.

D) Finance expenses

The Group's finance expenses in the reporting period amounted to NIS 1,951 million, as compared to finance expenses of NIS 1,442 million in the same period last year (after adjusting for one-time expenses of NIS 213 million recorded in 2010 on the impairment of the Group's investment in Lion).

The average balance of the Group's financial liabilities in the reporting period increased to NIS 23 billion, as compared to an average balance of NIS 21 billion in the same period last year, which also contributed to the increase in finance expenses. This increase in the average balance of financial liabilities was due to the initial consolidation of Roadchef, Delek France and Lion.

Furthermore, the increase in finance expenses was also affected by changes in the Israeli CPI, which went up 2.5% in 2011, as compared to an increase of 2.3% last year.

E) Finance income

The Group's finance expenses in the reporting period amounted to NIS 626 million, as compared to finance income of NIS 271 million in the same period last year.

This increase is due mainly to NIS 397 million in profit from the sale of Noble shares in the reporting period.

F) The Group's share in the profits of associate companies and partnerships, net

The following table details the Group's share in the results of its principal associates:

	2011	2010	10-12-2011	10-12-2010
Delek Automotive *)	(24)	10	(33)	10
Avner	104	80	24	4
IDE	70	61	11	10
Roadchef **)	-	(44)	-	(32)
The Phoenix associates	(21)	48	4	27
Other ***)	(352)	1	(295)	(11)
Total	(223)	156	(289)	8

*) Starting Q4/2010, when the Group lost control of Delek Automotive, the Group presents its investment in Delek Automotive as per the equity method - see also Note 14 to the financial statements.

**) Starting Q1/2011, Roadchef is no longer considered an associate, but rather a consolidated company. See also Note 14 to the financial statements.

***) In the reporting period, this item includes equity losses and provisions for impairment of an investment in Delek Real Estate to the amount of NIS 105 million. Furthermore, a provision was recorded for impairment of an investment in Delek Automotive to the amount of NIS 250 million. See also Note 14 to the financial statements.

- G)** The table below shows principal data from the Company's consolidated income statements (in NIS millions):

	2011	2010	10-12/2011	10-12/2010
Revenues	59,159	42,804 (*)	16,797	12,419
Cost of revenues	50,903	36,217 (*)	15,062	10,641
Gross profit	8,256	6,587	1,735	1,778
Sales, marketing and gas station operating expenses	4,157	3,502	1,117	979
General and administrative expenses	1,884	1,772	478	530
Other income (expenses), net	(602)	(88)	(629)	(130)
Operating profit	1,613	1,225	(489)	139
Finance income	626	271	(142)	24
Finance expenses	(1,951)	(1,655)	(498)	(600)
Profit (loss) after financing	288	(159)	(845)	(437)
Profit (loss) from disposal of investments in investees and others, net	3,749	(4)	3,689	(4)
Group's equity in earnings (losses) of associate companies and partnerships, net	(223)	156	(289)	8
Profit (loss) before income tax	3,814	(7)	2,555	(433)
Income tax	558	178	90	26
Profit (loss) from continuing operations	3,256	(185)	2,465	(459)
Profit from discontinued operations	-	2,139	-	1,819
Net profit	3,256	1,954	2,465	1,360
Attributable to -				
Equity holders of the parent	2,610	1,701	2,159	1,399
Non-controlling interests	646	253	306	(39)
	3,256	1,954	2,465	1,360

(*) Re-classified

H) Movement in comprehensive income (loss) (in NIS millions):

	2011	2010	10-12/2011	10-12/2010
Net profit	3,256	1,954	2,465	1,360
Other comprehensive income (loss):				
Gain (loss) from available-for-sale financial assets, net	(95)	371	159	208
Transfer to profit or loss from disposal of available-for-sale financial assets	(338)	(32)	(51)	(11)
Transfer to profit or loss from impairment of available for sale financial assets	119	7	27	5
Loss from cash flow hedges, net	6	(5)	12	19
Exchange differences on translation of foreign operations	358	(381)	98	(136)
Transfer to profit or loss of adjustments from translation of foreign operations	37	-	-	-
Group's share in other comprehensive income (loss) of associates, net	134	(85)	22	(86)
Other comprehensive income (loss) from continuing operations	221	(125)	267	(1)
Other comprehensive loss from discontinued operations	-	(2)	-	-
Amounts released following loss of control	-	(27)	-	(27)
Total other comprehensive income (loss)	221	(154)	267	(28)
Total comprehensive income	3,477	1,800	2,732	1,332
Attributable to:				
Equity holders of the parent	2,746	1,586	2,375	1,392
Non-controlling interests	731	214	357	(60)
	3,477	1,800	2,732	1,332

I) Highlights from the Company's consolidated income statements (NIS millions):

	1-3/11	4-6/11	7-9/11	10-12/11	2011
Revenues	13,121	14,026	15,215	16,797	59,159
Cost of revenues	11,198	11,884	12,759	15,062	50,903
Gross profit	1,923	2,142	2,456	1,735	8,256
Selling, marketing and gas station operating expenses	963	1,006	1,071	1,117	4,157
General and administrative expenses	446	508	452	478	1,884
Other income (expenses), net	83	-	(56)	(629)	(602)
Operating profit	597	628	877	(489)	1,613
Finance income	228	199	57	142	626
Finance expenses	(468)	(529)	(456)	(498)	(1,951)
Profit (loss) after financing	357	298	478	(845)	288
Gain (loss) from disposal of investments in investees and others, net	(1)	(1)	62	3,689	3,749
Group share in the earnings of partnerships and associates, net	84	(1)	(17)	(289)	(223)
Profit (loss) before income tax	440	296	523	2,555	3,814
Income tax	129	94	245	90	558
Net profit	311	202	278	2,465	3,256
Attributable to:					
Equity holders of the parent	210	101	140	2159	2,610
Non-controlling interests	101	101	138	306	646
	311	202	278	2,465	3,256

J) Movement in comprehensive income (loss) (in NIS millions):

	1-3/11	4-6/11	7-9/11	10-12/11	2011
Net profit	311	202	278	2,465	3,256
Other comprehensive income (loss):					
Gain (loss) from available-for-sale financial assets, net	(100)	(225)	(124)	135	(314)
Gain (loss) from cash flow hedges, net	20	(10)	(16)	12	6
Exchange differences on translation of foreign operations	14	(109)	392	98	395
Group's share of other comprehensive income (loss) of associates, net	(34)	3	143	22	134
Total other comprehensive income (loss)	(100)	(341)	395	267	221
Total comprehensive income	211	(139)	673	2,732	3,477
Attributable to:					
Equity holders of the parent	156	(207)	422	2,375	2,746
Non-controlling interests	55	68	251	357	731

4. Financial Position

The Group's total assets as of December 31, 2011, amounted to NIS 108 billion, compared with NIS 92 billion as of December 31, 2010. This increase is due mainly to the initial consolidation of Lion, Roadchef and the Avner Partnership.

Below is a description of the principal changes in assets and liabilities as of December 31, 2011, compared with December 31, 2010:

Cash and cash equivalents and short-term investments

The Group has cash and short-term investment balances of NIS 4.3 billion, consisting mainly of balances of NIS 0.5 billion in the headquarters companies, NIS 0.5 billion in Delek Europe, NIS 1.3 billion in The Phoenix, NIS 0.6 billion in Delek Energy, NIS 0.9 billion in Delek US, and NIS 0.2 billion in Republic.

Total current assets

The Group's total current assets (excluding assets held for sale) as of December 31, 2011, amounted to NIS 38.6 billion, compared with NIS 33.4 billion as of December 31, 2010. This change was mainly due to an increase in the ETF and short-term investments item in insurance companies, and to Lion's consolidation starting Q2/2011.

Total non-current assets

The Group's total non-current assets as of December 31, 2011, amounted to NIS 69.3 billion, as compared to NIS 58.3 billion as of December 31, 2010, an increase of NIS 11 billion. This increase is primarily due to initial consolidation of Avner in Q4/2011, which contributed mainly to the investment in oil and gas exploration item (NIS 9.4 billion), from initial consolidation of Roadchef in Q1/2011, which contributed mainly to property, plant and equipment (NIS 347 million), goodwill (NIS 822 million), and other intangible assets (NIS 709 million). Total non-current assets were also favorably influenced by Lion's consolidation in the second quarter of 2011, which contributed mainly to property, plant and equipment (NIS 1,058 million). This increase was partially offset by the sale of Noble shares in the first half of 2011.

Balance of short- and long-term financial liabilities

Total financial liabilities (to banks, others and debenture holders) as of December 31, 2011, amounted to NIS 24.7 billion, compared with NIS 21.4 billion as of December 31, 2010. This increase is mainly attributable to Roadchef's initial consolidation in Q1/2011, which contributed NIS 1,132 million, to initial consolidation of the Avner Partnership and Cohen Development in Q4/2011, which contributed NIS 1,010 million, and to a bond raising round in Q3/2011.

Contingent claims

In their report, the Company's auditors draw attention to legal actions brought against investees. For details, see Note 32 to the financial statements.

Additional information

For additional information regarding repayments of principal and interest on the debts of headquarter companies, see Appendix A to the Board of Directors' Report.

5. Sources of Finance and Liquidity

The net financial debt of the Company and the headquarters companies as of December 31, 2011: ⁽²⁾

	NIS millions
Liabilities	
Debentures	(8,373)
Bank loans	(515)
Loans from consolidated companies	(293)
Other	(185)
Total liabilities	(9,366)
Assets	
Cash	265
Financial investments	813
Loans to investees ⁽³⁾	1,236
Dormant shares	278
Other	10
Total assets	2,602
Net financial liability - headquarters companies	(6,764)

Debt raising:

In July 2011, the Company completed a NIS 467 million expansion of existing debenture series. In November 2011, the Company completed a private placement effected as an expansion of debenture series in consideration for NIS 261 million. For more information and details concerning these debenture raising rounds, see Note 27 to the financial statements.

Consolidated, the Company has a working capital deficit of NIS 3 billion, while the Company's separate working capital deficit is NIS 1 billion. As an investment management company operating in the oil and gas exploration and production, infrastructures, gas stations and refining, insurance and finance, automotive, and other industries, the Company review its liquidity based on its operations at the headquarters (separate) level, and for each investee at the investee level. The fact that the bulk of the Company's assets are free of any liens, its ability to dispose of holdings and its ability to recycle debt and/or obtain additional long-term loans (mainly in the oil and gas and infrastructures segments) provide the Company and its subsidiaries with financial flexibility and adequate liquidity. Therefore, the Company's consolidated and separate working capital deficit does not indicate any liquidity problems.

As of the financial statements' approval date, the Company and its headquarters companies have liquid balances of NIS 1.2 million.

² Headquarters companies: Delek Group, Delek Investments, Delek Petroleum, Delek Finance US Inc., Delek Infrastructures, Delek Europe Israel and Delek Hungary.

³ For information on the composition of loans to investees, see Chapter 4 of the periodic report.

6. Analysis of Operations by Segment

A. Fuel operations in the US

Delek US results as included in the Company's consolidated financial statements:

	2011	2010	10-12/2011	10-12/2010
	NIS millions	NIS millions	NIS millions	NIS millions
Revenues	25,755	14,019	7,453	3,582
Results of operations (excluding depreciation and general and administrative expenses)	1,603	505	140	117
Depreciation expenses	265	228	77	59
General and administrative expenses	291	217	73	47
Operating profit	1,065	58	(14)	9
Finance expenses, net	154	357	62	254
Net profit (loss) attributable to owners of the parent	551	(290)	(52)	(245)

Additional operational data:

		2011	2010	10-12/2011	10-12/2010
Refining operations					
	Contribution to results of operations (NIS millions)	1,348	214	86	63
Tyler refinery	Operational days	365	365	92	92
Tyler refinery	Average daily barrel sales	60,395	53,360	63,211	54,405
Tyler refinery	Average WTI barrel price in the period (USD)	95.07	79.5	93.93	85.16
Tyler refinery	Average refining margin (USD/barrel)	17.92	7.00	11.79	7.85
Tyler refinery	Direct production costs (USD/barrel)	5.27	5.21	4.62	5.51
El Dorado refinery	Operational days	247	-	92	-
El Dorado refinery דוראדו	Average daily barrel sales	76,153	-	75,694	-
El Dorado refinery דוראדו	Average MARS barrel price in the period (USD)	108.19	-	106.72	-
El Dorado refinery דוראדו	Average refining margin (USD/barrel)	9.02	-	2.07	-
El Dorado refinery דוראדו	Direct production costs (USD/barrel)	4.09	-	3.65	-
Marketing operations					
	Contribution to results of operations (NIS millions)	94	95	22	24
	Average daily barrel sales	15,493	14,354	15,337	14,352
Gas station operations					
	Contribution to results of operations (NIS millions)	161	196	32	30
	Average no. of stations in the period	394	428	383	417
	Station turnover (thousands of gallons)	409,446	423,509	103,497	184,103
	Margin per gallon (USD)	0.162	0.161	0.146	0.131

The Group's direct and indirect holdings in Delek US as of the balance sheet date total 68.3%. Delek US is a listed company in the US.

Analysis of the results of fuel operations in the US**Revenues**

Revenues for the reporting period totaled NIS 25,755 million, as compared to NIS 14,021 million in the same period last year. This increase is attributable to the initial consolidation of the El Dorado refinery in Q2/2011, an increase in average daily barrel sales in the Tyler refinery, and due to rising fuel prices which affected sales in both refining and marketing operations and in gas station operations.

Operating profit (before depreciation and administrative expenses)

Operating profit for the reporting period amounted to NIS 1,603 million, as compared to NIS 505 million in the same period last year, an increase of NIS 1,098 million.

The bulk of this increase in the results of operations (NIS 1,134 million) is attributable to the initial consolidation of the El Dorado refinery in the second quarter, which contributed NIS 340 million to operating results; and a sharp increase in the gross refining margin per barrel in the Tyler refinery, which went up from USD 7 per barrel to USD 17.92 per barrel, which was accompanied by increased regional demand. Furthermore, the Tyler refinery, which is fed mainly with West Texas Intermediate (WTI), continued benefiting from lower oil prices as compared to similar oil types.

Depreciation and general and administrative expenses

These expenses increased during the reporting year, mainly due to the initial consolidation of the El Dorado refinery (Lion).

Finance expenses, net

A provision for the impairment of the Company's investment in Lion was recognized in 2010, to the amount of NIS 213 million. After adjusting for this provision, finance expenses increased by NIS 10 million, due to increased expenses incurred through the Lion transaction, net of a decrease in expenses caused by a decrease in Delek US' debt.

Additional information

It is noted that there are a number of differences between the financial results of Delek US according to US GAAP as published, and their inclusion in the financial statements according to IFRSs applied in Israel. The principle difference stems from a different accounting policy for inventory - in the US, the cost of inventory is determined according to LIFO and FIFO, whereas IFRSs require the application of the average method.

For more information about Delek US' operations, see Note 14 to the financial statements and Section 1.7 in Part A of the periodic report - Description of the Corporation's Business.

B. Fuel operations in Israel**Data from the financial statements of Delek Israel:**

	2011	2010	10-12/2011	10-12/2010
	NIS millions	NIS millions	NIS millions	NIS millions
Revenues	6,259	5,136	1,523	1,324
Gross profit	764	775	173	188
Operating profit	139	188	20	31
EBITDA from continuing operations	226	290	44	53
Finance expenses, net	111	93	23	30
Delek Israel's share in results of associates	1	(8)	(3)	(14)
Net profit	18	60	(7)	(15)
Attributable to:				
Equity holders of the parent	17	56	(8)	(16)
Non-controlling interests	1	4	1	1
	18	60	(7)	(15)

As of the balance sheet date, the Group maintained an 86.9% interest in Delek Israel (Delek Israel is a public company whose statements are available to the public). For information concerning a purchase offer for shares in Delek Israel, see above.

Revenues

The year-on-year increase in revenues is due mainly to higher fuel prices in 2011 as compared with 2010, a quantitative increase in wholesale activities, and increased sales turnover in the Menta chain of convenience stores. These increases were partially offset by a quantitative decrease in fuel sales in the public refueling areas. Revenues in the Menta convenience store chain (net of concession sales) totaled NIS 276 million in the reporting period, as compared to NIS 228 million in the same period last year, an increase of 21.1%. Revenues from these operations in Q4/2011 totaled NIS 69 million, as compared to NIS 61 million in the same quarter last year, an increase of 13%. This increase in convenience store turnover was due both to an increase in the number of stores, which as of the reporting date totaled 187 stores as compared to 170 stores in the same period last year, and an increase in same-store sales.

Gross profit

Gross profit for 2011 totaled NIS 764 million, as compared to NIS 775 million in 2010, an increase of 1.4%. Gross profit in Q4/2011 totaled NIS 173 million, as compared to NIS 188 million in the same quarter last year, a decrease of 8%.

Gross profit was down in the reporting period, due to a reduction in retail margins from September 2011, which significantly undermined profitability in the refueling and service areas. Gross profit was also adversely affected by a quantitative decrease due, inter alia, to increased gasoline and diesel prices and stiff market competition, mainly in the discount channels, an erosion of gross margins in the lubricants segment caused by increased raw material prices and lower retail prices, and the sale of the Bitum subsidiary in January 2011. The decrease in gross profit was offset by increased profitability in the convenience store segment, and increased profitability in the direct marketing segment in off-station operations.

Gross profit in Q4/2011 was down as compared to the same quarter last year, mainly due to reduced retail margins on gasoline and a quantitative decrease and smaller margins in the refueling and service area segment, due to fuel prices and increased competition, and Jewish holidays which occurred in Q4 this year as compared to Q3 in 2010.

Sales, gas station operation and general and administrative expenses

In 2011, these expenses amounted to NIS 632 million, as compared to NIS 586 million in 2010, an increase of 7.8%. In Q4/2011, these expenses amounted to NIS 160 million, as compared to NIS 157 million in the same quarter last year, an increase of 1.5%. In Q2/2010, the Company recorded a one-time income of NIS 8 million from the cancellation of a provision for expenses for an options benefit to the Company's former CEO. In the reporting year, the Company recorded provisions for doubtful debt of NIS 10 million, mainly in consolidated companies in the direct marketing segment. After adjusting for this one-time income in 2010 and the extraordinary provision for doubtful debts in 2011, sales and general and administrative expenses grew by only NIS 28 million between periods.

The year-on-year increase in these expenses is attributable mainly to an increase in gas station operating expenses as a result of the transition to Company-operated gas stations and the opening of new stations; an increase in rental fees for new gas stations; increased operating expenses for the Company's convenience stores following the chain's expansion; increased clearing fees charged by credit card companies following the increase in interchange rates; increased municipal land tax payments and electricity costs; and an increase in the minimum wage and labor costs in the refueling areas.

For more information about Delek Israel's operations, see Note 14 to the financial statements and Section 1.8 in Part A of the periodic report - Description of the Corporation's Business.

C. Fuel operations in Europe

Fuel operations in Europe are managed by the consolidated company Delek Europe BV ("Delek Europe"), a subsidiary incorporated in the Netherlands and indirectly held through Delek Petroleum (80%) and "Delek" The Israel Fuel Corporation Ltd. (20%). Operations include marketing and distribution of fuel and oil products, operation of gas stations, operation of a chain of convenience stores and bakeries, carwash facilities, and various holdings in terminals.

On October 1, 2010, Delek Europe completed a transaction for the acquisition of BP's fuel operations in France.

Upon the transaction's completion, Delek Europe operates in four countries in Western Europe. Operations in Belgium, the Netherlands, and Luxembourg ("Benelux") are carried out through Delek

Benelux BV ("Delek Benelux"), while operations in France are carried out through Delek France BV ("Delek France"). The two companies are wholly-owned subsidiaries of Delek Europe, incorporated in the Netherlands.

For more information concerning the acquisition of operations in France by Delek Europe, see Note 14 to the 2011 annual financial statements.

Condensed statement of financial position of Delek Europe as of December 31, 2011 and 2010, as included in the Group's statements (in NIS millions):

	December 31, 2011	December 31, 2010
Cash	542	680
Current assets (excluding cash)	1,846	1,530
Investment in investees and long term receivables	151	110
Property, plant and equipment, net	1,974	1,732
Other property, net	1,475	1,477
Short-term credit and loans	289	247
Current liabilities (excluding short-term credit and loans)	2,077	1,991
Long-term loans from banks	1,912	1,701
Long-term loans from shareholders	606	568
Other long-term liabilities	450	422
Equity	654	600

Data from Delek Europe's income statement as included in the Group's statements (in NIS millions):

	1-12/2011 *	1-12/2010 **	10-12/2011	10-12/2010
	NIS millions	NIS millions	NIS millions	NIS millions
Revenues	16,285	11,367	4,355	4,413
Gross profit	1,931	1,384	432	472
Operating profit (loss)	194	183	19	35
Equity in earnings of investee partnerships	11	9	12	3
EBITDA	488	367	103	99
Finance expenses	(173)	(105)	(40)	(42)
Net profit	14	72	(7)	(14)
Average exchange rate for translation of financial statements (EUR/NIS)	4.98	4.88	5.02	4.92

* 2011 data includes Delek Benelux and Delek France's results.

** 2010 data includes Delek France's results for Q4 only.

EBITDA distribution across operations (in EUR millions):

	1-12/2011	1-12/2010 **	10-12/2011	10-12/2010
	EUR millions	EUR millions	EUR millions	EUR millions
Delek Benelux	65	66	16	11
Delek France	33	10	2	10

** 2010 data includes Delek France's results for Q4 only.

Analysis of Delek Europe's results in the reporting periods:**Revenues**

Revenues in the reporting period amounted to NIS 16,285 million, compared with NIS 11,367 million in the same period last year. The increase in revenues recorded this year from Delek France as compared to revenues recorded from Delek France in 2010 (for Q4 only), amounted to NIS 3,800 million. The remaining increase in revenues is due mainly to increased fuel prices and increased convenience store sales in Benelux, which were offset by a quantitative decrease in fuel sales.

Gross profit

Gross profit in the reporting period amounted to NIS 1,931 million, compared with NIS 1,384 million in the same period last year. Delek France's contribution to gross profit this year grew by NIS 500 million as compared to its contribution to gross profits last year (for Q4 only). The remaining increase in gross profits is mainly due to Delek Benelux, and was primarily caused by continued growth in convenience store operations.

Operating profit

Operating profit in the reporting period, after adjustment for one-time expenses, amounted to NIS 194 million, compared with NIS 183 million in the same period last year. Consolidation of Delek France's results in the reporting period contributed NIS 55 million to operating profit, as compared to NIS 15 million last year. Year-on-year, operating profit generated by Delek Benelux decreased by NIS 30 million. The decrease in operating profit is due mainly to the economic slowdown in Europe, which decreased the quantity of fuel sold in 2011, as compared to 2010, and the erosion of profitability and an increased operating expenses.

For more information about Delek Europe's operations, see Note 14 to the financial statements and Section 1.9 in Part A of the periodic report - Description of the Corporation's Business.

D. Motorway Service Area Operations in the UK

Delek Petroleum holds 100% of Delek Motorway Services' ("DMS") shares. DMS holds 100% of the shares in a UK company ("MSA") which holds RoadChef Limited. RoadChef Limited holds 28 motorway service areas in 20 different locations (including a recent acquisition - see below) in the UK, operating under the Roadchef brand. This entire group of companies is henceforth referred to as Roadchef.

Until the end of 2010, Delek Petroleum held 25% of the shares in Roadchef, and presented its investment as per the equity method. In the first quarter of 2011, Delek Petroleum completed the acquisition of 75% of Roadchef's outstanding shares. Consideration for the acquisition totaled GBP 86.25 million (approximately NIS 497 million), reflecting a value of GBP 115 million for Roadchef.

From Q1/2011, the Group fully consolidates Roadchef's results in its financial statements (for information concerning the completion of the Company's acquisition of Roadchef's shares as aforesaid, see Note 14 to the financial statements).

Data from Roadchef's statements of financial position as December 31, 2011 (in NIS millions):

	December 31, 2011 (*)
Current assets	77
Property, plant and equipment, net	428
Other property, net	708
Goodwill	772
Short-term credit and loans	(244)
Current liabilities (excluding short-term credit and loans)	(145)
Long-term loans from banks	(70)
Debentures	(819)
Other long-term liabilities	(23)
Reserve for deferred taxes, net	(109)
Shareholder loans	(1,364)
Capital deficit	789

(*) Data include classification of surplus acquisition costs.

Data from Roadchef's income statements from the date of its initial consolidation by the Group (in NIS millions):

Item	1-12/2011	10-12/2011
Revenues	1,156	249
Operating expenses	1,019	212
Depreciation	59	15
Other expenses	25	11
Operating profit	53	11
EBITDA (*)	156	38
Finance expenses on bank loans	81	22
Tax benefit	5	1
Net profit (loss)	(23)	(10)

(*) Reflects operational activities managed by Roadchef Ltd.

During the reporting period, Roadchef continued implementing its operating strategy which includes, inter alia:

- 1) Improving profitability by improving operating efficiency.
- 2) Using well-known brands and providing quality service.
- 3) Fast service times.
- 4) Expanding product offerings.
- 5) Competitive pricing.

Roadchef has signed a franchise agreement for managing and operating McDonald's branches on its sites. By the end of 2011, Roadchef completed construction of 9 on-site McDonald's branches, with 3 additional branches planned to be opened in 2012.

In August 2011, Roadchef completed the acquisition of a foreign company which owns a motorway service area in the UK. This acquisition was completed in consideration for GBP 10.65 million.

For more information about motorway service area operations in the UK, see Note 14 to the financial statements and Section 1.10 in Part A of the periodic report - Description of the Corporation's Business.

E. Oil and Gas Exploration and Gas Production Operations

Delek Energy Systems Ltd. ("Delek Energy" or "DES") is a public company in which the Company has an 86.9% interest as of the balance sheet date.

Operations in Israel are carried out through Delek Drilling Limited Partnership ("Delek Drilling") and Avner Oil Exploration Limited Partnership ("Avner") (jointly - "the Partnerships"), which are partners in the Yam Tethys project (together with Delek Investments) in developing the Tamar gas reservoir, and in developing an assessment of the Leviathan gas discoveries in Israel and the Aphrodite gas discoveries in Cyprus, and in other offshore oil rights, mostly off the coast of Israel.

It is noted that in the reporting period, Delek Energy completed the sale of all its oil and gas assets in the US.

For information on the acquisition of 52% of Cohen Development's shares, see Note 14 to the financial statements.

Below are the results of oil and gas exploration and production operations as included in the Group's results:

	2011	2010	10-12/2011	10-12/2010
	NIS millions	NIS millions	NIS millions	NIS millions
Revenues	723	558	150	137
Operating profit	484	175	100	(20)
EBITDA	693	368	147	73
Finance expenses, net	196	147	43	38
Group's share in results of Avner and other associates ^(*)	92	82	14	-
Net profit	197	64	31	(31)
Gas sales in BCM ^(**)	4.3	3.2	0.9	0.8

(*) Starting 2012, the results of the Avner Partnership will be consolidated with the results of the Company's operations following assumption of control in the general partner in Avner.

(**) The data relate to sales of gas by the entire Yam Tethys group, rounded to one tenth of one BCM.

Analysis of the results of operations in the gas segment:

Oil and gas exploration in the reporting period yielded profits of NIS 197 million, as compared to NIS 64 million in the corresponding period last year. Operating profit in Q4/2011 amounted to NIS 31 million, compared with a loss of NIS 31 million in the same period last year. This growth in profit was due mainly to natural gas sales in the Yam Tethys project.

This increase in the volume of gas sold to IEC during the reporting period as compared to the same period last year, is due mainly to a decrease in natural gas sales by EMG. It is noted, that the supply of natural gas to Israel by EMG was partially or fully disrupted several times in recent months, due to security and/or political developments in Egypt. Furthermore, information has recently appeared in the press that authorities in Egypt intend to re-examine the prices on Egypt's natural gas exports. These disruptions in EMG's supply of natural gas have led to the partners conducting spot sales of natural gas by the Yam Tethys project to EMG's clients, which required an alternative source for short periods of time. It is noted that the aforesaid increase in gas quantities supplied to IEC, is unusual in size and it is possible that the above gas supply rate will not continue in the future.

It is further noted that prices on the sale of natural gas to IEC have gone up. These transactions are carried out pursuant to a memorandum of understanding signed with IEC, and pertaining to the sale of additional quantities of natural gas starting July 1, 2009.

Increased profits were offset by expenses recognized in the reporting period for the Leviathan 2 drilling project. Drilling was stopped in the Leviathan 2 site prior to arriving at the target layer, due to a failure which led to the abandonment of the drill site. Total expenses recognized for the drill site in the reporting period amounted to NIS 22.8 million (net of NIS 21.2 million in income from insurance companies). It is noted that Delek Drilling and Avner has subscribed to 'Control of Well' insurance which covers expenses incurred in regaining control of a well, including redrilling costs, up to a maximum liability of USD 200 million (100%) per incident. On August 2, 2011, the limited partnerships received a letter from the insurance consultant. In his letter, the insurance consultant stated that, according to the information and facts available to him, the insurance consultant estimates that the limited partnerships will receive payment for covered damages (as defined in the policy) in connection with the Leviathan 2 drilling, subject to the terms of the policy and net of a USD 1.15 million deductible. However, it is noted that a dispute may arise concerning the extent of the covered damages and the date of the insurance payment.

In recent months, natural gas production capacity in the Mari B reservoir dropped significantly. This drop in production capacity reduced the supply of natural gas from the reservoir to the Yam Tethys project. Information provided to the partnerships by the operator, based on the operator's tests and analysis carried out both in-house and through third parties, indicates that production of natural gas from the Mari B reservoir, which led to frequent releases of pressure in the reservoir, caused more sinking than expected of soil layers above the reservoir and below the production platform. Sinking soil layers also contributed to the reduction and even loss of production capacity in some of the production drillings, so that natural gas is currently only produced in the 5, 9, and 10 drilling sites in the Mari B reservoir (and each of these sites identified increased water penetration into the production drillings, in

a manner that impedes production). It is noted, that the production platform in the Yam Tethys project is designed, both technically and in engineering terms, to accommodate sinking caused primarily by the settlement of soil layers above the reservoir and below the production platform, and at this stage, the production platform's sinking is within its designed tolerance.

The operator plans to produce natural gas from the reservoir at a rate which will maintain production capacity and will not damage the platform.

Furthermore, the partners in the project are actively developing the Noa reservoir, drilling in the Leviathan reservoirs of the Mari B (Pinnacles) reservoir, and the development of these reservoirs in the event of natural gas discoveries. This activity is aimed at initiating production, thereby minimizing the ongoing reduction in supply capacity and mitigating the effects of such reduction, while maintaining the integrity of the Yam Tethys project's production system.

As indicated in the reserves report, there is no change in the assessment of existing reserves in the reservoir (except for the reduction in actual production volumes). Therefore, the above developments are mainly reflected in a significant drop in production ability in the Mari B reservoir and the production facilities.

The decrease in natural gas supply capacity is expected to adversely affect the partnerships' financial results. However, at this stage, the partnerships are unable to assess with a high level of certainty the full commercial implications or the scope of these effects, mainly in light of the frequent developments in the project. However, for the sake of caution, Delek Drilling recognized a provision for losses in the reporting year for these events to the amount of USD 4.5 million (net of royalties).

The partnerships are conducting negotiations with their customers in connection with the aforesaid decrease in supply and its legal ramifications. The partnerships' position is that the decrease in supply capacity is due to force majeure events as defined in the gas supply agreements. Should this position be rejected, the partnerships are liable to incur penalties according to the mechanisms and limitations set forth in the gas supply agreements.

Revenues

In the reporting period, the segment's revenues from the sale of gas and oil, net of royalties, totaled NIS 723 million, compared with NIS 558 million in the same period last year, an increase of 30%. The increase in sales turnover is due to those factors detailed above.

It is noted that IEC's average daily purchase of natural gas from the partners varies, inter alia, in accordance with seasonal changes in electricity consumption, IEC's maintenance works and the rate at which EMG can supply natural gas to IEC. Since July 1, 2009, additional quantities of gas are sold in accordance with the terms set forth in the memorandum of understanding signed with IEC for the supply of additional quantities of gas to an annual amount of 1 BCM over a five-year period, for a total amount of 5 BCM.

In Q4/2011, the segment's revenues from the sale of gas and oil, net of royalties, totaled NIS 150 million, compared with NIS 137 million in the same quarter last year, an increase of 9%.

Finance expenses, net

Net finance expenses in the reporting period amounted to NIS 196 million, compared to NIS 147 million in the same period last year. Finance expenses were mainly due to interest on bank loans and debentures issued by Delek Energy and Delek Drilling, and due to an increase in the Israeli CPI and the revaluation of the USD in the reporting period, as compared to the same period last year.

Share in the results of Avner and other associates

In the reporting period, oil and gas exploration and production operations included income from holdings in Avner, an associate partnership, and in other associates, to the amount of NIS 92 million, compared with income of NIS 82 million in the same period last year. Of this amount, NIS 1.7 million are attributed to losses through updating the guarantee given for VOGIL (the guarantee was redeemed in the reporting period), and NIS 10.5 million in losses on the share in Matra's results.

Additional information

For more information about energy-segment operations, see Note 14 to the financial statements and Section 1.11 in Part A of the periodic report - Description of the Corporation's Business.

F. Insurance and Finance Operations

The Group holds approximately 56% of the shares of The Phoenix Holdings Ltd. and all the shares of Republic, which is an elementary insurance company operating in the US.

The Phoenix Holdings Ltd. ("The Phoenix")

Below are the principal data from The Phoenix's consolidated income statements (in NIS millions):

	2011	2010		10-12/2011	10-12/2010
Gross premiums earned	6,786	6,068		1,947	1,618
Premiums earned in retention	6,154	5,431		1,781	1,454
Net gains (losses) on investments, and finance income	(487)	3,148		486	1,166
Commissions, marketing, and other purchasing expenses	1,045	1,005		271	262
General and administrative expenses	930	903		239	262
Other expenses	158	110		120	67
Finance expenses	268	223		50	58
Share in the earnings (losses) of investees accounted for as per the equity method	(21)	50		3	27
Profit (loss) for the period	69	333		(70)	78
Profit (loss) for the period attributable to owners of the parent	54	309		(73)	70

A significant part of The Phoenix's asset portfolio is invested on the capital market. Therefore, capital market returns for the various investment channels have a material effect on the yields achieved for The Phoenix's customers and on The Phoenix's profits. Gains and losses on investments reflect capital market movements in Israel and abroad, and fluctuations in the Israeli CPI and the NIS exchange rates against primary currencies, whose aggregate effect on the financial margin is the main cause for fluctuations in the reported results.

In the reporting period, The Phoenix's results were materially affected by negative yields in the capital market, which were significantly lower than the yields achieved in the same period of 2010. Revenues from investments, including other comprehensive losses (pre-tax), amounted to losses of NIS 615 million, as compared to a profit of NIS 3,294 million last year. It is noted that this difference is mostly attributed to investment profit-sharing policies and did not directly influence The Phoenix's results.

Gross premiums earned on life, health, and general insurance in the reporting period amounted to NIS 6.8 billion, up 13.3% from the same period last year. In Q4/2011, premiums amounted to NIS 1.9 billion, an increase of 20.3% from the same quarter last year.

In the reporting period, commissions, marketing and other purchasing expenses totaled 15.4% of the gross premiums earned, as compared to 16.6% and 17.3% in 2010 and 2009, respectively. In Q4/2011, commissions, marketing and other purchasing expenses amounted to 13.9% of the gross premiums earned, as compared to 16.2% in the same quarter last year.

The percentage of general and administrative expenses out of gross premiums earned in the reporting period was 13.7%, as compared to 14.9% in 2010 and 2009. The percentage of general and administrative expenses out of gross premiums earned in the present quarter was 12.3%, as compared to 16.2% in the same quarter last year.

In February 2012, the Israeli Knesset's Finance Committee approved an amendment to the Supervision of Financial Services Regulations (Provident Funds) (Management Fees), 2012 ("the Regulations"). The amendment states that starting January 2014, the maximum annual management fees charged on provident funds and executive insurance without a guaranteed yield will be limited to 1.05% of each member's accrued balance, and 4% of current contributions. The amendment further states that in 2013, management fee payments will be limited to no more than 1.1% of each member's accrued balance, and 4% of current contributions.

Following the aforesaid, a NIS 113 million write-down was recorded in goodwill attributable to provident fund operations.

In the reporting period, The Phoenix did not charge variable management fees on profit-sharing policies marketed until 2004, due to negative yields recorded during the year in the capital market. Uncollected management fees due to negative yields until the coverage of investment losses on these policies are estimated at NIS 279 million as of December 31, 2011, as compared to NIS 38 million as of December 31, 2010. As of the end of February 2012, this amount totaled NIS 199 million.

Below are the principal data from The Phoenix's consolidated financial statements:

	2011	2010	10-12/2011	10-12/2010
Profit (loss) from life insurance and long term savings segment	(14)	64	(80)	(19)
Profit from health insurance segment	126	104	22	61
Profit from general insurance segment	142	220	45	34
Profit from financial services segment	95	112	18	31
Total profit from operating segments	349	500	5	107
Profit (loss) not attributed to reporting segments	(100)	(33)	(18)	(1)
Company's share in the net results of investees not included in the reported segments	(31)	24	2	14
Profit (loss) before income tax	218	491	(11)	120
Income tax	149	158	59	42
Profit (loss) for the period	69	333	(70)	78
Profit (loss) for the period attributable to owners of the parent	54	309	(73)	70

The Phoenix's share in the net results of investees in the reporting period amounted to a loss of NIS 21 million, as compared to gains of NIS 50 million in 2010. This decrease in income from investees is mainly attributable to Linchfield Limited, which primarily engages in parking lot holdings in London, and was due to an impairment recognized in the first six months of the year on these parking lots, and financing expenses recorded for this acquisition. The total effect of Linchfield's losses on the 2011 financial statements amounts to NIS 49 million. This investment has zeroed as of December 31, 2011.

Additional information

For more information about The Phoenix's operations, see Note 14 to the financial statements and Section 1.12 in Part A of the periodic report - Description of the Corporation's Business.

Republic Companies, Inc

Republic Companies, Inc ("Republic") is a wholly-owned subsidiary. Republic is one of the oldest companies in the US dealing in property and accident insurance (over 100 years of history). Republic holds insurance companies and agencies which deal primarily in property and other general insurance, particularly in Texas, Louisiana, Oklahoma, Mississippi, Arkansas, and New Mexico, in the US. In addition, Republic holds insurance licenses in 45 other states, with one license generating front insurance revenues for Republic.

Republic's operating segments:

Republic operates in 4 main segments:

- Personal Lines - Household property and accident insurance marketed through the company's network of approximately 850 active agents (personal insurance policies).
- Commercial Lines - Insurance for the commercial sector marketed through the company's network of agents.
- Program Management - Insurance through M.G.A. - independent brokers and underwriters connected to the company through unique, customized insurance programs marketed by brokers through their agents.
- Insurance Services - Operations in insurance services, front policies made in collaboration with leading insurers in the US, seeking to leverage the availability of Republic's operating license in Texas.

The results of Republic's operations as included in the Group's results:

	2011	2010	10-12/2011	10-12/2010
	USD millions	USD millions	USD millions	USD millions
Gross premiums earned	732	808	164	181
Premiums earned in retention	354	315	87	84
Investment and other income, net	40	45	7	12
Total revenues	394	365	93	101
Increase in insurance liabilities net of reinsurers	301	194	76	52
Commissions and other purchasing expenses	104	93	27	22
General and administrative expenses	50	64	21	34
Impairment of goodwill	61	-	61	-
Finance expenses	6	13	1	9
Total expenses	522	361	180	114
Profit (loss) before income tax	(128)	4	(87)	(13)
Net profit (loss)	(109)	(2)	(86)	(14)

Analysis of the results of Republic's operations as included in the Group's statements

Republic's losses as included in the Group's 2011 financial statements amount to USD 109 million, as compared to a total loss of USD 2 million in 2010. Losses in 2011 are comprised mainly of USD 49 million in operating losses in Republic's various operating segments, plus a writedown of goodwill due to the significant reduction in business and an appraisal-based impairment of goodwill to the amount of USD 61 million, and a USD 13 million provision for employee pension plans.

Operating losses in 2011 were due mainly to the following factors:

- Inclement weather conditions - Although no hurricanes were recorded in 2011, the large number of tornados, extreme winds, hailstorms, and fires which occurred mainly in Texas during the reporting year caused Republic to incur USD 64 million in losses after reinsurance, as compared to USD 23 million in such losses in 2010.
- In addition to inclement weather, in the reporting year Republic significantly increased its provision to claims and liabilities for expected claims, to the amount of USD 42 million. This increase is due mainly to the continuation of existing claims, and an increase in actual payments on past claims. This is explained primarily by economic conditions in the US, which is apparently causing an increase in insurance claims and a reduction in settlements which subsequently increase the amounts paid on these claims, mainly in the Commercial Lines segment and in auto insurance.

These extensive operating losses, and the increased actuarial provisions for general insurance which reduced Republic's equity (which is one of the main parameters for operating growth), have led Republic and the Group to re-examine the carrying amount of goodwill in Republic. Following this examination, a provision was recognized for impairment of goodwill, to the amount of USD 61 million (for more information on this writedown, see the valuation attached to this report, and Note 14 to the financial statements).

In 2011, revenues from premiums (gross) amounted to USD 732 million, as compared to USD 808 million in 2010. Stiff competition in the US market, exacerbated by the economic slowdown and capital surpluses recorded by market players, have led to the loss of some of Republic's customers and a reduction in gross premiums earned as compared to the previous year.

Insurance premiums earned in retention in 2011 amounted to USD 354 million, as compared to NIS 315 million in 2010. The year-on-year increase is explained by the fact that 2010 was still influenced by reinsurance purchases (quota share), which reduced insurance premiums in retention. These reinsurance arrangements in 2010 were due to management's decision to implement more conservative reinsurance policies, while increasing readiness to cope with extraordinary insurance events caused by severe weather.

Republic's equity attributable to owners of the parent, as included in the Group's financial statements as of December 31, 2011, amounted to USD 205 million.

For more information about Republic's insurance operations abroad, see Note 14 to the financial statements and Section 1.13 in Part A of the periodic report - Description of the Corporation's Business.

G. Automotive Operations

As aforesaid, Delek Automotive's results are not consolidated in the income statement, and are included under the 'Group's share in the equity of associate companies and partnerships' item. Below is an analysis of the results of the Group's automotive operations. On December 13, 2011, Delek Motors Ltd. acquired control in Kamor Motors Ltd., and as of this date Delek Motors Ltd., through Kamor Motors, imports and markets BMW and MINI vehicles and spares in Israel.

Following are the results of Delek Automotive Systems Ltd.'s ("Delek Automotive") operations:

	2011	2010	10-12/2011	10-12/2010
	NIS millions	NIS millions	NIS millions	NIS millions
Revenues	3,664	4,609	794	1,247
Gross profit	428	624	91	126
Sales, marketing and general and administrative expenses	72	75	17	23
Operating profit	357	550	70	104
EBITDA	367	562	72	108
Finance income (expenses), net	(201)	19	(13)	51
Net profit	121	428	48	115

As of the income statement date, the Group holds 32.8% of Delek Automotive (Delek Automotive is a public company which publishes its financial statements).

Analysis of the results of Delek Automotive's operations in the reporting periods:

Breakdown of Delek Automotive's sales by number of cars sold:

	2011	2010	10-12/11	10-12/10
MAZDA vehicles	21,234	31,856	3,019	9,019
FORD vehicles	11,610	10,855	4,070	3,065
Total vehicles sold	32,844	42,711	7,089	12,084
Delek Automotive's share of all vehicles sold in Israel (based on Licensing Bureau data)	14%	19%	14%	19%

- 1) 2011 was a record year in vehicle sales in Israel, with new vehicle sales totaling 231,000, up 4.5% from the previous year which was itself a record year. Delek Automotive's market share decreased to 14% in 2011, as compared to 19% in the previous year. This reduction in Delek Automotive's market share in 2011 was due, inter alia, to reduced competitiveness following the revaluation of the Japanese Yen during the year, which coincided with a more moderate revaluation in the import currencies of some of Delek Automotive's competitors. Furthermore, in light of the fact that until Q4/2011, Delek Automotive sold older-model Ford Focus vehicles, initially introduced over six years ago, while competitors benefited from newer models. This undermined competitiveness and contributed to the reduction in Delek Automotive's market share.
- 2) In 2011, Delek Automotive posted a net profit of NIS 121 million, as compared to NIS 428 million last year. Net profits were down in the automotive segment mainly to the revaluation of the Japanese Yen during the year by 13.1%. This revaluation undermined competitiveness, and contributed to a decrease in vehicle sales, which totaled 32,844 vehicles, as compared to 42,711 vehicles sold in 2010.

In Q4/2011, Delek Automotive posted a net profit of NIS 48 million, as compared to NIS 115 million in the same quarter last year. Net profit was down for the quarter due to lower profit margins caused by the stronger Yen and the decrease in vehicle sales during the quarter, which totaled 7,089 vehicles as compared to 12,084 vehicles sold in the fourth quarter of

2010. Gross profit margin was down to 11.7% in 2011, as compared to 13.5% in the same period last year, mainly due to automotive operations as a result of increased vehicle costs following the revaluation of the Japanese Yen as aforesaid.

- 3) In the accounting year, Delek Automotive recorded net finance expenses of NIS 201 million, mainly incurred in the third quarter of the year following the revaluation of the Japanese Yen. Following this revaluation, Delek Automotive recorded expenses of NIS 76 million on the revaluation of interim trade payable balances, and expenses of NIS 80million on the revaluation of interim bank loans. Furthermore, a NIS 41 million impairment was recorded on the investment in Ford Motor Company shares. Interest payments to banks totaled NIS 16 million. Finance income offsetting these expenses was due to recognition of the results and fair value of hedging transactions to the amount of NIS 9 million, and interest income on trade receivables balances of NIS 4 million.

For more information about Delek Automotive's operations, see Note 14 to the financial statements and Section 1.14 in Part A of the periodic report - Description of the Corporation's Business.

H. Additional Operations

1) Infrastructures

The Group operates in infrastructures through its wholly-owned subsidiary Delek Infrastructures Ltd., which holds 50% of IDE Technologies Ltd. ("IDE") and coordinates the development and operation of power stations in Israel and Brazil through subsidiaries. The contribution of the infrastructures segment to the Group's net profit in 2011, amounted to NIS 59 million, mainly stemming from profits recorded by IDE and the power station in Ashkelon. In the past few months, the Knesset Economic Affairs Committee requested that the relevant regulatory authorities submit their professional positions regarding the implications for the Israeli electricity market of private electricity generation by gas suppliers. If and to the extent that a legislative initiative be instituted to restrict private electricity generation by gas suppliers in Israel, such a development would negatively affect Delek Infrastructures.

2) Biochemicals

Gadot is a manufacturer of food supplements and chemicals for the food, health supplements, detergents and toiletries industries, in which the Group holds a 76.4% interest as of the balance sheet date.

Gadot manufactures crystalline fructose, citric acid, citric acid salts, phosphoric acid salts, and specialty citric-acid-based salts. Most of Gadot's sales are in European and North American markets, and its customers include some of the world's leading multinational companies in the food and detergent industries.

The biochemicals segment's contribution to the Group's net profit in the reporting period amounted to a loss of NIS 280 million, compared with a loss of NIS 40 million in the same period last year.

As of December 31, 2011, Gadot has a working capital deficit of USD 45.7 million, due mainly to long- and short-term liabilities undertaken to finance long-term investments (inter alia, in connection with the construction of Gadot's facility in China), which are due for repayment in the coming year. Furthermore, in 2011, Gadot recorded operating losses of USD 92 million (in 2010 - USD 7 million). These losses are due mainly to increased raw material prices, accrued losses in Gadot's facility in China, and a provision of USD 76 million for impairment of property, plant and equipment in the subsidiary in China and in the fructose segment in Israel (see also Note 17 to the financial statements). Losses in 2011 amounted to USD 103 million (in 2010 - USD 17 million), due mainly to the above factors, and a provision for the impairment of an investment in an associate. In addition, in 2011, Gadot recorded negative operating cash flows of USD 11 million (in 2010 - USD 13 million).

The Gadot group is considering a number of financing options, including pledges of support from Gadot's controlling shareholders, as detailed below. In addition, Gadot's management believes that it can dispose of assets if necessary. It is further noted, that according to Gadot's forecasts, starting 2012 the Gadot companies will once more yield positive cash flows from continuing operations. It is noted that the realization of Gadot's plan is not certain, as it is not under Gadot's full control, and depends, inter alia, on the willingness and ability of third parties to make investments and extend credit. However, Gadot's management estimates that Gadot will be able to meet its liabilities.

In this respect, it is noted that as of the financial statements' approval date, the balance of loans extended by Delek Investments and Properties Ltd. ("Delek Investments") to Gadot amounts to USD 47 million. It is further noted, that in addition to the extension of the loans, Delek Investments informed Gadot that if it is short on funding required to meet its liabilities, Delek Investments will assist Gadot in securing financing to an amount not to exceed USD 42 million.

For more information on additional operations, see Note 14 to the financial statements.

B. Market Risk Exposure and Management

1.

- A)** Company operations focus mainly on holding and managing shares in its subsidiaries. These are long-term investments and therefore these holdings are not hedged.

Risk management in subsidiary and associate companies is determined and carried out directly by the investees. Some of these companies are public companies and are listed on the stock exchange, and therefore proper disclosure of this subject is made in their financial statements.

- B)** The currency risk management officer in the Company is Mr. Ido Adar, MBA. In recent years, Mr. Adar has served as Company Treasurer, prior to which he served as head of the Treasury and Insurance Department in Delek Israel.

2. Description of market risks

- A)** As stated above, the Group is mainly a holdings and management company, and its principal exposure results from the market risks of its subsidiaries and associates ("Investees").

The principal risks in these companies are as follows:

- Changes in currency exchange rates

The Group and the investees have foreign-currency denominated loans, exposing the Group to changes in foreign currency exchange rates. Moreover, exchange rates are liable to affect the results of the Company's operations.

- Changes in interest rates

The Group and the investees have NIS-denominated loans at variable interest rates, and are consequently exposed to changes in the interest rates applied by Israeli banks. Some of the Group companies have taken out loans abroad, which are subject to variable interest rates as applied by overseas banks, which expose them to interest rate changes in those countries.

- Exposure to CPI increases

A considerable number of the Group's and the investee's long-term loans are denominated in NIS and linked to the Israeli CPI. The Group's management believes that in many cases, the Group's exposure to an increase in the Israeli CPI is a limited economic exposure, as it believes that the value of the Group's property, plant and equipment increases over time at least at the same rate as the CPI.

It is noted that some of the Group companies hedge against an increase in the Israeli CPI above a certain annual level.

- Economic slowdown and changes in the markets in which the Group operates

The Group has material operations in various countries around the world. Changes in those markets, especially economic slowdowns (including in Israel), is liable to adversely affect the operations of the Group and the investees.

- Capital market conditions

Changes in the prices of marketable securities held by the Group expose it to risks stemming, inter alia, from capital market volatility. A slump in capital markets in Israel and abroad could adversely affect the Group's ability to find sources of financing where necessary, as well as its ability to generate capital gains from the disposal of its investments. Likewise, a slump in capital markets could impede the ability of the Group and the investees to raise capital, and lead to a possible fall in the prices of the investees' securities following their issue on the various securities exchanges.

- B)** The Group is exposed to changes in the prices of raw materials, other prices and other economic indices that can materially affect the Group's assets and liabilities, including trade payables, trade receivables in Group companies, the value of their inventories, and other assets and liabilities.

- C) Currently, several countries in the Eurozone are experiencing a financial crisis. In light of this crisis, 2011 saw the downgrading of international credit ratings for several key countries in the Eurozone, including France, Spain, Italy, Ireland, Greece, Portugal, Belgium, Cyprus, and Slovenia. The credit rating for some of these countries was downgraded by more than one international rating agency. Furthermore, more and more international investment houses and analysts estimate that the European economy may be facing a recession, and that economic conditions in the Eurozone may continue to deteriorate, to the point that the Eurozone itself is disbanded. As of the reporting date, the Company did not recognize any material effects of this crisis on its financial position, the results of its operations, its liquidity, or its financial integrity.

3. Market risk management policies

- Overseas investees customarily finance their investments in each country in the investment currency of that country. The income of investees from income-generating assets which are intended to finance principal and interest payments, are in the local currency, as are all of their other assets, and therefore the investees are not economically exposed to changes in foreign currency exchange rates.
- In order to adjust for interest risks on loans taken by the investees for the purchase of their assets, the companies have set a policy whereby most of the loans that they raise outside of Israel are long-term fixed-interest loans.
- The Company and the investees customarily use, from time to time, currency options and other derivatives. These transactions are made with large financial corporations in Israel and overseas, for hedging and other purposes.

4. Supervision and implementation of market risk management policies

- The investees manage their market risks under the supervision of their boards of directors or through special board committees. The Group also receives assistance from external advisors with expertise in these markets.
- Risk management issues are also monitored through internal controls implemented by the Group and the investees.
- The Group's companies are required to provide full reports on the scope and type of their exposure, and the hedging methods that they employ or do not employ in connection with these exposures.

5. Sensitivity tests for changes in market factors

In accordance with the 2007 amendment to the Second Addendum to the Securities Regulations (Periodic and Immediate Reports), 1970, the Group tested sensitivity to changes in risk factors that influence the fair value of "sensitive instruments".

Sensitivity to foreign currency risks was tested for positions exposed to changes in the various exchange rates against the functional currency used by the Group companies. For example, for foreign currency positions in companies whose functional currency is the euro, the tests were for sensitive instruments that are exposed to the exchange rate of other foreign currencies against the euro.

Financial position statement items, such as CPI-linked loans and debentures were not included in the table detailing sensitivity to CPI fluctuations, as their fair value is subject to unpredictable changes in inflation expectations, reflected in changes in the linked NIS curve.

Sensitivity of financial instruments in the course of general business:

Description of parameters, assumptions and models

- a) The fair value of marketable securities is their market value.
- b) The fair value of loans and debentures was calculated by discounting future cash flows using an interest rate reflecting the financing costs of the Group and its subsidiaries as of the reporting date.

- c) The fair value of options and fair value changes in sensitivity testing were calculated according to the Black&Scholes model, using spot prices, standard deviations, and interest rates as specified in the tables below.
- d) The fair value of future contracts and changes in fair value in sensitivity testing were calculated by discounting each of the two "legs" of the transaction, while using spot prices and interest rates as specified in the tables below.
- e) Testing of sensitivity to changes in the interest rates on fixed-rate loans and debentures was carried out according to duration.
- f) Variable-rate loans and debentures were not included in the testing of sensitivity to interest rate changes, as the effects of interest rate changes on their fair value is negligible.
- g) Parameters:

Parameter	Source/treatment
NIS/Foreign currency exchange rate	Representative rates
Foreign/Foreign currency exchange rate	Calculated from representative rates
Interest rates	According to the risk-free interest rate curve
Standard deviations	Flat curve (ATM)

- h) Daily changes of more than 10% in the relevant risks:

Risk	Max. change	Date	Comments
Interest rates	%20	Assumption	Or two percentage points (200 base points), the higher of the two
Share prices	%20	Assumption	
Sugar prices	%15	Assumption	
Oil/fuel/gas prices	%25	Assumption	

- i) Derivative instruments in the Group's companies are used as hedges and are not recognized, unless stated otherwise.

Summary table (NIS millions)

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	(*)	%10	%5		-%5	-%10	(*)
USD/NIS		(19)	(10)	(487)	9	17	
EUR/NIS		0	0	4	(0)	(0)	
AUD/NIS		1	1	12	(1)	(1)	
USD/CNY		8	4	(86)	(5)	(10)	
CPI		7	4	(7,926)	(4)	(7)	
Nominal NIS-based interest rate	252	105	53	(3,265)	(53)	(105)	(253)
Real NIS-based interest rate	589	196	98	(7,273)	(98)	(196)	(589)
USD interest rate	(108)	(25)	(12)	1,526	13	25	118
EUR interest rate	39	4	2	(123)	(2)	(4)	(42)
GBP interest rate	104	49	25	(848)	(25)	(49)	(104)
Sugar prices	8	5	3	(3)	(3)	(5)	(8)
Oil and fuel prices	533	267	133	2,600	(133)	(267)	(533)
Share prices	87	43	22	435	(22)	(43)	(87)

- (*) See Section (h) above.

Sensitivity tests to changes in the CPI (NIS millions)

Sensitive instrument	Profit/(loss) from changes		Fair value	Profit/(loss) from changes	
	0.2%	0.1%		-0.1%	-0.2%
Other receivables	0	0	140	(0)	(0)
Credit from banks	20	10	(761)	(10)	(20)
Other payables	(0)	(0)	(80)	0	0
Debentures	(14)	(7)	(7,220)	7	14
Future contracts on CPI	2	1	(4)	(1)	(2)
Total	7	4	(7,926)	(4)	(7)

Sensitivity tests to changes in foreign currency/NIS exchange rates (NIS millions)**a. Sensitivity tests for changes in USD/NIS exchange rates**

Sensitive instrument	Profit/(loss) from changes		Fair value	Profit/(loss) from changes	
	10%	5%		-5%	-10%
	4.203	4.012		3.630	3.439
Cash	24	12	249	(12)	(24)
Trade and other receivables	11	5	393	(5)	(10)
Securities	11	6	110	(6)	(11)
Trade and other payables	(37)	(19)	(35)	19	37
Deposits	0	0	3	(0)	(0)
Credit from banks	(56)	(28)	(568)	28	56
Debentures	6	3	(167)	(4)	(8)
Liabilities to suppliers and other creditors	(48)	(24)	(479)	24	48
NIS/USD future contracts	70	35	7	(35)	(70)
Total	(19)	(10)	(487)	9	17

b. Sensitivity tests for changes in EUR/NIS exchange rates

Sensitive instrument	Profit/(loss) from changes		Fair value	Profit/(loss) from changes	
	10%	5%		-5%	-10%
	5.432	5.185		4.691	4.444
Cash	0	0	1	(0)	(0)
Trade receivables	0	0	4	(0)	(0)
Trade payables	0	0	1	(0)	(0)
Liabilities to suppliers and other creditors	(0)	(0)	(2)	0	0
Total	0	0	4	(0)	(0)

c. Sensitivity tests for changes in AUD/NIS exchange rates

Sensitive instrument	Profit/(loss) from changes		Fair value	Profit/(loss) from changes	
	10%	5%		-5%	-10%
	3.972	3.792		3.431	3.250
Shares abroad	1	1	12	(1)	(1)
Total	1	1	12	(1)	(1)

Sensitivity tests for changes in foreign/foreign currency exchange rates (NIS millions)**a. Sensitivity tests for changes in EUR/USD exchange rates**

Sensitive instrument	Profit/(loss) from changes		Fair value	Profit/(loss) from changes	
	10%	5%		-5%	-10%
	1.422	1.357		1.228	1.163
Cash	(3)	(2)	34	2	3
Trade and other receivables	(0)	(0)	14	0	0
Trade and other payables	12	6	(123)	(6)	(12)
EUR/USD future contracts	(8)	(4)	1	4	8
Total	0	0	(75)	(0)	(1)

b. Sensitivity tests for changes in the USD/CNY exchange rates

Sensitive instrument	Profit/(loss) from changes		Fair value	Profit/(loss) from changes	
	10%	5%		-5%	-10%
	6.931	6.616		5.986	5.671
Cash	(0)	(0)	3	0	0
Limited deposits	(0)	(0)	0	0	0
Other receivables	(0)	(0)	5	0	1
Short-term loans	7	4	(76)	(4)	(8)
Trade and other payables	2	1	(18)	(1)	(2)
Total	8	4	(86)	(5)	(10)

Sensitivity tests for changes in interest rates (NIS millions)**a. Sensitivity tests for changes in nominal NIS-based interest rate**

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	(*)	10%	5%		-5%	-10%	(*)
Government bonds	(7)	(1)	(1)	105	1	1	7
Corporate bonds	(1)	(0)	(0)	7	0	0	1
Debentures	226	99	50	(3,030)	(50)	(99)	(226)
Credit from banks	19	7	3	(417)	(3)	(7)	(19)
Trade and other receivables	(3)	(1)	(1)	67	1	1	3
CPI futures contracts	15	2	1	(4)	(1)	(2)	(16)
NIS/USD futures contracts	1	0	0	7	(0)	(0)	(1)
Total	252	105	53	(3,265)	(53)	(105)	(253)

(*) See Section (h) above.

b. Sensitivity tests for changes in real NIS-based interest rates

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	(*)	10%	5%		-5%	-10%	(*)
Loans to customers	(4)	(1)	(1)	72	1	1	4
Government bonds	(3)	(0)	(0)	102	0	0	3
Corporate bonds	(9)	(3)	(1)	106	1	3	9
Loans to associates	(4)	(1)	(1)	26	1	1	4
Credit from banks	28	6	3	(361)	(3)	(6)	(28)
Debentures	595	195	98	(7,220)	(98)	(195)	(595)
CPI futures contracts	(15)	(0)	(0)	(4)	0	0	16
Total	589	196	98	(5,084)	(98)	(196)	(588)

(*) See Section (h) above.

c. Sensitivity tests for changes in USD-based interest rates

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	(*)	10%	5%		-5%	-10%	(*)
Loans to customers	(1)	(0)	(0)	13	0	0	1
Debentures	(170)	(34)	(17)	1,903	17	34	180
Issued debentures	2	1	0	(49)	(0)	(1)	(2)
Credit from banks	20	5	3	(332)	(3)	(5)	(20)
NIS/USD futures contracts	(1)	(0)	(0)	7	0	0	1
EUR/USD futures contracts	(0)	(0)	(0)	1	0	0	0
IRS transactions	43	3	2	(16)	(2)	(3)	(43)
Total	(108)	(25)	(12)	1,526	13	25	118

(*) See Section (h) above.

d. Sensitivity tests for changes in EUR-based interest rates

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	(*)	10%	5%		-5%	-10%	(*)
EUR/USD futures contracts	0	0	0	1	(0)	(0)	(0)
IRS transactions	39	4	2	(124)	(2)	(4)	(42)
Total	39	4	2	(123)	(2)	(4)	(42)

(*) See Section (h) above.

e. Sensitivity tests for changes in GBP-based interest rates

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	(*)	10%	5%		-5%	-10%	(*)
Loans	104	49	25	(848)	(25)	(49)	(104)
Total	104	49	25	(848)	(25)	(49)	(104)

(*) See Section (h) above.

Sensitivity tests for changes in commodity prices (NIS millions)**a. Sensitivity tests for changes in the price of sugar**

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	15%	10%	5%		-5%	-10%	-15%
Futures contracts on sugar	8	5	3	(3)	(3)	(5)	(8)
Total	8	5	3	(3)	(3)	(5)	(8)

b. Sensitivity tests for changes in the price of oil

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	25%	10%	5%		-5%	-10%	-25%
Fuel inventory	518	259	130	2,591	(130)	(259)	(518)
Contracts on fuel	15	7	4	8	(4)	(7)	(15)
Total	533	267	133	2,600	(133)	(267)	(533)

Sensitivity tests for changes in share prices (NIS millions)

Sensitive instrument	Profit/(loss) from changes			Fair value	Profit/(loss) from changes		
	20%	10%	5%		-5%	-10%	-20%
Shares in Israel	66	33	16	328	(16)	(33)	(66)
Shares overseas	21	11	5	107	(5)	(11)	(21)
Total	87	43	22	435	(22)	(43)	(87)

6. Market risks in headquarters companies

As noted in Chapter 5A above, the Company and its fully-owned headquarters companies hold cash and short-term investments (including investments in available for sale financial assets), which as of December 31, 2011, amounted to NIS 1,078 million. The following table details the composition of the Company's portfolio as of December 31, 2011 (in NIS millions):

	Balance as of December 31, 2011
Cash and deposits	265
Foreign securities portfolio	68
Securities traded on the TASE	329
Corporate bonds (*)	162
Others (mainly government bonds)	254
Total	1,078

(*) Mainly marketable bonds on the TASE, mostly rated A or higher.

In 2011, the Group sold shares in Noble. The Group's pre-tax gains on such sales in 2011 amounted to NIS 397 million (2010 - NIS 38 million).

The following table details Israeli CPI data and exchange rates for the primary currencies used by the Group:

	EUR representative exchange rate	USD representative exchange rate	GBP representative exchange rate	Known CPI
As of	NIS	NIS	NIS	Points *)
December 31, 2011	4.938	3.821	5.892	115.97
December 31, 2010	4.738	3.549	5.493	113.09
December 31, 2009	5.442	3.775	6.111	110.57
Change during the year	%	%	%	%
December 31, 2011	—	7.7	7.3	2.5
December 31, 2010	(12.9)	(6.0)	(10.1)	2.3

*) 2006 = base index.

7. Linkage bases report for 2011 and 2010:

For information on the linkage bases report, see Note 28 to the financial statements.

C. Aspects of Corporate Governance

1. Community involvement and philanthropy by Group companies

The Company supports the community, primarily through the Delek Science, Education and Culture Foundation Ltd. ("the Delek Foundation"), which acts as the executive arm for the Group companies' community activities. The Delek Foundation's policy is to award scholarships to students at academic institutions and at secondary education institutions, and to make donations in the fields of education, culture, medicine and help for the needy.

The principle sources for Delek Foundation's income are donations by companies in the Delek Group and donations by the controlling shareholder.

In 2011, the Delek Foundation donated a total amount of NIS 10.380 million. Of this amount, NIS 3.299 million were donated in the form of scholarships to students at educational institutions throughout the country, and NIS 7.081 million were donated for various purposes, primarily in the fields of health, education, culture and help for the needy.

In 2009, the Company's Board of Directors decided to set up, as part of the Delek Foundation, an additional dedicated fund of NIS 18 million, to assist in the awarding of scholarships to soldiers in combat units.

These scholarships are awarded to discharged soldiers who are in Israel without their families, or who live in outlying areas or who are socio-economically underprivileged.

Each scholarship is for NIS 10,000 (a year) over the entire study period (3-4 years). In 2011, scholarships were awarded to 280 newly-released soldiers, in a total amount of NIS 2.8 million.

Each scholarship recipient is obligated to engage in some form of volunteer activity on behalf of the community.

2. Directors with accounting and financial expertise and independent directors

- A) The Company's Board of Directors has determined that there shall be a minimum of two directors having accounting and financial expertise.

The Company believes that since the holding company has a small board of directors (eight directors), and since these directors have extensive business experience (even those who do not meet the definition for 'accounting and financial expertise'), this minimum number enables the board of directors to fulfill its duties imposed by law and by the Company's constituent documents in all matters pertaining to examination of the Company's financial position and the drafting and approval of its financial statements.

- B) The following directors have accounting and financial expertise: Dr. Moshe Bareket, Mr. Yoseph Dauber (external director), Mr. Avi Harel, Prof. Ben-Zion Zilberfarb, and Mr. Moshe Amit. For information concerning their relevant experience and education, see Regulation 26 in Part D of the periodic report.

- C) Independent directors - In its articles, the Company has not adopted the "provision on the percentage of independent directors" as defined in Section 219(e) of the Companies Law.

3. Disclosure concerning the Company's internal auditor

A) The Company's internal auditor

- 1) Name of auditor: Michael Grinberg
- 2) Start of tenure: 1.1.2002
- 3) Qualifications:

The internal auditor meets the conditions set forth in Section 3(a) of the Internal Auditing Law. The internal auditor is qualified as follows: Certified Public Accountant, holds a BA in accounting and economics, a member of the Office of Internal Auditors in Israel and the Israel Institute of Internal Auditors, has considerable experience in the field of auditing (20 years in a variety of different internal auditing functions).

- 4) The internal auditor is in compliance with the provisions of Section 146(b) of the Companies Law, and Section 8 of the Internal Auditing Law.
- 5) Holdings in securities issued by the Company or an associate: The internal auditor holds 220 ordinary shares and 267 phantom options in the Delek Group Ltd.; 90 ordinary shares in Delek Energy Systems Ltd.; 5,099 participation units in the rights of the limited partner Delek Drilling Limite Partnership; and 30,098 participation units in the limited partner's rights in Avner Oil Exploration Limited Partnership. The Company believes that the above holdings do not affect the quality of the internal auditor's work.
- 6) Commercial ties: The internal auditor is a full-time employee of Delek Group Ltd.

The internal auditor also serves as internal auditor in Delek Energy Systems Ltd., Delek Drilling, Avner Oil Exploration, Delek Automotive Systems Ltd., and Delek Petroleum Ltd.

The internal auditor is considered a member of management and is regularly invited to participate in meetings of the Company's management, but does not take part in decision making.

The internal auditor is not a principal shareholder in the corporation, nor is he a relative of a principal shareholder in the corporation, nor is he the auditing accountant of any person acting on behalf of a principal shareholder in the corporation.
- 7) The internal auditor does not perform any other function in the corporation other than that of internal auditor. Furthermore, the internal auditor does not perform any function outside of the corporation which gives rise or which may give rise to a conflict of interests with his function as internal auditor. The Company believes that the internal auditor's service in the subsidiaries as aforesaid does not give rise to conflicts of interest with his position as internal auditor of the Company.

B) Method of appointment

The internal auditor's appointment was approved by the Company's Board of Directors on January 1, 2002, following the Audit Committee's recommendation.

The reasons for approving his appointment include his education, skills, and considerable experience in internal auditing.

C) Auditor's superior

The internal auditor reports directly to the chairman of the Delek Group.

D) Work plan

The corporation's internal audit department implements an annual work plan.

Considerations in determining the internal auditing work plan

The annual work plan is formulated, inter alia, based on the following: the risks underlying the Company's operations, previous experience, opportunities for streamlining and savings, regulation of Company operations, and review of the implementation of previous audit report recommendations.

The work plan is formulated, inter alia, in view of the risk survey carried out in October 2010.

The work plan includes certain regulatory issues which are re-examined each year.

The aforesaid auditing activities are carried out bearing in mind that the Group constitutes a holdings management company, and that its main subsidiaries employ separate internal auditors and maintain independent audit committees. The annual audit plan is proposed by the internal auditor. Special emphases are occasionally added by the CEO.

Transactions listed under Section 270 of the Companies Law, which were carried out in the reporting year, are examined by the internal auditor as part of his annual work plan. The internal auditor also examines other material transactions

as per the annual audit plan.

As the Company is a holdings management company, the audit plan is comprised to two main parts:

- 1) Audit of the Company's own operations (including, inter alia, compliance with procedures, cost controls, management of Company funds, reporting procedures, statutory compliance and control of decision implementation).

2) Ongoing monitoring of internal auditing in investees, as detailed below:

Persons involved in determining the work plan

The internal auditor, the CEO, the Board of Directors' Audit Committee.

Persons receiving and approving the work plan

The Board of Directors' Audit Committee.

Judgment in deviating from the work plan

Management, the Audit Committee, and the chairman of the Board of Directors can extend the scope of the plan, or order specific changes, upon the internal auditor's request or recommendation, or as instructed by the Committee.

E) Auditing of material investees

Internal auditing includes ongoing monitoring of adequate and proper internal auditing activities in all of the Group's investees.

All material investees employ internal auditors (as in-house employees or through outsourcing). Audit reports are discussed by the audit committees and/or by the boards of directors of these corporations, which include directors also serving as Company officers. The internal auditor reviews auditing activities in all investees, so as to verify that proper auditing is carried out in all investees.

As part of these activities, the auditor reviews audit reports issued in all the companies, or a summary of findings from these reports, annual and long-term audit plans, auditing budgets and a general review of auditing activities, in each of the Group's material investees.

In examining the plausibility of auditing activities in investees with an internal auditor function, the Company's internal auditor occasionally conducts discussions and general reviews aimed at verifying continuity of internal auditing activities in these corporations. The internal auditor is in direct contact with the internal auditors of these corporations.

F) Scope of employment

The corporation's internal auditor is a full-time employee and serves as internal auditor of the Company and some of the corporations that constitute material holdings of the Company, as follows:

Delek Energy Systems, Delek Drilling, Avner Oil and Gas, Delek Automotive Systems, Delek Petroleum.

In 2011, the annual number of hours worked by the internal auditor and other internal auditors employed on an outsourcing basis in the Company and in the Group companies in Israel and abroad, amounted to **44,400** work hours.

Hours invested in internal auditing activities:

Company	Work Hours	Comments
The Company	600 (*)	By the Group's internal auditor
Delek Automotive Systems	750	By the Group's internal auditor
Delek Energy Systems	200	By the Group's internal auditor
Delek Drilling	300	The Group's internal auditor (including 100 outsourced hours)
Avner Oil Exploration	300	The Group's internal auditor (including 100 outsourced hours)
The Phoenix	31,800	External auditors
Delek Israel	3,500	External auditor
Delek US	3,000	Internal audit department
Delek Europe	2,139	External auditor
Republic (US)	1,300	Company-employed internal auditor
IDE Technologies	280	External auditor
Gadot Biochemicals	238	External auditor

(*) Including ongoing review of internal auditing activities in all direct and indirect Company investees.

The Company's Board of Directors believes that the internal auditor's work plan and the number of work hours allocated for its implementation, meet the Company's needs. The Company can expand the scope of internal auditing activities if necessary.

G) The audit

In accordance with the internal auditor's declaration, audits are carried out in accordance with the internal auditing standards employed in Israel and around the world, and in accordance with internal audit professional guidelines, including the standards set forth by the Institute of Internal Auditors in Israel (IIA) and in the US (CIA), and in accordance with the Internal Auditing Law, 1992, and the Companies Law.

The Board of Directors is satisfied that the internal auditor has complied with all the aforesaid requirements.

H) Access to information

The internal auditor has full, unrestricted, continuous and direct access to the corporation's information systems, including financial data.

I) Internal audit report

Internal audit reports are submitted in writing, circulated, and discussed by the Company's Audit Committee. Furthermore, specific meetings and discussions are held by the audit committees of investees, concerning audit findings.

Audit reports have been submitted and discussed in the Company's Audit Committee on the following dates:

- Review of internal auditing activities in 2010 in Group investees:
 - submitted March 2011 and discussed by the Audit Committee in March 2011.
- Summary report for 2011: submitted on January 16, 2012, and discussed by the Audit Committee on February 20, 2012.
- Review of internal auditing activities in 2011 in Group investees: submitted February 2012.

Reports were submitted to the Chairman of the Board, to the CEO of the Company, and to the members of the Company's Audit Committee.

J) Board of Directors' assessment of the internal auditor's work

The Company's Board of Directors believes that the scope of internal auditing in 2011, the nature and continuity of these activities and the Company's internal auditor's work plan are reasonable, and achieve the purposes of the internal auditing function.

K) Remuneration

The internal auditor's employment terms are as follows:

- 1) Annual salary of NIS 877,000, and an annual bonus determined by the Company's CEO. In addition, the internal auditor has been granted phantom options.
- 2) The Board of Directors believes the internal auditor's remuneration does not affect or harm the exercise of his professional judgment.

4. Auditors' Fees

	For the year ended December 31							
	2011				2010			
	Audit and tax services		Other services		Audit and tax services		Other services	
	Hours	NIS '000	Hours	NIS '000	Hours	NIS '000	Hours	NIS '000
The Company and wholly owned HQ companies								
Kost Forer Gabbay and Kasierer	7,191	1,684	2,972	1,520	7,992	2,078	2,800	1,274
Other consolidated companies								
Gadot Biochemical Industries Ltd.								
Kost Forer Gabbay and Kasierer	2,690	529	370	72	2,500	568	-	-
Other auditors	572	295	496	262	2,602	997	132	117
Delek The Israel Fuel Corporation Ltd.								
Kost Forer Gabbay and Kasierer	10,867	1,665	377	223	9,826	1,458	1,400	350
Ziv Haft	1,139	228	-	-	1,474	182	-	-
The Phoenix Holdings Ltd.								
Mainly Kost Forer Gabbay and Kasierer and Pahan Kaneh and Co.	15,569	2,662	2,555	750	15,603	2,689	1,329	457
Kesselman & Kesselman	17,100	2,035	1,687	457	20,435	2,965	1,400	420
Delek Energy Systems Ltd.								
Mainly Ziv Haft	4,945	1,181	1,032	383	6,008	1,337	735	232
For Yan Tethys								
Ziv Haft, Alfaya & Alfaya	931	217	-	-	619	161	-	-
For Delek & Avner Yam Tethys Ltd.								
Ziv Haft & Kost Forer	21	12	-	-	57	38	-	-
Delek US								
Ernst & Young USA	8,202	9,781	1,016	1,242	6,297	5,359	-	-
Republic Group								
KPMG	6,000	2,501	120	81	5,700	2,426	100	68
Delek Europe								
Ernst & Young Netherland	7,527	4,673	-	-	5,079	2,990	16	20
Kost Forer Gabbay and Kasierer	550	94	55	30	275	70	-	-
Roadchef								
Ernst & Young England	4,132	2,438	287	235	-	-	-	-

5. Disclosure on the financial statements' approval process

The Company's Board of Directors is the corporate organ charged with overall supervision and approval of the financial statements. The Company's Board of Directors has appointed a committee for examining the financial statements. This committee is not the Audit Committee, and is separate from the Audit Committee, although the committees share the same members.

A) The committee and its members

The committee comprises 3 members as follows: Mr. Yoseph Dauber, committee chairman (external director); Prof. Ben-Zion Zilberfarb (external director); and Mr. Avi Harel. All three members have accounting and financial expertise. All committee members have submitted declarations detailing their skills, education, and experience, and based on these signed declarations, the Company has determined that they are able to read and understand financial statements. For more information on directors serving on the committee, see Chapter 4.

B) The financial statements approval process

- 1) The Financial Statements Examination Committee formulated its recommendations to the Company's Board of Directors in its meetings of March 20, 2012, March 22, 2012, and March 27, 2012 (this last meeting convened solely to review the full notes to the financial statements).
- 2) All committee members participated in the above meeting.
- 3) In addition to the committee members, the March 20, March 22 and March 27, 2012 meetings were attended by the Chairman of the Board, Mr. Gabi Last; CEO of the Company, Mr. Asaf Bartfeld; CFO of the Company, Mr. Barak Mashraki; the Company's comptrollers, Mr. Amit Kornhauser and Mrs. Tamar Rozenberg; the internal auditor, Mr. Michael Grinberg; the Company's legal counsel, Mrs. Liora Prat-Levin; external accountants; and other persons in the Company.
- 4) The committee examined the assessments and estimates used in the financial statements, internal control of financial reporting, the scope and propriety of disclosure made in the financial statements, adopted accounting policies and accounting methods applied on material matters in the Corporation, valuations, including underlying assumptions and estimates, which serve as the basis for data included in the financial statements. The committee's discussions were based on materials brought before the committee on these matters by the Company's management, and questions and answers discussed during the meeting including the external auditor's remarks on these issues.
- 5) The committee unanimously recommended that the Board of Directors approve the financial statements for 2011. The committee submitted its recommendations to the Company's Board of Directors in writing on March 22, 2012 (provided that no change be made following the additional meeting of March 27, 2012, and no such change was made)
- 6) The Board of Directors discussed the Financial Statements Examination Committee's recommendations and the financial statements in its meeting of March 29, 2012.
- 7) The Board of Directors believes that the Financial Statements Examination Committee's recommendations were submitted a reasonable amount of time prior to the Board of Director's meeting.
- 8) The Company's Board of Directors adopted the Financial Statements Examination Committee's recommendations, and on March 29, 2012, resolved to approve the Company's financial statements for 2011.

6. Classification of Non-Significant Transactions

On August 6, 2008, an amendment to the Securities Regulations (Periodic and Immediate Reports), 1970 ("the Reporting Regulations") came into effect. Under the amendment, some of the reporting requirements applicable to public companies were expanded, where they concern transactions with controlling shareholders or with another person in which the controlling shareholder has a personal interest ("Controlling Shareholder Transactions"), even for transactions which are not extraordinary transactions as defined in the Companies Law, but excluding transactions for which the latest financial statements have determined them to be non-significant, as provided in Section 64(3)(d)(1) of the Securities Regulations (Preparation of Annual Financial Statements), 1993.

On March 30, 2009, the Company's Board of Directors resolved to adopt, for the first time, guidelines and principles for classifying a transaction as a non-significant transaction, both as regards transactions with principal shareholders listed in the financial statements, and as regards controlling shareholder transactions. Following discussions with the Israel Securities Authority, on August 30, 2009, the Company's Board of Directors resolved to set forth stricter guidelines for classifying transactions as non-significant, as detailed below. These guidelines and principles were determined, inter alia, with attention to the nature of the Company as one of the largest holdings companies in Israel with very extensive operations, to the value of the Company's assets, the diversity of its operations, the nature of its transactions, and the extent of their cumulative effect on the Company's operations and the results thereof.

The Company's Board of Directors has determined that a transaction will be deemed non-significant if it meets all of the following conditions:

- A) Its value does not exceed 0.1% of the Company's equity net of non-controlling interest, as stated in the Company's most recent annual financial statements.
- B) It does not constitute an extraordinary transaction (as defined in the Companies Law).
- C) The transaction is also qualitatively non-significant.
- D) In long-term transactions (e.g. - multi-year property leases), the non-significance of the transaction will be examined on an annual basis (for example - does the annual lease exceed the aforesaid amount).
- E) In insurance transactions, the premium will be examined as representing the transaction's value, as opposed to the scope of the insurance coverage provided.
- F) Each transaction will be examined individually, but the non-significance of related or contingent transactions will be examined in aggregate.
- G) Where a question arises concerning the application of the above criteria, the Company will exercise judgment and will examine non-significance based on the aim of the reporting regulations and guidelines above.

7. Remuneration of principal shareholders and senior officers

As required by the Regulations, in its meeting of March 29, 2011, the Company's Board of Directors examined the terms of employment and remuneration for those officers listed in Chapter 4 of the periodic report - as required by Regulation 21 ("Regulation 21").

For this examination, the Board of Directors received, ahead of time, relevant data concerning the employment terms of all of the officers. The Board was also presented with comparative data prepared by Kesselman Finance (PWC Israel) regarding the officers receiving remuneration from the Company, regarding the remuneration of holders of similar positions in companies with similar enterprise market values.

The Company's Board of Directors examined the remuneration of each of the officers receiving remuneration from the Company, determined the information and criteria for examination, and based on these data - the connection between the amount of the remuneration and the actions and contributions to the Company made by each of the officers during the reporting period. The Board of Directors believes that the remuneration of each of the officers receiving remuneration from the Company, detailed in Regulation 21 of Chapter 4 to the periodic report, reflects those officers' contribution to the Group, and is fair and reasonable as detailed below.

The remuneration of the other officers listed under Regulation 21, serving as officers in public companies under the Company's control, is reviewed and approved by the independent organs of those public companies paying such remuneration, and is reviewed by the Company as detailed below.

A) Company officers

Mr. Gabriel Last

Mr. Gabriel Last has been serving as Chairman of the Company's Board of Directors since 2003. Mr. Last also serves as a director in various Group companies, including Delek Israel, Delek Energy, Delek Infrastructure, Delek US, Delek Europe, and others. For details concerning the terms of Mr. Last's employment, see Regulation 21 in the periodic report.

As part of the examination of Mr. Last's remuneration in 2011, the Board of Directors examined the terms of his employment, the historic background for the remuneration, Mr. Last's functions and

responsibilities, his contribution to the Company and its results in the reporting year, his status, experience and relevant skills, and the terms given to holders of similar positions in companies with a similar enterprise market value. Based on the information and criteria below, prescribed by the Board of Directors, the Board of Directors has determined as follows:

As chairman of the Group, Mr. Last is responsible for the Board of Directors' activities and the Group's strategy. Mr. Last possesses extensive managerial knowhow and experience, and has created an effective work environment together with the Group's executives, and through the operations of the Board and its committees. This is also true of the board of the Company's subsidiaries in which Mr. Last serves as a director and acts to promote and develop the Company and its major investees.

The terms of Mr. Last's employment were determined several years ago and match his position and status. The remuneration mechanism consists of a fixed, reasonable base salary, plus an annual bonus determined by the Company. Mr. Last was granted warrants for his services as an executive chairman on Delek Energy's board of directors until February 2010, and warrants for his services as a director in Delek US. However, except for these allotments, he does not receive additional remuneration from those companies in which he serves as director.

Based on all the aforesaid, considering the remuneration mechanisms for holders of similar positions, Mr. Last's contribution to the Company and to the Group's subsidiaries in the reporting year and the results of these companies' operations, the Board of Directors believes his remuneration to be fair and reasonable.

Mr. Last's bonus for 2011 has yet to be discussed and approved.

Mr. Asaf Bartfeld

Mr. Asaf Bartfeld has been serving as CEO of the Company since 2003. In addition, Mr. Bartfeld serves as a director in various Group companies, including Delek Energy, Cohen Development, and Delek Petroleum. Mr. Bartfeld also serves as a director in various Group companies, including Delek Energy, The Phoenix, Delek Israel, Delek Europe, Republic, Cohen Development, and others.

For details concerning the terms of the CEO's employment, see Regulation 21 in the periodic report.

As part of the examination of Mr. Bartfeld's remuneration in 2011, the Board of Directors examined the terms of his employment, the historic background for the remuneration, Mr. Bartfeld's functions and responsibilities, his contribution to the Company and its results in the reporting year, his status, experience and relevant skills, and the terms given to holders of similar positions in companies with a similar enterprise market value. Based on the information and criteria below, prescribed by the Board of Directors, the Board of Directors has determined as follows:

As CEO of the Group, Mr. Bartfeld is party to determining the Group's strategy and is charged with its implementation and with the daily management of the Company's operations. Mr. Bartfeld is involved in all aspects of the Company's operation and serves as a director in all material investees. Mr. Bartfeld has extensive professional and managerial experience and carries out his duties with remarkable success and devotion to promoting and developing the Group's business. Furthermore, Mr. Bartfeld's position entails great personal responsibility. Mr. Bartfeld has led the Group to profitability and has established the Group as a leading holdings company, while generating value for the Group's shareholders. Mr. Bartfeld's contribution to the Company in the reporting period was very significant, including in the following matters: acquisition of control in Roadchef, recruitment of long-duration debt, and acquisition of control in Cohen Development. It is noted, that Mr. Bartfeld does not receive additional remuneration for his services as a director in the Group's subsidiaries, except for options in Delek US.

Based on all the aforesaid, considering the remuneration mechanisms for holders of similar positions, the Board of Directors' satisfaction with the CEO's performance, and considering the complicated nature of his position, his skills, experience, and responsibility, and bearing in mind the scope of the Group's operations, his contributions to the Company and its subsidiaries in 2011, the Group's results, and the various considerations detailed above, the Board of Directors believes Mr. Bartfeld's remuneration to be fair and reasonable.

Mr. Bartfeld's bonus for 2011 has yet to be discussed and approved.

Mr. Barak Mashraki

Mr. Barak Mashraki has been serving as CFO of the Company since January 1, 2008, and was appointed as Senior VP in 2011. Mr. Mashraki also serves as a director in the Group's subsidiaries.

For details concerning the terms of Mr. Mashraki's employment, see Regulation 21 in the periodic report.

As part of the examination of Mr. Mashraki's remuneration in 2011, the Board of Directors examined the terms of his employment, the historic background for the remuneration, Mr. Bartfeld's functions and responsibilities, his contribution to the Company and its results in the reporting year, his status, experience and relevant skills, and the terms given to holders of similar positions in companies operating in similar fields. Based on the information and criteria below, prescribed by the Board of Directors, the Board of Directors has determined as follows:

Mr. Mashraki is extremely well versed in the Company's affairs, and particularly as regards accounting and financial aspects of its operations. The Board of Directors discussed Mr. Mashraki's significant contribution to the Group's financial reporting activities, accounting and taxation issues, the Group's financing and capital raising activities, his contribution to investor relation activities and the management of the Group's market risks.

The terms of Mr. Mashraki's employment match his position and responsibilities. His remuneration consists of a fixed, reasonable base salary, an annual bonus determined by the Board of Directors, and a phantom bonus. The remuneration mechanism, and namely the phantom options, increases identification with the Company, its goals and commercial success, connects the remunerated officer directly with the Company's performance, results and financial position, and requires consistent achievement, growth and streamlining.

Based on all the aforesaid, considering the remuneration mechanisms for holders of similar positions, the Board of Directors' satisfaction with Mr. Mashraki's contribution to the Group in the reporting year, and particularly his contribution to the finalization of transactions such as the acquisition of control in Cohen Developments and capital raising activities through expansion of debenture series, recycling of loans and raising new financing and debentures by expansion of series, and the various considerations detailed above, the Board of Directors believes his remuneration to be fair and reasonable.

Mr. Mashraki's bonus for 2011 has yet to be discussed and approved.

It is noted that, in addition to their base salaries, Mr. Last, Mr. Bartfeld and Mr. Mashraki's remuneration also includes loans for purchasing securities issued by Group companies, phantom options (in the case of Mr. Bartfeld and Mr. Mashraki), and an option for annual bonuses, as determined by the competent corporate organs. The latter is usually granted after examining the Company's results in the previous reporting year and the officer's contribution to these results. The Board of Directors believes the above remuneration structure to create a proper balance between fixed remuneration and performance-based remuneration - which is based both on the prices of the subsidiaries' securities over the years (which are the major factor determining the Company's value), and based on an annual review by the competent corporate organs of the officers' achievements and contributions. The remuneration structure also properly balances monetary remuneration (which influences Company cash flows) and securities-based remuneration.

B) Officers in subsidiary companies

1) In private subsidiaries

The Board of Directors examined the remuneration paid to Mr. Zion Ginat, who ended his tenure with the subsidiary Delek Benelux in the reporting period, and has determined the terms of his employment to have been fair and reasonable considering his contribution to developing and promoting Delek Benelux's operations, his contribution to completion of the acquisition of BP's fuel operations in France, and considering the remuneration structure for persons holding similar office.

The equity-based remuneration (options to shares in Delek Benelux accounting for 2.5% of its capital) was granted Mr. Zion Ginat under the terms of his employment upon the start of his tenure, which remuneration was aimed at increasing his identification with Delek Benelux, its goals and commercial success. The terms of Mr. Zion Ginat's employment, including the equity-based remuneration, were approved by the board of directors of Delek Europe (a foreign subsidiary incorporated in the Netherlands) which includes 3 independent directors. The Board of Directors believes, in light of the above reasons and considering the remuneration structure for persons holding similar office, the equity-based remuneration granted as aforesaid in Mr. Ginat's employment agreement, i.e. - options to shares amounting to 2.5% of Delek Benelux's capital, was fair and reasonable. It is noted and emphasized that the payment made to Mr. Zion Ginat following the exercise of the put option on his vested options (2.5% of Delek Benelux's capital) upon termination of his employment, was based on an independent valuation carried out by Deloitte Belgium and PWC Israel which determined Delek Benelux's value upon termination of Mr. Ginat's employment, and all as prescribed in Mr. Ginat's options agreement.

2) In listed public companies:

Information concerning remuneration of officers in Delek Energy Systems Ltd., The Phoenix Holdings Ltd., and Delek USA (jointly - "the Subsidiaries") - Mr. Eyal Lapidot, Mr. Gideon Tadmor, Mr. Uzi Yemin and Mr. Yitzhak Oz. The above officers receive remuneration as detailed in Regulation 21 from public companies controlled by the Company, whose shares are traded on the TASE or NYSE. Their remuneration is reviewed and approved by the independent organs of these subsidiaries.

The remuneration of each of the above officers was presented to the Board of Directors by the CEO of the Company, Mr. Asaf Bartfeld, who also serves as a director in the subsidiaries which reviewed the relevant remuneration. This presentation was accompanied by documents submitted to the boards of the subsidiaries, detailing the information and criteria used by the board of directors of each of the subsidiaries to determine the reasonability of the remuneration for each of the officers in the subsidiaries in the reporting period. These documents further detailed that each of the above officers meets the requirements of his office, based on which the subsidiary's board of directors determined whether the terms and the remuneration are fair and reasonable. These documents also included a review of the remuneration given to holders of similar offices. This review was followed by a presentation of the report issued by the subsidiaries' boards of directors (in the case of Delek USA - Schedule 14A was presented), and the details included in that report on each officer. After reviewing the processes implemented in each of the subsidiaries, the Company's Board of Directors believes that these subsidiaries' examination of the reasonability and fairness of the remuneration was adequate.

C) Other Company directors (excluding the Chairman and external directors)

The remuneration paid to the other directors is determined in accordance with the Companies Regulations (Rules Regarding Remuneration and Expenses of External Directors), to the maximum amount prescribed in the remuneration regulations for annual remuneration and per-meeting remuneration. This does not include Mr. Moshe Amit, who receives the fixed amount and not the maximum amount, and the remuneration is paid to the subsidiary Delek Israel, and Mr. Elad Sharon (Tshuva), the son of the controlling shareholder who serves as deputy executive chairman and is also entitled, in addition to the maximum remuneration, to reimbursement of 60% of his office rental and secretary expenses, car and telephone expenses, and to reimbursement for expenses incurred through work-related travel and accommodations abroad. Elad Sharon notified the Company of his waiver of these reimbursements starting May 2011, and of his directors' remuneration starting March 2011.

The Board of Directors reviewed the remuneration paid to Mr. Elad Sharon (Tshuva), and determined it to be fair and reasonable.

Considering the directors' involvement in the Company's operations and the responsibilities attached to their positions, and considering the fact that the remuneration in the regulations, as aforesaid, is as customary and is fair and reasonable.

D. Disclosure relating to the Company's financial reporting

1. Critical accounting estimates

For information about main accounting estimates, see Note 2B to the financial statements.

2. Events after the income statement date

For details of material events after the income statement date, see Chapter A to the Board of Directors' Report.

E. Dedicated disclosure for debenture holders

Series	Issue date	Original par value	Par value balance as of Dec. 31, 2011	Stated interest rate	Linkage	Carrying amount as of Dec. 31, 2011	Interest accrued in the books	Repayment years	Stock exchange value as of Dec. 31, 2011	Material series	Trustee
		NIS millions	NIS millions			NIS millions	NIS millions				
א'	12/2005	166	28	4.85%	CPI	32	-	2012	Non-marketable	No	BLL Trust Company 8 Rothschild Blvd. Tel Aviv Tel.: 03-5170777 – Idit Prizar
א"א'	7/2006	468	357	5.40%	CPI	411	5	2018	Non-marketable	No	BLL Trust Company 8 Rothschild Blvd. Tel Aviv Tel.: 03-5170777 – Idit Prizar
ב'	11/2006	1,100	596	5.35%	CPI	691	8	2015-2017	Non-marketable	Yes	Reznick Trusts Ltd. 14 Yad Harutzim St. Tel Aviv Tel: 03-6393311 – Liat Bachar-Segal
ג'	3/2007	913	913	Until listing - 5.1% + after listing - 4.6%	CPI	1,073	13	2013-2014, 2019-2021	996	Yes	Hermetic Trust (9175) Ltd. 113 Hayarkon St. Tel Aviv Tel: 03-5274867 – Dan Avnon
ד'	7/2009+6/2010	419	419	8.5%	-	419	7	2018	421	No	Clal Finance Trusts 2007 Ltd. 37 Brhin Road Tel Aviv Tel" 03-6274827 – Yuval Likber
ה'	7/2009 7/2011+11/2009+11/2011	1,486	1,486	8.5%	-	1,486	26	2015-2017	1,529	Yes	Clal Finance Trusts 2007 Ltd. 37 Brhin Road Tel Aviv Tel" 03-6274827 – Yuval Likber
ו'	9/2009	260	260	5.5%	-	260	5	2012-2015	254	No	Strauss Lazar Trust Ltd. 17 Yitzchak Sadeh, Tel Aviv Tel: 03-6237777 – Uri Lazar
ז'	9/2009	90	90	Variable	-	90	-	2012-2015	84	No	Strauss Lazar Trust Ltd. 17 Yitzchak Sadeh, Tel Aviv Tel: 03-6237777 – Uri Lazar
ח'	11/2009+6/2010+7/2011	1,062	1,062	6.1%	CPI	1,120	12	2016-2022	1,070	Yes	Clal Finance Trusts 2007 Ltd. 37 Brhin Road, Tel Aviv Tel: 03-6274827 – Yuval Likber
ט'	11/2010	560	560	4.65%	CPI	576	4	2019-2022	463	Yes	Gafni Trusts Ltd. Hataas 4, Ramat Gan Tel: 03-6070370 – Tzuri Galili
י'	6/2007	500	500	4.50%	CPI	583	13	2012, 2019-2021	518	Yes	Aora Fidelity Trust Ltd. 12 Begin Rd., Ramat Gan Tel: 03-7510566 – Iris Shalbin
יא'	10/2007 +7/2009	1,293	970	4.75%	CPI	1,109	10	2011-2014	1,108	Yes	Strauss Lazar Trust Ltd. 17 Yitzchak Sadeh, Tel Aviv Tel: 03-6237777 – Uri Lazar
יב'	4/2010	255	255	4.1%	-	255	2	2012	254	No	Strauss Lazar Trust Ltd. 17 Yitzchak Sadeh, Tel Aviv Tel: 03-6237777 – Uri Lazar

Bonds (Series G and H) were repaid in full in the reporting period.

Notes:

- 1) The Company meets all the terms of the debentures. Furthermore, the Company meets all the terms of its obligations under the deed of trust.
- 2) Information regarding the debenture ratings:

Series	Rating company	Current rating	Rating upon issue	Rating company	Current rating	Rating upon issue
J	Midroog	A1	-	S&P Maalot	A	AA
K	Midroog	A1	-	S&P Maalot	A	AA
L	Midroog	A1	-	S&P Maalot	A	AA
M	Midroog	A1	-	S&P Maalot	A	AA
N	Midroog	A1	A1	S&P Maalot	-	-
O	Midroog	A1	A1	S&P Maalot	-	-
P	Midroog	A1	A1	S&P Maalot	-	-
Q	Midroog	A1	A1	S&P Maalot	-	-
R	Midroog	A1	A1	S&P Maalot	-	-
S	Midroog	A1	A1	S&P Maalot	-	-
V	Midroog	A1	-	S&P Maalot	A	AA
W	Midroog	A1	-	S&P Maalot	A	AA
AD	Midroog	A1	A1	S&P Maalot	-	-

Details of the Company's liability certificates:

In January 2011, S&P Maalot confirmed an A rating for S&P Maalot-rated debenture series and changed their rating outlook to negative.

In July 2011, Midroog confirmed an A1 rating for Midroog-rated debenture series and changed their rating outlook to negative. Furthermore, Midroog announced an A1 rating for an extension of existing series for raising a total of up to NIS 701 million.

In December 2011, S&P Maalot confirmed an A rating for S&P Maalot-rated debenture series and changed their rating outlook to stable.

For information on the Company's current rating reports, see Appendix B to the Board of Directors' Report.

F. Additional Information**1. Buyback of securities**

- A) On August 31, 2011, the Company's Board of Directors approved a debenture purchasing plan for up to NIS 100 million by the subsidiary Delek Investments and Properties Ltd., or a new company under full Company ownership. For more information, see the Company's immediate report of September 1, 2011 (ref. 2011-01-261747), quoted here by way of reference.
- B) On September 12, 2011, the Company's Board of Directors approved a share purchasing plan for up to NIS 40 million by the subsidiary Delek Investments and Properties Ltd., or a new company under full Company ownership. For more information, see the Company's immediate report of September 12, 2011 (ref. 2011-01-271635), quoted here by way of reference.

After publication of the aforesaid purchasing plan, the subsidiary Delek Investments purchased 18,354 shares in consideration for NIS 9.8 million.

2. Dividends

- A) In March 2011, the Company's Board of Directors resolved to distribute a dividend of NIS 200 million. The dividend was distributed in April 2011.
- B) In May 2011, the Company's Board of Directors resolved to distribute a dividend of NIS 105 million. The dividend was distributed in June 2011.
- C) In August 2011, the Company's Board of Directors resolved to distribute a dividend of NIS 100 million. The dividend was distributed in September 2011.
- D) In November 2011, the Company's Board of Directors resolved to distribute a dividend of NIS 100 million. The dividend was distributed in December 2011.
- E) Subsequent to the financial position statement date, in March 2012, the Company's Board of Directors resolved to distribute a dividend of NIS 120 million.

3. Company employees

The Board of Directors would like to thank the Company's management, the management of the Company's investees, and to all the employees for their dedicated work and their contribution to the advancement of the Company.

Sincerely

Gabriel Last
Chairman of the Board

Asi Bartfeld
CEO

Appendix A to the Board of Directors' Report

Breakdown of principal and interest payments on the debentures and bank loans of the headquarters companies as of December 31, 2011 (in NIS millions):

Delek Group - Headquarters

		2012	2013	2014	2015	2016	2017 onwards	Total
Debtentures	Principal	861	643	643	901	912	4,149	8,109
	Interest	472	431	401	373	310	662	2,649
Bank loans	Principal	20	20	20	20	10	230	320
	Interest	15	14	13	12	11	11	76
	Total	1,368	1,108	1,077	1,306	1,243	5,052	11,154

Delek Investments and Properties

		2012	2013	2014	2015	2016	2017 onwards	Total
Bank loans	Principal	38	24	2	-	46	-	110
	Interest	4	3	2	3	2	-	14
	Total	42	27	4	3	48		124

Delek Finance US

		2012	2013	2014	2015	2016	2017 onwards	Total
Bank loans	Principal	115	-	-	-	-	-	115
	Interest	4	-	-	-	-	-	4
	Total	119	-	-	-	-	-	119

Delek Petroleum

		2012	2013	2014	2015	2016	2017 onwards	Total
Debtentures (1)	Principal	-	120	90	59	29	-	298
	Interest	17	15	7	3	1	-	43
	Total	17	135	97	62	30	-	341

(1) The debtentures do not include debtentures raised in the past and given as a loan (BTB) to Delek Israel.

Appendix B to the Board of Directors' Report

The following is a current rating report issued by Standard & Poor's Maalot Ltd. for the Company's debentures.



Please note that this translation was made for the company's use only and under no circumstances obligates Standard & Poor's Maalot. In the case of any discrepancy with the official Hebrew version published on December 26, 2011, the Hebrew version shall apply.

12 Abba Hillel Silver St.
Ramat-Gan 52506
Israel
+972 3 7539700 Tel
+972 3 7539710 Fax

26 December, 2011

Delek Group

Delek Petroleum

'ilA' Ratings Affirmed; Outlook Revised To Stable

Primary Credit Analyst: Itzik Maissi, Tel Aviv, Itzik_maissi@standardandpoors.com

Secondary Credit Analyst: Yuval Torbati, Tel Aviv, yuval_torbati2@standardandpoors.com

Overview

- Delek Group's performance in 2011 exceeded our expectations following strong cash flow generation from increased gas sales and good refining margins in U.S.
- While we forecast weaker cash flow and higher capital expenditure in 2012, we estimate that cash generation will be significantly boosted in 2013 on higher gas sales.
- We are affirming our 'ilA' long-term corporate credit rating on energy and infrastructure conglomerate, Delek Group, and its fully owned subsidiary, Delek Petroleum, while revising the outlook to stable from negative.
- The stable outlook reflects our expectations that the group's performance will weaken in 2012 but rebound in 2013.

Rating Action

On Dec. 26, 2011, Standard & Poor's Maalot affirmed the 'ilA' ratings on Israel-based energy and infrastructure conglomerate, Delek Group Ltd., and its fully owned subsidiary, Delek Petroleum Ltd., and at the same time, we revised the outlook to stable from negative.

Rationale

The affirmation of the ratings on Delek Group and Delek Petroleum and the revision of the outlook to stable reflect the group's performance in 2011, which exceeded our expectations. The group generated strong cash flow from increased sales of natural gas, due to increases in both volume and sale prices, as well as from good refining margins in the U.S., which improved the group's consolidated credit measures. We anticipate that the group will likely see EBITDA increase in 2011 to new Israeli shekel (NIS) 3.4 billion (approximately \$900 million) from NIS1.3 billion in 2010. We also anticipate that full adjusted ratio of FFO (funds from operations) to debt will reach about 14% in 2011, up from 7% in 2010, and higher than our earlier estimate of 11%. In our base case scenario, though, we expect a double-digit decline in EBITDA in 2012, assuming a reduction in gas sales and weaker U.S. refining margins, while the fuel retail segment should stay

www.maalot.co.il



Please note that this translation was made for the company's use only and under no circumstances obligates Standard & Poor's Maalot. In the case of any discrepancy with the official Hebrew version published on December 26, 2011, the Hebrew version shall apply.

12 Abba Hillel Silver St.
Ramat-Gan 52506
Israel
+972 3 7539700 Tel
+972 3 7539710 Fax

relatively stable. We believe the contribution of the insurance and financial activities to the group's cash flow will continue to be low, although we do anticipate that the group will continue to receive dividends from Delek Automotive Systems and IDE Technologies. At the same time we expect an increase in capital expenditure (capex) spending to about NIS2 billion in 2012, mainly for continued development of the Tamar gas field and for investments in the refining segment. In our view, this combination of lower EBITDA and rise in investments will cause weaker credit measures in 2012 and a decline in FFO/debt to about 11%. However, we expect an increase in EBITDA starting 2013 once Tamar start producing, which will likely return credit measures to levels we consider as commensurate with the current rating, that is of FFO to debt of more than 12%. We also expect the group to divest from some of its noncore assets in the next two years, and to use most of the proceeds to pay off debt.

We continue to believe that the group will pursue with what we perceive as an aggressive financial policy, mainly through distributing dividends of 50% of net income, which derives, in our opinion, from the controlling shareholder's financing needs. In our forecast, we assume that the group will continue with its policy, but that dividend distribution from revaluation gains, or after asset disposal, will be limited.

The ratings on the group continue to reflect our assessment of: an increase in cash generation in 2013 as Tamar comes on line; other significant gas discoveries; the group's competitive positioning in fuel marketing in Europe and Israel; its holdings in insurance companies which are characterized by low risk; adequate business and geographic diversification; adequate financial flexibility provided by the listed nature of its main holdings; and management policy to sell assets and reduce debt. Mitigated factors include: the group's capital structure, which continues to be characterized by high leverage as a result of rapid business growth in recent years, financed mostly by debt; and a dividends policy which we regard as aggressive given the sources available.

Liquidity

We view the group liquidity as "less than adequate" according to our criteria. We examine the group liquidity at the level of the holding company and the fully-owned finance companies. We estimate the ratio between the sources and uses for the group in the next 12 months as 1.0x, and lower than 1.0x in 2013. This is based on the level of cash and our estimate of receipts, such as dividends or loan repayments from related parties. Our scenario does not include receipts in respect of asset realization or debt refinancing through uncommitted credit lines.

In our base case scenario we assume that the sources of Delek Group as of Sept. 30, 2011 include:

- Cash and short term financial assets (most of which we believe will be converted to cash by the end of 2011) of NIS1,829 million;
- Dividend income, management fees and interest income of NIS580 million till the end of 2013;
- Gas royalties and loans repayments from related parties of NIS470 million till the end of 2013;
- New bond issuance of NIS261 million, already received in November 2011.



Please note that this translation was made for the company's use only and under no circumstances obligates Standard & Poor's Maalot. In the case of any discrepancy with the official Hebrew version published on December 26, 2011, the Hebrew version shall apply.

12 Abba Hillel Silver St.
Ramat-Gan 52506
Israel
+972 3 7539700 Tel
+972 3 7539710 Fax

On the other hand we assume that the main uses of Delek Group as of Sept. 30, 2011 include:

- Interest expenses of NIS1,180 million till the end of 2013;
- Debt repayment of NIS2,650 million till the end of 2013;
- Investments in subsidiaries of NIS110 million (mainly in Gadot Biochemical Industries and Delek Infrastructure;
- General and administrative expenses of NIS70 million;
- Dividend declared of NIS100 million.

We note that the group has adequate financial flexibility provided by the listed nature of its assets, by the fact that most of its assets are free of any liens or financial covenants but could be pledged in order to receive additional funding, and by its ability to realize a considerable proportion of its holdings in subsidiaries without forgoing control.

We also consider the group's standing in the local capital markets and with local banks as a positive factor. However, we believe that the extension of the debt restructuring at sister company, Delek Real Estate (rated D), affects the group's ability to make a public bond issue. We anticipate that Delek Group will likely raise part of its debt repayments in 2013 in the coming quarters, and that the major shareholder will quickly reach an agreement on the debt arrangement at Delek Real Estate. We recognize that the company is part of a single borrowing group of companies controlled by Mr. Yitzhak Tshuva, and as such may be restricted in its access to Israeli banks.

Outlook

The stable outlook reflects our expectation that the group's performance will weaken in 2012 but rebound in 2013 once production begins at the Tamar gas field. We therefore anticipate that credit measures will likely be weaker in 2012 but will return to levels we consider commensurate with the current rating from 2013. This will include fully adjusted FFO to debt of at least 12%. We also expect the group to strengthen its liquidity over the next few quarters, and that the controlling shareholder will shortly reach a debt arrangement at Delek Real Estate, thereby increasing Delek Group's accessibility to raise public debt.

We could consider a negative rating action if the group fails to maintain the ratios that we consider commensurate with the current rating. This could happen if there are unforeseen delays in Tamar's development, lower sales than forecast, lower refining margins in the U.S. than we estimated, or shareholder friendly dividend distribution.

A positive rating action is less likely in the near term given the group's high capex needs and still high leverage. However, we would consider a positive rating action if Delek Group manages to reduce leverage faster than we estimate, bringing FFO to debt of at least 20% over time. In our view this scenario would require a very good refining market, the disposal of some non-core assets, with most of the proceeds being used to lower debt, and significantly lower dividend distribution than in recent years.

Rating Methodology

Given Delek's holding structure and management, we consider it a conglomerate that operates mostly in the energy and infrastructure fields. We therefore examine its risk profile by analyzing and assessing the company's consolidated

www.maalot.co.il



Please note that this translation was made for the company's use only and under no circumstances obligates Standard & Poor's Maalot. In the case of any discrepancy with the official Hebrew version published on December 26, 2011, the Hebrew version shall apply.

12 Abba Hillel Silver St.
Ramat-Gan 52506
Israel
+972 3 7539700 Tel
+972 3 7539710 Fax

business and financial risk, where the financial risk analysis is based on the company's adjusted consolidated financial statements excluding its insurance and financial activities, which includes debt at the level of Phoenix Holdings, full consolidation of the Avner Oil & Gas Exploration partnership, and various adjustments in respect of leases and employee pension liabilities. Debt coverage ratios at the holding company level are important as we analyze the company's ability to service debt raised at the holding company level, given that this debt is subordinate, both legally and structurally, to debt raised by the operating companies. We therefore examine the group's liquidity at the level of the holding company and the fully owned financial companies. The loan-to-value (LTV) ratio serves as a measure of the group's financial flexibility and its ability to realize part of its assets or to pledge assets in favor of new credit facilities. Delek Group's LTV, by our calculation—using market prices, a conservative assessment of non-tradable assets, including short-term investments and loans to interested parties as part of the portfolio, while not taking treasury shares and outstanding loans to Delek Real Estate into account—stood at 48% in mid-December 2011, up from about 40% at the start of the year.

Related Criteria And Research

- Methodology And Assumptions: Standard & Poor's Standardizes Liquidity Descriptors For Global Corporate Issuers, July 2, 2010
- Criteria Methodology: Business Risk/Financial Risk Matrix Expanded, May 27, 2009
- Criteria | Corporates | Rating Methodology For European Investment Holding And Operating Holding Companies, May 28, 2004

The above criteria can be found on Standard & Poor's website at www.standardandpoors.com

Ratings List

	To	From
Delek Group	ilA/Stable	ilA/Negative
Bond Series F	ilA	ilA
Bond Series G	ilA	ilA
Bond Series H	ilA	ilA
Bond Series I	ilA	ilA
Bond Series J	ilA	ilA
Bond Series K	ilA	ilA
Bond Series L	ilA	ilA
Bond Series M	ilA	ilA
Bond Series N	ilA	ilA
Bond Series O	ilA	ilA



Please note that this translation was made for the company's use only and under no circumstances obligates Standard & Poor's Maalot. In the case of any discrepancy with the official Hebrew version published on December 26, 2011, the Hebrew version shall apply.

12 Abba Hillel Silver St.
Ramat-Gan 52506
Israel
+972 3 7539700 Tel
+972 3 7539710 Fax

	To	From
Delek Petroleum	ilA/Stable	ilA/Negative
Bond Series A	ilA	ilA
Bond Series D	ilA	ilA
Bond Series E	ilA	ilA
Bond Series G	ilA	ilA
Bond Series H	ilA	ilA

Standard & Poor's Maalot ratings are based on information received from the Company and from other sources that Standard & Poor's Maalot believes to be reliable. Standard & Poor's Maalot does not audit the information it receives nor does it verify the correctness or completeness of such information.

It is hereby clarified that Standard & Poor's Maalot rating does not reflect risks relating to and/or arising from breaches, through intent or oversight, of any of the obligations included in the bond documents and/or the incorrectness or inaccuracy of any of the representations contained in the documents relating to the bond offering that is the subject of this rating, Standard & Poor's Maalot report or the facts that form the basis for the opinions expressed to Standard & Poor's Maalot as a condition for the giving of the rating, fraudulent or dishonest acts of commission or omission, or any other act that contravenes the law.

The ratings could be revised as a result of changes to the information received or for other reasons. The rating should not be perceived as expressing any opinion concerning the price of the securities on the primary or secondary market. The rating should not be perceived as expressing any opinion concerning the advisability of buying, selling or holding any security.

© Standard & Poor's Maalot reserves all rights. This summary is not to be copied, photographed, distributed or used for any commercial purpose without Standard & Poor's Maalot consent, except to provide a copy of the whole report (with an acknowledgement of its source) to potential investors in the bonds that are the subject of this rating report for the purpose of their reaching a decision concerning the acquisition of the aforesaid bonds.

Appendix C to the Board of Directors' Report

The Group attaches the following economic studies to its financial statements:

- A. Valuation of goodwill and intangible assets recognized on the purchase of shares in The Phoenix Holdings Ltd.
- B. Examination of the impairment of an investment in an associate company - Delek Automotive Systems Ltd.
- C. Examination of the recoverable amount of goodwill in Republic.

Jerusalem, March 26, 2012

To:
The Delek Group Ltd.
7 Giborei Israel, St.
Netanya

Dear Sirs,

Assessment of goodwill and other intangible assets recognized following the acquisition of Phoenix Holdings Ltd. shares by the Delek Group

1. General

In January 2012, I was asked by your CFO to apply IFRS in order to assess whether goodwill and other intangible assets recognized in the books of the Delek Group Ltd. ("the Delek Group") have declined in value following the acquisition of Phoenix Holdings Ltd. Shares ("the Phoenix" or "the Company"), as described in section 6 below.

In addition, I was asked to apply IFRS in order to assess any change in the "useful" life and amortization period of intangible assets (insurance portfolios) to which some of the excess purchase price has been allocated, as estimated in my previous opinion reports as regards the allocation of purchase price.

2. Details relating to my education and professional experience are presented in appendix A of this opinion report.
3. For the purpose of my work I have drawn on accounting standards, financial statements and data as follows:
 - 3.1. Phoenix audited financial statements for the year 2010 and for previous years.
 - 3.2. Phoenix reviewed financial statements for the interim period ending on September 30, 2011.
 - 3.3. A report on the embedded value (EV) of Phoenix, as of December 31, 2010 (as included in the Company's Q1 statements for 2011 ("the EV report").
 - 3.4. Additional information that I received from the Company's actuary, inter alia, for the purpose of assessing changes in the embedded value since December 31, 2010.
 - 3.5. Ernst & Young - *Embedded Value Results* as of December 31, 2010.
 - 3.6. Ernst & Young - *European Embedded Value Results 2010*.
 - 3.7. International Accounting Standard 36 : "Impairment of Assets" ("IAS 36") and International Accounting Standard 38 : "Intangible Assets" ("IAS 38")
 - 3.8. Previous opinion reports that I have presented on the impairment of goodwill, as of December 31, 2007; September 30, 2008; December 31, 2008; September 30, 2010; December 30, 2011.
 - 3.9. Y. Eden and Ben-Ami Zuckerman, "the riddle of the embedded value", *Banking Quarterly*, Vol. 163, February 2010, pp. 14-39. (in Hebrew).
 - 3.10. Y. Eden, "the embedded value and its creator", *The Accountant*, Vol. 23, October 2010, pp. 23-27. (in Hebrew).
 - 3.11. Analytical survey of the "Insurance Sector", conducted by Leader Capital Markets Ltd., dated December 14, 2011.
 - 3.12. A Phoenix presentation entitled "profit-focused growth", which was included in an immediate report issued by the Company on January 25, 2012.
 - 3.13. A Standard and Poor's announcement, dated January 12, 2012, regarding the upgrade of Phoenix Holdings Ltd. Issuer rating from ilA to ilA+.
 - 3.14. The Ministry of the Treasury's plan to increase competition in the pension savings market, as published in November, 2010 (the "Treasury Plan").

- 3.15. The Dai-Inchi Life Insurance Company, Ltd. Disclosure of European Embedded Value as of March 31, 2011.
- 3.16. An immediate report issued by IDE Ltd. on February 18, 2010. This report includes A Kesselman Finance Ltd. assessment of the value of IDE Insurance Co. Ltd.
- 3.17. The 2012 Financial Services (Provident Funds) (Management Fees) Regulations ("the Management Fee Regulations").
4. I have no knowledge of any information that may indicate the implausibility of the data I have drawn on. I did not consider the data independently, and thus this opinion does not validate the verity, integrity or accuracy of these data.
The effective date of this opinion is March 31, 2012.
5. Use of forward looking information
 - 5.1. In order to assess the impairment of goodwill and other intangible assets, I have assessed the fair value of the Company's life insurance portfolio. I assessed the Company's Life Insurance portfolio (both the present portfolio and the future one) on the basis of forward looking information that included, inter alia, forecasts, assessments and estimates relating to future events or matters, that may or may not come to pass and are not under the control of Phoenix and/or the Delek Group. Such forward looking information does not constitute a proven fact and is based solely on my subjective assessment, which relied on general information available to me at the time of writing.
 - 5.2. Moreover, I have also conducted an assessment of the value of the Company's non-Life insurance portfolio (both the present portfolio and the future one) in which I also relied on forward looking information with which the Company's management provided me in regard to the expected profit in each of its insurance branches. Such forward looking information is uncertain information in regard to the future based on information available to the company at the time of writing, and comprising estimations or intentions of the Company's management at the time of writing. Should these estimations of the management fail to materialize, the actual results may materially differ from the assessed results or the results implied by such information.
6. **Description of the acquisition transaction, excess purchase price allocation, and recognized goodwill**
 - 6.1. At the end of 2005, through its wholly owned subsidiary, Delek Investments and Properties Ltd. ("DIP"), the Delek group acquired 25.01% of Phoenix shares ("the First Acquisition"). In June 2006, DIP exercised an acquisition option and acquired 8.03% additional Company shares ("the Second Acquisition"). In the course of November 2006, through its wholly owned subsidiary, Delek Capital Ltd. ("Delek Capital"), the Delek group acquired 28.5% of Phoenix issued share capital, in exchange for the sum of NIS 939.6 millions (including transaction expenses).¹ Following the November 2006 acquisition of 28.5% ("the Third Acquisition"), the Delek Group became the controlling shareholder of the Company and held 61.55% of Phoenix share capital and 59.83% of voting rights. After the structural changes made in the Delek Group at the end of 2010, all Phoenix shares were unified under Delek Investment and Properties.
The total holding of the Delek Group in Phoenix as of 31.12.2011 was 56.7%. This percentage also reflects additional acquisitions and share issues to third parties that were carried out from the date of acquisition to the 31.12.2011.
 - 6.2. A total of NIS 311,694,000 was recognized as the goodwill accruing to this acquisition transaction in the Delek Group's financial statements as of December 31, 2011.

¹ The remuneration paid amounted to NIS 924.3 million, while the transaction costs (mainly for the protection transaction) amounted to NIS 15.3 million.

- 6.3. Table 1 below presents excess purchase price balances arising from said acquisitions, as included in the Delek Group's financial statements for the year ending December 31, 2011:

Table 1 – Excess purchase price balances arising from Phoenix acquisitions as presented in the Delek Group Financial Statements as of December 31, 2011:

	Total The Delek Group (thousands)
Excess purchase price allocated to life insurance portfolio	247,244
* Reserves for tax	(87,277)
	159,967
Excess purchase price allocated to non-life portfolio	6,211
* Reserves for tax	(2,769)
	3,442
Interim summary	163,409
Goodwill	311,694
	<u>475,103</u>
Of which	
Future worth of life portfolio	44,298
Future worth of non-life portfolio	27,816
Not allocated	239,580
	<u>311,694</u>

* The reserve amounts were adjusted for the tax rates established in the 2011 Tax Burden Change Law (Legislation amendments), approved by the Knesset on January 2012.

7. The balance of the equity allocated to the majority holders of Phoenix, as included in the audited balance sheet as of September 30, 2011, was NIS 2,593.3 million. Phoenix market capitalization on that date was NIS 2,152.3 million². Phoenix market capitalization rate as of December 31, 2011³ was NIS 2,388.2 million, and at the time of writing (according to the closing rate as of March 15, 2012) the market cap was NIS 2,181.9 million. The Delek Group holds (as described in section 6.1 above) 56.7% of Phoenix issued and paid-up share capital. Delek Group's investment in Phoenix was carried as NIS 1,945 in the Delek Group balance sheet as of September 30, 2010 and as NIS 1,937 in the balance sheet as of September 30, 2011.

8. Phoenix operational results over the first nine months of 2011

- 8.1. The Company shareholders share in the net profits for the interim period comprising the first nine months of 2011, amounted to NIS 127 million, as compared with a net profit of NIS 239 in the first nine months of 2010, and a profit of NIS 309 million for 2010 in its entirety.
- 8.2. Table 2 presents the main results drawn from the Company's consolidated financial statements:

² Market cap as of September 27, 2011, the last trading day of 2011 Q3. This market cap value also includes the value of the NIS 5 par value shares that were removed from trade as of January 25, 2012 and were included in the maintenance list. These shares were included according to a market cap of NIS 197.8 million.

³ Market cap as of December 29, 2011, the last trading day of 2011. This market cap value also includes the value of the NIS 5 par value shares as discussed in the previous footnote.

Table 2 – Phoenix Holdings Ltd. – Abstract of consolidated results (NIS millions):

	<u>For the period</u>		<u>For the year</u>
	<u>ending September 30</u>	<u>2010</u>	<u>ending</u>
	<u>2011</u>	<u>2010</u>	<u>2010</u>
Total profit (loss) from life insurance and long-term savings	50	131	103
Profit from health insurance	69	83	115
Profit (loss) from non-life insurance segments	43	205	264
Total profit from financial services segment	<u>77</u>	<u>81</u>	<u>112</u>
Total profit (loss) from operating segments	239	500	594
Profit (loss) not allocated to the reported operating segments	(152)	1	19
The Company's share in the net results of held companies that are not allocated to the reported operating segments	(33)	10	24
Total profit (loss) before income tax	54	511	637
Income tax	<u>(28)</u>	<u>(162)</u>	<u>(205)</u>
Total profit (loss) for the period	26	349	432
Total profit (loss) for the period allocated to the Company's shareholders	14	332	408

9. Impairment test method

- 9.1. The possibility that goodwill has been impaired was tested according to the rules and guidelines established in IAS 36 and IAS 38.
- 9.2. Since goodwill cannot be measured separately from operations, the accepted method for testing for impairment is to estimate the recoverable amount of each cash generating unit to which the acquired goodwill, or part of it, is allocated, and compare it with the carrying amount of the assets and obligations (including the acquired goodwill) associated with that unit. If the recoverable amount is lower than the carrying amount of the unit, the difference will be deducted from the goodwill allocated to that unit.
- 9.3. Recoverable amount:
Section 18 of IAS 36 defines recoverable amount as "**the higher of an asset's fair value less costs to sell an asset or cash-generating unit and its value in use**". In our case, subject to the provisions of IAS 36 section 20, we have chosen to test the value in use for the Company.
- 9.4. Value in use:
According to IAS 36 section 31, estimating the value in use of an asset involves the following steps:
 - (a) Estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and
 - (b) Applying the appropriate discount rate to those future cash flows.
- 9.5. For the purpose of my test, I classified (consistently with my opinion on purchase price allocation – PPA) the recognized goodwill into three groups:
 - 9.5.1. Goodwill reflecting the future value of the life insurance business.
 - 9.5.2. Goodwill reflecting the future value of non-life insurance business.
 - 9.5.3. Additional unallocated goodwill reflecting, inter alia, the controlling premium and the synergy between the insurance business and other Phoenix operations.
- 9.6. Table 3 below, presents data regarding the composition of the book value of the investment in Phoenix as carried in Delek Group's books as of September 30, 2011.

Table 3 – Book value of cash-generating units (in NIS millions)

	Total The Delek Group
<u>Life Insurance:</u>	
Existing portfolio	953.4
Future portfolio	132.3
Total per unit	<u>1,085.7</u>
<u>Non-life insurance:</u>	
Existing portfolio	46.6
Future portfolio	<u>72.6</u>
Total per unit	<u>119.2</u>
Total insurance operations	1,204.9
Other	492.5
Unallocated goodwill	<u>239.6</u>
Total	<u>1,937.0</u>

- 9.7. We shall now examine Delek Group's share in the recoverable value of Phoenix Life and Non-Life insurance segments and compare it to the book value of each cash-generating unit described in table 3 above. In addition, we will compare the recoverable value of Phoenix insurance business (life and non-life) to their book value and add the unallocated goodwill amounting to NIS 239.6 million (as shown in table 3 above).
10. Recoverable amount of the life insurance business
- 10.1. It is necessary to survey the Company's expected cash flows for the next decades in order to test the recoverable amount of the life insurance business. This test requires a great deal of information that is in part based on actuarial assumptions, including morbidity and mortality assumptions, assumptions regarding early redemption of policies and other assumptions regarding reinsurance, rate of claims, rate of fees and general expenses.
- 10.2. To the best of my knowledge, the best source for these data is the embedded value report issued by Phoenix. I have also adopted the previous tests of goodwill impairment that I conducted in previous years. To the best of my knowledge, this is the accepted practice of other analysts and assessors in Israel and overseas. Nevertheless, consideration should be given to the fact that the actuarial estimate of embedded value does not necessarily reflect the fair value (in the accounting sense) of the life insurance portfolio. Nevertheless, as mentioned above, the embedded value does reflect a great deal of information and I found it appropriate to use it as the basis for my assessment of the value of the life-insurance business as of 31.12.2011.
- 10.3. As regards the importance and reliability of the embedded value report, it should be noted that according to the new capital requirements imposed by the Insurance Commissioner the embedded value of the insurance, health and pension portfolios of the insurance companies, must all be taken into consideration.
- The embedded value is an assessment of the value of the life insurance and health portfolios and the pension management business.⁴ The businesses included in the value calculations of the insurance and health portfolios are:
- Personal long-term policies in the life and health portfolios as of 31.12.2011.

⁴ It was only in the 2009 Embedded Value report that Phoenix first published the EV of its pension management business.

- Future increase in premiums of existing policies and one-time deposits as a result of wage increases.
 - Group policies in the life and health portfolios as of 31.12.2011. Under the rules and principles instituted by the Insurance Commissioner, the profits of such policies were only assessed up to their next renewal date.
- 10.4. The embedded value is mainly calculated using actuarial methods of discounting future profits (see also, section 10.12.1 below). **It is important to stress that from a theoretical point of view the embedded value calculated according to the rules and principles instituted by the Insurance Commissioner in Israel⁵, provides the most appropriate assessment offered by insurance theory for the assessment of a life portfolio's value.**
- 10.5. The model is based on the assumption that no correlation liable to materially influence the embedded value exists between the assumption of a non-market risk model (such as demographic or operational risks) and a market risks model.
- 10.6. Additionally, the model assumes that insurance reserves are invested in riskless assets. The actual investment policy of an insurance company, specifically its decision to invest insurance reserves in risky financial assets too, does not increase or change the embedded value.
- 10.7. At the time of writing, Phoenix had not published its embedded value report for 2011. For this reason I have used the 2010 embedded value as the basis of assessment, and used data I received from the Company's actuary to assess whatever changes have taken place in the embedded value over the course of 2011.
- 10.8. The embedded value as of December 31, 2010 (including allocated equity) was NIS 5,234.1 million, as detailed in table 4 below:

Table 4 – Embedded Value as of 31.12.2010 (NIS Millions)

Adjusted equity	VIF Insurance – life & LTC	VIF Insurance – Health	VIF Management – Pension	Deducting Required Insurer's Equity	Total
1,443.0	2,815.0	812.0	250.8	(86.7)	5,234.1

- 10.9. The health insurance business (not the LTC business) was traditionally included in the non-life statements. Thus, in order to maintain consistency with previous opinion reports, they were considered in the present report in the context of the recoverable non-life business value calculations.⁶
- 10.10. The following adjustments were made in the data of table 4, in order to assess the value in force (VIF) of the life and LTC insurance business as of 31.12.2011:
- 10.10.1. Calculation of future returns and recapitalization according to the binding interest vector as of 31.12.2011: The non-risk insurance rates as of the end of 2011 were different than the non-risk interest rates at the end of 2010 (as detailed in appendix B of the document). According to our assessment, the change in interest vector leads to a derecognition of NIS 78 million from the portfolio's VIF.
- 10.10.2. Taxation rate updates: The value of the portfolio as of the end of 2010 was assessed according to the taxation rates then expected under the 1969 Law of Increased Economic Efficiency (legislative amendments for the implementation of the economic plan for the years 2009 and 2010), which assumed a gradual decrease in the taxation rates imposed on

⁵ See also Insurance Commissioner's Circular 2007-1-11 dated August, 12, 2007.

⁶ For the purpose of accounting reporting, the health insurance business (both individual and group) and the LTC insurance business are part of a separate operational segment than other forms of insurance.

companies, until the level in 2016 would be as low as 18%. The total taxation rate applicable to financial institutions (of which the Company is one – Companies Tax and taxation of capital gains) was 35.34% and expected to gradually decrease to the level of 29% from the year 2016 and on.

At the beginning of January 2010, the Knesset passed the 2011 Law of Change in the Tax Burden (legislative amendments) ("the Amendment") following the recommendations of the Trachtenberg Committee. According to the Amendment, the rate of Companies Tax for the period 2012 and thereafter will be 25% and the total taxation rate imposed on the Company as a financial institute will be 35.34%. In view of this update, NIS 219 million should be derecognized from the assessment of the VIF.

10.10.3. Updated derecognition of "loss" of future variable management fees, owing to the accumulated negative yields of participating insurance policies:

According to the terms of the profit-participating policies issued during the period 1991 to 2003 (inclusive), Phoenix is entitled to receive variable management fees only if it attains positive yields during that period. Management fees are not paid in the event of negative yields, so long as the cumulative calculations indicate that the profits attained do not exceed the losses accumulated in the policies. The value of the management fees that will not be collected because of negative yield (until a positive yield is attained, as above) was NIS 627.3 million as of December 31, 2008, NIS 226 million as of December 31, 2009 and NIS 38 million as of December 31, 2010 (future values before the influence of taxes). As indicated by the Company Board of Directors' report as of September 30, 2011, the estimated value of the management fees that will not be collected because of the negative yield (until a positive yield is achieved, as above) as of October 31, 2011 has increased to NIS 211 million⁷. The estimated value of management fees not collected because of negative yields as of December 31, 2012 was about NIS 280 million.

According to our estimate, the negative yields attained in 2011 will lead to a decrease of about NIS 125 in the portfolio VIF⁸.

10.10.4. Inclusion of the estimated value of new businesses (VNB) added over the course of 2011: According to initial data received from the company, new business attained in the Life and LTC branches in the course of 2011, will add an additional NIS 200 million to the embedded value⁹.

10.10.5. The derecognition of the income component expected in 2011 on account of the 2011 income assessment (realized and added to the Company's equity): According to our assessment should be derecognized by NIS 42 million.

10.10.6. Additional adjustments required because of change in other model parameters, are expected to lead to the recognition of NIS 55 million in the portfolio VIF. These adjustments include, inter alia, corrections to the embedded value as of the end of 2010, and the effect of changes in the operational and demographic assumptions.

10.11. **After said adjustments were made, it was found that the embedded value of the long-term life and LTC insurance policies is estimated at NIS 2,606 million**, as detailed in Table 5 below (as compared with NIS 2,815 million as of 31.12.2010 as detailed in Table 4 above).

⁷ Before the influence of taxes

⁸ In tax deducted terms

⁹ This addition will be distributed in the following way in the 2011 Embedded Value report: the actual influence of new businesses on 2011 profits will be classified as adjusted equity, while the profits expected from new businesses from 2011 and on, will be classified as VIF.

**Table 5 – Estimated Portfolio VIF for Life and LTC business
as of 31.12.2011 (NIS millions)**

Portfolio VIF as of 31.12.2010	2,815
Decrease because of change in the interest vector	(78)
Decrease because of change in the taxation rate	(219)
Influence of 2011 yields	(125)
Increase because of new businesses	200
Realization in 2011	(42)
Other adjustments	55
Estimated value as of 31.12.2011	2,606

I would like to emphasize the fact that this is an estimation prepared on the basis of the assumptions guiding the calculation as of 31.12.2010, coupled with the above described adjustments, and that it does not reflect the Company's work plan for the coming years.

10.12. Adjustment of Discount Rates:

10.12.1. The embedded value was calculated by means of the "Best Estimate Assumptions" method, i.e., assumptions that are the product of extrapolating existing knowledge into the future in the context of the environment in which the Insurance Company is operating, and without any conservative coefficients. The embedded value model utilizes a financial technique known as the "Certainty Equivalent Approach". This approach synchronizes cash flows with the market risks embedded within them, thus discounting them at the same riskless rate of interest. Such riskless interest is also used to assess the expected returns on investments. Capitalization is carried out on the basis of the riskless "interest vector" as of 31.12.2011 ("the Interest Vector").

The embedded value is calculated on the basis of the financial theory that claims investors do not require additional recompense in discount interest for risks that are not market risks, so long as they are able to spread the uncertainty by holding a diverse and varied investments portfolio. Thus, if such a condition is taken as given, the handling of risks that are not market risks is carried out on the basis of the Best Estimate Assumption and discounting cash flows at the riskless interest rate.

10.12.2. In the present opinion report, I have found it appropriate to adopt a more careful approach, according to which one should discount future cash flows by a higher rate of interest than that of the riskless interest rate (used to assess the expected return on investments). The higher rate of discount is supposed to express the total ensemble of risks to which an insurance company is exposed (institutional risks, investment risks, insurance risks and operational risks):

(a) Institutional risks arise from legislative amendments and various decrees issued by the Capital Market Commissioner, which are intended to increase transparency and the ability of people to move from one long-term savings channel to another. In this context, one should be mindful of the plan to establish a pension clearing house, and the Treasury's plan to increase competition in the pension savings market, as published in November 2010¹⁰. One should be mindful of the fact that the embedded value report did not take into account the possible future influence of such

¹⁰ The plan requires changes in existing legislation for its implementation.

"mobility" arrangements that will allow life insurance policy holders to transfer their savings to other long term savings channels. At this stage, one cannot assess the future impact such arrangements may have, if any, on the embedded value. The main concern is that the entry of large banks into the pension advisory services market, is liable to increase the damage.

- (b) Investment risks arise from the fact that insurance reserve life spans are significantly longer than the life of riskless financial assets that are available for investment.
- (c) Insurance risks arise from possible deviations from assumptions regarding mortality, morbidity and early redemption rates taken into account when the embedded value was calculated.
- (d) Operational risks arise from exceptions and malfunctions in the course of the Company's regular business.

10.12.3. In the course of 2008, in order to calculate the embedded value, the leading European insurance companies have added an additional "Liquidity Premium" reflecting the market's low liquidity, in the range of 1% to 3%. IN 2009, thanks to the recovery of the capital markets, the Liquidity Premium has been reduced to about 1% on the average. I assume that it may be increased again, in view of the current crisis in Europe's financial markets.

Japanese insurance companies usually add a risk premium to the interest vector, in order to reflect the actual investment mix of life insurance reserves.¹¹

10.12.4. Other value assessors in Israel often add, for the purpose of discounted future cash flows, an additional risk premium to the riskless interest rates already included in the "interest vector".¹² Nevertheless, there is no theoretical basis for assessing the additional risk premium to be included in the calculations, if at all. In my estimation, this is no more than a "rationalization" intended to explain the phenomenon whereby the market prices of traded insurance companies currently reflect less than 50% of the embedded value of insurance companies.¹³ In some cases, it turns out that the additional risk premium reflects risk factors specific to a certain company.¹⁴

10.12.5. On February 27, 2012, the Knesset Finance Committee approved the Management Fee regulations. Seemingly, these regulations, at least as far as this can be foreseen at the end of 2011, do not have any effect on the embedded value of the existing insurance portfolio, for they will only apply to new insurance policies issued from 1.1.2013 and on. There is however some concern that reduced management fees in alternative saving channels, may lead to an increase in the mobilization and early redemption rates of the policies in the existing portfolio.

10.12.6. Table 6 below, presents an analysis of the estimated embedded value of the Company's life and LTC insurance businesses sensitivity to an additional risk premium:

¹¹ See for example, the report of the Japanese insurance company Dai-Inchi as of 31.3.2011, published 11.05.2011.

¹² Thus, for example, Kesselman Finance Ltd.'s assessment of the value of IDE Insurance Co. Ltd., posited a risk premium of 3% over the interest vector.

¹³ See for example Eden and Zuckerman (2010) referenced in section 3.9 above, and Eden (2010) referenced in section 3.10 above. The transaction in which Shlomo Eliyahu acquired the control of Migdal Insurance Co. from the Italian Generali Group at the beginning of March 2012, also reflects an EV/EBITDA of 50%.

¹⁴ See for example, Leader Capital Markets Ltd. analytical survey, referenced in section 3.11 above.

Table 6 – Sensitivity of Portfolio VIF as of 31.12.2011 to additional risk premium rate

	Rate of additional risk premium					
	<u>0.50%</u>	<u>1.00%</u>	<u>1.50%</u>	<u>2.00%</u>	<u>2.50%</u>	<u>3.00%</u>
Reduction in embedded value In NIS millions	(144)	(275)	(393)	(501)	(599)	(689)
Reduction in %	-5.5%	-10.6%	-15.1%	-19.2%	-23.0%	-26.4%

- 10.12.7. Discounting according to interest rates higher by 3.0% than the riskless interest rate included in the "interest vector" as of 31.12.2011, will lead to a reduction of NIS 689 million in embedded value.¹⁵
- 10.12.8. This additional discount rate was established according to my best estimate and on the basis of my professional experience. In previous opinion reports, I have established a premium of 2%, but in view of the new management fee regulations, and the increase in the capital market Liquidity Premium, I have found it appropriate to increase it to 3.0%. In my estimation, a 3.0% risk premium appropriately reflects the risks detailed above.
- 10.12.9. After the added discount, the estimated embedded value of the Company's life and LTC insurance businesses as of 31.12.2011 was NIS 1,917 (=2,606-689) deducting an amortization of NIS 76 million for the required capital costs¹⁶, so that the embedded value of the Company's life insurance portfolio is NIS 1841 million (=1,917-76).
- 10.13. First, I tested for a devaluation in the value of the existing life insurance portfolio carried on the companies' books. Table 7 below indicates that **the recoverable amount of the existing portfolio in the Delek Group is no less than the amount included in the financial statements.**

Table 7 – the recoverable amount and book value of the existing life insurance portfolio (in NIS millions)

	Rate of additional risk premium			
	<u>1.50%</u>	<u>2.00%</u>	<u>2.50%</u>	<u>3.00%</u>
Total Embedded Value – Amended	<u>2,136.7</u>	<u>2,028.7</u>	<u>1,930.7</u>	<u>1,840.7</u>
Delek Group's share - 56.7%	1,211.5	1,150.2	1,094.7	1,043.7
Book value	<u>953.4</u>	<u>953.4</u>	<u>953.4</u>	<u>953.4</u>
Surplus	258.1	196.8	141.3	90.3

10.14. Value of future life insurance portfolio

- 10.14.1. The estimated value of new business after tax (VNB) obtained in 2011, as stated in section 10.10.3 above, was NIS 200 million. In the course of 2010, the company obtained a similar result of NIS 215 million. It should be emphasized that in 2011 Phoenix attained an exceptional increase (as compared with its competitors) in income derived from new premiums.¹⁷

¹⁵ In my previous opinion report for 2010, the addition of 2% to the discount rate, led to a decrease of 20.4% in the portfolio VIF.

¹⁶ The capital cost is the tax discount on investment profits for the existing portfolio. Please note that because of the increase in taxation rates (as detailed in section 10.10.2 above), there has also been an increase in the relative cost of capital.

¹⁷ In this regard, see also Leader Capital Markets Ltd. analytical survey (referenced in section 3.11 above).

- 10.14.2. The expenses expected during the first year of new business (due to fees and other acquisition costs) should be deducted from this value. A rough estimate indicates that such expenses amount to 50% of VNB.¹⁸ In order to maintain consistency with my estimation of the value of the existing life insurance portfolio, I have established a higher discount rate than the interest vector for this case as well. Consistent with my previous opinion reports, I have found it appropriate to establish an additional risk premium of 3.0%.

Table 8 – Sensitivity of VNB as of 31.12.2011 to additional risk premium rate

Reduction in VNB in %	Rate of additional risk premium					
	<u>0.50%</u>	<u>1.00%</u>	<u>1.50%</u>	<u>2.00%</u>	<u>2.50%</u>	<u>3.00%</u>
	-6.0%	-11.5%	-16.0%	-20.5%	-24.5%	-28.0%

- 10.14.3. After the added discount, the estimated average value of new insurance and LTC insurance business (VNB) is NIS 72 million (=100-28). On deducting an amortization of NIS 6 million for the required capital costs, the embedded value of the Company's life insurance portfolio is NIS 66 million (=72-6).
- 10.14.4. The new management fees regulations have established an upper limit of 1.05% management fees on policies issued from January 1, 2013 and on. As far as I was able to learn, the rate of management fees proposed in policies currently issued is 1.15%. The significance of this is that the maximum rate is higher than the average rate by 8.7%. Nevertheless, one should consider the fact that owing to the present variability in management fees, the effective rate of profit loss was even higher (for it is highly probable that in policies where the rate is higher than the allowed limit the Company would not be able to compensate itself for management fee losses by raising the management fees on policies where the management fee rate is lower). Moreover, an increase in public awareness and sensitivity to the issue of management fees may motivate insurance companies to bring their management fee rates even lower than what the regulations require.
- 10.14.5. In last years opinion report I multiplied the discounted value of the future life portfolio by a P/BV of 8, which seemed to me appropriate as a discount rate for new businesses, which involve a higher level of uncertainty than the cash flows of existing policies. In view of the new management fees, I have found it appropriate to decrease the P/BV to a rate of 6.6 (a decrease of 17.5%).
- 10.14.6. The value of the future life insurance portfolio is thus estimated in the range of NIS 291.9 million and 329.3 million, as detailed in Table 9 below:

Table 9 – Estimated value of future life insurance portfolio (in NIS millions)

	Rate of additional risk premium		
	<u>2.00%</u>	<u>2.50%</u>	<u>3.00%</u>
Amended VNB	88.0	82.5	78.0
P/BV of 6.6	<u>6.6</u>	<u>6.6</u>	<u>6.6</u>
Value of Future Portfolio	580.8	544.5	514.8
Delek Group's share – 56.7%	329.3	308.7	291.9
Book value	132.3	132.3	132.3

¹⁸ In 2010 the combined VNB of the life and health insurance businesses was NIS161. This sum comprises an initial loss of NIS 150 million and an expected later profit of NIS 311.

- 10.14.7. This estimation of the value of the future life-insurance portfolio, significantly exceeds the book value allocated to the future life insurance portfolio (NIS 132.3 million, as detailed in Table 3 above). Therefore, I believe that the **recoverable amount of the Delek Group's future life and LTC insurance portfolios exceeds the amount recognized in the financial statements.**

11. Recoverable amount of the Company's pension fund management business:

- 11.1. Phoenix manages three pension funds; Veteran Pension Fund, Comprehensive Pension Fund and General Pension Fund. Table 10 presents the total scope of these Funds' assets as of December 31, 2009, 2010 and 2011.

Table 10 – Total scope of assets held by pension funds managed by the Phoenix Group (in NIS millions)

	December 31		
	<u>2011</u>	<u>2010</u>	<u>2009</u>
Amit Veteran Pension Fund	816	791	754
Phoenix Comprehensive Pension	4,192	3,393	2,424
Phoenix General Pension	<u>53</u>	<u>44</u>	<u>32</u>
Total	5,061	4,228	3,210

Source: The funds' monthly reports.

- 11.2. In my previous opinion reports I estimated the recoverable amount of the Company's pension funds business on the basis of a P/BV value of about 2.5% of the managed assets. I used this P/BV value to estimate the value of the pension fund management business as of December 31, 2010 at NIS 105.7 million ($=4,228 \times 2.5\%$).
- 11.3. Commencing from 2009, Phoenix incorporates information on the embedded value of pension fund management in its Embedded Value report. The VIF of Phoenix pension business portfolio, as included in its Embedded Value report of December 31, 2010 was NIS 249.1 million¹⁹. This amount is significantly higher than the estimate derived from a P/BV value of 2.5% of the managed assets.
- 11.4. Because of the simplicity and intelligibility of the previous estimate, I found it appropriate to continue to estimate the value of Phoenix pension business according to a P/BV value of 2.5% of the managed assets.²⁰ Under this assumption the estimated value of the Phoenix pension funds business as of December 31, 2011 is NIS 126.5 million ($=5,061 \times 2.5\%$).
12. Assessment of recoverable amount for the life insurance unit
- 12.1. The recoverable amount for the life insurance unit comprises three elements:
- The recoverable amount of the existing life insurance portfolio;
 - The recoverable amount of the future life insurance portfolio;
 - The recoverable amount of the Company's pension funds.
- 12.2. Table 11 below presents a summary of the recoverable amount assessment for the life insurance unit (value per 100% holding)

¹⁹ Based on the embedded value for 2010, the profit amounted to NIS 120.5 million.

²⁰ To the best of my knowledge, this is the currently accepted method to assess the fair value of companies that manage pension funds.

Table 11 – Value of Life Insurance Unit in NIS millions (per 100% holding)

	NIS Millions
Value of existing life insurance portfolio	1,840.7
Value of future life insurance portfolio	514.8
Value of pension business	<u>126.5</u>
Total	2,482.0

13. Comparing the recoverable amount to the book value of the life insurance unit

- 13.1. Table 12 presents a comparison between the book value (including allocated goodwill) and the recoverable amount of the investment in the life insurance unit.

Table 12 – Life Insurance Business – Comparison between Book Value and Recoverable Amount (in NIS millions)

Value per 100% life insurance unit	2,482.0
Delek holding percentage	56.7%
Recoverable amount	1,407.3
Book value including allocated goodwill	<u>1,085.7</u>
Surplus	321.6

13.2 **The data indicate that the total value of the goodwill allocated to this unit has not been impaired.**

14. Recoverable Amount of the non-life insurance business:

- 14.1. In my previous opinion reports I included the health segment within the non-life insurance business, in conformity to the then customary classification in insurance company statements up to 2007, inclusive. Other non-life insurance businesses include the following operational segments and insurance branches: Property damage auto liability coverage, mandatory auto liability coverage, liability insurance, and other non-life insurance. The following is an estimation of the value of each of these insurance segments/branches:

14.2. The Health Branch:

- 14.2.1. As detailed in Table 4, the report regarding the Company's embedded value incorporates the embedded value of the health insurance policies.
- 14.2.2. The embedded value of the existing health insurance portfolio was estimated in the December 31, 2010 report at NIS 812 million.
- 14.2.3. After carrying out similar adjustments to those detailed in section 10.10 above,²¹ the initial estimate of the embedded value of the Company's health insurance business is NIS 792 million, as detailed in Table 13 below.

Table 13 – Estimated VIF for the health insurance business (in NIS millions)

Portfolio VIF as of 31.12.2010	812
Decrease because of change in the interest vector	(1)
Decrease because of change in the taxation rate	(65)
Increase because of new businesses	107
Realization in 2010	(51)
Other adjustments	<u>(10)</u>
Estimated value as of 31.12.2011	792

²¹Please note that the negative yields attained in 2010 do not materially affect the health insurance portfolio VIF.

- 14.2.4. This estimate was prepared on the basis of the assumptions that guided the calculations as of 31.12.2010, while carrying out the above detailed adjustments, and does not take the Company's work plan for the coming years into account.
- 14.2.5. For the sake of caution, I have found it appropriate to estimate the value of the health insurance business on the basis of discount coefficients higher by 2.0% to 3.0% than the interest vector on which the embedded value report is based. The results of these calculations are detailed in Table 14 below.

Table 14 – Recoverable Value of Existing Health Insurance Portfolio (in NIS millions)

	Rate of additional risk premium		
	<u>2.0%</u>	<u>2.5%</u>	<u>3.0%</u>
Estimate of embedded health business value as of December 31, 2010	792	792	792
Amortized amount in NIS millions	(151)	(181)	(209)
Amortized amount in %	-19.1%	-22.9%	-26.4%
Amended estimation	641	611	583
Reduced capital requirements – 2.5%	<u>(23)</u>	<u>(23)</u>	<u>(23)</u>
Amended estimation	618	588	560

- 14.2.6. Following the added discount rate of 3.0%, the estimated embedded value of the Company's life and LTC insurance businesses as of 3.12.2011 is estimated at NIS 583 million (=792-209). Once an amortization of NIS 23 million is deducted for the required capital costs, the embedded value of the Company's life insurance portfolio is NIS 560 million (583-23).
- 14.2.7. The estimated VNB obtained in the course of 2011 was NIS 170 million as compared with NIS 67 million in 2010 (before profits realized in the course of the calculation year were allocated to the adjusted equity according to the taxation rates that were known at the time). From this value, one should deduct the expenses expected during the first year of new business (due to fees and other acquisition costs). A rough estimate indicates that such expenses amount to 50% of the value of the new business.
- 14.2.8. In order to maintain consistency with my estimation of the value of the existing life insurance portfolio, I have established a higher discount rate than the interest vector. I tested the effects of an additional discount rate of 2.0% to 3.0% on VNB. I also indicated the cost of the required capital (about NIS 3.2 million).
- 14.2.9. As state above, I multiplied the discounted value of the future life portfolio by a P/BV of 8, which seemed to me appropriate as a discount rate for new businesses in the area of health insurance.
- 14.2.10. Table 15 presents the estimated value of the Company's future health insurance portfolio:

Table 15 – Estimated value of future health insurance portfolio (in NIS millions)

	Rate of additional risk premium		
	<u>2.0%</u>	<u>2.5%</u>	<u>3.0%</u>
2010 VNB	54	54	54
Amortized amount in NIS millions	(8)	(9)	(11)
Amortized amount in %	-14.0%	-16.8%	-19.6%
Amended estimation	46	45	43
Amended estimation after capital requirements	42.8	44.5	43.0
P/BV	8	8	8
Future portfolio value	343	356	344

- 14.2.11. The total estimated recoverable amount of the Company's health insurance business is in the range of NIS 904 million (=343+560) and NIS 961 million (=343+618).
- 14.3. The non-life Branch (excluding health):
- 14.3.1. One should distinguish between the underwriting results of operations in the non-life branch, which reflect the profit generated by insurance operations, including an imputed investment profit of 3%, and the general results of branch operations that also reflect (in addition to the underwriting results) the actual investment profits (losses), above (below) the imputed investment profit.
- 14.3.2. Table 16 below, presents an analysis of the profits achieved by the Phoenix in 2010 and in the first nine months of each of the years 2010 and 2011, distinguishing between the underwriting results and the profits (losses) created during each of these period by investing insurance reserves.

Table 16 – Non-Life Segment Profitability Analysis (NIS Millions)

	<u>1-9/2011</u>	<u>1-9/2010</u>	<u>2010</u>
Underwriting Results			
Property damage auto liability coverage	19	50	55
Mandatory auto liability coverage	59	14	30
Liability insurance	31	20	36
Fire, property, homeowners and other	<u>43</u>	<u>54</u>	<u>56</u>
Total Underwriting Results	<u>152</u>	<u>138</u>	<u>177</u>
Investment profit (loss) beyond imputed investment profit	(32)	21	43
Other comprehensive profit	(77)	46	44
Profit (loss) from regular investments including comprehensive profit	<u>(109)</u>	<u>67</u>	<u>87</u>
Total comprehensive profit from the non-life insurance segment	<u>43</u>	<u>205</u>	<u>264</u>

- 14.3.3. The data indicate that over the first nine months of 2011, the Company has attained an underwriting profit of NIS 152 million in the non-life business segment (as compared with an underwriting profit of NIS 138 million over the parallel period in 2010)²². However, owing to a material loss of NIS 109 million (some of which was allocated to the comprehensive profit items), as compared with a comprehensive profit of NIS 67 from investments in the first nine months of 2010, the comprehensive profit attained from the non-life segment was just NIS 43 million (as compared with a comprehensive profit of NIS 205 million over the parallel period in 2010).
- 14.3.4. In view of the volatility of the Company's underwriting results over the last three years, and for caution's sake, I have found it appropriate to assume that the "normalized profit" before the tax expected from the non-life segment (underwriting profit plus imputed investment profit) is NIS 100 million per year²³. This is a similar assumption to the one I made last year.
- 14.3.5. From this expected profit, I deducted the expected tax, based on the presently known tax rates for financial institutions (including profit tax) as detailed in section 10.10.2 above.
- 14.3.6. I estimated the value of the non-life insurance segment according to a P/BV of 7. This P/BV reflects the large equity required by the regulations to offset income from premiums in the non-life insurance business²⁴. The result obtained was NIS 453 million $[=100 \times (1 - 35/34\%) \times 7]$.
- 14.3.7. The total recoverable amount of the non-life insurance business, including the Company's health insurance business, is thus in the range of NIS 1,357 million $(=904+453)$ and NIS 1,413 million $(=960+453)$.
- 14.3.8. Table 17 present a comparison between the book value (including allocated goodwill) and the recoverable amount of the investment in the non-life segment. Since, even according to the lower end of the range, the recoverable value is higher than the book value, there is no need to compare with the higher recoverable amount value.

Table 17 – Non-life insurance business – Comparison of book value and recoverable amount (in NIS millions)

Value of 100% holding – low value	1,357
Delek Group holding	<u>56.7%</u>
Recoverable Amount	769.3
Book value including allocated goodwill	<u>119.2</u>
Surplus	650.1

²² Consideration should be given to the fact that the insurance reserves in the mandatory auto liability coverage and the liability insurance segments in 2011 were discounted at a higher rate than in 2010, because of the increase in the riskless interest rate. This fact explains the increase in underwriting profit carried for 2011. When the effect of the change in discount rate is neutralized, it becomes evident that the underwriting results for 2011 have taken a slight turn for the worse as compared with 2010.

²³ Average for the past four years, taking into account the grossed over underwriting profits for 2011, i.e., NIS 126 million.

²⁴ In their assessment of the value of IDE Insurance Co. Ltd., Kesselman Finance Ltd. (see section 3.15 above) assumed a growth rate of 3% and a discount rate of 12%, with consideration for the capital adjustments required by the regulator. In my previous opinion report I established a P/BV of 8.

14.3.9. **The data unequivocally indicate that the goodwill allocated to this unit at the level of the Delek Group has not been impaired.**

15. Testing for the impairment of goodwill not directly allocated to cash-generating units:

15.1. Table 18 below presents a general comparison between the recoverable amounts of the life and non-life insurance units, and their book value, including their allocated and unallocated goodwill. **The calculation was carried out on the basis of the more rigorous assumptions.**

Table 18 – General Comparison (in NIS millions)

		See above in section
Life insurance unit recoverable amount	1,407.3	13
Non-life unit recoverable amount	<u>769.3</u>	14
Total value of recoverable amount	<u>2,176.6</u>	
Life insurance unit book value	1,085.7	
Non-life unit book value	119.2	
unallocated goodwill	<u>239.6</u>	
Total book value	<u>1,444.5</u>	
Total surplus	732.1	

15.2. The data indicate that goodwill not directly allocated to the cash-generating units was not impaired, nor was the comprehensive goodwill amount carried on Delek Group's books as of December 31, 2011.

16. Amortization period of purchase price allocated to existing insurance portfolios.

16.1. In my previous opinion reports I recommended that the purchase price allocated to the existing life insurance portfolio be amortized in parallel with the portfolio's maintenance rate. I believe this period may be estimated at 15 years on the average, which is the maximum amortization period for deferred acquisition costs (DAC). No data or information that may lead me to change this recommendation has come to my attention.

16.2. In previous opinion reports, I calculated the amortization period of the Company's existing non-life portfolio, as the weighted average of various amortization periods for the different insurances branches. The weighted average of these amortization periods (based on the data of the previous forecast) was 7.3 years. The data included in my new forecast did not lead to any material change in the weighted average of the amortization period.

17. Summary of Opinion

- 17.1. **In my estimation, in view of the tests I conducted, as of December 31, 2011, there has been no impairment in the unallocated goodwill attributed to Phoenix life and non-life insurance business (including the health insurance business).**
- 17.2. **Moreover, neither the value of the goodwill not directly allocated to cash-generating units, nor the comprehensive goodwill amount carried on the Delek Group's books as of December 31, 2011 have been impaired.**
- 17.3. To the best of my understanding, there has been no change whatsoever in the economic lifespan of the insurance portfolios to which some of Phoenix excess purchase price has been allocated, and there is no need to change their amortization period.
- 17.4. I am aware that you wish to use my opinion in order to prepare the Delek Group's financial statements as of December 31, 2011, and if necessary, also attach it to the financial statements and make it public, and I agree to this.
- 17.5. I would like to point out that I have no personal interest whatsoever in the shares of the companies mentioned in this opinion report.
- 17.6. I would like to add that up to the end of 2008, I served as a member on the Phoenix "Expanded Nostro" investments committee, and that in the past I have provided the Phoenix group with a number of economic/accounting reports on an ad hoc basis. Moreover, in 2010, I provided Delek Motorway Services with a value assessment fairness opinion, and in 2011, (together with Dr. Dan Elnatan) I provided Delek - the Israel Petroleum Company Ltd. with an economic opinion on the issue of marketing margin, which was presented to the petroleum administration at the Ministry of Infrastructures.

Respectfully,
Prof. Yoram Eden
C.P.A.

Appendix A – Prof. Yoram Eden

The following are details of my education and professional experience:

1. Academic education:
Full professor, the academic track, Administration College
PhD in accounting and financing - Tel-Aviv university
MBA (com laude) – Tel-Aviv University
B.A. in accounting – Tel-Aviv University
B.A. in economics – The Hebrew University – Jerusalem
2. Training and academic and professional activities:
 - 2.1 Academic activities:
During the period 2000-2007 I served as dean of the School of Business Administration, the academic track, Administration College.
Guest lecturer in Baruch College, the City University of New-York.
Academic editor of the "Accountant" periodical, since October 1991.
During the period 2000-2006 I served as a senior member of the academic staff on the Auditor's Council.
I presently chair the examinations committee of the Auditor's Council.
During the period 2000-2004, I have served as a member of IFAC's (International Federation of Accountants) Education Committee.
I have published many articles in the professional press and academic periodicals in Israel and overseas.
 - 2.2 Training and professional activities:
I am a licensed CPA since July 1978.
I am a member of the Institute of Certified Public Accountants in Israel since 1988.
I am the director and chairman of the investment committee of Infinity - Central Provident Pension Funds, Ltd. and an outside director at Shlomo Insurance Company Ltd.

Appendix b – riskless interest rates (spot) as of

<u>End of</u>	<u>As of end of 2011</u>	<u>As of end of 2010</u>
2011		-0.14%
2012	0.911%	0.19%
2013	0.747%	0.55%
2014	0.746%	0.90%
2015	0.887%	1.22%
2016	1.184%	1.49%
2017	1.484%	1.73%
2018	1.719%	1.93%
2019	1.915%	2.10%
2020	2.084%	2.24%
2021	2.235%	2.36%
2022	2.362%	2.46%
2023	2.461%	2.55%
2024	2.539%	2.63%
2025	2.601%	2.70%
2026	2.649%	2.76%
2027	2.690%	2.81%
2028	2.726%	2.86%
2029	2.759%	2.90%
2030	2.789%	2.94%
2031	2.817%	2.97%
2032	2.843%	3.01%
2033	2.867%	3.03%
2034	2.890%	3.06%
2035	2.911%	3.08%
2036	2.932%	

Delek Group Ltd.

Impairment valuation of the investment in Delek Automotive Systems Ltd. in
implementation of IAS 28, Investments in Associates and IAS 36
Impairment of Assets.

As of December 31, 2011

Kesselman Finance
Trade Tower, 25 Hamered Street, Tel Aviv 68125
PO Box 452, Tel Aviv 61003
Tel: 972-3-7954588
Fax: 972-3-7954789

Tel Aviv, March 19, 2012

To
Delek Group Ltd.

Dear Sirs,

Re: Impairment valuation of the investment in Delek Automotive Systems Ltd. in implementation of IAS 28, Investments in Associates, and IAS 36 Impairment of Assets, as of December 31, 2011 by Delek Group.

Kesselman Finance Price Waterhouse Coopers Ltd. ("PwC Israel") was requested by you to conduct a valuation of Delek Automotive Systems Ltd. ("**Delek Automotive**" or "**the Company**"), aimed at examining whether the carrying value of Delek Group Ltd.'s ("**Delek Group**") investment in the Company, as at December 31, 2011 ("**the Estimation Date**") was impaired in the implementation of IAS 28 *Investments in Associates* ("**IAS 28**") and IAS 36 *Impairment of Assets* ("**IAS 36**") by Delek Group.

The purpose of our study is to assist Delek Group management in evaluating the foregoing impairment ("Impairment Valuation"). This paper was prepared under the terms specified in the letter of intent between us dated January 26, 2012.

Our study will serve to value the impairment of Delek Group's investment in Delek Automotive, as at the valuation date, for financial reporting purposes only. Therefore, this paper should not be used for any other purpose. It should be noted that Delek Group cannot use the study, information and/or products we give them, in full or in part, without our prior approval. Nevertheless, it is agreed that Delek Automotive Group is permitted to attach the product of our study to reporting under the Securities Law, 1968 or its regulations and to any other reporting submitted under security laws.

This report includes:

1. This letter describing the purpose and scope of the study and presenting its conclusions;
2. A detailed report describing the purpose and scope of the study, a description of the Company and business environment, the estimation and valuation method, and presents its results, including appendices;
3. Disclaimer

Section 33 of IAS 28 prescribes that since goodwill, which is included in the carrying amount of an associate, is not separately recognized, its impairment loss cannot be examined separately. Instead, the impaired loss of the carrying value of the investment in an associate under IAS 36 should be examined by comparing the recoverable amount ("Recoverable Amount") of the investment to the carrying amount ("Carrying Amount"). Section 6 of IAS 36 defines the carrying amount as "the amount at which an asset is recognized in the balance sheet after deducting accumulated depreciation and accumulated impairment losses."

Recoverable amount

Section 18 of IAS 36 defines a recoverable amount as *"the higher of the fair value less costs to sell of an asset or cash generating unit (CGU) and its value in use."*

Section 19 stipulates that: *"It is not always necessary to determine both the fair value less costs to sell of an asset and its value in use. If one of these amounts is greater than the asset's carrying amount, the asset is not impaired, and it is not necessary to estimate the other amount."*

Value in use

For the study, we estimated the value in use of Delek Automotive.

Standard 36 determines how to measure the value in use of an asset or CGU.

Under section 31 of IAS 36: *"Estimating the value in use of an asset involves the following steps:*

(a) estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and (b) applying the appropriate discount rate to those future cash flows."

Section 33 of IAS 28 defines that:

"In determining the value in use of the investment, an entity estimates:

its share of the present value of the estimated future cash flows expected to be generated by the associate, including the cash flows from the operations of the associate and the proceeds on the ultimate disposal of the investment; or the present value of the estimated future cash flows expected to arise from dividends to be received from the investment and from its ultimate disposal."

To evaluate the recoverable amount of Delek Group's investment in Delek Automotive, we evaluated Delek Automotive's value in use using the DCF method.

The impairment loss valuation was based on information and information sources included in the financial statements of the auditors of both Delek Automotive and Kamor Motors Ltd. ("**Kamor Motors**") for 2006-2011, the Company management's budget for 2012, Delek Automotive management's evaluations and forecasts, meetings with Delek Automotive management, other operating information, market research, and public information concerning the Company's area of operation. The data, information, forecasts, explanations and representations which we used ("**the Information**") were not verified by us independently and we do not express an opinion concerning their accuracy and completeness. Nevertheless, we conducted various studies concerning the plausibility of the information and forecasts. These studies included, *inter alia*, analyzing financial statement, operating reports, historical information and other financial information. In any event, even if we conducted plausibility tests as aforesaid, our study shall not be considered to be or be a confirmation to the completeness or accuracy of the information provided by us.

Although we analyzed financial and accounting information during our study, our work did not include auditing Delek Automotive or Delek Group's books under customary auditing rules. Therefore we do not assume responsibility or express an opinion concerning the reliability, accuracy and relevance of the information supplied to us by Delek Group, the Company or anyone on their behalf.

Generally, forecasts relate to future events and rely on reasonable assumptions on the forecast date. These assumptions may change over the projected period and thus, our forecasts as at the valuation date could be different from the actual financial results and/or valuations conducted later on. Therefore, the forecasts cannot be related to on the level of confidence attributed to audited financial statement information and we do not express an opinion concerning the compatibility of our forecasts with the actual financial results received.

Economic valuation does not assume to be an accurate science and its conclusions in many cases depend on subjective considerations of the valuator. Therefore, there is no single undisputed fair value and we usually determine a reasonable fair value range. Since in this case, the purpose of the valuation requires a specific value, a value was determined which represents a reasonable assessment of the fair value of the assets valued. Although we believe that the value which we determined is reasonable, based on the information provided to us, another valuator may have reached a different value.

We wish to note that we have no personal interest in the Company, Delek Group or their securities, beside the fees paid to us for this paper. We are independent of the Company or Delek Group as defined in the Auditors' Law, 1955 and the regulations thereunder, including Auditors Regulations (Conflict of Interests and Reduced Independence because of Other Occupation) (Temporary Order), 2003, auditing standards, professional etiquette of the Israel Bar Association, and the resolution of the Securities Authority under section 9(B) of the Securities Law, 1968. We also note that our fees are independent of the results of this paper.

Below is further information required under the minimum disclosure guidelines required in valuations and with respect to them, and rules concerning appendices for reporting under the Securities Law, 1968, as published by the Securities Authority.

Contract information

The study was ordered by Delek Group Ltd.;

The contract between PwC Isr and Delek Group is dated January 26, 2012.

The valuator's information and professional experience

This paper was prepared by a team headed by Dr. Tzur Fenigstein, CPA, partner at Kesselman & Kesselman, and an expert in finance and valuations. Tzur holds a BA in Accounting and Economics and an MBA in Business Administration (Cum Laude) from Tel-Aviv University, and Ph.D in Philosophy (particulars of Dr. Fenigstein's education and professional experience are specified in Appendix 1).

Delek Group Ltd and Delek Automotive Ltd. were not evaluated by us in the last three years.

For any questions, please contact Dr. Tzur Fenigstein, CPA, at tel. 03-7954588 or Moran Sarussi, CPA, at tel. 03-7955048.

Sincerely,

Kesselman Finance Price Waterhouse Cooper Ltd.

Disclaimer

Our work is intended to be used by Delek Group management only and the purpose described in the accompanying letter only and it may not be used for any other purpose. We do not bear any liability, contractual or other, towards others, with respect to the services or any products or consulting provided.

Without our written consent, you may not transfer the product, as defined in the letter of intent between us, to any third party; publish anything we have provided or publicly refer to PwC Isr, Price Waterhouse Coopers or services, or guarantee or approve anything else based on the services. Under no circumstances, whether consent is provided or not, shall we be responsible towards a third party that our opinion is transferred to.

Notwithstanding the above, it is agreed that you will be permitted to attach the product of the valuation to reports under the Securities Law, 1968 or regulations thereunder, and to any other report submitted under securities laws, and we will cooperate as required, and without derogating from the generality of the aforesaid, including by signing the documents required for the above reporting.

During our work, we received information, as defined in the letter accompanying this work, from Delek Group, Delek Automotive and/or anyone on their behalf. The responsibility for the above information is that of its providers. Our work did not include checking and/or verification of the information which we received as aforesaid. In light of this, our work will not be considered and shall not represent approval of the accuracy and completeness of the information given to us. Under no circumstances will we be liable for any loss, damage, cost or expense incurred in any manner from fraudulent acts, false representations, deceit, provision of incorrect and incomplete information and withholding of information on the part of Delek Group, Delek Automotive and/or anyone on their behalf, or any other reliance on the aforesaid information, subject to that set forth above.

Since PwC Isr is in no way liable towards third parties in any matter concerning the services and product, the customer agrees to indemnify PwC and release it from any liability concerning any third party claim and/or demand arising from provision of the services and/or from the product supplied under this agreement and concerning any damages, arrangements, losses, liabilities, the related costs and expenses, including and without any limitation - reasonable legal fees, excluding if and as long as it is determined finally that these arose from grave negligence of PwC Isr or from mala fide unlawful behavior on its part with respect to the aforesaid services and/or product.

Under no circumstances, unless determined absolutely that PwC Isr acted with grave negligence or mala fide unlawful behavior, will PwC Israel bear liability towards Delek Group or any of its managers, directors, employees or shareholders or towards another third party, whether on damage or contractual grounds or any other claim or grounds for any amount beyond double the fees paid to us by Delek Group under the letter of intent with respect to the specific service which the claim concerns.

Although we were given financial and accounting information during our work, it did not include auditing of Delek Group and/or Delek Automotive's books under customary auditing laws. Therefore, we do not assume responsibility or express an opinion concerning the correctness of the information provided to us by Delek Group, Delek Automotive and/or anyone on their behalf.

Our work is not a due diligence test and should not be depended on as such.

Contents

<u>Chapter</u>	Page
1. Valuation summary	1
2. Description of the Company	2
3. Description of the business environment	11
4. Valuation method	28
5. Valuation	31
Appendices	
1 Appendix: CV of the valuator, Dr. Tzur Fenigstein	41

Chapter 1

Valuation summary

- Delek Automotive is a public company held by Delek Group (32%), the Company CEO, Mr. Gil Agmon, (38%), institutional investors and the public.
- Delek Automotive's main area of operation is import, distribution and sale of Mazda and Ford vehicles and spare parts.
- On December 13, 2011, Delek Automotive completed the acquisition of Kamor Motors Ltd. ("the Acquisition") The operations acquired in the acquisition are the import and sale of BMW and Mini Cooper vehicles and spare parts.
- PwC Isr was by requested by Delek Group to conduct a valuation of Delek Automotive aimed at examining whether there has been a decrease in the carrying value of Dekel Group's investment in the Company on the valuation date, upon implementation of IAS 28 and IAS 36 by the Group. To this end, we valued the value in use of Delek Automotive using the DCF method.
- The valuation of Delek Automotive's value in use was based on information and information sources included in the audited financial statements of Delek Automotive and Kamor Motors for 2006-2011, the Company management's budget for 2012, Delek Automotive management's valuations and forecasts, meetings with Delek Automotive management, other operating information, market research, and public information concerning the Company's area of operation.
- As with all economic valuations, this does not assume to determine the Company value accurately and attempts to reach a reasonable value range based on the information referred to above. Changes in this or other information may, of course, affect the valuation results.
- Following is the value in use of Delek Automotive as of the valuation date as valued under the provisions of IAS 28 and IAS 36 (in NIS millions):

NIS thousands	December 31, 2011
Value of Delek Automotive's operation	3,734
Financial liabilities, net	(705)
Value in use of Delek Automotive	3,028

- In our estimation, as at the valuation date, as described in this paper and under the provisions of IAS 28 and IAS 36, the recoverable amount Delek Automotive fluctuates between NIS 2.9 billion and NIS 3.2 billion ($\pm$ 5% of the value in use, as estimated using the DCF method).

Chapter 2

Description of the Company

Description of the Company's operation

Impact of exchange rate fluctuations on the Company's operation

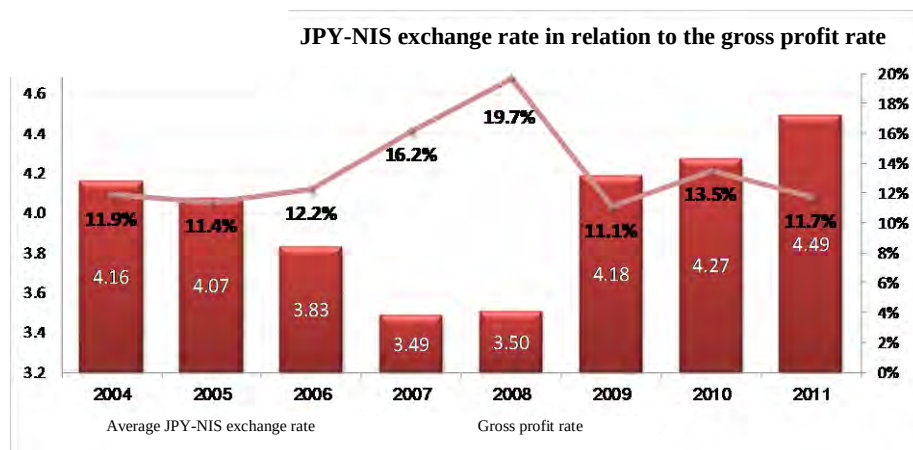
- As aforesaid, the Company purchases inventory in USD, Euro and primarily JPY. Exchange rate fluctuations in these currencies against the NIS may cause changes in the inventory purchase prices and could change the Company's sales volume and profitability.
- Its operations are also affected by the foreign currency cross-rates, primarily of the USD and JPY. This impact is expressed both in the Company's capacity to compete with the discounts and prices of its competition, whose import currency is primarily USD, and the Company's vehicle delivery mix.

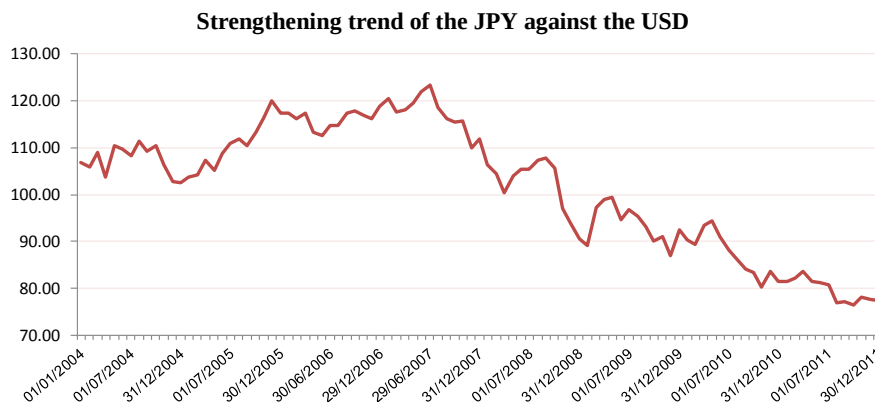
Recently, the USD has begun to erode against the JPY, impairing the Company's capacity to grant its customers discounts and attractive prices, like in the past on Mazda models, the leading vehicle brand in Israeli vehicle delivery over the past decade, while the Company's competition have shown attractive prices for their imported vehicles.

As a result thereof, in 2011, there was a substantial drop in the volume of Mazda deliveries and the Company's profitability from vehicles, while at the same time maintaining a relatively fixed delivery volume of Ford vehicles.

Due to the ongoing strengthening of the JPY in recent years, the global Mazda vehicle manufacturers have begun building a production plant for Mazda 2 and 3 models in Mexico, which is expected to be complete in 2014. This factory will allow Mazda to sell the vehicles in its production in both JPY and USD.

- The graphs below represent the correlation between the JPY-NIS exchange rate and the gross profit rate and the development of the USD-JPY cross-rate.





- Delek Automotive is a public company held by Delek Group (32%), the Company CEO, Mr. Gil Agmon, (38%), institutional investors (8%) and the public (22%).
- Since 1994, Delek Automotive operates through other companies and enterprises that it owns ("**the Company**") in two main areas of operation: Import and sale of vehicles and spare parts and provision of garage services.
- On December 13, 2011, Delek completed the Kamor acquisition through its subsidiary Delek Motors. Following completion of the acquisition, Delek Motors Ltd. holds 100% of Kamor Motors Ltd. shares. Under the acquisition, the BMW and Mini Cooper vehicle import and sales operations (including the trade-in operations) and the spare part operations in Israel were acquired.
- In the vehicle import segment, the Company imports, distributes and sells spare parts for all Mazda (mostly manufactured in Japan), and Ford (mostly manufactured in Europe) and also holds the franchise in Israel to distribute vehicles, accessories and spare parts made by Lincoln, although as of the valuation date, the Company does not sell these vehicles and spare parts.

The Company's deliveries are to private and institutional customers, such as leasing companies, car hire companies and the Government Vehicle Administration, while the rate of vehicle deliveries to private customers in 2009, 2010 and 2011 was 36%, 33% and 38% respectively of the Company's total vehicle deliveries.

Marketing and distribution are carried out through the Company's showrooms and those operated by independent agents. The marketing and distribution operations of Mazda and Ford vehicles are carried out through eight Company showrooms and eight operated by independent agents. The sales and marketing operations of BMW vehicles are carried out directly by the Company through three showrooms and direct sales by the Company's franchisee. The sales and marketing operations of Mini Cooper are conducted through a separate showroom.

- In the spare parts and garage services segment, the Company engages in the import, distribution and sale of spare parts for all Mazda, Ford, BMW and Mini Cooper vehicles. The spare parts are supplied to the Company by the different vehicle manufacturers. The Company imports the spare parts primarily from Japan and Europe. It also operates service centers (central garages) where it provides maintenance and repair services to its customers as well as support and training services for the network of agents and services centers of Mazda, Ford, BMW and Mini Cooper vehicles.

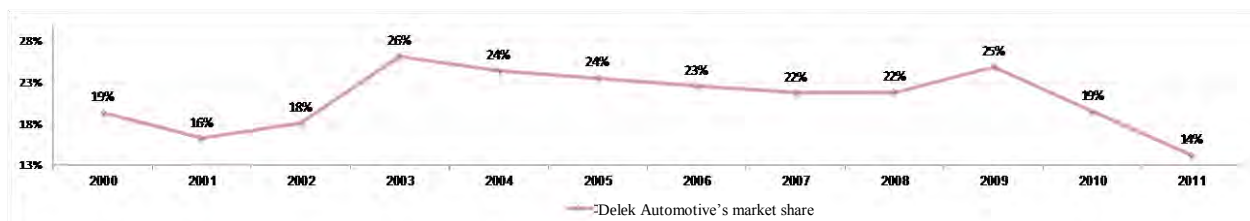
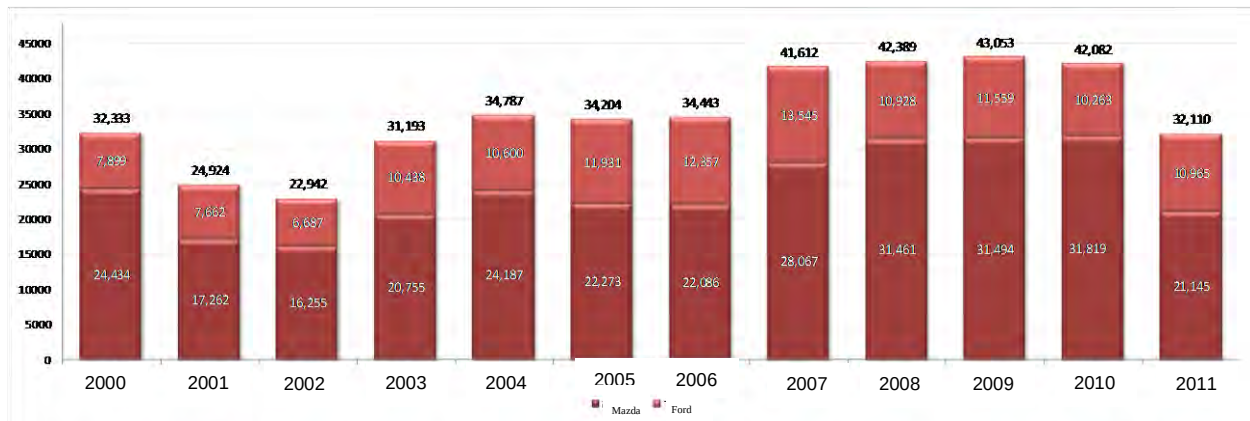
The Company's main customers in the spare parts and garage services are service centers, distributors, the central garage's customers, institutional customers and insurance companies.

The spare parts marketing and distribution operations are carried out through garages authorized as service centers and also through different spare parts traders and distributors in Israel.

- The Company's operations in the vehicle and spare part import segment are conducted in foreign currency. Therefore, it is exposed to exchange rate fluctuations of those currencies.

Vehicle deliveries and market share

The following graphs show data concerning the Mazda and Ford deliveries and the Company's market share in 2000-2011.



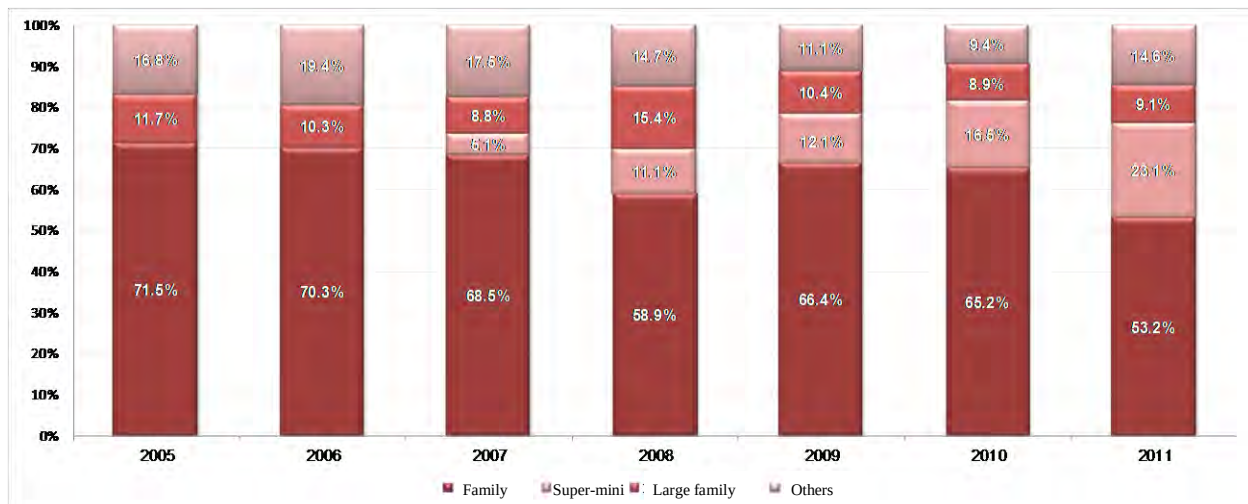
Vehicle deliveries

- In 2011, the Company's Mazda and Ford vehicle deliveries totaled 32,110 new cars compared to 42,082, 43,053 and 42,389 in 2010, 2009 and 2008 respectively.
- Between the last quarter of 2008 and the second half of 2009, the Company's deliveries were affected by the global crisis whose signs were also felt in the Israeli vehicle market and expressed in a sharp decline in demand for new vehicles. With recovery from the crisis in the second half of 2009, the Company's deliveries grew and it ended 2009 with record deliveries and a market share of 24.9%. Since 2010, with the strengthening of the JPY exchange rate in parallel to the weakening of the USD rate (cross-impact), the Company recorded a decline in market share to 19.5%. In 2011, the cross-impact trend of the strengthening JPY against the USD continued, affecting the demand for Mazda vehicles.
- All in all, the Mazda deliveries totaled 21,145 in 2011 (66% of Mazda and Ford deliveries), 31,819 in 2010 (76%), 31,494 in 2009 (73%) and 31,461 in 2008 (74%). The change in delivery mix between Mazda and Ford was also affected by launching of the new Ford Focus in the last quarter of 2011, as described further on.
- In the last three months of 2011, Mazda deliveries totaled 2,805 only (43.7% of Mazda and Ford deliveries).

The following graph shows the monthly distribution of rate of Mazda and Ford vehicle deliveries and the Company's deliveries of the total market vehicle deliveries in 2011 and the initial two months of 2012:



The following graph shows the data concerning the distribution by category of the Company's Mazda and Ford deliveries in 2005-2011



- The Company imports, sells and distributes cars belonging to different categories, mainly the following: The family, large family (executive), super-mini, leisure-off-road, and mini-van (others) categories.
- In recent years, changes have occurred in the Company's delivery mix based on categories in parallel to the market trends. The super-mini category has displayed a steady rise since 2007 at the expense of a decline in the remaining market segments, including the leisure-off-road vehicles and mini-vans.
- The Mazda 2 along with the Ford Fiesta led the vehicle deliveries in the super-mini category.
- At the end of 2011, the Company launched the new Ford Focus model, which is expected to strengthen the vehicle deliveries in the family category. Furthermore, in 2012, other models in different categories are expected to be launched, including the Mazda CX5 mini jeep in March (leisure-off-road) and the new Mazda 6 in the third quarter (large family), both equipped with Mazda's new SkyActive engines, characterized by low pollution rating and relatively low fuel consumption for gasoline cars. The other launches anticipated in 2012 include Ford Transit models in June-July (commercial), Ford Kuga in September-October (leisure-off-road) and the new Ford Connect in September (light commercial).
- Following the foregoing Kamor acquisition of December 13, 2011, the Company began importing and marketing cars in the luxury and premium categories.

Strengths and critical success factors

- **Existence of a wide product line** - the Company imports, sells and distributes models designed for different market segments to create a wide product portfolio that provides a solution for the different vehicle market categories.
- **Trade relations with the manufacturers** - the Company maintains trade relations with Mazda and Ford manufacturers for close to two decades, allowing it to obtain good vehicle purchase prices and other conditions that enable it to compete in the Israeli market.
- **Trade relations with leasing and car hire companies** - the Company has good trade relations with the leasing and car hire companies, which are key customers.

Key risks and weaknesses

- **Dependence on manufacturers** -the Company depends entirely on the manufacturers of the vehicles which it imports. Non-renewal or cancellation of the agreements will materially affect the Company's business. The Company is also dependent on the models produced by the manufacturers and the cost determined by them.
- **Currency exposure** - exchange rate fluctuations of the currencies in which the Company purchases the vehicles that it sells, JPY, USD and Euro, may affect its profitability. Cross-rate fluctuations may affect its capacity to compete with its competition.
- **Licenses and permits** - the Company operates as a vehicle importer to Israel and other countries subject to licenses and permits. Cancellation of licenses and/or permits and/or impairment in their conditions may adversely affect the Company's sales and financial results.
- **Intensification of competition in the spare parts market and decrease in prices** - mainly following an order issued by the Antitrust Commissioner allowing servicing at non-authorized garages (i.e. no commitment to buy spare parts from the Company).
- **Committees for increasing competition in the vehicle market** - an industry risk stemming from possible regulatory changes in the industry due to the work of the Zelicha Committee for Examination of Competition in the Vehicle Market (primarily the option examined was restricting the number of brands imported by a single importer).

Financial results

The following represents Delek Automotive's consolidated and audited statements of income for 2009-2011:

NIS thousands	2009	2010	2011*
Sales	4,743,628	4,609,858	3,663,896
Vehicle sales	4,360,592	4,191,322	3,260,455
Spare parts and garage service sales	383,036	418,536	403,441
Cost of sales	4,218,468	3,986,275	3,235,523
Gross profit	525,160	623,583	428,373
Gross profit rate (%)	11.1%	13.5%	11.7%
Sales and marketing expenses	40,477	45,251	44,234
General and administrative expenses	27,781	29,711	28,163
Increase in value of investment property under construction	-	1,000	750
Other revenues	329	212	81
Operating profit	457,231	549,833	356,807
Operating profit rate (%)	9.6%	11.9%	9.7%
Financing income	124,675	79,286	16,607
Financing expenses	(17,647)	(60,503)	(210,228)
Company's share of profits of associates	1,446	1,476	1,627
Profit before income tax	565,705	570,092	164,813
Income tax	131,980	142,228	38,945
Net profit	433,725	427,864	125,868

* The operating results shown in the financial information for 2011 exclude Kamor's results, the acquisition of which was completed on December 13, 2011.

Analysis of financial results

- Most of the Company's revenues stem from its commercial operations in the vehicle import and sales segment, which represented 91% of its total revenues in 2009-2011.
- In 2011, the Company recorded a decrease in revenues from NIS 4,609.9 million in 2010 to NIS 3,663.9 million in 2011. This drop in its revenues arose mainly from the decline in vehicle deliveries which as stated above totaled 32,110 in 2011 compared to 42,082 in 2010. This decrease in vehicle deliveries already began in 2010, after the Company achieved a relatively high volume for all deliveries in the car market in 2009 and recorded a record share of 24.9% in relation to the last four years.
- According to the Company management, the decrease in market share in 2011 arises primarily from impairment of the Company's competition capacity, because of the strengthening of the Japanese vehicles during the year along with the weakening of the currency in the countries of origin of the competition's imports. The Company's capacity to compete was impaired in 2011, because until the fourth quarter of 2011, it sold an old Ford Focus model which was launched over six years ago, while its competition benefited from new models.
- The Company's car sale cost over the years is volatile and affected mainly by exchange rate fluctuations of the currencies in which it purchases the vehicles, primarily JPY, and its volume of deliveries. Based on the trends described above, the Company's vehicle sale cost rose from 87.3% in 2010 to 89.6% in 2011. The analysis of the Company's vehicle sale cost in 2006-2011 shows that its average vehicle sale cost percentage was 86.9%.
- The vehicle sale cost is a primary factor impacting the Company's gross profitability. Based on the trends described above, the Company's gross profit rate dropped from 13.5% in 2010 to 11.7% in 2011. It should be noted that according to the Company management, an improvement in the Company's gross profitability is expected, due to of launching the new Ford Focus. This improvement was not yet expressed in 2011 due to its launch only in the last quarter the year and the volume of discounts granted to customers for the sale of the old Ford Focus inventory towards arrival of the new model.
- The Company's operating profit in 2011 amounted to NIS 356.8 million compared to NIS 549.8 million in 2010 and NIS 457.2 million in 2009. The operating profit percentages of the total revenues in these periods were 9.7%, 11.9% and 9.6% respectively and were primarily affected by the vehicle sales price changes in these periods.
- The Company's net profit in 2011 was NIS 125.9 million compared to NIS 427.9 million in 2010 and NIS 433.7 million in 2009. The high fluctuations in the Company's net profit in these periods were affected by revaluation of loans and liabilities to suppliers for exchange rate fluctuations, mainly of the JPY, and revaluation of the fair value of financial assets measured through profit and loss. In 2011, the Company's net finance expenses totaled NIS 193.6 million compared to net finance income of NIS 18.8 million in 2010 and NIS 107.0 million in 2009.

The following shows Delek Automotive's consolidated, audited balance sheets as at December 31, 2009-2011:

NIS thousands	2009	December 31 2010	2011*		2009	December 31 2010	2011*
<u>Current assets</u>				<u>Current liabilities</u>			
Cash	17,637	3,843	323,055	Borrowings from banks and others	519,716	582,857	1,232,079
Customers	1,052,027	1,258,653	668,991	Current maturities of debentures	-	-	15,906
Other receivables	23,363	14,538	27,510	Trade payables	984,603	1,264,779	728,150
Taxes receivable	2,791	1,774	32,580	Other payables	199,833	171,150	147,445
Inventories	619,262	955,054	920,264	Current tax liabilities	19,570	5,182	3,860
Total current assets	1,715,080	2,233,862	1,972,400	Dividend declared	113,731	155,492	-
				Total current liabilities	1,837,453	2,179,460	2,127,440
<u>Non-current assets</u>				<u>Non-current liabilities</u>			
Customers	341,935	81,080	-	Debentures	-	-	33,408
Loans	33,229	34,531	42,199	Liability for issuance of restricted shares	32,612	8,124	-
Investments in associates and partnerships	31,599	35,294	37,405	Bank loans	4,529	4,414	4,002
Investments in available-for-sale financial asset	93,353	-	-	Employee benefit liabilities	1,389	1,956	2,889
Securities at fair value through profit or loss	83,050	218,456	184,508	Deferred taxes	-	7,076	15,768
Investment property	-	-	9,785	Total non-current liabilities	38,530	21,570	56,067
Investment property under construction	23,778	27,661	38,661				
Property, plant and equipment	242,057	234,481	247,907				
Intangible assets	-	-	88,451				
Goodwill	-	-	147,820				
Deferred taxes	1,744	415	487				
Total current assets	850,745	631,918	797,223	<u>Equity</u>	689,842	664,750	586,116
Total assets	2,565,825	2,865,780	2,769,623	Total equity and liabilities	2,565,825	2,865,780	2,769,623

* The December 31, 2011 balance sheet includes the merger of Kamor, the acquisition of which was completed on December 13, 2011.

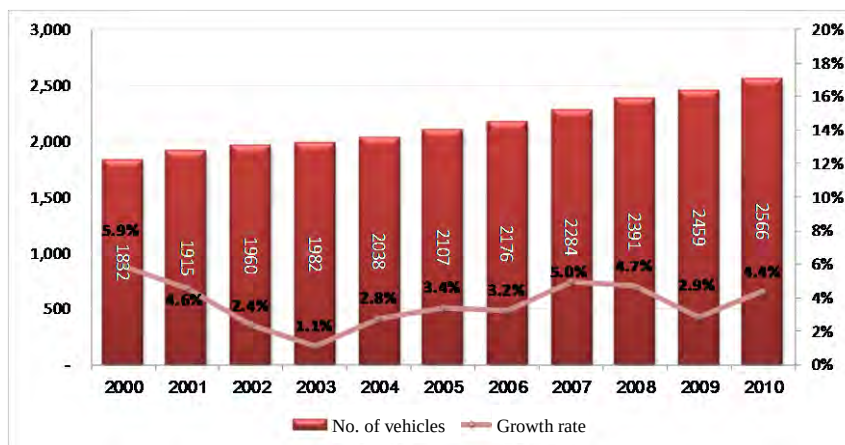
Chapter 3

Description of the business environment

The private car market

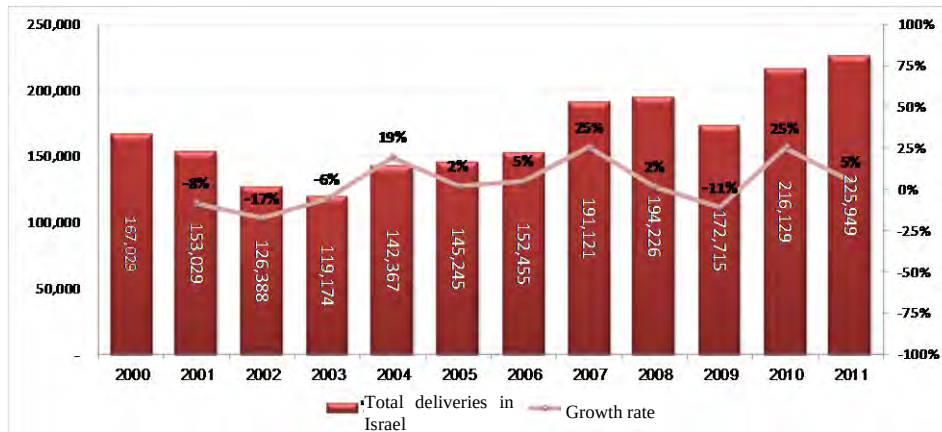
General

- The Israeli car market consists of the primary market, i.e. the new car market which is mostly sold by the car importers, and the secondary market, i.e. the second-hand car market. There is not private car industry in Israel and vehicles are imported at prices fixed in negotiations in a sophisticated global market environment between the overseas manufacturers and the Israeli importers.
- The Israeli car market differs from most others worldwide due to its geographic isolation and high import taxes (purchase taxes of up to 112% of the CIF price for European and US cars and 127% on those from Asia, including customs duty and VAT). The high customs duties together with the level of available income, the low measure of development infrastructures compared to other western countries and the proximity between Israel's population centers are the main factors for the low Israeli motorization rate compared to Western Europe and the US.
- In recent years, the number of motor vehicles in Israel has grown, where in 2010 there were 2.5 million, a 4% rise compared to 2009. The import value of vehicles in Israel also climbed in 2010 to USD 4 billion compared to USD 3.2 billion in 2009.
- The Israeli car market includes several importers of cars from different places worldwide. The market is characterized by fierce competition because of the relatively large number of players and a limited buying potential. Currently 21 vehicle importers compete in the market, when the eight major importers together hold 80% of the market share in this segment. In 2010, the car market reform entered into force, allowing parallel import. The reform enables car importers to contract with a car manufacturer or a car manufacturer's authorized agent to import a car to Israel which is also imported by the direct importer, as described further in this chapter.
- The following graph describes the development of the number of vehicles in Israel in the last decade (thousands):



- One of the obvious indices to examine the growth trends in the private car market is the new car delivery index. In the last decade, the quantity of new vehicle deliveries in Israel* soared from 167,029 in 2000 to a record 225,814 in 2011.
- The quantity of deliveries between 2007 and 2010 was characterized by many fluctuations, while from end 2008 to end 2009 there was an exceptional drop in demand arising, inter alia, from the global recession and credit crisis, which impaired the leasing companies - the primary customers in the Israeli car industry.

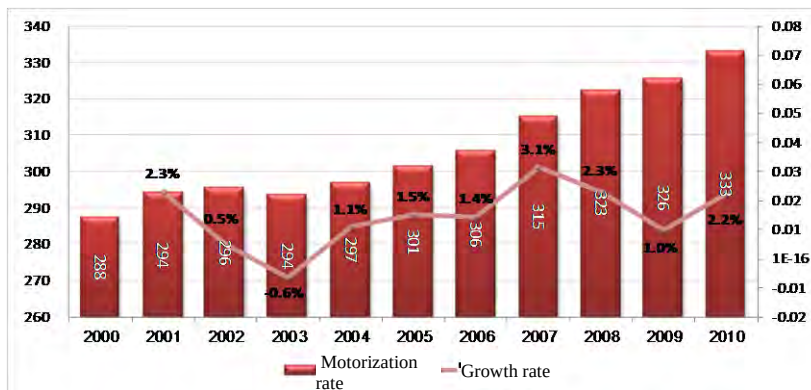
- In 2010, the demand for new vehicles strengthened due to recovery from the economic crisis. Most of the growth in demand stemmed from increased purchases of the leasing companies and purchases which were postponed because of the crisis in 2009.
- In 2011, the growth rates continued and 225,814 new vehicles were delivered, reflecting 4.5% growth compared to the same period the previous year. However, the vehicle importers believe that with respect to 2012, a drop in demand on the part of the private and leasing customers is expected compared to the demand in 2011.
- The following graph describes the new vehicle deliveries in Israel* between 2000 and 2011 and the annual growth rate:



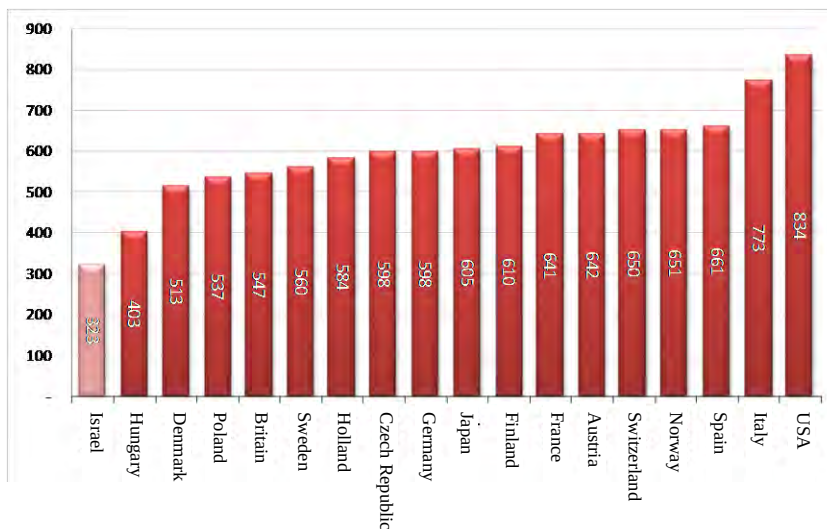
- It can be said that there is correlation between the volume of new car deliveries and the economic situation. So in the periods of economic slowdown (2002-2003 and end 2008 to end 2009) a sharp decline in demand for cars and an increase in the car importer's inventory were recorded. By comparison, in the years following the slowdown periods, which are usually characterized by high growth, an upturn in demand for new vehicles and high sales volumes were recorded (2007-2008 and 2010-2011). One of the key factors affecting this correlation is the volume of purchases of the leasing companies as set out above, which freeze the demand during slowdowns and accelerate it during growth.

* Excluding bus, truck and motorcycle deliveries.

- The motorization rate is measured by the quantity of vehicles per thousand inhabitants and is the most common index in international comparisons in matters concerning economic development and environmental protection. The motorization rate in Israel increased steadily in the past decade. In 2010, the motorization rate was 333 cars per thousand persons while in 2000 it was 288 cars per thousand persons, an average annual increase of 1.4%.
- The growth in motorization rate stems mainly from the private sector. In the last decade, the compound annual growth rate (CAGR) of private vehicle and motorcycle motorization was 1.8% and 2.0% respectively, while there was a decline in the motorization CAGR of commercial vehicles, such as trucks and minivans, of 0.5% and 2.8% respectively.
- The following graph describes the development of the motorization rate in Israel:



- The motorization rate in Israel is low compared to other western countries. For comparison, the USA motivation level is 850 cars per 1,000 residents and in other countries like Norway, Spain, Austria, Japan and Switzerland, it is 600-700 per thousand residents.
- The following graph describes the motorization rate in Israel compared to other western countries, in 2008.



Customers

- The customers may be divided into three main groups:
 - **Private customers** - this group includes private individuals who usually purchase a car for private use, while in most cases one vehicle is purchased in a single transaction.
 - **Corporate customers** - this group includes companies, businesses and various organizations such as government institutions. These customers purchase vehicles for their business operations and as company cars for their employees. Mostly, vehicles are purchased in collective purchases, allowing the granting of quantity discounts and better credit terms.
 - **Leasing and car hire companies** - this group includes companies offering short or long term vehicle hire/leasing services. The companies designate the vehicles for private companies and customers. The majority of leasing purchases are for businesses. The leasing companies are the primary customer in the purchase of new vehicles, inter alia, because of high volume purchases and high turnover of fleet vehicles (every three years). It is noted that some of the leasing companies have direct or indirect ownership relations with one or other vehicle importer.
- There is a difference in the considerations between private customers, corporate customers and leasing companies in selecting vehicles. Private customers are affected primarily by parameters including: Price, personal income level, decline in vehicle value, mechanical characteristics (engine capacity, fuel consumption, accessories), insurance, comfort and design, while the considerations of the corporate customers and leasing and car hire companies include: the discount rate for a collective purchase, value in use (preference for vehicles where the taxes imposed in their use are attractive for their customers), list price (this price is not the purchase price, but the higher the price, the higher the inventory value) and credit terms.
- The vehicle industry is characterized by relatively high customer loyalty among private customers. Private customers who purchase a vehicle and are satisfied with it will be inclined to purchase it again. On the other hand, the leasing companies and corporate customers are characterized by low loyalty since from most of their viewpoints the price and benefits are the primary consideration to conduct a transaction.

Competition

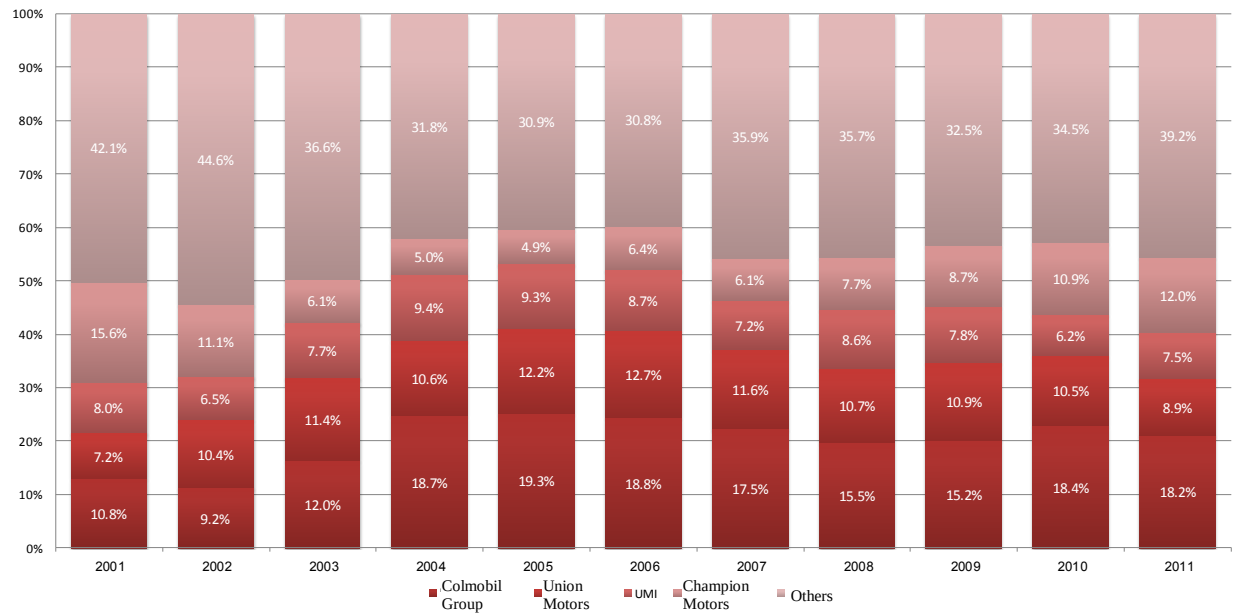
- The Israeli vehicle industry includes several importers, while each represents one or several global vehicle manufacturers.
- Since April 2010, following the vehicle market reform, there are several parallel import options. Accordingly, importers may import the same make and standard of car as the direct importer. Until the reform, the market was characterized by an oligopoly structure since every importer held the exclusive franchise of one or more specific manufacturers. As a result of this market structure, most of the competition occurs between vehicles belonging to the same category and not necessarily between the variety of different vehicles of that importer. It should be noted that as of the valuation date, despite the reform, there is still no parallel representation of a specific manufacturer by more than one importer.
- The rate of competition in the Israeli vehicle industry is high and affected mainly by factors such as positioning, price and service level. Product positioning is one of the most important parameters which importers always invest in to market the vehicle which they import as "luxury", "safe" or "reliable", and to motivate the customers to buy a specific vehicle as opposed to competing vehicles. The industry's marketing methods include launching new models, expanding the imported vehicle range and offering attractive payment terms, special offers and discounts.
- The Israeli vehicle industry is characterized by fierce competition in all types of vehicles (small, family, off-road, etc.). In 2011, over 45% of the market share of new vehicle deliveries was held by five leading brands (Hyundai, Mazda, Toyota, Kia and Chevrolet), which enjoyed high demand in both the private and institutional markets. Over the years, the competition between the two

leading brands, Mazda and Hyundai, has decreased in the sales table, because of the success of the new models which Hyundai launched and the development of the mini category following the green tax reform. In 2010, Mazda led with a market share of 14.7% of the new car deliveries while Hyundai's market share was 14.1%. In 2011, Hyundai became Israel's best-selling brand with a market share of 14.6% with Mazda in second place with a market share of 9.4% only.

- Currently, most of the industry's operations are carried out by ten vehicle importers which imported 94% of the total new vehicles delivered in 2011.
- The main vehicle importers are (market share in 2011):
 - Colmobil Ltd. - Mitsubishi, Hyundai, Mercedes and Smart importers (18.2%);
 - **Delek Motors Ltd., Mazda, Ford, BMW and Mini Cooper importers (14.7%*);**
 - Champion Motors Ltd. - Volkswagen, Skoda, Audi and Seat importer (12.0%);
 - Union Motors Ltd. - Toyota and Lexus importer (8.9%);
 - Carasso Motors Ltd. - Renault-Nissan and Infiniti importer (8.4%);
 - Telcar Ltd. - Daihatsu, Kia and SsangYong importer (8.1%);
 - Universal Motors Ltd. Delek Automotive - Chevrolet, Buick, Cadillac, Opel and Isuzu importer (7.5%);
 - David Lubinski Ltd. - Peugeot and Citroen importer (6.9%);
 - Automotive Equipment and Vehicles Ltd. - Chrysler, Porsche, Jeep, Suzuki and Dodge importer (5.9%); and
 - Mayer's Cars and Trucks Ltd. - Honda, Volvo and Jaguar importer (3.7%).
- Since 2001, there has been no material change in the market share of the key private vehicle market players. However, Carasso and David Lubinski's market share declined from 8% and 13% respectively in 2001 to 4% and 7% respectively in 2011. In contrast, the market shares of Korea Motors and Colmobil rose from 2% and 11% respectively in 2000 to 7% and 18% respectively in 2011.
- Delek Automotive, which was the largest importer in the market for over a decade, maintained a market share of 22% in 2001-2010, but recorded a decline of 14% in 2011. In 2011, for the first time in the last decade, Colmobil Group held the largest market share. From analyzing the market shares, it can be seen that the five large importers maintained their relative overall share of the market, while the remaining importers together represented 30%-40% of the total market.

* Including the BMW and Mini Cooper market share in 2011, even though these were acquired as part of the Kamor acquisition only in December 2011.

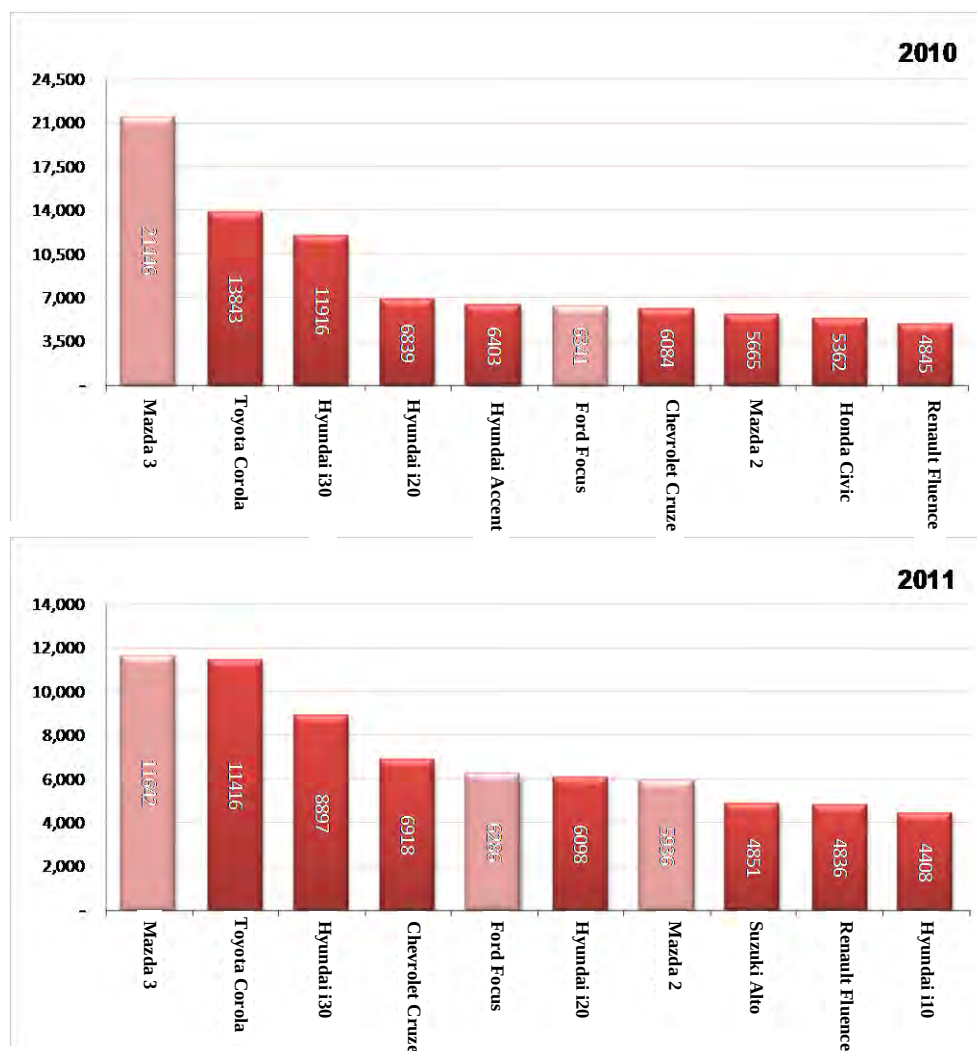
- The following graph describes segmentation of the market share (quantity of new vehicles delivered) by main importer in 2001-2011 (%):



The following shows the segmentation of new car deliveries by brand in 2009-2011:

Brand	No. of vehicles delivered in 2009	Market share	No. of vehicles delivered in 2010	Market share	No. of vehicles delivered in 2011	Market share
Hyundai	20,305	11.8%	30,453	14.1%	33,060	14.6%
Mazda	31,494	18.2%	31,819	14.7%	21,145	9.4%
Toyota	18,401	10.7%	22,289	10.3%	19,719	8.7%
Kia	4,214	2.4%	9,513	4.4%	15,606	6.9%
Chevrolet	11,492	6.7%	9,734	4.5%	13,937	6.2%
Suzuki	6,277	3.6%	12,218	5.7%	12,155	5.4%
Volkswagen	7,481	4.3%	11,514	5.3%	11,762	5.2%
Ford	11,559	6.7%	10,263	4.7%	10,965	4.9%
Nissan	6,987	4.0%	6,784	3.1%	10,030	4.4%
Skoda	4,980	2.9%	7,491	3.5%	9,221	4.1%
Renault	5,196	3.0%	8,019	3.7%	8,785	3.9%
Peugeot	4,429	2.6%	6,063	2.8%	8,104	3.6%
Citroen	6,006	3.5%	6,250	2.9%	7,565	3.3%
Honda	7,882	4.6%	8,275	3.8%	7,271	3.2%
Mitsubishi	4,969	2.9%	8,432	3.9%	6,950	3.1%
BMW	950	0.6%	1,017	0.5%	1,101	0.5%
Mini Cooper	38	0.0%	96	0.0%	135	0.1%
Others	20,055	11.6%	25,899	12.0%	28,438	12.6%
Total	172,715	100%	216,129	100%	225,949	100%

The following graphs show the quantity of deliveries of the ten best-selling models in 2010-2011*:



- The three top selling models in 2010 maintained their position in 2011.
- Chevrolet Cruze and Mazda 2 grew (in annual terms) by 14% and 5% respectively in delivery quantity in 2011 compared to 2010.
- Mazda 3, Toyota Corolla, Hyundai i30 and Hyundai i20 showed a decrease (in annual terms) of 46%, 18%, 25% and 11% respectively in 2011 compared to 2010.
- In 2011, Suzuki Alto and Hyundai i10 managed slide up the top ten list at the expense of Hyundai Accent and Honda Civic.

*Source: Israel Vehicle Importers Association.

Trends

- The Ministry of Transport's declared policy is to encourage the use of alternative ignitions to reduce air pollution and vehicle fuel consumption. In June 2009, the Finance and Environmental Protection Ministers announced a plan to create economic incentive to reduce environmental pollution. As part of the plan, a "green scale" was fixed for rating vehicles according to pollution level measured by the weighted public costs of pollutant emissions, and the purchase tax is calculated on the basis of this rating. Moreover, reduced purchase tax was fixed for hybrid cars (30%) and pollution-free cars (e.g. electric cars) (10%), for several limited years, subject to the pollution level of these vehicles.
- **Hybrid cars** - in 2008, for the first time ever the Ministry of Transport approved the import of hybrid cars, which integrate gasoline and electric engines, and in December 2010 it approved the import of hybrids combining diesel and electric engines. As of December 2010, there are over ten thousand hybrid cars and eight thousand hydrocarbon gas-powered cars (cooking gas) on Israel's roads. The hybrid car market share in Israel is similar to that in other western countries, i.e. 2%. The hybrid car prices are higher than those of cars sold by the importers in the parallel categories, despite their substantial tax breaks. In 2011, the hybrid category began to stir with deliveries of 2,000 units in the first half of the year compared to 3,000 units in 2010. The category includes 11 cars, the most obvious being Honda Insight and Toyota Prius, each with a market share of a third.
- **Electric cars** - as part of the increasing environmental awareness as well as the rising fuel prices, the leading vehicle manufacturers worldwide have begun selling economical and hybrid cars and developing electric cars. Car manufacturer Tesla Motors was the first, when it began developing the Tesla Roadster in 2004 and selling it in 2008. Since 2010, other car manufacturers, such as Mitsubishi and Nissan began selling electric cars in the US and other countries across the globe.
- In Israel, a business initiative called Better Place, which was founded in 2007 by Shai Agassi, began operating with the aim of converting the fuel-based transport infrastructure into a renewable energy based infrastructure. The Better Place project defines several components: Electric car, charging infrastructure deployed at stations throughout Israel, and service. This is in addition to the business model which is part of the package. The model is similar to that of the mobile phone companies - a monthly payment for use of the charging services. In November 2010, for the first time ever Better Place received Ministry of Transport approval to import 13 Renault electric cars and in 2011 it began selling them.
- In November 2010, the Ministry of Transport also approved the import by Carasso of a Renault Kangoo prototype and two weeks later, the import by Colmobil of three Mitsubishi trial electric cars. In December 2010, David Lubinski received Ministry of Transport approval to import two electric cars, Peugeot and Citroen.
- **Chinese cars** - the Chinese car market has developed quickly in recent years. Currently, China has over a hundred vehicle manufacturers, although most of them do not sell outside China. In April 2010, the Ministry of Transport for the first time approved testing a SAIC prototype at the Regulation Department for Chinese Vehicles. SAIC is China's largest vehicle manufacturer, mainly for the domestic market. Based on documentation submitted to the Ministry of Transport's Vehicle Division, the Chinese cars meet the Israeli vehicle standards, including the break and lighting systems
- In May 2010, the import of MG SAIC models by David Lubinski was approved. This was approved despite the numerous difficulties stemming from the great differences in attention to safety and air pollution between Chinese products and the current norm in western countries.
- Until recently, most Chinese products failed to achieve sufficient results in crash tests and problems of compliance with Euro 5 air emission standards were also discovered.

- In 2012, the Chinese vehicles are not expected to reach the market since the demand in the Chinese market exceeds the supply. Therefore, the Chinese car manufacturers have no reason to invest the capital required to market and adapt the vehicles to the stringent European crash and emission standards.
- **Luxury categories** - In 2009-2010, deliveries of traditional luxury cars in Israel began to rise. This trend changed in 2011 and most luxury categories dropped relative to 2010, due, *inter alia*, to a change in mix of the luxury categories. In practice, the leisure-off-road luxury car category strengthened at the expense of traditional luxury cars and in 2011 increased by 21% compared to 2010.

Mini and super-mini cars -

- In the last two years, a fuel price rise trend began in combination with the reforms encouraging the transition to "cleaner" vehicle, such as the green tax, which increased the small vehicle sales. This trend led to a rise in sales of vehicles in the fuel-saving mini and super-mini category and a rise in sales of environmental-friendly vehicles, such as the hybrids. Consequently, the market share of brands selling small, economical vehicles grew on account of others in the industry. The demand for cheap, economical vehicles also led to a drop in prices of the more established cars belonging to the mini category and launching of new mini cars.
- The low prices offered in the mini category intensified the competition in the segment and simultaneously even affected the prices of the super-mini category. Recently, the prices of models belonging to the category decreased substantially and consequently, sales of vehicles in the larger categories, such as the compact-families, were impaired. As of the valuation date, the Company has no model in the mini category. The Company's Mazda 2 and Ford Fiesta models are more luxurious and thus belong to the super-mini category. The main competition in this category are: Hyundai i20, Seat Ibiza, Opel Corsa and Daihatsu Sirion.
- The deliveries of the mini category increased substantially from 2,500 in 2009 to over 8,000 in 2010 and 20,000 in 2011.
- The super-mini deliveries also grew, despite the new popularity of the competing mini category. The volume of vehicle deliveries in this category rose from 13,000 in 2009 to 28,000 in 2010. In 2011, the super-mini category increased by 4%, a rate similar to that of the entire market.
- In 2012, as part to the growing trend of the mini and super-mini categories and the increasing competition, further price decreases of small cars and the entry of new contenders in the segment are expected.

Regulation

- In recent years, the Ministry of Finance and Ministry of Transport have been taking steps to reduce the market concentration in the Israeli vehicle industry and introducing tax, standardization and regulation reforms. Among the goals of these reforms are: Opening the vehicle market to competition, reducing the market concentration level, decreasing the air pollution levels and increasing the safety level of the vehicles. Following is a description of the obvious trends in the industry:
- **Parallel import of vehicles to Israel** - In April 2010, the Control of Commodities and Services Order (Vehicle Import and Servicing)(Amendment), 2010 allowing parallel import entered into force. Under the order, a vehicle importer will be permitted to contract with an imported vehicle manufacturer or its authorized agent and import into Israel passenger vehicles weighing no more than 3.5 tons of the same make and standard as imported by the direct importer. To receive a vehicle import license, the applicant must comply with the terms prescribed by the competent authority, e.g. being a duly registered corporation, having bank guarantees in the amounts fixed and a marketing and maintenance system. The order also stipulates that a parallel importer may not import over three vehicle brands, subject to the authority's capacity to change the number of products for compliance with the terms fixed in the order.

The purpose of the parallel import reform is to allow entry of new competition into the market, which may bring about increased competition primarily in certain market segments, such as the luxury and executive cars. Currently, the impact of parallel import has not yet been felt in practice, the main reason being the difficulty of the parallel importer to purchase large quantities of inventory (like the primary importer), and thereby to obtain a quantity discount and compete with the primary importer. Another reason is the lack of garages held by the parallel importer to receive auxiliary services as with the primary importer.

- **Green tax** - In August 2009, a new taxation method entered into force aimed at creating economic incentives to reduce environmental pollution. A green index which rates the vehicles on the basis of their pollution level was fixed as part of the green tax reform. Purchase tax is determined according to this rating. Therefore, since November 2009, purchase tax of 83% is imposed on a new vehicle, with a fixed tax reduction based in the measure of the vehicle benefit based on the green index, while the tax benefit fluctuates between NIS 2,000 and NIS 15,000 based on the green index. Reduced purchase tax of 30% and 10% is also imposed on hybrid and electric vehicles respectively, subject to their pollution level. The green tax primarily increased the luxury vehicle prices, while the impact on the family cars is not material. One of the effects of the green tax combined with the fuel price rise is growth of the mini car category in Israel as aforesaid.
- In August 2010, the Tax Authority announced that as from 2012 it intends updating the division into the pollution levels so that the conditions for the relatively low pollution levels will be stricter.
- **Linear value in use method** - the value in use is the amount for the gross salary of an employee who has a company car from the employer and is the financial value of the benefit for private use of the car. Until January 2010, the customary value in use method was based on groups under which distribution of the vehicles was based on seven price groups, while the value in use was determined as a fixed amount in every company. The group price method led to substantial differences in some of the vehicle prices in the industry and allowed substantial discounts to leasing companies for vehicle purchases. As a result, it was decided that as from January 2010, the value in use of a vehicle would be calculated as a percentage of the vehicle consumer price.
- The connection between the value in use and the vehicle value could be an incentive of the vehicle importers to reduce the car prices. The calculation method change also reduces the obligation of the importers to match the car prices to the price groups and expands the ability of employees with company cars to choose cars from different price categories. The linear value in use method in combination with the green tax reform also allows employees to benefit from a vehicle with a lower value in use by choosing less polluting vehicles, which are charged lower purchase tax and lower consumer prices accordingly. However, increasing the value in use gradually since 2008 through 2011 as set out in the new income tax regulations could lead to a reduction in demand for operating leasing and, accordingly, a drop in the volume of vehicle purchases by the leasing companies which will be partially offset by the transition to employees' direct purchases.
- **Safety accessories** - in recent years, there is a global trend concerning the safety level of vehicles. This trend also affects the vehicle industry in Israel. The purchase tax imposed on a vehicle is affected, *inter alia*, by credit granted for installing safety accessories in the vehicle.

As part of the green tax reform, it was decided in November 2009 to reduce the purchase tax for a vehicle to 83% against cancellation of the tax benefit for the stability control system (EPS), because as of January 2010, the vehicle importers are committed to market vehicles equipped with an EPS, excluding the types of vehicles exempt from installation under the European standards. Moreover, the law obliges installation of other safety accessories, like: Two air cushions minimum and an ABS system which prevents skidding on wet or smooth roads.

- **Recording the vehicle manufacture date on the license** - On April 1, 2008, an amendment to the Transport Regulations, 1961 canceling recording the vehicle manufacture year on the license entered into force. Instead, the date the vehicle reaches the road is recorded in the license since then. Entities in the industry believe that this change may possibly be another consideration of

car buyers with respect to the date of purchase of the vehicle so that, e.g. towards the end of a calendar year, perhaps new car buyers will prefer to delay the purchase until the beginning of the following year for the date of the vehicle reaching road in the license to be in the new year and not the previous year. This amendment to the transport regulations stipulates that vehicles may not be imported over 12 months after their manufacture date. Therefore, the vehicle importers are obligated to record vehicles which are in their inventory for over 12 months in their name and pay the purchase tax imposed on every vehicle, thereby making those vehicles "first hand" or alternatively to export them overseas. The actual significance is that vehicles which are in Israel for over 12 months are recorded in the importer's name and the next purchase will be considered second hand, which may affect the results of the vehicle companies.

- **Standardization** - the Standardization Department at the Ministry of Transport's Vehicle Division annually defines the changes in mandatory requirements for the different vehicle types for the following year's models, indicating the amendments set in the European standards, and also the special requirement for Israel. The requirement in the Transport Regulations is for European Common Market standards. Nevertheless, for cars manufactured in NAFTA countries: the US, Canada and Mexico, the requirement is for the American Standard and several Israeli standardization provisions. Vehicles not meeting the requirements are not permitted to be imported into Israel. In December 2011, with the purpose of increasing competition in the vehicle industry and bringing about a decrease in the vehicle prices resulting from the differences in the Euro-USD exchange rate, the Ministry of Transport approved importing vehicles meeting the American standards whose factory is in Japan, provided they are also manufactured in NAFTA countries.
- **Committee for examination of competition in the vehicle market** - On August 24, 2011, the Minister of Transport, Mr. Israel Katz, decided to set up a public committee led by Prof. Yaron Zalicha, aimed at formulating recommendations to remove barriers leading to increased competition in the vehicle market and reduced tariffs for the consumer. The decision which led to establishing this committee was taken following the Ministry of Transport's decision to develop the vehicle import industry for free competition and allow parallel import of cars, as described above.

As part of the committee's work, the primary role was to analyze the industry's barriers and the possibilities for removing them so that the market concentration is reduced and the car prices decreased, and to examine the vehicle market taxation. In addition to Zalicha, the committee was joined by representatives of both the Tax Authority and the Antitrust Commissioner, aimed at allowing the committee to submit conclusions both on taxation of the vehicle industry and to formulate complementary measures to increase competition in the industry.

The committee proposed alternatives for implementation of reforms to improve competition in the vehicle industry and, *inter alia*, the cross-costs between the vehicle importers and leasing companies, vehicle garages and spare parts importers. Another matter dealt with in the committee is promoting legislation obliging vehicle importers to provide warranty and service for vehicles imported to Israel.

The following are among the committee's main recommendations:

- Changing the vehicle value in use calculation method for tax purposes.
- Restricting the vehicle importers' import agreements so that an importer holding above 8% of the market may hold a vehicle importation agreement with one vehicle company only and import all of that company's brands without limitation and independent of the market share that it holds.
- Limiting the vehicle importers' holding in leasing and/or car hire companies so that a direct vehicle importer cannot hold shares of a leasing and/or car hire company and also, directly or indirectly, in more than one garage which will serve as a service and training center for the vehicles which it imports, unless it obtains approval from the Ministry of Transport;
- Permitting importation of a vehicle manufactured in American standards, whether produced in the US or elsewhere, provided that the model vehicle is marketed in the US and approved by the

American Association for Laboratory Accreditation (A2LA) under the provision of the European law on this matter.

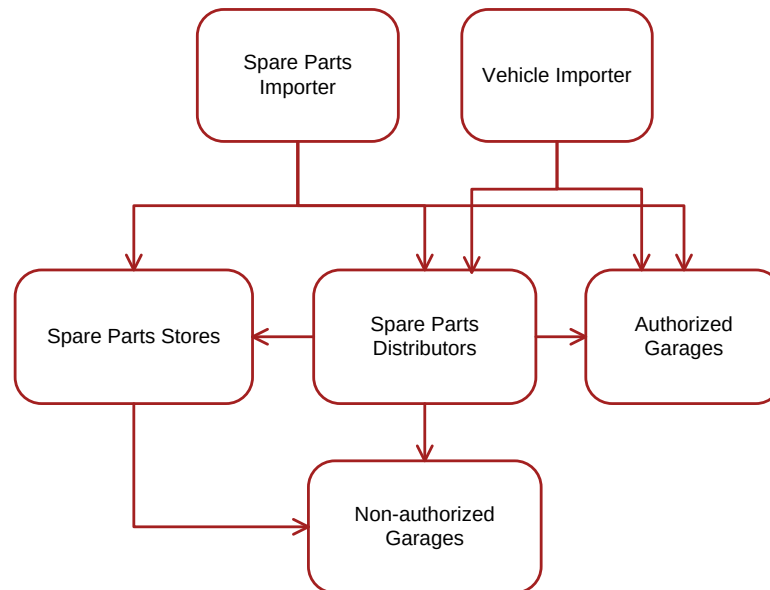
- Restricting tax benefits concerning leasing companies holding a market share of above 15%.
- Limiting the difference between a new vehicle price in a more expensive transactions (for private customers) and the price in a cheaper transaction (for leasing companies, e.g. after deducting an institutional discount). The difference will be maximum 5% of the more expensive vehicle price, including the financial value of the benefit to the customer in or after the transaction.
- Obliging importers of all vehicle types, including personal importation advisors, to obtain a valid import license from the Ministry of Transport.
- Canceling the requirements to obtain the direct importer's consent for provision of garage services as a condition to importing a vehicle by personal import.
- Transferring recall responsibility to the direct importer, independent of the type of import, through which the vehicle arrives in Israel, including models not imported by the direct importer. The direct importers will be obligated to provide warranty for the imported vehicles even if not imported through them, provided the manufacturer's warranty applies to the country of origin.

As of the valuation date, the Zalicha Committee and Knesset Committee's recommendations have not yet been approved.

Spare parts and garage services market

- The scope of the Israeli spare parts and garage services market derives from the scope of the Israeli vehicle market, car type and vehicle age. The total import value for vehicle accessories and spare parts in 2010 was USD 400 million compared to USD 374 million in 2009, representing a growth rate of 7%.

The following diagram describes the spare parts supply process in the Israeli spare parts market:



- Among the entities operating in the spare parts market are the vehicle importers, which supply original spare parts for the types of vehicles imported by them, importers of original spare parts (parallel import), compatible spare parts (non-original) importers, wholesalers which purchase spare parts from the importers and sell them to retailers, used spare parts distributors, spare parts reconditioners and the end users (garages, car hire and leasing companies, vehicle fleets and insurance companies).
- The Israeli market is characterized by competition mainly between the original spare parts sales versus the cheaper alternatives, spare parts from disassembly and reconditioned spare parts. However, some parts have a copyright symbol engraved on them so there is no production of spare parts and competition is limited. The measure of control of the Ministries of Transport and Trade & Industry and Tax Authority, the traders' conduct and the non-original spare parts inventory adapted to the vehicles which the Company imports all affect operations in the spare parts segment.
- Other factors increasing the competition in the industry are: The rise in import of alternative spare parts manufactured in the Far East and intervention of the Antitrust Commissioner. The Commissioner permits vehicle owners to carry out services and repairs in the warranty period even at non-authorized garages without it affecting the new vehicle warranty with restrictions prescribed in the Commissioner's order and permits the garage operators to purchase spare parts from any supplier and not only the vehicle importer, provided they meet the quality requirements and compatibility as defined in this order.
- In recent years, the volume of operations in the spare parts and garage services segment has begun increasing due to the growth in the vehicle sales volume. Nevertheless, there are other factors affecting the profitability in the spare parts and garage services segment.

- In April 2003, the order issued by the Antitrust Commissioner under Section 50B of the Antitrust Law, 1988 regulating the vehicle industry operation entered into force. This order also has a substantial effect on the spare parts segment, especially on the following points:
 - An importer is forbidden to restrict an authorized garage in any matters concerning spare parts purchasing or use, independent of the vehicle age, and in the warranty period, subject to the requirements of the order and excluding the cases stated therein.
 - An importer is forbidden to make receiving service at an authorized garage or using a certain or original spare part a condition for the validity of the warranty, apart from the terms specified in the order, i.e. a vehicle owner may choose where to repair his vehicle and which type of spare part to use even in the warranty period.
 - Only in cases where a part is replaced under the warranty where the importer bears minimum 90% of the replacement cost is the importer entitled to coerce the customer or garage owner to use the original part purchased from it.
- Commodities and Services Price Control Order (Vehicle Import and Servicing), 1978 imposes obligations on the vehicle importer, such as supply of spare parts for imported vehicles for seven years minimum and opening one service garage minimum in each district.
- In June 2010, a private bill was submitted to the Knesset Economic Committee under which repairing a vehicle at an garage not authorized by the Ministry of Transport would be forbidden.
- In October 2010, the Ministry of Transport initiated a new procedure regulating the importation of alternative spare parts under which spare parts sold in Europe or the US which meet the procedure conditions may be imported to Israel. The new procedure facilitated the import of alternative spare parts which are not full compatible with the models marketed in Israel. The cost of these parts is lower and the availability higher and thus it could increase the price competition in the spare parts market.
- Below are the main conclusions of the Zalicha Committee concerning spare parts, garages and insurance companies:
 - The requirement to allow special import of spare parts will be replaced by a list of parts which will be forbidden to import unless they meet the safety requirements. Any spare part excluded from the list may be imported.
 - The preconditions for issuing a spare parts import license connected to vehicle safety will be canceled.
 - Importers will be forbidden to control and interfere with the garage repairs and services.
 - All importers will be forbidden to refuse to sell spare parts to any entity. The sale will be at a uniform price, besides a 5% quantity discount.
 - It will be possible to purchase spare parts from any garage. Garage owners will be obliged to carry out repairs even if the spare part was purchased by the customer from another source, provided it is new.
 - It will not be possible to cancel the vehicle warranty for including a certain spare part. Use of non-original spare parts or non-authorized vehicle repairs will not affect the manufacturer's warranty.

As of the valuation date, the Zalicha Committee and Knesset Committee's recommendations have not yet been approved.

Chapter 4

Valuation method

Valuation method

- Section 33 of IAS 28 prescribes that since goodwill, which is included in the carrying amount of an associate, is not separately recognized, its impairment loss cannot be examined separately. Instead, the impaired loss of the carrying value of the investment in an associate under IAS 36 by comparing the recoverable amount of the investment to the carrying amount.

Recoverable amount

- Section 18 of IAS 36 defines a recoverable amount as "the higher of the fair value less costs to sell of an asset or cash generating unit (CGU) and its value in use."
- Section 19 stipulates that: "it is not always necessary to determine both the fair value less costs to sell of an asset and its value in use. if one of these amounts is greater than the asset's carrying amount, the asset is not impaired, and it is not necessary to estimate the other amount."
- Section 20 stipulates that: "It may be possible to determine the fair value less the cost to sell even if an asset is not traded in an active market." However, sometimes it will not be possible to determine fair value less costs to sell because there is no basis for making a reliable estimate of the amount obtainable from the sale of the asset in an arm's length transaction between knowledgeable and willing parties. In this case, the entity may use the asset's value in use as its recoverable amount."

Value in use

- For the study, we estimated Delek Automotive's value in use which Delek Group management identified as a smaller cash-generating unit. IAS 36 determines how to measure the value in use of an asset or CGU.
- Under section 31 of IAS 36 standard: *"Estimating the value in use of an asset involves the following steps:*
 - (a) *estimating the future cash inflows and outflows to be derived from continuing use of the asset and from its ultimate disposal; and*
 - (b) *applying the appropriate discount rate to those future cash flows."*
- Section 33 of IAS 28 prescribes that: "In determining the value in use of the investment, an entity estimates:
 - (a) *its share of the present value of the estimated future cash flows expected to be generated by the associate, including the cash flows from the operations of the associate and the proceeds on the ultimate disposal of the investment; or*
 - (b) *the present value of the estimated future cash flows expected to arise from dividends to be received from the investment and from its ultimate disposal."*
- Under section 33 of IAS 36: "In measuring the value in use, an entity shall:
 - (a) *base cash flow projections on reasonable and supportable assumptions that represent management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset. Greater weight shall be given to external evidence.*

- (b) *base cash flow projections on the most recent financial budgets/forecasts approved by management, but shall exclude any estimated future cash inflows or outflows expected to arise from future restructurings or from improving or enhancing the asset's performance. Projections based on these budgets/forecasts shall cover a maximum period of five years, unless a longer period can be justified.*
- (c) *estimate cash flow projections beyond the period covered by the most recent budgets/forecasts by extrapolating the projections based on the budgets/forecasts using a steady or declining growth rate for subsequent years, unless an increasing rate can be justified. This growth rate shall not exceed the long-term average growth rate for the products, industries, or country or countries in which the entity operates or for the market in which the asset is used, unless a higher rate can be justified."*

Valuation method chosen

- The DCF method was chosen to value the value in use of Delek Automotive.
- The DCF method is based on evaluating the capacity of a business to generate cash flows. Accordingly, the value of a business is evaluated by the future discounted cash flows it is expected to generate. The future cash flows are discounted using the cost of capital representing the risk in the business' operations and expressing the return an investor would expect to make from a business with a similar risk.

The DCF method is the most accepted method, based on the most solid theory. To use this method, a financial model which projects the sales, cost of sales, management and sales expenses, taxes and investments must be built to derive the projected cash flows.

The main advantage of the method is its match for the specific business and that fact that it addresses unique factors in the evaluated business. This characteristic brings about a relatively high measure of accuracy.

The disadvantage of the method is in the difficulty in projecting relevant future revenues, expenses and investments and determining the appropriate cost of capital.

Valuation principles

- The valuation stages of the DCF method include:
 - Analyzing the Company's area of operation.
 - Forecasting the revenues in the Company's area of operation.
 - Analyzing the expense structure and projecting the expenses required to achieve revenues analyzed.
 - Forecasting the investment required in the projected period.
 - Building financial forecasts, including profit and loss and cash flow free forecasts.
 - Calculating the economic value of the Company's operation by capitalization of the free cash flow for the projected period and the value of operations at the end of the projected period, using a weighted cost of capital adjusted for the business risk involved in the Company's area of operation.
 - Calculating the fair value of the Company's equity by adding the non-operating assets less the financial liabilities from the total economic value of the Company's operation.
- To value Delek Israel's value in use using the DCF method, the nominal free cash flow from the Company's operations was projected for a period of five years from the valuation date ("**the Projected Period**") and the discounted value of operations at the end of the projected period. Since it was assumed that the Company is a going concern and will continue to exist also after

the end of the *projected* period, the value of the Company's operations at the end of this period was determined accordingly as the present cash flow value to infinity, based on the representative cash flow for the period, assuming that the representative cash flow will grow at a nominal rate of 3% per annum. The weighted cost of capital based on which the free cash flow was discounted, which reflects the business risk in the Company's operation, was set at 11%.

- The valuation was based on information and information sources included in the audited financial statements of Delek Automotive and Kamor Motors for 2006-2011, the Company management's budget for 2012, Delek Automotive management's valuations and forecasts, meetings with Delek Automotive management, other operating information, market research, and public information concerning the Company's area of operation.

Chapter 5

Valuation

Forecast

Summary of Delek Automotive's projected profit and loss:

NIS thousands	2012	2013	2014	2015	2016	Representative year
Vehicle sales	3,997,367	3,907,936	3,930,542	4,073,458	4,207,148	4,308,865
Spare parts and garage service sales	383,400	391,068	398,889	406,867	415,004	423,305
Total sales	4,380,767	4,299,004	4,329,431	4,480,325	4,622,153	4,732,169
*Cost of sales	3,864,434	3,765,296	3,774,563	3,889,593	4,014,859	4,110,820
Gross profit without depreciation	516,333	533,708	554,867	590,732	607,294	621,349
Gross profit rate (%)	11.8%	12.4%	12.8%	13.2%	13.1%	13.1%
* Sales and marketing expenses	72,596	72,617	73,571	75,522	77,385	78,864
*General and administrative expenses	43,704	42,290	43,084	44,367	45,619	46,666
EBITDA	400,033	418,800	438,213	470,843	484,290	495,819
Depreciation	10,227	11,796	13,365	14,203	14,311	14,000
Operating profit	389,806	407,005	424,848	456,640	469,979	481,819
Operating profit rate (%)	8.9%	9.5%	9.8%	10.2%	10.2%	10.2%
Profit before income tax	389,806	407,005	424,848	456,640	469,979	481,819
Income tax	97,452	101,751	106,212	114,160	117,495	120,455
Operating profit after tax	292,355	305,253	318,636	342,480	352,485	361,364

* Without depreciation and amortization.

Forecast of revenues

- As set out above, Delek Automotive's revenues include revenues from vehicle and spare sales and garage services.
- Its revenues from vehicle sales include those from the sale of Mazda, Ford, BMW and Mini Cooper cars.
- To project the revenue from vehicle sales, we evaluated the scope of the Israeli vehicle delivery market in the projected years. For this purpose, we relied on the industry and Company's estimations, the economy growth forecast, the population and the vehicle delivery growth rates in previous years.
- The Israeli vehicle market reached record vehicle deliveries in 2011 with 226,000 deliveries. This trend continued the previous record of 216,000 vehicle deliveries in 2010. Based on the industry estimations, in 2012, a drop in demand is expected. It was therefore assumed that the volume of vehicle deliveries in this year is expected to total 207,000 vehicles only.
- As from 2013, the demand is expected to recover gradually to the growth trend witnessed in 2010-2011. Accordingly, we estimated that the volume of deliveries would amount to 214,000 vehicles in 2013 and 222,000 in 2014. It was assumed that the volume of vehicle deliveries would grow by 2.6% in 2017 and 2018, based on the weighted growth rate of the vehicle industry in the last decade.
- The volume of vehicle sales was calculated on the basis analyzing historical market share data and future trends in the Mazda, Ford, BMW and Mini Cooper market analysis. According to the Company management, the vehicle delivery mix is expected to change in the forthcoming years. Ford vehicles are expected to lead the Company's delivery volume, following the anticipated launch of the new Ford models, primarily the new Ford Focus launch at the end of 2011 which has been highly successful worldwide. All in all, based on the range and similar to the Company management's evaluations, it was assumed that the Ford vehicle deliveries will total 21,000 vehicles in 2012.

Following the trend which began in the second quarter of 2011 and strengthened in the last quarter of 2011, the Company management anticipates a decline in the Mazda vehicle market in 2012, because of the strong JPY exchange rate versus the NIS and the USD. However, the Company management estimates that the launch of the CX5 mini jeep at the end of the first quarter of 2012 and the new Mazda 6 at the end of 2012, both with the new Mazda SkyActive technology, will lead to a rise in Mazda deliveries starting from the second quarter of 2012 and the pursuing years. All in all, due to the anticipated decline of the Mazda market share in 2011, it was assumed that the Mazda vehicle deliveries would amount to 12,000 in 2012.

Following the Kamor acquisition, the Company began re-branding the BMW and Mini Cooper vehicles in a process including a new price policy and targeting a wider audience than in the past. The Company management estimates that these changes will allow increasing its vehicle market share. All in all, based on the Company management's evaluations, it was assumed that the BMW vehicle deliveries would total 2,000 in 2012.

- For the remaining projected years, it was assumed that the Mazda, Ford, BMW and Mini Cooper vehicle deliveries would improve in accordance with the vehicle delivery growth of the entire market and the expected Mazda, Ford, BMW and Mini Cooper vehicle delivery growth as estimated by the Company. However, to reflect the possibility of overcoming the market competition, it was assumed that the Company's market share would decrease gradually from 17.2% on 2012 to 15.7% from 2014 onwards.
- The Company's revenues in spare parts and garage services primarily include its revenues from spare part sales, while the remaining revenues from this segment arise from providing garage services, including maintenance and repairs for the its customers and support and training services for the nationwide service center network.
- Based on the Company management's budget for 2012 and the historical data analysis, a decline of revenues from spare part sales and garage services was assumed for 2012, due to the drop in its projected new vehicle demand this year. As from 2013, with the gradual recovery of vehicle demand, an annual growth rate of 2% was assumed.

Gross profit

- The cost of sales, excluding depreciation and amortization, is composed of the cost of vehicles sold, the cost of spare parts and garage services, wages and related expenses, and other expenses. The Delek Automotive's vehicle COGS (Cost of Goods Sold) was 89.6% in 2011 and 87.3% in 2010. The change in profitability arose mainly from the JPY to NIS and USD exchange rate fluctuations which directly affected the vehicle purchase prices and the vehicle industry-based sales price range.
- Based on past information and the Company's estimation, it was assumed that the vehicle COGS rate would be 89.0% in 2012 and would gradually improve to 87.7% in the representative year. The factors for the projected gross profit rate improvement are the change in the vehicle sales mix, update of the inventory purchase terms with the manufacturers and expected development of the Mazda plant in Mexico in 2015, which as aforesaid, will allow purchasing Mazda 2 and Mazda 3 vehicles in USD.
- Delek Automotive's spare parts and garage services COGS was 64.6% in 2011 and 66.6% in 2010. Based on past information, it was assumed that the spare parts and garage services COGS rate would be 65.6% in the projected years, the same as in 2010 and 2011.
- The wages and related expenses amounted to NIS 32.5 million in 2011 and NIS 31.4 million in 2010. It was assumed that in the projected year, these expenses would increase 1.5% plus adjustments for the changes in the Company's revenues.
- The other expenses amounted to NIS 14.2 million in 2011 and NIS 11.2 million in 2010. It was assumed that in the projected year, these expenses would increase by 1.5% plus adjustment for the changes in the Company's revenues.
- Accordingly, it was assumed that the Company's gross profit rate would be 11.8% in 2012 and would gradually improve to 13.1% in the representative year.

Sales and marketing expenses

- The Company's sales and marketing expenses, with depreciation and amortization neutralized, include advertising expenses (less the overseas manufacturer's participation), agents fees, wages and related expenses and other expenses.

The Company's advertising expenses amounted to NIS 22.5 million in 2011 and NIS 21.5 million in 2010. Following the foregoing Kamor acquisition in December 2011, the Company management estimates that the advertising expenses will increase to NIS 42 million in 2012, 1.0% of the Company's projected revenues in that year. Similarly, it was assumed that in the remaining years, the projected expenses would be 1.0% of the Company's projected revenues.

The Company's remaining sales and marketing expenses amounted to NIS 19.4 million in 2011 and NIS 21.3 million in 2012. Following the foregoing Kamor acquisition, the Company management estimates that the sales and marketing expenses would rise to NIS 30.6 million in 2012, 0.7% of the Company's projected revenues in that year. The increase of these expenses is mainly from the wage expenses for Kamor's sales and marketing staff who were absorbed in the Company. Similarly, it was assumed that in the remaining years, the projected sales and marketing expenses would be 0.7% of the Company's projected revenues.

All in all, it was assumed that the Company's sales and marketing expenses would be 1.7% in the projected and representative years.

General and administrative expenses

- The general and administrative expenses, without depreciation and amortization, comprise mainly wages and related expenses and other expenses.
- The general and administrative expenses amounted to NIS 27.6 million in 2011 and NIS 29.1 million in 2010. Following the foregoing Kamor acquisition, the Company management estimates that the general and administrative expenses will rise in 2012 to NIS 43.7 million, 1.0% of the Company's projected revenues in that year. The growth of these expenses is mainly from other expenses which the Company incurred with respect to the Kamor operation. It is noted that according to the Company management, Kanor's management staff are not expected to be absorbed in the Company. It was assumed that in the remaining years, the projected general and administrative expenses would be 1.0% of the Company's projected revenues.

Income tax

- The assumed income tax rate was based on the expected statutory tax rate in Israel in the projected and representative years, as of the valuation date.
- On July 23, 2009, the Economic Efficiency Law was published in the Official Gazette setting out , *inter alia*, a gradual reduction of the companies tax rate from the 2011 tax year onwards. Under this law, the companies tax rate would be reduced by 1% annually so that it would drop to 24% in 2011 and continue to decline to 20% in 2015 and would stabilize at 18% from 2016 onwards.
- On October 30, 2011, the Knesset approved the tax chapter of the Trachtenberg Committee for Social and Economic Change report, which included, *inter alia*, cancellation of the above Economic Efficiency Law. Based on the committee's recommendations, the companies tax rate will increase in 2012 to 25% and on this basis, the tax rate of 25% was assumed for the projected and representative years.

Capital expenditure and depreciation costs

- According to the Company management, following the Kamor acquisition it plans to invest substantially in renovating and setting up showrooms and service centers in the next three years. Accordingly and based on the Company's budget, it was estimated that the Company's investments would amount to NIS 153 million in 2012-2014, NIS 7 million in 2015-2016 and NIS 14 million in the representative year. It was assumed that in the representative year, the annual depreciation is equal to the annual investment in property, plant and equipment.

Investment in working capital

- The Company's working capital comprises mainly trade payables, inventory and trade receivables balances.

Due to the nature of the operation, the Company holds relatively high inventory balances and provides high customer credit terms. Therefore, it is required to invest in working capital with the growth in operations.

The working capital required for the Company's operation in the projected years and representative year was estimated on the basis of analyzing the trade payables, trade receivables and inventory days for 2010 and 2011.

Accordingly, for the projected years and representative year, it was assumed that the payables credit days would be 78, the receivables credit days 89 and the inventory credit days 90.

Weighted cost of capital

- For the purpose of discounting the Company's free cash flow, a discount rate reflecting the time value of the money and the business risks involved in the Company's operation were used. This rate was estimated at the weighted average cost of capital using the following formula:

$$WACC = K_e(e\%) + K_d(d\%)(1-T_c)$$

Where:

WACC = Weighted average cost of capital

K_e = Rate of return on equity

$e\%$ = Equity as a percentage of the total assets

K_d = Rate of debt

$d\%$ = The debt as a percentage of the assets

T_c = Companies tax rate

The rate of return on the equity or the cost of equity required is determined using the Capital Asset Pricing Model (**CAPM**). The cost of equity under CAPM comprises the long-term risk-free interest rate plus the average capital market risk premium multiplied by the Company's relative risk coefficient, beta, which reflects the sensitivity of the investment in the Company to fluctuations in the overall capital market based on the following formula:

$$K_e = R_f + \beta(R_m - R_f) + SFP$$

Where:

R_f - risk-free interest rate. The risk-free interest rate is determined based on the nominal rate of return of Israeli government Shahaar bonds (for 15 years) - 5.15%.

β - Relative risk coefficient. This coefficient reflects the relative risk involved in a certain investment and is based on the level of compliance between the return on investment and the return of the entire capital market. When this coefficient is greater than 1, the value of the business is highly sensitive to market condition changes (i.e. in the event of a recession the business would more impaired than businesses in other industries and in the event of prosperity, the business would be more positively affected than businesses in other industries). When this coefficient is less than 1, the value of the business is less sensitive than average to changes in market conditions.

For the purpose of the valuation, we took to the β for the Company's operation from an average betas of public companies operating in similar segments to that of the Company ("**the Comparable Companies**") The betas calculated for the comparable companies are levered equity betas which also take into consideration the shareholders' risk from the financial debt of each company. Therefore, to calculate the unlevered beta for each of the comparable companies, the net working capital component was neutralized from the levered betas of these companies. The average unlevered betas obtained in this manner (representing the unlevered beta of the industry) were relevered based on the average leverage rate of the comparable companies. The beta estimated in this manner (relevered equity beta) is 1.01.

Rm-Rf - the average market risk premium - the cost of capital is estimated using the international investor method, i.e. from the viewpoint of an investor whose portfolio is diversified globally. In this approach the country risk is inherent in the risk-free interest rate. The average market risk premium required by an international investor is 5.5%. This premium is based on the average risk premium of the world's developed markets (USA, Western Europe and Japan).

SFP - the small firm risk premium in terms of market value - the premium reflecting the surplus risk in investments in companies with a low market value compared to companies in the American market was added to the cost of investment obtained from the CAPM model. This premium was calculated on the basis of the historical differences in returns of companies with a relatively low market value in the American market, which on average in the case of Delek Automotive is 1.9% per annum.***

Based on these parameters, the required rate of return on the equity was fixed at 12.6%.

Kd - the rate of the Company's debt (net of tax) was set at 6.2%.

Based on these parameters, the WACC (rounded) is 11%, as specified in the following table:

Weighted average cost of capital WACC	
Risk-free interest rate (Rf)	5.15%
Market risk premium (Rm-Rf)	5.5%
Beta (β)	1.01
Small-firm premium (SFP)	1.9%
Cost of capital (Ke)	12.6%
Leverage ratio	19%
Rate of debt (Kd)	8.3%
Long-term tax rate	25%
Rate of debt, net of tax (Kd)	6.2%
WACC (rounded)	11%

* The benchmark companies are: Lithia Motors Inc, AutoNation Inc, Group 1 Automobile, Sonic Automobile Inc, Asbury Automotive Group, Automotive Group Holdings Limited, Penske Automotive Group, Vertu Motors PLC.

** Source: PwC

** Source: Ibbotson Associates, Inc[Valuation Edition Yearbook2011]

Free cash flow forecast

NIS thousands	2012	2013	2014	2015	2016	Representative year
Operating profit after tax	292,355	305,253	318,636	342,480	352,485	361,364
Depreciation	10,227	11,796	13,365	14,203	14,311	14,000
Capital expenditure	(51,000)	(51,000)	(51,000)	(3,500)	(3,500)	(14,000)
Investment in working capital	(50,826)	16,069	(5,940)	(29,556)	(27,806)	(21,567)
Free cash flow	200,756	282,118	275,061	323,627	335,490	339,797

Non-operating asset balance and financial liabilities

- As of the valuation date, the Company's consolidated non-operating assets include cash and cash value of NIS 323 million, securities at a fair value through profit or loss of NIS 185 million, investment property (including that under construction) of NIS 48 million and loans granted of NIS 42 million.
- The Company's consolidated financial liabilities include bank and other short-term borrowings and bank loans totaling NIS 1,236 million, debentures of NIS 49 million, employee benefit liabilities of NIS 3 million and net deferred tax liability of NIS 15 million.

The value in use in the DCF method

The following table shows a summary of the value in use as of the valuation date:

NIS thousands	December 31, 2011
Value of Delek Automotive's operation	3,734
Financial liabilities, net	(705)
Value in use of Delek Automotive	3,028

In our opinion, as at the valuation date, as described in this paper and under the provisions of IAS 28 and IAS 36, the recoverable amount of Delek Automotive fluctuates between NIS 2.9 billion and NIS 3.2 billion ($\pm$ 5% of the value in use, as estimated using the DCF method).

Sensitivity analyses

The following table shows the sensitivity analysis of Delek Automotive's value in use in relation to the capitalization rate and the long-term growth rate (NIS million):

		Weighted average cost of capital WACC				
Long-term growth rate		12.0%	11.5%	11.0%	10.5%	10.0%
	2%	2,389	2,552	2,733	2,936	3,164
	3%	2,616	2,810	3,028	3,276	3,559
	4%	2,899	3,137	3,408	3,721	4,086

The following table shows sensitivity analysis of Delek Automotive's value in use in relation to the cost of vehicle sold (COGS) in the representative year (NIS million):

Cost of vehicles sold, out of vehicle sales				
89.2%	88.7%	87.7%	86.7%	86.2%
2,644	2,770	3,028	3,275	3,402

Comparison with the market value

- The table below shows Delek Automotive's market value as of the valuation date compared to its average market value in periods of 6 and 12 months ended on the valuation date and compared to its market value after the valuation date (March 21, 2012) as derived from the TASE share price in those periods (NIS millions).
- The difference between Delek Automotive's value in use and the market value derived from the TASE share price on the valuation date may arise from the fact that, as of the valuation date, the market investors apparently do not take into consideration the full impact of the re-organization which may stem from the Kamor acquisition, the improvement in volume of vehicle deliveries which the Company management estimates following the launch of new Ford Focus, the Mazda CX5 and 6 models and the improvement in profitability rate which the Company management expects from the enhanced terms agreed with the vehicle manufacturers. From the valuation date to March 21, 2012 (56 trading days), Delek Automotive's market value rose by 36%, reaching NIS 2.9 billion.

The graph below shows the changes in Delek Automotive's share price in the year preceding the valuation date (January 1, 2011 through December 31, 2011) and from the valuation date through March 21, 2012.

	Market value (NIS millions)	Adjusted closing price	High price	Low price
Valuation date - December 31, 2011	2,150	23.1	23.3	22.6
Average of six months ended on valuation date	2,765	29.8	30.3	29.2
Average of 12 months ended on valuation date	3,440	36.2	37.6	36.7
March 21, 2012	2,916	30.9	31.1	29.4



Appendix 1: CV of the valuator, Dr. Tzur Fenigstein.

Education:

2010 - PhD in Philosophy from Tel-Aviv University.

1989 - MBA in Business Administration from Tel-Aviv University (Cum Laude).

1986 - CPA.

1983 - MA in Accounting and Economics from Tel-Aviv University.

Professional experience:

2001 onwards - Partner at Kesselman and Kesselman Price Waterhouse Coopers and Manager of Finance and Economics at PwC Isr. Our experience includes project management and research in financial and strategic consulting, preparing expert opinions, preparing economic papers in the public policy and regulation segments, valuating companies and preparing business plans. Since 2006, Tzur serves as CEO of PwC Isr.

1995 - 2001 - Member of the Management and Director of Finance and Economics at Pwc Isr.

1994 - 1995 - Deputy CEO of S.Z.Y.R. Holdings & Investments Ltd., the industrial investment arm of Cee Investments Ltd.

1993 - 1994 - Transaction Manager in the Private Transaction Department at Poalim Capital Markets and Investments Ltd.

1990 - 1993 - Project Manager and Senior Consultant at Yaad Business Development Ltd.

1989 - 1990 - Auditor at accounting firm Somekh Chaikinm.

Projects and research managed at Kesselman Finance include, *inter alia*:

Valuations, preparation of feasibility studies and writing business plans for companies and firms from all fields of the economy;

Preparation of position papers of macro-economics and micro-economics for various bodies aimed at showing their position concerning structural changes in the economy;

Instruction and active guidance of various economic papers for leading companies in the economy;

Preparation of expert opinions on different economic issues as part of clarifications of legal claims.

Delek Group, Ltd

Management Report

Goodwill Recoverability of Republic Companies, Inc.



Year ended, December 31, 2011

Management Report Goodwill Recoverability of Republic Companies, Inc. December 31, 2011

Index

Executive Summary.....	3
General Company Overview.....	4
P&C Industry Overview.....	6
2011 Weather Events/Adverse Reserve Development.....	7
US Economic Overview.....	8
Valuation Approach under IFRS.....	9
Discussion of Valuation Approaches.....	10
Analysis of Potential Triggering Events.....	13
Valuation Conclusion.....	15
Appendix	16

Executive Summary

Delek Group Ltd acquired the stock of Republic Companies, Inc. (“RCI or Republic”) on December 7, 2006. The total acquisition price was \$298MM. RCI is a US holding company of a group of insurance carriers and related entities that provide personal and commercial insurance products (designated in the industry as “The Republic Group” or “Republic”). The Republic Group primarily distributes insurance products to individuals and small to medium sized business through a network of independent agents primarily in Texas, Louisiana, Oklahoma, New Mexico, Mississippi and Arkansas. In addition, the Republic Group capitalize on the group’s unique combination of charters and licenses to develop and manage target niche insurance products that are distributed through managing general agents and other producers in many additional states. RCI applied fair value accounting at December 7, 2006 when it was acquired the Delek Group Ltd.

Delek Group Ltd. considers RCI and its parent company Delek Finance US Inc. (“DFUSI”) as one individual Cash Generating Unit under guidance provided by International Accounting Standards (“IFRS”). IFRS accounting standards require annual testing of goodwill and other intangible assets for impairment and require more frequent testing when internal or external conditions or events trigger a decline in value. IFRS requirements regarding testing of goodwill and intangibles assets are provided in IAS 36 *Impairment of Assets*.

The carrying value of goodwill and intangibles for this cash generating unit as of December 31, 2011 were ~\$266MM. During the fourth quarter of 2011, it was determined that RCI had incurred triggering events that required an evaluation of potential goodwill and intangible asset impairment. Various generally accepted valuation methodologies were used to determine the fair value of RCI but the a discounted cash flow of earnings method (income approach) and the Guideline Company Method (market approach) were primarily relied upon for this evaluation as of December 31, 2011. Based upon the analysis, it was determined that the fair value of RCI was \$205MM and that the aggregate goodwill of RCI was impaired by ~US\$61MM

Summary Valuation	Value in \$MM			
	Low	Selected	Med	High
Fair Value of Equity	\$ 201	\$ 208	\$ 218	\$ 235
less: Cost to Sell	\$ 3	\$ 3	\$ 3	\$ 4
Fair Value less Costs to Sell	\$ 198	\$ 205	\$ 215	\$ 231
Carrying Value		266		
Indicated Impairment		<u>\$ (61)</u>		



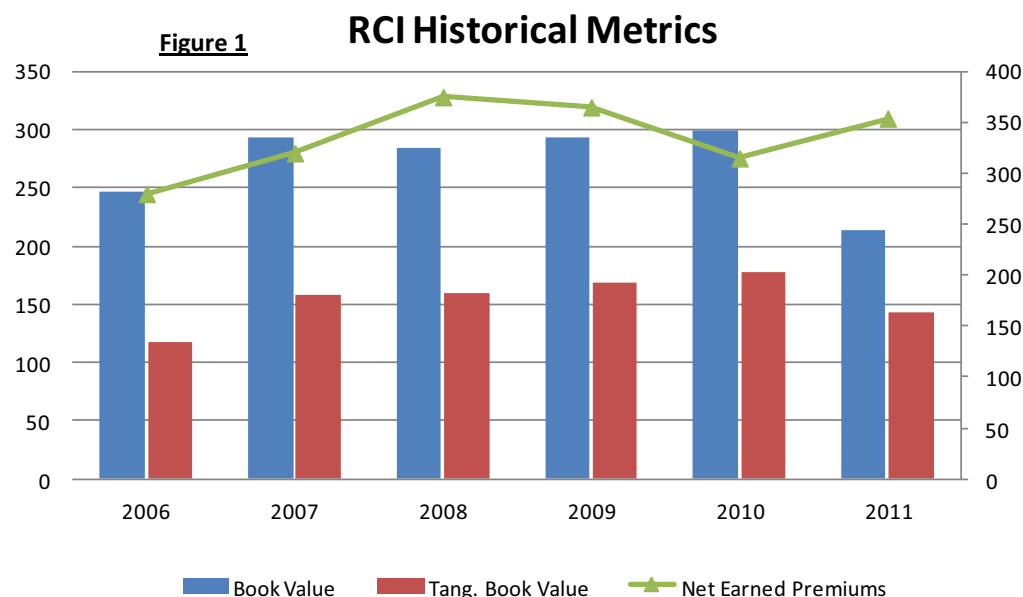
General Overview of The Republic Group

Republic has 108 years of experience in the Southwestern United States, primarily focusing on Texas, Louisiana, Oklahoma, Arkansas, Mississippi and New Mexico. Republic focuses on individuals and small- to mid-sized commercial line policyholders, utilizing multiple distribution networks including independent agencies, affiliated general agencies and unaffiliated general agencies. Republic concentrates primarily on short-tail insurance products (such as property and vehicle insurance, small commercial lines auto insurance, liability insurance and related workers compensation) as compared with long-tail insurance products (such as product liability, medical malpractice, environmental liability and errors and omissions products), because it estimates that such products and their ensuing liabilities are easier to price, thereby reducing the fluctuations in the underwriting outcome. Republic targets underserved markets often overlooked by larger national competitors. Republic does not provide life insurance or health insurance. Republic is rated A- (Excellent) by AM Best (confirmed in February 2012).

Republic's eight insurance companies and four affiliated general agencies operate through lines of business which vary by types of products and services and type of distribution network. Republic's personal line group provides personal insurance for homeowners and personal automobile liability and physical damage lines and is distributed through a network of independent agencies and owned general agencies. Republic's commercial lines group provides property, casualty, auto and farm insurance to small to mid-sized businesses, farms and municipalities and is distributed through a network of independent agencies and owned general agencies. Republic's program management group utilizes the Republic group's unique combination of charters and licenses to write premiums through specialty underwriters who have an established niche product or market access through a distribution plan of unaffiliated general agencies and managing general agencies. Republic's insurance services group makes available the unique combination of charters and licenses to larger national carriers and other regional carriers on a fronting basis with no net underwriting exposures, and receives fee income for these services. Republic's overall balance softens the impact of market changes, underwriting cycles and weather events, meaning that Republic's success is not tied or exposed to the performance of a single segment or line of business.

As a part of Republic's strategy of focusing on short-tail lines of business, underserved markets and pricing its products to provide adequate profits throughout its underwriting cycle, Republic provides its agents and managing general agencies ("MGAs") with access to capital, licenses and charters in markets that larger insurance companies often overlook and with products not always available from other insurers. The agents and MGAs have the authority to offer policies subject to specific guidelines set by Republic and provide policyholders with the services provided by a regular insurance company, including underwriting, billing and claims administration; however, they are prohibited by law from issuing their own policies.

Consistent with this strategy, Republic also issues insurance policies for low-value dwellings and for farm and ranch insurance business. Proprietary technology developed for Republic allows it to manage its risk aggregations, thus helping it seek profitable areas and provide tailored policies for its targeted markets.

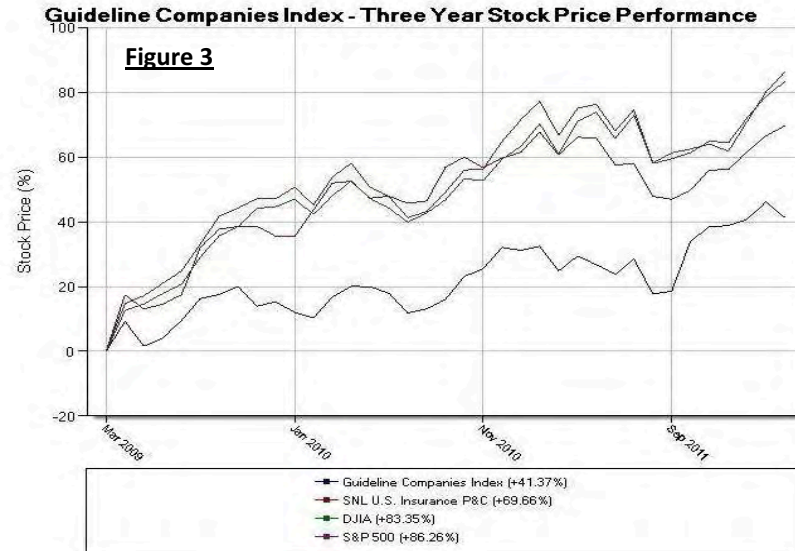
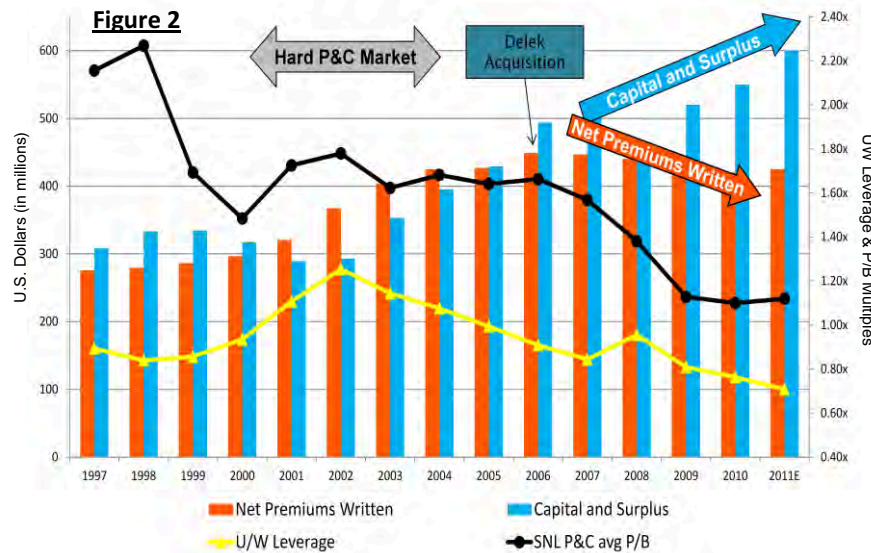


RCI Sources of Income (\$ M M)						
	2006	2007	2008	2009	2010	2011
Underwriting	15	18	(55)	(32)	(3)	(79)
Investments	15	23	9	37	32	24
Other	9	9	10	9	4	8
Operating Income	39	50	(36)	14	33	(47)

Financial Highlights (figure 1):

- The book value of equity decreased from \$293MM as of 12/31/10 to \$213MM as of 12/31/11
- Tangible book value of equity also decreased from \$175MM as of 12/31/10 to \$144MM as of 12/31/11
- Gross Written Premiums have trended higher during recent years, but declined during 2011 due to soft market conditions and loss of certain programs
- Net Earned Premiums increased during 2011 from 2010 due to quota share reinsurance treaty, but are expected to decline with forecasted reductions in Net Written Premiums
- Total losses were at record highs during 2008 and 2011 due to historic spring weather events and adverse loss development
- Underwriting Leverage is stressed at 1.64x as of 12/31/11, increased from 1.41x at 12/31/10 impairing Republic's growth opportunities

P&C Industry Overview



Overall Property and Casualty Insurance Marketplace

- NWP may grow modestly as surplus flattens; soft market conditions may continue in casualty lines
 - Despite major 2011 cat activity, industry surplus is forecasted to remain at historic levels
 - Hard market yet to fully materialize (due to high surplus and declining premium base)
 - Increased property lines 2011 cat activity & model changes allowed reinsurers to raise rates for 2012
- Casualty pricing was positive in Q3 2011; ended 30 consecutive quarters of declining rates
- Current underwriting leverage at historic lows but could flatten during 2012
- Very low investment yield environment

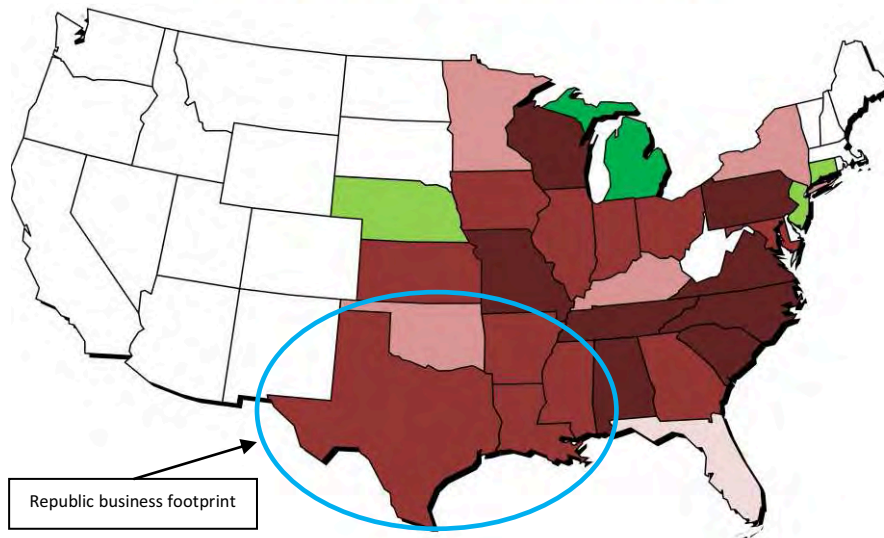
P&C Equity Performance Marketplace

- Industry price to book valuation ratio decreased 50% since Delek acquisition
- Recent uptick in number of M&A deals (deals are primarily P/B ~ 1.0x, P/TB ~ 1.25x)
- Total M&A deal numbers are low compared to historical activity
- Bid/Ask spreads continue to be very wide with no impending change
- Public stock market(s) not likely receptive in near future; no significant P&C space activity since 2007
 - Stalled economic recovery; volatile stock market; undervalued P&C stock prices

2011 Weather Events/Adverse Reserve Development



Figure 4 2011 Spring Storm vs. Historical Averages



2011 Spring Weather Events:

During Q2, 2011, Republic incurred significant weather events, including wind, hail and tornado losses. Some of the largest frequency in storms occurred within Republic's primary footprint as indicated in Figure 4

- Q2, 2011 storms were the largest events in over 50 years.
- thunderstorm losses were 5 times the national long-term average
- 12 states experienced losses 2 – 5 times their long term average
- 6 states have experienced losses > 10 times the long-term average

Total impact to Republic in 2011 was ~\$64MM

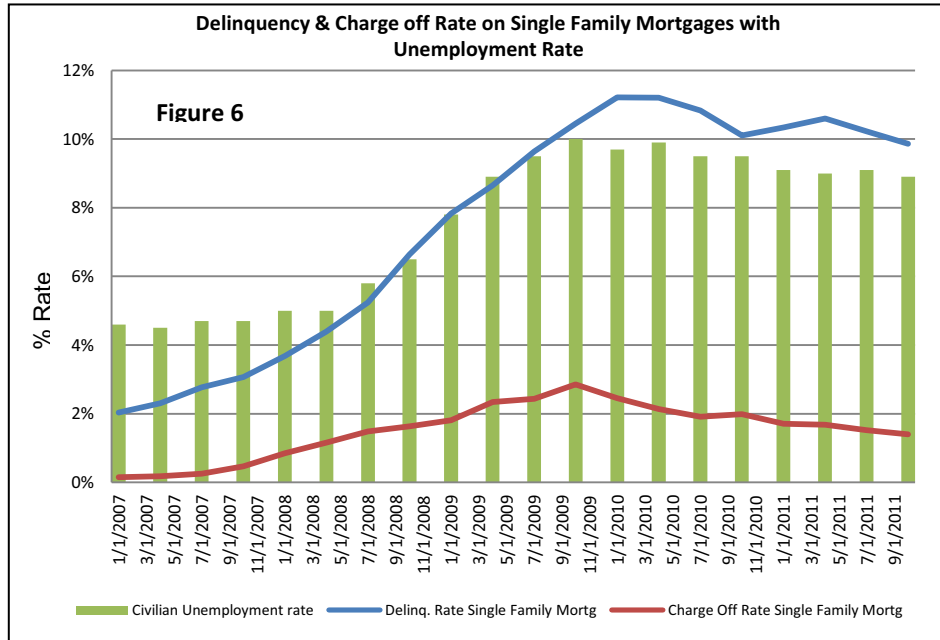
Adverse Reserve Development

- Increase in Certain Lines of Business (figure 5):
 - Commercial Auto Liability, General Liability & Workers Comp
- Key Drivers:
 - Liability lines greatly affected by **rising medical costs**
 - Increasingly complex claims & **higher litigation cost**
 - Adjustments in Claims process in mid-2011
 - Rising claim severities
- Total impact to Republic in 2011 was ~\$42MM

Adverse Reserve Development Summary by unit

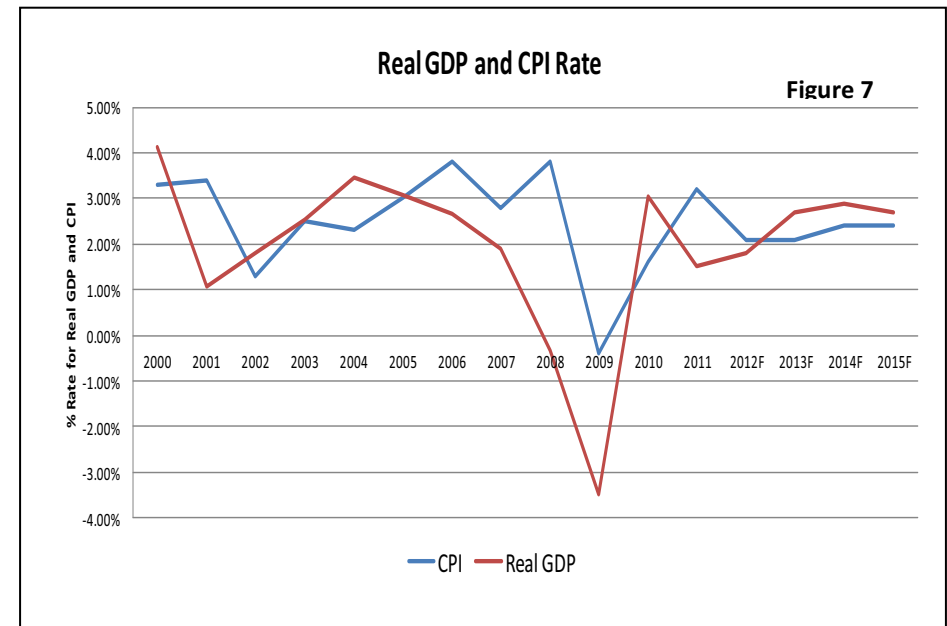
Figure 5 Business Unit	Approximate Net Adverse Development (\$MM)
Personal Lines (ex-cat)	7
Commercial Lines (ex-cat)	30
Program Management	5
Net Total	<u>42</u>

U.S. Economic Overview



- The primary driver for the sluggish US economy is driven by the overall housing market.
- Overall delinquency and rise in loan charge offs remains a drag on U.S. economy; **(figure 6)**
- Adverse housing is highly correlated to the U.S. unemployment rate.
- Continued uncertainty related to healthcare reform causing increasing medical costs
- Stock market volatility (DJIA) has ranged between 10,000 - 13,000 in past 12 months
- Despite the perceived uncertainty there is plenty of liquidity in the marketplace
- U.S. debt downgrade from AAA status
- Poor economic conditions adversely impacted P&C underwriting & investment performance

- The U.S. economy is expected to grow by ~2-3% **(figure 7)**
- The U.S. Federal Reserve is not expected to raise interest rates until 2014
- Rising commodity prices such as oil, have caused increase in CPI during recent months. Inflation expected to rise with rising oil prices
- Overall Consumer Confidence is rising in December, 2011
- Unemployment rate is declining in recent months; expected to remain above 8% throughout 2012
- European sovereign debt issues remain concern for U.S market; such issues have had a large & far reaching effect (spillover into U.S.)



Valuation Approach under IFRS

Under IFRS, the higher of the value in use or fair value less costs to sell is calculated and compared to the book value of Republic. Delek Capital Ltd. elected to use the same methodology as under US GAAP to determine the fair value of Republic. Below highlights the requirements under IAS 36:

1. Identify the cash-generating unit for goodwill testing (Republic treated as one cash generating unit)
2. Estimate the discounted cash flows of Republic
3. Determine the higher of the value in use or the fair value less costs to sell
4. Determine the amount of the impairment, if any.

The impairment model under IAS 36 is similar to the process defined by SFAS 142 (ASC 350). The impairment test under IAS 36 is required at the cash generating unit. RCI believes the “cash generating unit” application under IAS 36 is substantially the same as the “reporting unit segments” required under SFAS 142 (ASC 350). The threshold for IAS 36 testing is based on the higher of the value in use or fair value less cost to sell. The value in use is generally based on an income approach (i.e. discounted cash flows). Therefore, the goodwill adjustment for IFRS purposes may be slightly different than the adjustment for US GAAP purposes. IAS 36 does not include a step two process; accordingly, any identified impairment is recorded only as a result of the step one process. If the fair value is less than the book value of Republic, then an impairment loss is recognized in the statement of income for that amount.

Discussion of Valuation Approaches

The valuation analysis of Republic included two approaches, a “Market Approach” based on comparable public peer companies (Peer Company) and an “Income Approach” based on discounted cash flows (DCF). An analysis was conducted at the total company CGU level. A “Cost Approach” was not appropriate for this analysis. The computed results from the Market Approach and the Income Approach were weighted higher towards the Income Approach based on continued disparity between bid/ask spreads for the P&C Insurance industry. The weighted average FMV was then increased for the control premiums that would exist in a change of control scenario. The historical control premiums have ranged between 10% and 25%. However, subsequent market rebounds and subsequent increases in acquisition activity may significantly increase this factor in future analysis. The approach to estimating the fair values of Republic, includes:

- Selection & analysis of comparable companies based on business descriptions/product mix/size/geography to assess market multiples
- Preparation of a Discounted Cash Flow (DCF) analysis for Republic
- Selection of comparable transactions based on industry affiliation, business description, and availability of certain transaction data in order to assess the costs to sell applicable to Republic

To estimate the fair value of Republic, Delek Group Ltd. considered the following three generally accepted approaches to valuation:

- Market Approach
- Income Approach
- Cost Approach

Based on the analysis, all three approaches were considered and the market approach and income approach were chosen most appropriate to apply. Moreover, the following valuation methods were utilized to value the fair value of equity for Republic:

- Guideline company method (Market Approach); weighted 35%
- Guideline company method to also estimate costs to sell applicable to Republic (See Exhibit 6)
- DCF method (Income Approach); weighted 65%

Discounted Cash Flow Approach

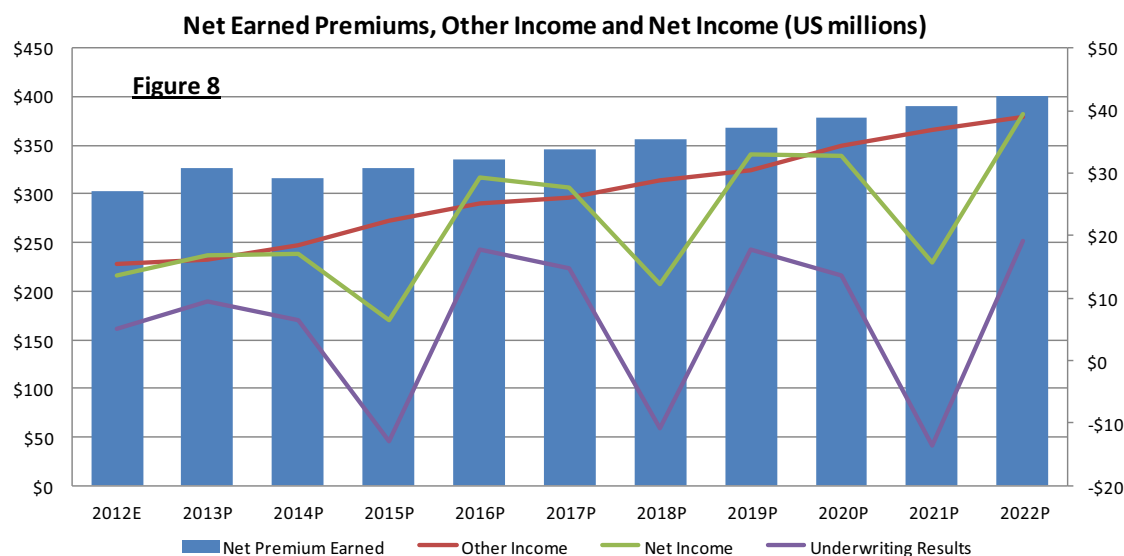
The DCF valuation approach is based on projected excess cash flows from operations. Excess cash flows are computed as the amount of operating capital in excess of the statutorily required operating capital necessary for the mix of business. This excess cash flow is presumed dividend out to the shareholders. The excess cash flow is discounted using a discount rate based on a CAPM model which includes consideration for risks specific to the property and casualty industry and risks specific to RCI. The DCF valuation also includes a terminal value for the last year of the analysis

based on a 10 year average price to earnings multiple which is discounted using the same discount rate used for the excess cash flows computation. The average price earnings multiple applied for the terminal value computation was 11x.

The discount rate used for the DCF models included the following components (traditional CAPM model factors):

Risk free rate:	20 year US Treasury rate
Equity risk premium rate:	excess of the risk-free rate required by equity investors (often referred to as the “K-factor” by equity investors)
Leverage adjustment:	adjustment of the excess equity risk rate for levered capital (Republic’s current debt structure)
Unsystematic size risk:	incremental risks associated with small cap entity
Unsystematic company risk:	incremental risk associated with operations of Republic

See calculations of final discount rates in Exhibit 3



Primary cash flow assumptions:

- Steady Growth in Premiums (~3%)
- Large losses periodically driven by excess catastrophic events; based on historical catastrophic losses
- Steady incline in other forms of revenue, such as Investment Income driven by higher returns in future periods
- Steady incline in debt interest rates with the expected rise in future interest rates
- Blended tax ratio of 32%
- Cost of Equity (discount rate) determined at 14.3%



Peer Company Evaluation:

The Peer Company valuation approach included various comparable companies based on business descriptions, product mix, capital size, geography and other similar factors. The peer companies selected included in this analysis, include One Beacon Insurance Group, Ltd, State Auto Financial Corp., Harleysville Group, Inc., Safety Insurance Group, Inc., United Fire & Casualty Company, RLI Corp, Meadowbrook Insurance Group, Inc., Hallmark Financial Services, Inc., AmTrust Financial Services, Inc., Selective Insurance Group Inc., Donegal Group Inc., Navigators Group Inc., Towers Group Inc. and Employers Holdings Inc.

Information for the peer companies was obtained from public sources including SEC filings, coverage analyst's write-ups, corporate websites, AM Best rating agency analysis, statutory insurance company filings, etc.

The following widely-used metrics were used in evaluating the peer companies:

Price / Tangible Book Value

Price / Earnings

The Price / Tangible Book Value metric is the most frequently used metric in the valuing property and casualty insurance companies due to the significant capital required to write premiums. Although not directly focused on capital, the Price / Earnings metric is heavily used in the property and casualty industry in regression analysis based on *return* on equity. The Price/Book Value multiple was not used given Republic's high intangible leverage compared to peer companies. Below includes the summary indications for the market multiples used in the market approach; see full selections and calculations incorporated within the guideline company method in exhibit 5 of the Appendix

Guideline Company Multiples			
	Price/Tangible Book	Price/2012 Earnings	Price/2013 Earnings
Max	2.7	19.5	16.8
Upper Quartile	1.4	15.6	13.2
Mean	1.3	12.6	11.1
Median	1.1	11.7	10.5
Lower Quartile	0.9	10	9.1
Low	0.8	7	6.1
Selected Multiple	1.3	12.6	11.1

Analysis of Potential Triggering Events

During the fourth quarter of 2011, Republic experienced many events that required evaluation of potential triggering events, thus, a need to update the goodwill recoverability analysis performed in Q2, 2011. Events that are typically evaluated in accounting as potential triggering events include: a significant adverse change in legal factors or in the business climate, an adverse action or assessment by a regulator, unanticipated competition, a loss of key personnel, a more-likely-than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of, the testing for recoverability under Statement 144 of a significant asset group within a reporting unit, recognition of a goodwill impairment loss in the financial statements of a subsidiary that is a component of a reporting unit, other impairment charges or valuation allowances, recent cash or operating losses for a reporting unit due to market conditions with an expectation they may continue, weakness in a particular industry (e.g., airlines, auto, banks, retail, etc.), inability to meet quarterly expectations or downward revisions to forecasts for future periods, restructuring plans (e.g., store closures, layoffs, etc.).

During Q4, 2011, Republic incurred additional losses from continued adverse development from prior years and prior quarters causing further stress to Republic's statutory surplus. Additionally, Republic determined that its prior estimates of 2011 weather losses were understated and increased its ultimate projected loss for such events. Republic's available underwriting capacity was reduced because of the decline in statutory surplus from these losses. Republic has certain limitations and leverage exposures, including underwriting leverage whereby Republic should not in the current environment write premium above a certain underwriting leverage ratio. Therefore this stress to statutory surplus resulted in a change to Republic's near-term earnings forecasts. To illustrate, the amount of statutory surplus held by Republic indicates the amount of premium that can be written by Republic. The metric utilized in the insurance industry to evaluate such stress is described as underwriting leverage, or amount of net written premium as a percentage of statutory surplus. Republic's general guide to maintain viable underwriting leverage & reduce risk of downgrade is to not exceed 1.5x in the current soft market underwriting environment. During 2011, Republic's underwriting leverage reached a high level of 1.64x, caused primarily by the following:

- 1) Large catastrophic losses related to spring storms; historic events that caused significant amounts of damage
- 2) Adverse Development in multiple lines of business, primarily in Commercial Lines business. The total amount of adverse development was ~\$41MM, ~\$30MM driven by Commercial business

The loss of surplus reduces Republic's underwriting capacity which has an adverse impact on future revenue growth and resulting profitability of Republic. As a result, Republic needed to reduce projected net written premium, which in turn reduces future amounts of net earned premium (revenue). The primary result of this action was not proceeding to replace premiums in the Program Management business during the near term to



replace the premiums recently lost from a significant program in 2011. This loss of profitability and growth reduces future earnings and resulting cash flows that could be distributable to Delek Group Ltd.

Based on the above discussion, it was determined that a goodwill triggering event occurred during Q4, 2011, thus a complete goodwill impairment evaluation of the Republic CGU was performed as of 12/31/11.

Valuation Conclusion

Qualitative risks that add pressure to Republic's valuation and provide reasons to select valuations in the lower end of the range include:

- The risk profile of Republic has increased recently due to loss of statutory surplus and underwriting losses
- Republic's mix of business is more property weighted than casualty weighted. The recent years' weather volatility has resulted in a significant decline in property focused insurer valuations. Therefore, the control premium for property weighted insurers may be less than for other insurers.
- Republic's earnings projections have been significantly adversely impacted by the increased weather volatility – thus justifying a higher discount rate for valuation purposes
- As a result of the large underwriting losses, AM Best lowered the outlook of Republic from "Stable" to "Negative"
- After the close of 2011 year, Republic lost its President/CEO.

Based upon the fair value analysis, the range of potential valuations is indicated in the matrix below:

Recoverable Amount Indications				
CRP	Control Premium			
		20.0%	25.0%	30.0%
	0.5%	\$ 211.0	\$ 220.0	\$ 231.0
	1.0%	\$ 205.0	\$ 215.0	\$ 224.0
	1.5%	\$ 198.0	\$ 208.0	\$ 217.0

Above indications are calculated as fair value less selling costs
as prescribed by IFRS accounting rules; total selling costs approximate 15%

Delek Group Ltd. has historically valued Republic utilizing a 20% control premium and it believes this is still appropriate due to risk factors noted above. Accordingly, Delek Group Ltd. selected a 20% control premium factor in its value of Republic as of December 31, 2011. The goodwill impairment of Republic for the fourth quarter 2011 is computed as follows:

Estimate of goodwill impairment (in MM's)		
Estimated FV of Republic	\$	205
Carrying value Republic	\$	266
Implied impairment of Republic	\$	(61)

APPENDIX

Valuation Exhibits – The Republic Group

12/31/2011

Delek Group Ltd.

Table of Contents As of December 31, 2011

Exhibits

Exhibit 1	Summary of Values - Republic Companies, Inc.
Exhibit 2	Discounted Cash Flow Analysis - Republic Companies, Inc.
Exhibit 3	Cost of Equity
Exhibit 4	Market Approach Summary - Republic Companies, Inc.
Exhibit 5	Guideline Company Information
Exhibit 6	Costs to Sell Calculation



Exhibit 1
Delek Group Ltd.

Summary of Values
As of December 31, 2011

(\$millions)

<u>Valuation Methods</u>	<u>Exhibit</u>	<u>Weighting</u>	<u>Low</u>	<u>Mid</u>	<u>High</u>
Discounted Cash Flow Method	Exhibit 4	65.0%	\$ 192	\$ 213	\$ 234
Guideline Company Method	Exhibit 6	35.0%	218	227	236
Concluded Range of Fair Value of Equity			\$ 201	\$ 218	\$ 235
Less: Costs to Sell	Exhibit 8		(3)	(3)	(4)
Range of Fair Value less Costs to Sell (Recoverable Amount)			\$ 198	\$ 215	\$ 231
Carrying Value			266	266	266
Difference			\$ (68)	\$ (52)	\$ (35)



**Exhibit 2
Delek Group Ltd.**

**Discounted Cash Flow Analysis - Republic Companies, Inc.
As of December 31, 2011**

(US\$ millions)

				For years ended December 31,																
Fiscal Year	12/31/2009	12/31/2010	12/31/2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	
Gross Written Premiums	\$ 911	\$ 808	\$ 732	\$ 750	\$ 757	\$ 790	\$ 819	\$ 850	\$ 876	\$ 902	\$ 929	\$ 957	\$ 986	\$1,015	\$1,046	\$1,077	\$1,109	\$1,142	\$1,177	
Net Written Premiums	327	334	334	300	319	322	331	341	351	362	373	384	395	407	420	432	445	458	472	
Net Earned Premiums	365	315	354	303	326	317	326	336	346	357	367	378	390	401	413	426	439	452	465	
% Growth in Net Earned Premiums	-2.7%	-13.7%	12.2%	-14.4%	7.8%	-2.9%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	
Loss Incurred (xcat)	(173)	(132)	(185)	(117)	(123)	(129)	(129)	(132)	(136)	(140)	(143)	(148)	(152)	(157)	(162)	(167)	(172)	(177)	(182)	
Cat Loss Incurred	(52)	(20)	(60)	(26)	(23)	(27)	(52)	(26)	(28)	(57)	(31)	(31)	(64)	(33)	(34)	(70)	(36)	(77)	(38)	
LAE Incurred	(44)	(42)	(56)	(40)	(42)	(43)	(43)	(43)	(46)	(46)	(47)	(54)	(51)	(53)	(54)	(58)	(58)	(59)	(61)	
Total Losses	(269)	(194)	(301)	(183)	(188)	(199)	(224)	(201)	(210)	(243)	(222)	(233)	(268)	(243)	(250)	(295)	(265)	(313)	(281)	
Commissions	(72)	(58)	(69)	(60)	(63)	(59)	(61)	(61)	(63)	(65)	(67)	(69)	(71)	(73)	(75)	(78)	(80)	(82)	(85)	
Premium Taxes	(13)	(19)	(16)	(11)	(12)	(10)	(10)	(10)	(10)	(11)	(11)	(11)	(12)	(12)	(13)	(13)	(13)	(14)	(14)	
Other U/W Expense	(47)	(49)	(48)	(47)	(49)	(45)	(48)	(48)	(51)	(51)	(53)	(54)	(56)	(58)	(59)	(61)	(63)	(65)	(67)	
Change in DAC	2	(1)	2	1	(6)	1	1	1	1	1	1	1	1	1	1	1	1	1	1	
Total Expenses	(130)	(126)	(131)	(116)	(130)	(113)	(117)	(119)	(123)	(126)	(130)	(134)	(138)	(142)	(146)	(150)	(155)	(159)	(164)	
Underwriting Income	(34)	(5)	(79)	4	8	5	(14)	16	13	(13)	16	12	(15)	17	18	(20)	19	(21)	20	
Net Investment Income	17	15	16	16	16	19	22	26	26	28	29	33	36	38	39	46	48	50	53	
Realized Gain (Loss)	20	17	9	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Other Income	11	7	(13)	7	7	8	8	8	9	9	9	10	10	10	11	11	11	11	12	
Operating Income	14	33	(68)	26	32	32	16	50	48	24	55	55	30	65	67	37	78	41	85	
Interest Expense	(6)	(6)	(6)	(6)	(6)	(7)	(6)	(7)	(7)	(6)	(6)	(7)	(7)	(7)	(8)	(8)	(8)	(8)	(8)	
Earnings Before Taxes	8	27	(74)	21	26	25	10	43	41	18	48	48	23	58	59	29	70	33	77	
Income Taxes				(7)	(9)	(8)	(3)	(14)	(13)	(6)	(15)	(15)	(7)	(19)	(19)	(9)	(22)	(10)	(25)	
Net Income				14	17	17	6	29	28	12	33	33	16	39	40	20	48	22	52	
Underwriting Leverage				1.55	1.60	1.61	1.61	1.63	1.63	1.66	1.66	1.66	1.69	1.69	1.72	1.72	1.72	1.72	1.77	
Return on Equity				7.0%	8.3%	8.7%	3.2%	14.2%	13.1%	5.7%	14.8%	14.3%	6.9%	16.6%	16.8%	8.0%	18.6%	8.5%	19.8%	
Total Liabilities				584	571	566	574	573	579	598	604	616	638	646	657	683	691	717	724	
Stat. Surplus (BOY + 90 Percent GAAP NI as Estimate of Stat NI-5/12 Debt Service Div.)				228	221	226	217	243	246	239	260	265	257	281	289	274	306	290	325	
Statutory NWP (includes \$22m policy fees above GAAP NWP)				322	342	345	354	364	374	385	396	407	418	430	443	455	468	481	495	
Computed U/W Leverage				1.41	1.55	1.52	1.63	1.50	1.52	1.61	1.52	1.53	1.63	1.53	1.53	1.66	1.53	1.66	1.52	
Maximum Underwriting Leverage				1.55	1.60	1.61	1.61	1.63	1.63	1.66	1.66	1.66	1.69	1.69	1.72	1.72	1.72	1.72	1.77	
Required capital (using maximum U/W Leverage)				208	214	214	220	224	230	233	238	245	248	255	258	265	273	281	281	
Excess capital to be dividended (additional capital contribution)				20	7	13	(2)	20	16	6	22	20	9	27	30	8	33	10	45	
Periods Discounting				0.501	1.502	2.502	3.502	4.502	5.502	6.502	7.502	8.502	9.502	10.502	11.502	12.502	13.502	14.502	15.502	
Present Value Factor	14.3%			0.935	0.818	0.716	0.626	0.548	0.479	0.419	0.367	0.321	0.281	0.246	0.215	0.188	0.165	0.144	0.126	
Present Value of Cash Flow				19	6	9	(1)	11	8	3	8	6	3	7	7	2	5	1	6	
Present Value of Discrete Cash Flows				98																
Present Value of Terminal Year Value @ 11x1				72																
Indicated Fair Value of Equity - (Non-Controlling, Marketable Basis) (Rounded)				\$ 171																
Plus: Control Premium				25%																
Indicated Fair Value of Equity - (Controlling, Marketable Basis) (Rounded)				\$ 213																

Sensitivity Table			
Control Premium	Discount Rate		
	13.7% 14.3% 15.0%		
	20%	216	205 192
	25%	225	213 200
	30%	234	222 208

Implied multiples	
Price/TBV	1.2
Price/2012 E	12.5

Exhibit 3
Delek Group Ltd.
 Cost of Equity
 As of December 31, 2011
 (US\$ millions)

		Total Book Value of	Total Book Value of	Total Market Value of	Total Market Value of				Levered Equity	Unlevered
Ticker	Guideline Companies	Debt [1]	Preferred [1]	Equity [2]	Capital	Debt to Capital	Equity to Capital	Marginal Tax Rate	Beta [3]	Beta [4]
OB	OneBeacon Insurance Group, Ltd.	\$ 270	-	\$ 1,464	\$ 1,733	15.6%	84.4%	32.0%	0.9	0.8
STFC	State Auto Financial Corp.	117	-	549	666	17.5%	82.5%	37.2%	0.9	0.8
HGIC	Harleysville Group Inc.	119	-	1,536	1,655	7.2%	92.8%	41.5%	0.3	0.3
SAFT	Safety Insurance Group Inc.	-	-	615	615	0.0%	100.0%	41.2%	0.7	0.7
UFCS	United Fire Group, Inc	70	-	515	584	11.9%	88.1%	42.8%	0.9	0.9
RLI	RLI Corp.	100	-	1,564	1,664	6.0%	94.0%	38.1%	0.6	0.6
MIG	Meadowbrook Insurance Group Inc.	108	-	545	654	16.6%	83.4%	38.2%	0.9	0.8
HALL	Hallmark Financial Services Inc.	61	-	135	196	31.1%	68.9%	38.3%	1.0	0.8
AFSI	AmTrust Financial Services, Inc.	686	-	1,473	2,160	31.8%	68.2%	39.6%	0.9	0.7
SIGI	Selective Insurance Group Inc.	262	-	983	1,245	21.1%	78.9%	40.9%	1.0	0.9
DGIC.B	Donegal Group Inc.	75	-	420	495	15.2%	84.8%	41.5%	0.6	0.6
NAVIG	Navigators Group Inc.	114	-	677	791	14.4%	85.6%	39.6%	0.5	0.4
TWGP	Tower Group Inc.	403	-	823	1,226	32.9%	67.1%	39.6%	0.7	0.6
EIG	Employers Holdings, Inc.	132	-	681	813	16.2%	83.8%	38.3%	1.0	0.9
						Average	17.0%	83.0%		0.7
						Median	15.9%	84.1%		0.8
						Selected				0.8
		Low	Mid	High						
Unlevered Equity Beta		0.8	0.8	0.8	Unlevered Equity Beta = Levered Equity Beta / [1 + (1 - Tax Rate) x Debt-to-Equity].					
Debt to Equity		54.0%	58.2%	63.1%	Selected capital structure based on actual capital structure of the Reporting Units as of December 31, 2011.					
Selected Subject Tax Rate		32.0%	32.0%	32.0%						
Relevered Equity Beta		1.09	1.1	1.14	Levered Equity Beta = Unlevered Equity Beta x [1 + (1 - Tax Rate) x Debt-to-Equity].					
Risk-Free Rate		2.6%	2.6%	2.6%	20-Year U.S Treasury as of the Valuation Date. Source: Capital IQ.					
Equity Risk Premium		7.0%	7.0%	7.0%						
Levered Equity Beta		1.1	1.1	1.1						
Cost of Equity Capital		10.2%	10.4%	10.6%	Cost of Equity Capital = Risk-Free Rate + (Equity Beta x Equity Risk Premium).					
Unsystematic Risk Factors:										
Size Premium		2.9%	2.9%	2.9%	9th Decile Small Stock Premium. Source: SBBI Yearbook 2011.					
Company-Specific Risk Premium		0.5%	1.0%	1.5%						
Cost of Equity Capital		13.7%	14.3%	15.0%						



**Exhibit 4
Delek Group Ltd.**

Market Approach Summary - Republic Companies, Inc.
As of December 31, 2011
(US\$ millions)

Guideline Company Method

Price/Tangible Book	Range of Multiples	0.8 - 2.7
	Upper Quartile	1.4
	Mean	1.3
	Median	1.1
	Lower Quartile	0.9
	Selected Multiple	1.3
Price/2012 Earnings	Range of Multiples	7.0 - 19.5
	Upper Quartile	15.6
	Mean	12.6
	Median	11.7
	Lower Quartile	10.0
	Selected Multiple	12.6
Price/2013 Earnings	Range of Multiples	6.1 - 16.8
	Upper Quartile	13.2
	Mean	11.1
	Median	10.5
	Lower Quartile	9.1
	Selected Multiple	11.1

Selected Financial Information

Tangible Book Value of Equity	\$	143
2012 Earnings		14
2013 Earnings		17

Indicated Fair Value of Equity

	<u>Weight</u>	
Tangible Book Value of Equity	33.3%	\$ 187
2012 Earnings	33.3%	172
2013 Earnings	33.3%	<u>187</u>
Indicated Fair Value of Equity (Non-Controlling, Marketable)		\$ 182

	Low	Mid	High
Plus: Control Premium	20%	25%	30%
Indicated Fair Value of Equity (Marketable)	\$ 218	\$ 227	\$ 236



Exhibit 5
Delek Group Ltd.
 Guideline Company Information
 As of December 31, 2011
 (US \$Millions, except per share price)

	OneBeacon Insurance Group, Ltd.	State Auto Financial Corp.	Harleysville Group Inc.	Safety Insurance Group Inc.	United Fire Group, Inc.	RLI Corp.	Meadowbrook Insurance Group Inc.	Hallmark Financial Services Inc.	AmTrust Financial Services, Inc.	Selective Insurance Group Inc.	Donegal Group Inc.	Navigators Group Inc.	Tower Group Inc.	Employers Holdings, Inc.				
Name:	OB	STFC	HGIC	SAFT	UPCS	RLI	MIG	HALL	AFSI	SIGI	DGIC.B	NAVIG	TWGP	EIG				
Ticker:	OB	STFC	HGIC	SAFT	UPCS	RLI	MIG	HALL	AFSI	SIGI	DGIC.B	NAVIG	TWGP	EIG				
FY End:	December	December	December	December	December	December	December	December	December	December	December	December	December	December				
Source:	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ	CapitalIQ				
															Min	Max	Median	Average
Market Capitalization:																		
Shares Outstanding	95	40	27	15	26	21	51	19	62	55	26	14	41	38				
Price	\$ 15	\$ 14	\$ 57	\$ 40	\$ 20	\$ 73	\$ 11	\$ 70	\$ 24	\$ 18	\$ 16	\$ 48	\$ 20	\$ 18				
Market Cap	1,464	549	1,536	615	515	1,564	545	135	1,473	983	420	677	823	681				
9/30/2011 Book Value of Equity	1,100	601	752	655	685	867	580	212	838	1,087	388	803	1,014	506				
Guideline Company Financial Information:																		
Total Assets	5,925	2,812	3,282	1,489	3,605	2,794	2,342	744	5,419	5,749	1,285	3,670	4,347	3,514	744	5,925	3,398	3,356
Tangible Book Value	1,100	601	752	655	654	758	472	139	545	1,101	383	797	646	458	139	1,101	650	647
LTM Earnings	83	(206)	2	22	(3)	135	48	(11)	116	28	4	26	85	56	(206)	135	27	27
5-Year Average Earnings	80	(17)	59	58	34	119	43	12	99	66	20	46	82	86	(17)	119	59	56
LTM Net Earned Premiums (12/31/10)	1,488	1,257	866	552	469	493	660	278	746	1,417	378	660	1,293	322	278	1,488	660	777
LTM EPS	0.9	(5.1)	0.1	1.4	(0.1)	6.3	0.9	(0.6)	1.9	0.5	0.2	1.8	2.1	1.5	(5.1)	6.3	0.9	0.8
5-Year Average EPS	0.8	(0.4)	2.1	3.7	1.0	5.6	0.8	0.6	1.8	1.2	0.8	3.7	2.4	1.9	(0.4)	5.6	1.5	1.8
2012 EPS	1.1	N/A	2.9	3.7	N/A	4.5	1.1	0.1	2.9	1.6	N/A	2.7	2.9	1.5	0.1	4.5	2.7	2.3
2013 EPS	1.6	N/A	N/A	3.7	N/A	4.4	1.2	0.5	3.1	1.7	N/A	2.8	3.3	1.7	0.5	4.4	2.3	2.4
LTM Return on Equity	7.6%	nmf	0.2%	3.4%	nmf	15.6%	8.3%	nmf	13.8%	2.6%	1.1%	3.2%	8.4%	11.0%	0.2%	15.6%	7.6%	6.8%
5-Year Average ROE	13.4%	5.5%	7.9%	9.5%	5.9%	14.9%	8.9%	9.2%	18.0%	6.4%	5.4%	6.2%	12.0%	19.1%	5.4%	19.1%	9.0%	10.2%
LTM EPS Growth	-30.2%	nmf	-97.2%	-61.4%	-107.5%	4.6%	-15.2%	-258.9%	-20.5%	-59.7%	-64.2%	-58.1%	-26.3%	-6.0%	-258.9%	4.6%	-58.1%	-61.6%
FY2012 EPS Growth	27.8%	nmf	nmf	157.9%	nmf	-28.8%	15.5%	-109.0%	54.1%	204.8%	nmf	49.7%	37.5%	2.6%	-109.0%	204.8%	32.6%	41.2%
FY2013 EPS Growth	42.3%	N/A	N/A	0.3%	N/A	-1.2%	10.1%	900.0%	8.9%	10.1%	N/A	4.9%	15.3%	11.8%	-1.2%	900.0%	10.1%	100.3%
Calculated Multiples																		
Price/LTM Earnings	17.6	nmf	nmf	28.0	nmf	11.6	11.3	nmf	12.7	34.9	nmf	26.4	9.7	12.2	9.7	34.9	12.7	18.3
Price/Book	1.3	0.9	2.0	0.9	0.8	1.8	0.9	0.6	1.8	0.9	1.1	0.8	0.8	1.3	0.6	2.0	0.9	1.2
Price/Tangible Book	1.3	0.9	2.0	0.9	0.8	2.1	1.2	1.0	2.7	0.9	1.1	0.8	1.3	1.5	0.8	2.7	1.1	1.3
Price/2012 Earnings	13.8	N/A	19.5	10.9	N/A	16.2	9.8	nmf	8.3	11.4	N/A	17.7	7.0	11.9	7.0	19.5	11.7	12.6
Price/2013 Earnings	9.7	N/A	N/A	10.8	N/A	16.4	8.9	14.0	7.6	10.4	N/A	16.8	6.1	10.6	6.1	16.8	10.5	11.1

Notes:

Source: Capital IQ.



Exhibit 6
Delek Group Ltd.
Costs to Sell Calculation
As of December 31, 2011

					Costs to Sell (% of transaction amount) [1]
Closed Date	Target	Acquirer	Industry Classifications	Target Business Description	
10/19/2011	FPIC Insurance Group Inc.	The Doctors Company	Property and Casualty Insurance	FPIC Insurance Group, Inc., together with its subsidiaries, operates as an insurance carrier in the medical professional liability (MPL) insurance sector of the property and casualty insurance industry.	1.2%
3/28/2011	Mercer Insurance Group, Inc.	United Fire & Casualty Company	Property and Casualty Insurance	Mercer Insurance Group, Inc., through its subsidiaries, provides a range of property and casualty insurance products to individuals, and small and medium-sized businesses in the United States.	1.5%
11/30/2010	American Physicians Service Group Inc.	ProAssurance Corporation	Property and Casualty Insurance	American Physicians Service Group, Inc. operates as the holding company for a key operating subsidiary, APS Insurance Services, Inc., which provides medical professional liability insurance and related services for physicians and other healthcare providers primarily in Texas.	1.0%
11/13/2009	Specialty Underwriters' Alliance, Inc.	Tower Group Inc.	Property and Casualty Insurance	Specialty Underwriters' Alliance, Inc., through its subsidiary, CastlePoint National Insurance Company, provides specialty commercial property and casualty insurance products in the United States.	1.3%
12/1/2008	Philadelphia Consolidated Holding Corp.	Tokio Marine & Nichido Fire Insurance Co., Ltd.	Property and Casualty Insurance	Philadelphia Consolidated Holding Corp., doing business as Philadelphia Insurance Companies, engages in designing, marketing, and underwriting commercial property and casualty, and management and professional liability insurance products.	0.6%
7/31/2008	ProCentury Corporation	Meadowbrook Insurance Group Inc.	Property and Casualty Insurance	ProCentury Corporation, through its subsidiaries, operates as a property and casualty insurance holding company in the United States.	1.3%
6/4/2008	The Commerce Group, Inc.	Mapfre SA	Property and Casualty Insurance	The Commerce Group, Inc. operates as a holding company. The company, through its subsidiaries, provides personal and commercial property and casualty insurance products and services.	0.5%
6/19/1999	Chubb Specialty Insurance	The Chubb Corporation	Property and Casualty Insurance	Chubb Specialty Insurance offers property and casualty insurance services.	0.7%
6/18/1999	Amerin Corporation	Radian Group Inc.	Property and Casualty Insurance	As of June 9, 1999, Amerin Corporation was acquired by Radian Group Inc. Amerin Corporation provided private mortgage insurance coverage to mortgage bankers, savings institutions, commercial banks, and other lenders through its subsidiary, Amerin Guaranty Corporation, as of March 31, 1999.	0.6%
2/17/1998	Capital Markets Assurance Corporation	MBIA Inc.	Property and Casualty Insurance	In February 1998, Capital Markets Assurance Corporation's parent company CapMAC Holdings, Inc. was acquired by MBIA, Inc. Previously, Capital Markets Assurance Corporation, a monoline stock insurance company, offered financial guarantee and surety insurance, as of September 30, 1997.	0.6%

High	1.5%
Low	0.5%
Average	0.9%
Median	0.9%
Selected	1.0%

Notes:

Source: CapitalIQ.

[1] Costs to sell data reflect financial advisor fees.

Chapter C



Financial Statements

for December 31, 2011



Delek Group



Delek Defines Energy

Delek Group Ltd.
Consolidated Financial Statements as of December, 2011

Contents

	<u>Page</u>
Auditor's Report about the audit of the financial statements	2
Auditor's report about the audit of internal controls over financial reporting	3
Consolidated Balance Sheets	5-6
Consolidated Statements of Income	7
Consolidated Statements of Comprehensive Income	8
Consolidated Statements of Changes in Equity	9-11
Consolidated Statements of Cash Flows	12-17
Notes to the Consolidated Financial Statements	18-218
Appendix to the Financial Statements – Principal Partnerships and Investees	219-221

Auditor's Report
The Shareholders of Delek Group Ltd.

We have audited the accompanying consolidated balance sheets of Delek Group Ltd. ("the Company") as of December 31, 2011 and 2010 and the related consolidated statements of income, comprehensive income, changes in equity and the cash flows for each of the years ended on December 31, 2011, 2010 and 2009. These financial statements are the responsibility of the Company's management and board of directors. Our responsibility is to express an opinion on these financial statements based on our audit.

We did not audit the financial statements of certain subsidiaries, whose assets constitute approximately 30% and 33% of total consolidated assets as of December 31, 2011 and December 31, 2010, respectively, and whose consolidated revenues constitute approximately 4.6%, 7.72% and 8.1% of total consolidated revenues for the years ended December 31, 2011, 2010 and 2009, respectively. Furthermore, we did not audit the financial statements of certain investments in companies which are accounted for using the equity method, the investment in which amounted to NIS 704 million and NIS 1,594 million as of December 31, 2011 and 2011, respectively, and the Company's share of their earnings amounted to NIS 134 million, NIS 231 million and NIS 238 million for the years ended December 31, 2011, 2010 and 2009, respectively. The financial statements of those companies were audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based solely on the reports of the other auditors.

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

In our opinion, based on our audits and on the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2011 and 2010 and the results of their operations, changes in equity and cash flows for each of the years ended on December 31, 2011, 2010 and 2009, in conformity with International Financial Reporting Standards (IFRS) and with the provisions of the Israeli Securities Regulations (Annual Financial Statements), 2010, insofar as the provisions of these standards apply to insurance subsidiaries.

Without qualifying our opinion, we draw attention to Note 32(A) to the consolidated financial statements with respect to lawsuits filed against Group companies.

We have also audited, in conformity with Audit Standard 104 of the Institute of Certified Public Accountants in Israel, "Audit of Internal Control over Financial Reporting", internal controls over the Company's financial reporting as of December 31, 2011, and our report of March 29, 2012 includes an unqualified opinion of the effective fulfillment of these components.

Tel Aviv
March 29, 2012

Kost Forer Gabbay & Kasierer
Certified Public Accountants

**Auditor's report to the shareholders of Delek Group Ltd.
about the audit of internal controls over financial reporting
in accordance with section 9B(C) of the Securities Regulations
(Periodic and Immediate Reports), 1970**

We have audited the internal controls over the financial reporting of Delek Group Ltd. and its subsidiaries (together: "the Company") as of December 31, 2011. The controls were determined as explained in the following paragraph. The Company's board of directors and management are responsible for maintaining effective internal control over the financial reporting and for their assessment of the effectiveness of these internal controls over the financial reports attached to the periodic report at this date. Our responsibility is to express an opinion on the Company's internal controls over financial reporting based on our audit. We did not audit the effectiveness of the internal controls over the financial reporting of consolidated subsidiaries whose consolidated assets and revenues represent 24% and 2% respectively, of the amounts in the consolidated financial statements as of December 31, 2011 and the year then ended. The effectiveness of the internal controls over the financial reporting of those companies was audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to the effectiveness of the internal controls over the financial reporting of those companies, is based on the reports of the other auditors.

The internal controls over financial reporting which we audited were determined in accordance with Audit Standard 104 of the Institute of Certified Public Accountants in Israel, Audit of Internal Controls over Financial Reporting ("Audit Standard 104"). These controls are: (1) entity-level controls, including controls over the process for preparation and closing of financial reports and information technology general controls (ITGC); (2) cash and securities portfolio management process in the Company; (3) debt management process in the Company; significant processes in the consolidated statements that are managed in certain material companies are: (4) revenue cycle; (5) purchases and inventory cycle; (6) insurance reserves and contingent claims and financial investments of insurance companies ("the audited controls").

We conducted our audit in accordance with Audit Standard 104, which requires us to plan and perform the audit to identify the audited control components and to obtain reasonable assurance about whether these control components were effective in all material respects. Our audit included obtaining an understanding of the internal control over financial reporting, identifying the audited controls, assessing the risk for material weaknesses in the audited controls, and testing and evaluating the effectiveness of the planning and implementation of these controls based on the assessed risk. Our audit, regarding these controls, included performing other procedures, as we considered necessary under the circumstances. Our audit referred only to the audited controls, as opposed to internal control over all the significant processes regarding financial reporting, therefore our opinion refers to the audited controls only. Additionally, our audit did not refer to the reciprocal effects between the audited controls and those that are unaudited, therefore, our opinion does not take into account such possible effects. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinion in respect of the aforesaid.

Due to its inherent limitations, internal control over financial reporting in general, and internal control components in particular, may not prevent or disclose misstatement. Moreover, drawing forward-looking conclusions based on any present assessment of effectiveness involves risks that the controls may become inadequate due to changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

As described in the Directors' Report and Company management regarding the effectiveness of the internal control on the financial reporting ("the assessment of effectiveness report"), the assessment of effectiveness report does not include an assessment of the effectiveness of internal controls in respect of Lion Oil Company ("Lion"), which was acquired in the reporting period and was consolidated in the Company's consolidated financial statements as of December 31, 2011, and whose net assets less liabilities amounted to NIS 824 million as of December 31, 2011, and whose gain from this company amounted to NIS 56 million for the period beginning on April 29, 2011 (the date control was achieved in the acquired company) and ended on December 31, 2011. Accordingly, the audit of the internal controls over the financial reporting of the Company does not include our opinion of the internal controls of Lion.

In our opinion, based on our audit and on the reports of the other auditors, the Company has implemented effectively, in all material aspects, the audited control components as of December 31, 2011.

We have also audited, in accordance with generally accepted auditing standards in Israel, the Company's consolidated financial statements as of December 31, 2011 and 2010 and for each of the three years in the period ended December 31, 2011 and our report, dated March 29, 2012, includes an unqualified opinion of these financial statements, based on our audit and the reports of the other auditors, with reference to the contents of Note 32A to the consolidated financial statements regarding claims filed against Group companies.

Tel Aviv
March 29, 2012

Kost Forer Gabbay & Kasierer
Certified Public Accountants

Consolidated Balance Sheets

		December 31	
		2011	2010
	Note	NIS millions	
<u>Current assets</u>			
Cash and cash equivalents	3	3,610	3,443
Performance-based cash and cash equivalents in insurance companies	4	1,276	607
Short-term investments of the finance sector (mainly exchange-traded funds and deposits)	5	19,435	18,246
Short-term investments in insurance companies	11	1,717	1,660
Other short-term investments	6	715	1,008
Trade receivables	7	4,182	3,036
Insurance premium receivable	8	961	932
Other receivables	9	1,212	888
Current tax assets		88	81
Reinsurance assets	28	1,916	1,814
Inventory	10	3,041	1,273
Deferred acquisition costs in insurance companies	18	428	393
		38,581	33,381
Assets held for sale		-	59
		38,581	33,440
<u>Non-current assets</u>			
Financial investments of insurance companies	11	34,413	33,559
Long-term loans, deposits and receivables	12	758	589
Investments in other financial assets	13	500	2,527
Investments in associates and partnerships	14	2,333	3,801
Investment property	15	560	384
Investments in oil and gas exploration and production	16	11,463	1,523
Reinsurance assets	29	1,658	1,773
Property, plant and equipment, net	17	9,610	7,474
Deferred acquisition costs in insurance companies	18	761	721
Structured bonds	19	736	775
Goodwill	20	3,707	3,173
Other intangible assets, net	20	2,540	1,747
Deferred taxes	42(F)	280	272
		69,319	58,318
		107,900	91,758

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Balance Sheets

	Note	December 31	
		2011	2010
		NIS millions	
<u>Current liabilities</u>			
Interest bearing loans and borrowings	21	6,455	4,058
Trade payables	22	4,758	2,343
Other payables	23	5,249	3,810
Exchange-traded funds and deposit	24	18,962	17,927
Current tax liabilities		30	50
Financial derivatives		15	17
Liabilities for insurance contracts	30	6,032	5,478
		41,501	33,683
Liabilities associated with assets classified as held for sale		-	25
		41,501	33,708
<u>Non-current liabilities</u>			
Loans from banks and others	25	4,331	4,254
Debentures convertible into Company shares	26	-	247
Other debentures	27	13,241	12,117
Structured bonds	19	735	755
Financial derivatives		102	108
Employee benefit liabilities	29	274	209
Liabilities for insurance contracts	30	34,198	33,375
Provisions and other liabilities	31	1,020	908
Deferred taxes	42(F)	1,408	1,200
		55,309	53,173
<u>Capital</u>	34		
Share capital		13	13
Share premium		1,624	1,622
Option warrants and proceeds from conversion option		32	32
Retained earnings		3,723	1,618
Exchange differences on translation of foreign operations		(140)	(539)
Capital reserve from transactions with holders of non-controlling interests		(451)	(126)
Other reserves		(110)	156
Treasury shares		(131)	(124)
<u>Total equity attributable to equity holders of the parent</u>		4,560	2,652
<u>Non-controlling interests</u>		6,530	2,225
<u>Total equity</u>		11,090	4,877
		107,900	91,758

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

March 29, 2012

Date of approval of the financial
statements

Gabriel Last
Chairman of the
Board

Asi Bartfeld
CEO

Barak Mashraki
CFO

Consolidated Statements of Income

		Year ended December 31		
		2011	2010	2009
		NIS millions		
		(Other than earnings (loss) per share)		
	Note			
Revenues	44(B)	59,159	42,804 *)	37,043 *)
Cost of revenues	36	50,903	36,217 *)	31,154 *)
Gross profit		8,256	6,587	5,889
Selling, marketing and gas station operating expenses	37	4,157	3,502	3,385
General and administrative expenses	38	1,884	1,772	1,623
Other revenues (expenses), net	39	(602)	(88)	269
Operating income		1,613	1,225	1,150
Finance income	40	626	271	508
Finance expenses	40	(1,951)	(1,655)	(1,432)
		288	(159)	226
Gain (loss) from disposal of investments in partnerships and investees, net	14	3,749	(4)	518
Group's share in the gains (losses) of investees accounted by equity, net		(223)	156	91
Income (loss) before taxes on income		3,814	(7)	835
Taxes on income	42(G)	558	178	83
Gain (loss) from continuing operations		3,256	(185)	752
Income from discontinued operations, net	14	-	2,139	451
Net income		3,256	1,954	1,203
Attributable to:				
Equity holders of the parent		2,610	1,701	864
Non-controlling interests		646	253	339
		3,256	1,954	1,203
<u>Net earnings (loss) per share attributable to equity holders of the parent (NIS)</u>	43			
<u>Basic net earnings (loss)</u>				
Gain (loss) from continuing operations		231.69	(26.05)	55.18
Earnings from discontinued operations		-	176.75	21.72
		231.69	150.70	76.90
<u>Diluted net earnings (loss)</u>				
Gain (loss) from continuing operations		231.46	(26.05)	54.52
Earnings from discontinued operations		-	176.71	20.44
		231.46	150.66	74.96

*) Reclassified

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Comprehensive Income

	Year ended December 31		
	2011	2010	2009
	NIS million		
<u>Net income</u>	3,256	1,954	1,203
Other comprehensive income (loss) from continuing operations (net of tax effect):			
Gain (loss) for available-for-sale financial assets	(95)	371	349
Transfer to the statement of income for disposal of available-for-sale financial assets	(338)	(32)	(82)
Transfer to the statement of income for impairment of available-for-sale financial assets	119	7	2
Gain (loss) for cash flow hedges	6	(5)	(115)
Exchange differences on translation of foreign operations	358	(381)	19
Transfer to the statement of income for exchange differences on translation of foreign operations	37	-	-
Other comprehensive income (loss) of associates	134	(85)	12
Other comprehensive income (loss) from continuing operations	221	(125)	185
Other comprehensive loss from discontinued operations	-	(2)	(309)
Amounts released following loss of control	-	(27)	523
Total other comprehensive income (loss)	221	(154)	399
Total comprehensive income	3,477	1,800	1,602
Attributable to:			
Equity holders of the parent	2,746	1,586	1,113
Non-controlling interests	731	214	489
	3,477	1,800	1,602

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Changes in Equity

	Attributable to equity holders of the Company										
	Share capital	Share premium	Option warrants	Retained earnings	Exchange differences on translation of foreign operations	Capital reserve from transactions with non-controlling interests	Other capital reserves	Treasury shares	Total	Non-controlling shareholders	Total equity
						NIS Millions					
Balance as of January 1, 2011	13	1,622	32	1,618	(539)	(126)	156	(124)	2,652	2,225	4,877
Net income	-	-	-	2,610	-	-	-	-	2,610	646	3,256
Other comprehensive income (loss)	-	-	-	-	402	-	(266)	-	136	85	221
Total comprehensive income (loss)	-	-	-	2,610	402	-	(266)	-	2,746	731**)	3,477
Acquisition of treasury shares by a subsidiary	-	-	-	-	-	-	-	(10)	(10)	-	(10)
Sale of treasury shares by a subsidiary	-	2	-	-	-	-	-	3	5	2	7
Dividends	-	-	-	(505)	-	-	-	-	(505)	-	(505)
Cost of share-based payment, net	-	-	-	-	-	-	-	-	-	75	75
Exercise of warrants for shares by non-controlling interests	-	-	-	-	-	40	-	-	40	115	155
Acquisition s from holders of non-controlling interests	-	-	-	-	(3)	(292)	-	-	(295)	(242)	(537)
Put option for in a subsidiary	-	-	-	-	-	(99)	-	-	(99)	(21)	(120)
Options exercised for shares of a subsidiary	-	-	-	-	-	-	-	-	-	3	3
Expiry of option warrants in a subsidiary	-	-	-	-	-	2	-	-	2	(2)	-
Dividend to non-controlling interests	-	-	-	-	-	-	-	-	-	(58)	(58)
Acquisition of a subsidiary	-	-	-	-	-	-	-	-	-	3,611	3,611
Consolidation of a financial asset classified as available for sale	-	-	-	-	-	-	-	-	-	86	86
Deconsolidation of a subsidiary	-	-	-	-	-	-	-	-	-	(12)	(12)
Sale of shares to non-controlling interests, net	-	-	-	-	-	24	-	-	24	17	41
Balance as of December 31, 2011	13	1,624	32	3,723	(140)	(451)	(110)	(131)	4,560	6,530	11,090

*) Mainly capital reserve for available-for-sale financial assets

**) Composition of comprehensive income of non-controlling interests:

Net income attributable to non-controlling interests	646
Loss for available-for-sale financial assets, net	(46)
Gain from cash flow hedges, net	3
Exchange differences on translation of foreign operations	119
Other	(5)
Share in other comprehensive income, net of associates	14
Total comprehensive income attributable to non-controlling interests	<u>731</u>

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated statements of changes in equity**Attributable to equity holders of the Company**

	Share capital	Share premium	Option warrants	Retained earnings	Exchange differences on translation of foreign operations	Capital reserve from transactions with non-controlling interests	Other capital reserves *)	Treasury shares	Total	Non-controlling shareholders	Total equity
						NIS Millions					
<u>Balance as of January 1, 2010</u>	13	1,590	25	877	(166)	-	(102)	(129)	2,108	2,480	4,588
Net income	-	-	-	1,701	-	-	-	-	1,701	253	1,954
Other comprehensive income (loss)	-	-	-	-	(373)	-	258	-	(115)	(39)	(154)
Total comprehensive income (loss)	-	-	-	1,701	(373)	-	258	-	1,586	214***)	1,800
Sale of treasury shares by a subsidiary	-	3	-	-	-	-	-	5	8	3	11
Acquisition of shares from non-controlling interests	-	-	-	-	-	(148)	-	-	(148)	(56)	(204)
Exercise of warrants	-**)	29	-	-	-	-	-	-	29	-	29
Dividends	-	-	-	(960)	-	-	-	-	(960)	-	(960)
Conversion component for convertible debentures (net of issue expenses)	-	-	7	-	-	-	-	-	7	-	7
Cost of share-based payment, net	-	-	-	-	-	-	-	-	-	42	42
Exercise of warrants for shares by non-controlling interests	-	-	-	-	-	(12)	-	-	(12)	21	9
Expiry of warrants in a subsidiary	-	-	-	-	-	8	-	-	8	(8)	-
Deconsolidation of a subsidiary	-	-	-	-	-	-	-	-	-	(336)	(336)
Sale of shares to non-controlling interests, net	-	-	-	-	-	26	-	-	26	-	26
Issue of shares to non-controlling interests	-	-	-	-	-	-	-	-	-	24	24
Dividend to non-controlling interests	-	-	-	-	-	-	-	-	-	(159)	(159)
<u>Balance as of December 31, 2010</u>	<u>13</u>	<u>1,622</u>	<u>32</u>	<u>1,618</u>	<u>(539)</u>	<u>(126)</u>	<u>156</u>	<u>(124)</u>	<u>2,652</u>	<u>2,225</u>	<u>4,877</u>

*) Mainly capital reserve for available-for-sale financial assets

***) Represents an amount less than NIS 1 million

****) Composition of comprehensive income of non-controlling interests:

Net income attributable to non-controlling interests	253
Gain from available-for-sale financial assets, net	48
Exchange differences on translation of foreign operations	(78)
Share in other comprehensive loss of associates, net	(9)
Total comprehensive income attributable to non-controlling interests	<u>214</u>

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Changes in Equity

	Attributable to equity holders of the Company							Non-controlling shareholders	Total equity	
	Share capital	Share premium	Option warrants	Retained earnings	Exchange differences on translation of foreign operations	Other capital reserves *)	Treasury shares			Total
	NIS million									
Balance as of January 1, 2009	13	1,583	-	1,052	(928)	(97)	(105)	1,518	2,845	4,363
Net income	-	-	-	864	-	-	-	864	339	1,203
Other comprehensive income	-	-	-	-	188	61	-	249	150	399
Total comprehensive income	-	-	-	864	188	61	-	1,113	489***)	1,602
Acquisition of treasury shares	-	-	-	-	-	-	(33)	(33)	-	(33)
Sale of treasury shares by a subsidiary	-	6	-	-	-	-	9	15	8	23
Acquisition of shares from non-controlling interests	-	-	-	-	-	-	-	-	(109)	(109)
Distribution of subsidiary shares as a dividend in kind	-	-	-	(679)	574	(66)	-	(171)	(835)	(1,006)
Dividends	-	-	-	(360)	-	-	-	(360)	-	(360)
Issuance of options	-	-	25	-	-	-	-	25	-	25
Conversion of convertible debentures into Company shares	-**)	1	-	-	-	-	-	1	-	1
Cost of share-based payment, net	-	-	-	-	-	-	-	-	44	44
Acquisition of a subsidiary	-	-	-	-	-	-	-	-	55	55
Decrease in ownership and issuance of shares in subsidiaries	-	-	-	-	-	-	-	-	130	130
Dividend to non-controlling interests	-	-	-	-	-	-	-	-	(147)	(147)
Balance as of December 31, 2009	13	1,590	25	877	(166)	(102)	(129)	2,108	2,480	4,588

*) Mainly capital reserve for available-for-sale financial assets

**) Represents an amount less than NIS 1 million

***) Composition of comprehensive income of non-controlling interests:

Net income attributable to non-controlling interests	339
Gain from available-for-sale financial assets, net	92
Loss from cash flow hedges, net	(19)
Exchange differences on translation of foreign operations	78
Share in other comprehensive loss of associates, net	(1)
Total comprehensive income attributable to non-controlling interests	489

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows

	Year ended December 31		
	2011	2010	2009
	NIS million		
<u>Cash flows from operating activities</u>			
Net income	3,256	1,954	1,203
Adjustments to reconcile cash flows from continuing operating activities (a)	(1,085)	(1,418)	1,742
Net cash flows from continuing operating activities	2,171	536	2,945
Net cash flows from discontinued operating activities	(70)	508	333
Net cash flows from (used in) operating activities	2,101	1,044	3,278
<u>Cash flows from investing activities</u>			
Purchase of property, plant and equipment and intangible assets	(1,105)	(875)	(1,513)
Acquisition of investment property	(134)	(17)	(6)
Proceeds from sale of property, plant and equipment and investment property	24	48	117
Proceeds from property damage insurance, net	-	15	162
Proceeds from sale (acquisition) of financial assets, net	1,527	(1,220)	(185)
Loans to associates, net	(161)	(39)	(13)
Short-term investments, net	277	(72)	36
Increase in joint ventures for oil and gas exploration	(981)	(307)	(353)
Proceeds from sale of oil and gas assets	572	-	-
Proceeds from sale of investments in associates, net	89	33	409
Proceeds for disposal of investments in previously consolidated subsidiaries (c)	18	911	317
Investment in investees and partnerships accounted for using the equity method	(153)	(117)	(109)
Acquisition of operations, associates and available-for-sale financial assets consolidated for the first time (b)	(675)	(1,059)	136
Collection (grant) of loans to others, net	14	29	(102)
Net cash used for continuing investing activities	(688)	(2,670)	(1,104)
Net cash from (used for) discontinued investment activities	-	(4)	329
Net cash used for investment activities	(688)	(2,666)	(775)

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows (Contd.)

	Year ended December 31		
	2011	2010	2009
	NIS million		
<u>Cash flow from finance activities</u>			
Short-term loans from banks and others, net	279	451	(1,322)
Sale of shares to non-controlling interests	9	34	95
Acquisition of shares from non-controlling interests	(318)	(204)	(103)
Receipt of long-term loans	4,264	4,653	3,992
Repayment of long-term loans	(4,248)	(4,918)	(3,684)
Issue of shares to non-controlling interests	3	24	216
Exercise of warrants for subsidiary shares	10	9	-
Dividends paid	(505)	(1,143)	(177)
Dividend paid to non-controlling shareholders in subsidiaries	(56)	(25)	(51)
Exercise of warrants for Company shares	-	16	-
Acquisition of treasury shares	(10)	-	(33)
Sale of treasury shares	9	11	31
Cash of a previously consolidated subsidiary distributed as a dividend	-	-	(349)
Payment of contingent liability for a put option to non-controlling interests	(141)	(179)	(340)
Issue of debentures and debentures convertible into shares (less issuance expenses)	1,415	2,894	2,769
Buyback of debentures	(6)	-	-
Issue of warrants by the Company	-	-	25
Repayment of debentures	(1,267)	(708)	(443)
Net cash (used for) continuing finance activities	(562)	960	626
Net cash used for discontinued finance activities	-	(268)	(551)
Net cash from (used for) finance activities	(562)	692	75
<u>Exchange differences on balances of cash and cash equivalents – continuing operations</u>	(15)	(112)	6
<u>Exchange differences on balances of cash and cash equivalents from discontinued operations</u>	-	-	16
<u>Increase (decrease) in cash and cash equivalents – continuing operations</u>	906	(1,286)	2,473
<u>Increase (decrease) in cash and cash equivalents – discontinued operations</u>	(70)	236	127
<u>Cash and cash equivalents at the beginning of the period (including performance-based balance)</u>	4,050	5,100	2,500
<u>Cash and cash equivalents at the end of the period (including performance-based balance)</u>	4,886	4,050	5,100

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows (Contd.)

		Year ended December 31		
		2011	2010	2009
		NIS million		
(A)	<u>Adjustments to reconcile cash flows from continuing operating activities:</u>			
	Adjustments to profit or loss:			
	Income from discontinued operation, net	-	(315)	(451)
	Depreciation, depletion, amortization and impairment of assets	1,861	1,128	963
	Deferred taxes, net	337	5	109
	Decrease in employee benefit liabilities, net	(7)	(4)	(2)
	Decrease of loans granted, net	270	7	1
	Loss (gain) from issue of shares to a third party in an associate	(2)	4	(5)
	Gain from the sale of property, plant and equipment, real estate and investments, net	(165)	(113)	(713)
	Gain from revaluation of an investment after following acquisition of control	(3,684)		
	Loss (gain) from the sale of investments in subsidiaries	-	(1,824)	4
	Gain on involuntary conversion of assets	-	(15)	(162)
	Gain from negative goodwill	-	-	(15)
	Group's share in losses (earnings) of partnerships and associates, net (1)	371	(117)	(67)
	Change in fair value of financial assets and financial derivatives, net	(127)	208	59
	Increase in long-term liabilities, net	548	274	845
	Increase (decrease) in deferred acquisition costs	(63)	(80)	36
	Cost of share-based payment	78	68	52
	Change in financial investments of insurance companies, net	(1,544)	(4,529)	(5,216)
	Investments net of proceeds from the sale of available-for-sale assets in insurance companies, net	654	(367)	365
	Increase in reserves and contingent liabilities in insurance companies	6,958	5,614	6,102
	Decrease (Increase) in reinsurance assets	171	(130)	(532)
	Gain from premature payment and exchange of debentures	-	-	(82)
	Changes in operating assets and liabilities:			
	Increase in trade receivables	(931)	(421)	(540)
	Decrease (increase) in other accounts receivable	(187)	351	210
	Increase in inventory	(807)	(86)	(271)
	Increase in other assets, net	(161)	(43)	(516)
	Increase in trade payables	1,480	428	736
	Increase (decrease) in other accounts payable	(6,135)	(1,461)	832
		(1,085)	(1,418)	1,742
	(1) Net of dividends received	148	39	24

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows (Contd.)

	Year ended December 31		
	2011	2010	2009
	NIS million		
(B) <u>Acquisition of operations, associates and available-for-sale financial assets consolidated for the first time</u>			
Working capital, net (excluding cash and cash equivalents)	1,005	(341)	124
Capital gain from revaluation of an investment following acquisition of control	3,683		
Short-term finance investments	-	-	(9,462)
Finance investments for holders of ETFs and deposit certificates	(465)	-	(2,057)
Property, plant and equipment, investments and other property (including goodwill)	(3,233)	(1,166)	(1,319)
Long term receivables	(65)	(17)	-
Deferred taxes	(48)	9	-
Investments in oil and gas exploration	(9,397)		
Short-term finance liabilities	-	-	9,255
Current liabilities	238	237	-
Non-current liabilities	1,536	194	3,102
Investment and loan to an associate	1,073	(39)	107
Liability for debentures, ETFs, reverse certificates and complex certificates	466		
Offset of loans to an associate	393	-	-
Issue of shares to sellers	151	-	-
Holders of non-controlling interests	3,701	-	-
Elimination of investments in investees and associates, loans to associates and available-for-sale financial assets	287	64	386
	<u>(675)</u>	<u>(1,059)</u>	<u>136</u>
(C) <u>Proceeds from disposal of investments in previously consolidated subsidiaries (c)</u>			
Working capital	-	1,065	-
Oil and gas assets	-	-	332
Short-term investments of the finance sector and in insurance companies	-	(18)	-
Investment property and property, plant and equipment	-	260	-
Goodwill	-	15	-
Assets classified as available for sale	55	-	-
Other non-current assets	-	361	-
Credit from banks and others	-	(832)	-
Non-current liabilities	-	(48)	-
Liabilities attributable to assets classified as held for sale	(25)	-	-
Non-controlling interests	-	(336)	-
Non-controlling interests attributable to deconsolidation of a company	(12)	-	-
Investment in a company accounted for at equity	-	(1,353)	-
Capital reserve	-	(27)	(2)
Receivables for the disposal of an investment in a subsidiary	-		(9)
Gain (loss) for the sale of subsidiaries	-	1,824	(4)
	<u>18</u>	<u>911</u>	<u>317</u>

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows (Contd.)

	Year ended December 31		
	2011	2010	2009
	NIS million		
(D) <u>Significant non-cash activities</u>			
Purchase of property, plant and equipment and intangible assets	107	23	395
Liability for decommission of assets	-	8	1
Dividend payable to non-controlling shareholders in subsidiaries	-	-	22
Dividend declared	-	-	183
Dividend payable by associates	-	51	-
Exchange of debentures	-	-	658
Exercise of warrants	-	13	-
Liability for the acquisition of shares from non-controlling interests	-	8	-
Repayment of loans provided to an associate against issue of a capital note in a subsidiary	394	-	-
Consolidation for the first time of an available-for-sale financial asset in return for issue of shares in a subsidiary	151	-	-
Credit disposal of property, plant and equipment	-	-	-
Acquisition of shares of a subsidiary for participation units of an associate partnership and consolidated partnership	415	-	-
Investment in oil and gas assets	268	190	43
Acquisition of participating units in an associate against issue of shares in a subsidiary	-	-	250
Receivables for the sale of an investee	-	-	9
Put option for shares and option warrants of a subsidiary	123	-	-
Receivables for disposal of investment in available for sale financial assets	149	-	-
Receivables for the acquisition of an investee	-	99	-

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows (Contd.)

		Year ended December 31		
		2011	2010	2009
		NIS million		
(E)	<u>Cash and cash equivalents</u>			
	Cash and cash equivalents at the beginning of the period:			
	Cash and cash equivalents	3,443	3,997	1,895
	Performance-based cash and cash equivalents in insurance companies	607	1,103	605
		4,050	5,100	2,500
	Cash and cash equivalents at the end of the period			
	Cash and cash equivalents	3,610	3,443	3,997
	Performance-based cash and cash equivalents in insurance companies	1,276	607	1,103
		4,886	4,050	5,100
(F)	<u>Additional information on cash flows</u>			
	Cash paid during the period for:			
	Interest	1,179	893	902
	Taxes on income	453	361	111
	Cash received during the period for:			
	Interest	893	461	997
	Dividends	202	54	156
	Taxes	53	72	-

The accompanying notes and the appendix are an integral part of the consolidated financial statements.

Notes to the Consolidated Financial Statements

NOTE 1 – GENERAL

- A.** Delek Group Ltd. ("the Company") is a holding company which holds two major companies that coordinate the operations of the Group companies as follows: Delek Petroleum Ltd. ("Delek Petroleum"), which coordinates the fuel sector and the operation of gas stations and convenience stores in Israel, Europe and the USA, including the operation of the oil refinery and marketing of fuels in the USA; and Delek Investments and Properties Ltd. ("Delek Investments"), which coordinates the remaining operations of the Group, including automotive, oil and gas exploration and production, insurance in Israel and in the USA, infrastructure, automotive, biochemistry, and other operations. See also Note 44 regarding the operating segments of the Group.

On December 28, 2011, the Company completed the acquisition of the shares of Cohen Development and Industrial Buildings Ltd. ("Cohen Development"). Accordingly, as from this date, the Group consolidates the financial statements of Avner Oil Exploration – Limited Partnership ("Avner Partnership") and following acquisition of control, the Group recognized a gain of NIS 3.6 million from revaluation of the balance of the investment in Avner Partnership immediately prior to achieving control. See also Note 14(M)(6) below.

- B.** As of December 31, 2011, the Group has a consolidated working capital deficit in the amount of NIS 3 billion, mainly due to long- and short-term liabilities assumed to finance long term investments, which are due for repayment in the coming year.

The management of the Company and the subsidiaries believes that it is able to achieve cash flow sources to continue investments and repay liabilities due, inter alia, to the companies' ability to generate cash flows from operating activities, the significant volume of assets (which are unencumbered and in some cases marketable) that are exercisable if necessary and due to the estimate of Group companies that they are able to continue to raise short and long-term financing. In this context, it is noted that the Company believes that the finance agreement signed for the Leviathan project in December 2011, and the finance arrangements for the Tamar project (see Note 16 below) will also allow continued financing of the investments and repayment of short term liabilities.

C. Definitions

In these financial statements -

The Company	- Delek Group Ltd.
The Group	- The Company and its subsidiaries and partnerships which are consolidated in the consolidated financial statements
Subsidiaries	- Companies and partnerships controlled by the Company (as defined in IAS 27, Revised) and their financial statements are consolidated with the financial statements of the Company
Associates	- Companies and partnerships over which the Company has significant influence or has a contractual arrangement for joint control and the Group investment in these companies is accounted for using the equity method
Investees	- Subsidiaries or associates and partnerships See also the appendix to the financial statements listing the principle partnerships and investees
Interested parties and controlling shareholders	- As defined in the Israeli Securities Regulations (Annual Financial Statements), 2010
Related parties	- As defined in IAS 24 (Revised)
CPI	- The Consumer Price Index published by the Central Bureau of Statistics in Israel
USD	- US dollar

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES

A. Basis of presentation

The financial statements of the Company have been prepared on a cost basis, except for investment property, derivative instruments (including embedded derivatives) and certain financial instruments, current tax assets and liabilities, deferred tax assets and liabilities, and liabilities in respect of share-based payments, which are measured at fair value. In addition, investments are accounted for using the equity method.

The Company has elected to present the statement of income using the function of expense method.

Basis of preparation of the financial statements

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). These standards include the following:

1. International Financial Reporting Standards (IFRS)
2. International Accounting Standards (IAS)
3. International Financial Reporting Interpretations Committee (IFRIC) and Standing Interpretations Committee (SIC)

Furthermore, the financial statements have been prepared in conformity with the provisions of the Israeli Securities Regulations (Annual Financial Statements), 2010, insofar as these regulations are applicable to consolidated insurance companies.

Consistent accounting policy

The accounting policies applied in the consolidated financial statements have been applied consistently to all the periods presented, except as mentioned below.

Changes in accounting policy in view of adoption of new standards

IAS 24 – Related Party Disclosures

The amendment to IAS 24 ("the amendment") clarifies the definition of a related party in order to simplify the identification of such relationships and to eliminate inconsistencies in its application. In addition, government-related companies are provided a partial exemption of disclosure requirements for transactions with the government and other government-related companies. The amendment is effective retrospectively in the financial statements for annual periods commencing from January 1, 2011.

Retrospective application of the amendment did not have a material effect on the Group's financial statements.

IAS 32 – Financial Instruments: Presentation - Classification of Rights Issues

The amendment to IAS 32 ("the amendment") determines that rights, options or warrants to acquire a fixed number of the Company's equity instruments for a fixed amount of any currency are classified as equity instruments if the Company offers the rights, options or warrants pro rata to all of its existing owners of the same class of its non-derivative equity instruments. The amendment is effective retrospectively in the financial statements for annual periods commencing from January 1, 2011.

Retrospective application of the amendment did not have a material effect on the Group's financial statements.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

IFRS 3 (Revised) – Business Combinations

The amendments to IFRS 3 (Revised) address the following issues:

A) Measurement of non-controlling interests

The amendment limits the circumstances in which it is possible to choose the measurement of non-controlling interests based on their fair value on the date of acquisition or at the present ownership instruments' share in the recognized amounts of the acquiree's identifiable net assets. According to the amendment, this option is only available for types of non-controlling interests that entitle their holders to present ownership interests and a proportionate share to the entity's net assets in the event of liquidation (usually shares). In contrast, other types of non-controlling interests (such as options that represent equity instruments in the acquiree) do not allow such choice and must be measured at fair value on the acquisition date, unless another measurement basis is required by IFRSs such as in IFRS 2. The amendment is applied retrospectively from initial application of IFRS 3.

Retrospective application of the amendment did not have a material effect on the Group's financial statements.

B) Share-based payment awards in a business combination

The amendment elaborates the accounting treatment of a business combination that refers to the exchange of the acquiree's share-based payment transactions (whether it is obligated or chooses to exchange them) with the acquirer's share-based payment transactions. Accordingly, the acquirer must allocate a value on the acquisition date and an expense in the period following the acquisition date. However, if the award expires as a result of the business combination and is exchanged for a new award, the value of the new award in accordance with IFRS 2 will be recognized as an expense in the period following the acquisition date and will not be included in the purchase price. Furthermore, if share-based payment awards are not exchanged, then, if the instruments have vested, they will form part of the non-controlling interests and are measured pursuant to the provisions of IFRS 2. If the instruments have not vested, they will be measured at the value that would have been used had they been re-granted on the acquisition date whereby this amount is allocated between the non-controlling interests and the post-acquisition expense. The amendment is applied retrospectively from initial application of IFRS 3.

Retrospective application of the amendment did not have a material effect on the Group's financial statements.

C) Transition provisions for accounting for contingent consideration in a business combination that occur prior to the adoption of IFRS 3 (Revised)

According to the amendment, the amendments to IFRS 7, IAS 32 and IAS 39 which prescribe that contingent consideration in a business combination is within the scope of these standards, do not apply to contingent consideration in respect of a business combination whose acquisition date preceded the date of adoption of IFRS 3 (Revised). For this contingent consideration, the provisions of IFRS 3 prior to the amendment will continue to apply. The amendment is applied retrospectively from January 1, 2011.

Retrospective application of the amendment did not have a material effect on the Group's financial statements.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

IFRS 7 – Financial Instruments: Disclosure

The amendment to IFRS 7 ("the amendment") clarifies the disclosure requirements prescribed by the standard. The standard emphasizes the interaction between the quantitative disclosures and qualitative disclosures about the nature and extent of the risks arising from financial instruments. The disclosure requirements for collateral held by the Company have been reduced and the disclosure requirements for credit risk have been revised. The amendment is effective retrospectively in the financial statements for periods starting from January 1, 2011.

Retrospective application of the amendment did not have a material effect on the Company's financial statements.

IFRIC 14 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

The amendment to IFRIC 14 ("the amendment") provides guidance on assessing the recoverable amount of a defined benefit plan asset. The amendment allows a company to account for the prepayment of a minimum funding requirement as an asset. The amendment is effective retrospectively in the financial statements for periods starting from January 1, 2011.

Retrospective application of the amendment did not have a material effect on the Group's financial statements.

IFRIC 19 – Extinguishing Financial Liabilities with Equity Instruments

IFRIC 19 ("the Interpretation") addresses the accounting treatment of transactions in which financial liabilities are settled by issuing equity instruments. According to the Interpretation, equity instruments issued as a replacement of a debt instrument are measured at fair value unless this cannot be reliably measured, in which case they are measured at the fair value of the financial liability when extinguished. The difference between the carrying amount of the financial liability extinguished and the fair value of the equity instruments issued is recognized in profit or loss. The Interpretation is applied retrospectively from January 1, 2011.

Retrospective application of the Interpretation did not have a material effect on the Group's financial statements.

B. Estimates, assumptions and judgments

The preparation of the financial statements requires the managements of the Company and subsidiaries to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income, expenses and capital. These estimates and underlying assumptions are reviewed regularly. Changes in the accounting estimates are reported in the period of the change in estimate. The main estimates and assumptions applied in the financial statements concerning uncertainties at the balance sheet date and the critical estimates computed by the Group that may result in a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

– Impairment of non-financial assets

The Group evaluates the need to record an impairment of the carrying amount of non-financial assets, including property, plant and equipment, intangible assets with a defined useful life, and investments accounted for according to the equity method, whenever events or changes in circumstances indicate that the carrying amount is not recoverable. See section U below.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

In addition, the Group reviews goodwill for impairment at least once a year. This requires management to assess the expected future cash flows from continued use of the cash-generating units and also to select a suitable discounted rate for these cash flows. See additional information in section U below.

As from the acquisition date, goodwill is allocated to a cash-generating unit or a group of cash-generating units which are expected to generate benefits from the synergy of the combination.

– Impairment of financial assets at amortized cost

When there is objective evidence of impairment on loans and borrowings recorded at amortized cost, or on available-for-sale financial assets, the amount of the loss is recognized in profit or loss. See Note L below. Management is required to determine whether there is such objective evidence.

Impairment of available-for-sale financial assets

At each balance sheet date, the Group reviews whether there is objective evidence that the value of an asset has been impaired. In testing impairment, the Group has made judgments as to indications that support objective evidence of impairment of these assets. See also section L.

– Embedded derivatives

The Group assesses whether an embedded derivative is required to be separated from the host contract, and in particular, whether the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract. If separation of the embedded derivative is required, then this component will be measured separately from the host contract as a financial instrument at fair value through profit or loss, or the entire instrument will be measured, according to the applicable measurement provisions.

– Doubtful accounts

The allowance for doubtful accounts is determined in respect of specific debts whose collection, in the opinion of the Company's management, is doubtful. The Company also recognizes a provision for groups of customers that are collectively assessed for impairment based on their credit risk characteristics. Impaired debts are derecognized when they are assessed uncollectible.

– Determining recoverability of deferred acquisition costs

Acquisition costs of life assurance policies are deferred and amortized over the term of the policy. Recoverability of deferred acquisition costs is assessed once a year using assumptions regarding the cancellation, mortality and morbidity rates and other variables. If these assumptions are not realized, accelerated amortization or even derecognition of the deferred acquisition costs could be required.

– Liabilities for insurance contracts

Liabilities for insurance contracts are based on actuarial assessment methods and on assessments of demographic and economic variables. The actuarial estimates and assumptions are based on past experience and are based, primarily, on the past behavior and claims which represent what will happen in the future. The changing risk factors, frequency or severity of the events, and the change in the legal situation could have a material effect on the level of liabilities for insurance contracts.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

– Estimate of proven gas reserves

The estimate of the proven and developed gas reserves are used to determine the amortization rate of the assets used in the operations over the reporting period. Depreciation of investments associated with discovery and production of proven and developed gas reserves is based on the depletion method. According to this method, in each accounting period the assets are depreciated at a rate determined by the number of units of gas actually produced, divided by the proven and developed gas reserves remaining according to estimates. The estimated gas volume in producing reservoirs during the reporting period is calculated each year, inter alia, based on assessments of oil and gas reserves by external experts. The estimate of the proven and developed gas reserves according to these principles is subjective, based on different assumptions and the estimates of experts and might sometimes vary significantly. Given the significant amounts of the Group's depreciation expenses, these changes can have a material effect on the operating results and the financial position of the Group. See section U below for further details of assessment of impairment.

– Liability for decommission of assets

The Group recognizes an asset and a liability for its liability for decommission of assets, mainly the drilling rig. The timing and amount of the economic resources required to decommission the liability are based on the management's assessment are assessed in each period to assess the appropriateness of these assessments.

– Useful life of oil and gas assets

The useful life is based on the management's assessments for the period in which the assets will generate revenue, which are reviewed in each period to assess the appropriateness of these assessments. Changes in the management's assessments could lead to material changes in the carrying amount of the oil and gas assets and the depreciation expenses recognized in the statement of comprehensive income. In addition, future agreements, to the extent that they are signed, in respect of possible use of the Yam Tethys production facilities will have implications on the depreciation manner and period of these facilities.

– Deferred tax assets

A deferred tax asset is recognized for unused carryforward tax losses and temporary differences to the extent that it is probable that future taxable profits will be available against which the losses can be utilized. Management judgment is required to determine the amount of the deferred tax asset that can be recognized based upon the likely timing and the level of future taxable profits together with future tax planning strategies. See additional information in section W below.

– Legal claims

When assessing the possible outcomes of legal claims that were filed against the Company and its investees, the Group companies relied on the opinions of their legal counsel. These opinions are based on the best of their professional judgment, and take into consideration the stage of the proceedings and historical legal precedents in respect of various issues. Since the outcomes of the claims will ultimately be determined in the courts, these results could differ from the assessments.

In addition to these claims, the Company is exposed to unasserted legal claims, inter alia, where there is any doubt as to the interpretation of the agreement and/or the provisions of the law and/or their implementation. This exposure is brought to the attention of the Company and its investees in several ways, including through customer applications to Group entities, in particular to the Group's public complaints officer, through customer complaints to the public inquiries unit in the supervisor's office, and through claims (other than class action suits) filed at the court.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

These issues are brought to the attention of the Group's management insofar as the relevant entities identify that the claims could have widespread implications. When assessing the risk arising from these unasserted allegations/claims, the Group companies rely on internal assessments of the relevant parties and the management, which assess the prospects of a claim being filed and the chances for its success, if filed. The assessment is based on experience gained with respect to filing claims and the analysis of each claim. By their nature, in view of the preliminary stage of the clarification of the legal claim, the actual outcome could be different from the assessment made before the claim was filed.

– Determining fair value of an unquoted financial instrument

The fair value of non-marketable debentures, loans and deposits is based on the discounted cash flow model. The interest rates used for discounting are determined by a company that provides interest rate quotations for risk ratings.

– Classification of insurance contracts and investment contracts

Insurance contracts are contracts in which the insurer takes a significant insurance risk for another party. Management considers each contract, or a group of similar contracts, and if they involve significant insurance risk, they should be classified as either insurance contracts or investment contracts.

– Classification and designation of financial investments

Management exercises judgment when classifying and designating the financial investments into the following groups:

- Financial assets at fair value through profit or loss
- Held-to-maturity investments
- Loans and borrowings
- Available-for-sale financial assets

See also section K below.

C. Consolidated financial statements

As from January 1, 2010, the date of first-time adoption of IFRS 3 (Revised) and IAS 27 (2008), the Group applies the accounting policy required under these standards for business combinations and transactions with non-controlling interests.

The consolidated financial statements include the statements of companies that are controlled by the Company (subsidiaries). Control exists when the Company has the power, directly or indirectly, to govern the financial and operational policies of the controlled company. When assessing control, the effect of potential voting rights on the balance sheet date is taken into account. The financial statements are consolidated from the date that control is obtained and ends when such control ceases.

Significant intragroup balances and transactions and gains or losses arising from transactions between the Group companies have been eliminated in full in the consolidated financial statements.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

In the consolidated financial statements, the Group eliminates fair value measurement of securities of Group companies (shares of the Company and its subsidiaries and debentures issued by Group companies), which are held by special purpose companies that issue and manage exchange-traded funds and by profit-sharing policies of insurance companies, and account for these holdings in accordance with generally accepted accounting principles for the acquisition (sale) of treasury shares, acquisition (sale) of shares of subsidiaries and cross-holding of debentures, including the effect of tax, if required. The securities of associates held by special purpose companies are classified in the Group's consolidated financial statements as financial assets at fair value through profit or loss (as presented in the financial statements of the special purpose companies).

The non-controlling interests represent their share in the comprehensive income (loss) of the subsidiaries and fair value of the net identifiable assets upon the acquisition of the subsidiaries. They are presented in equity separately from the equity attributable to the parent.

As from January 1, 2010, the acquisition of non-controlling interests by the Group is recognized as an increase or decrease in equity (capital reserve from transactions with non-controlling interests) and is calculated as the difference between the consideration paid by the Group and the proportionate amount of the non-controlling interests acquired at the date of acquisition (when non-controlling interests also include a share of other comprehensive income, the Company reattributes the cumulative amounts recognized in other comprehensive income between the equity holders of the Company and the non-controlling interests). If the difference is negative, a decrease in capital (capital reserve from transactions with non-controlling interests) is recognized in the amount of this difference.

Upon the disposal of an interest in a subsidiary that does not result in a loss of control, an increase or decrease is recognized in equity (capital reserve for transactions with non-controlling interests) for the amount of the difference between the consideration received by the Group and the carrying amount of the non-controlling interests in the subsidiary which have been added to the Company's equity, also taking into account also the disposal of a portion of any goodwill in the subsidiary and any exchange differences from foreign operations which have been recognized in other comprehensive income, based on the relative decrease in the interests in the subsidiary.

Transaction costs for transactions with holders of non-controlling interests are also recognized in equity.

Cash flows from transactions with holders of non-controlling interests (with no change in control status) are classified in the statement of cash flows as financing activities.

Until December 31, 2009, additional goodwill was recognized in respect of the acquisition of non-controlling interests and the effect of the sale of non-controlling interests was recorded in profit or loss.

As from January 1, 2010, losses are attributed to non-controlling interests even if they result in a negative balance of non-controlling interests in the consolidated statement of financial position.

Until December 31, 2009, such losses were entirely attributed to the equity holders of the parent unless the non-controlling interests were obligated and able to make additional investments. Losses accrued through December 31, 2009, were not reallocated between the equity holders of the parent and the non-controlling interests.

Upon loss of joint control by the Group, any retained investment is recognized and measured at fair value. The difference between the carrying amount of the former company under joint control as of the date on which joint control ceases and the aggregate fair value of any remaining investment and the consideration from disposal is recognized in profit or loss. If the Group has significant influence over the remaining investment, it is as accounted for as an investment in an associate.

Jointly controlled operations are joint ventures where each party uses its own assets for the joint operation. The consolidated financial statements include the assets that the Group controls and the liabilities that it incurs in the course of pursuing the joint operation, and the expenses that the Group incurs and its share of the income that it earns from the joint operation.

The financial statements of the Company and its subsidiaries are prepared at the same dates and for the same periods. The accounting policy in the financial statements of the subsidiaries is applied uniformly and consistently with the accounting policy in the Company's financial statements.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

Joint ventures and special purpose companies ("SPC")

1. A joint venture is a contractual arrangement whereby two or more parties undertake oil and gas exploration operations in a jointly-owned asset. Certain joint ventures involve joint operations by the partners in one or more asset that invested in the joint venture.

Transactions that do not have a formal requirement for unanimous agreement of the joint venture partners appear that they do not fulfil the definition of joint control under IAS 31. However, a review of these transactions demonstrates that the transactions themselves have no rights in the assets and have no binding commitments on behalf of the participants. The agreements are directly between the participants and the third party. Any participant may pledge its rights in the assets and is entitled to the economic benefits from the transaction. As a result, the participants have a proportionate share in the assets and liabilities attributable to the joint venture.

For the rights of the partnership in the joint venture operations, the partnership recognized the following in its financial statements:

- a) The share of the joint venture assets
 - b) Any liabilities it undertook
 - c) The share in any liabilities incurred jointly in respect of the joint venture
 - d) Any revenues arising from its right in the joint venture
 - e) Any expenses arising from its right in the joint venture
2. The partnership's financial statements include the full share of the partnership in the assets and liabilities arising from raising funds through the SPCs, which were established for the purpose of raising funds from abroad in 2005, 2010 and 2011.

D. Functional currency and foreign currency

1. Functional currency and presentation currency

The presentation currency of the financial statements is the NIS, which is the functional currency of the Company.

The functional currency, which is the currency that best reflects the economic environment in which the Company operates and conducts its transactions, is separately determined for each investee, including associates, and is used to measure its financial position and operating results. The Company's functional currency is the NIS.

When the functional currency of the investee differs from the functional currency of the Company, that entity represents a foreign operation whose financial statements are translated so that they can be included in the consolidated financial statements as follows:

- A) Assets and liabilities for each reporting date (including comparative data) are translated at the closing rate at the date of each balance sheet. Goodwill and any fair value adjustments to the carrying amount of the assets and liabilities at the acquisition date of a foreign operation are accounted for as assets and liabilities of the foreign operation and are translated at the closing rate, at every balance sheet date.
- B) Income and expenses for each period presented in the statement of income (including comparative data) are translated at average exchange rates for the presented periods; however, if exchange rates fluctuate significantly, income and expenses are translated at the exchange rates at the date of the transactions.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

- C) Share capital, reserves and other changes in capital are translated at the exchange rate prevailing at the date they are incurred.
- D) Retained earnings are translated on the basis of the opening balance, which was translated according to the exchange rate on that date and other relevant movements, (such as a dividend) in the period in which they were translated as described in subsections (B) and (C) above.
- E) All exchange differences are recognized as other comprehensive profit (loss) in a separate item under capital, in capital reserve - Exchange differences on translation of foreign operations.

Upon the full or partial disposal of a foreign operation, the full or partial gain (loss), respectively, recognized in other comprehensive income is reclassified in profit or loss. As from January 1, 2010, upon the partial disposal of a subsidiary that is a foreign operation which disposal results in the loss of control of the subsidiary, the cumulative gain (loss) recognized in other comprehensive income is transferred to profit or loss whereas upon the partial disposal of a subsidiary that is a foreign operation which disposal results in the retention of control, the relative portion of the cumulative amount recognized in other comprehensive income is reattributed to non-controlling interests.

Intragroup loans for which settlement is neither planned nor likely to occur in the foreseeable future, are, in substance, a part of the investment in that foreign operation and are accounted for as part of the investment and the exchange rate differences arising on these loans are recognized in the same component of equity as described in subsection (e) above.

Exchange differences in respect of financial instruments in foreign currency that constitutes a net investment hedge are recorded, net of tax effect, in other comprehensive income (loss).

2. Transactions, assets and liabilities in foreign currency

Transactions denominated in foreign currency (other than the functional currency) are recorded on initial recognition at the exchange rate at the date of the transaction. After initial recognition, monetary assets and liabilities denominated in foreign currency are translated at each balance sheet date into the functional currency at the exchange rate at that date. Exchange differences, other than those capitalized to qualifying assets or carried to equity in hedging transactions, are recognized in the statement of income. Non-monetary assets and liabilities measured at cost are translated at the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currency and measured at fair value are translated into the functional currency using the exchange rate prevailing at the date when the fair value was determined.

3. Index-linked monetary items

Monetary assets and liabilities linked to the changes in the Israeli Consumer Price Index ("Israeli CPI") are adjusted at the relevant index at each balance sheet date according to the terms of the agreement. These linkage differences arising from the adjustment are recognized in the statement of income.

E. Operating cycle

The Company's normal operating cycle does not exceed one year. Accordingly, the current assets and current liabilities include items the realization of which is intended and anticipated to take place within the period of the Company's normal operating cycle.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

F. Cash equivalents

Cash equivalents are considered as highly liquid investments, including unrestricted short-term bank deposits with an original maturity of three months or less from the date of acquisition, which are not pledged.

G. Cash and cash equivalents for performance-based contracts

Cash and cash equivalents for performance based contracts include cash earmarked to liabilities for performance based life assurance policies. Insurance regulations in Israel restrict the use of these funds.

H. Short-term deposits

Short-term bank deposits are deposits with an original maturity of more than three months from the date of acquisition. The deposits are presented according to their terms of deposit.

I. Allowance for doubtful accounts

1. The allowance for doubtful accounts is determined in respect of specific debts whose collection, in the opinion of the Company's management, is doubtful. The Company also recognizes a provision for groups of customers that are collectively assessed for impairment based on their credit risk characteristics. Impaired debts are derecognized when they are assessed as uncollectible.
2. A) Provisions for doubtful accounts in respect of premiums receivable in general insurance business are calculated, inter alia, according to the extent of amounts due and in respect of loans that are secured by mortgage over real estate assets and other loans. The provision was based on the extent of the arrears, plus a general provision, which reflect the assessment of the subsidiaries of the risks involved
- B) The subsidiaries set up provisions for doubtful accounts in respect of reinsurers' debts whose collection is doubtful on the basis of individual risk estimates and on the basis of the scope of the debt.
In addition, for determining the reinsurers' share in outstanding claims and in insurance reserves, the insurance subsidiaries take into account, among other things, an assessment of the likelihood of collection from the reinsurers, while the reinsurers' share, as mentioned, is computed on an actuarial basis. The share of those reinsurers who are in financial difficulties is computed in accordance with the actuary's estimation, which takes all the risk factors into account. When reinsurers are in difficulties, they may raise various arguments that relate to recognition of the debt. In such cases, the insurance subsidiaries take into account, when setting up the provisions, the reinsurers' willingness to make cut off agreements.
- C) Credit granted for acquisition of securities

The provision for doubtful accounts in respect of a loan provided for the acquisition of securities is included when there is objective evidence that the Group is unable to collect the amounts owed to it under the original terms of the debt balance. Impairment of the customer's securities used as collateral for long-term borrowings and without the inflow of cash and/or securities indicates that there is impairment in the debt balance.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

J. Inventory

Inventories are measured at the lower of cost and net realizable value. The cost of inventories comprises costs of purchase and costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated selling costs.

Cost of inventories is assigned as follows:

Fuels and consumer goods	– The cost of fuel in operational inventory is based on the quarterly weighted average. The cost of consumer goods inventory is based on the retail inventory method.
Refinery inventory	– The cost of crude oil is based on the quarterly weighted average. The cost of distillates includes production costs.
Other	– Based mainly on moving average

The Company periodically evaluates the condition and age of inventories and makes provisions for slow moving inventories accordingly.

If in a particular period production is not at normal capacity, the cost of inventories does not include additional fixed overheads in excess of those allocated based on normal capacity. Such unallocated overheads are recognized as an expense in the statement of income in the period in which they are incurred. Furthermore, cost of inventories does not include abnormal amounts of materials, labor or other costs resulting from inefficiency.

K. Financial Instruments

1. Financial assets

Financial assets within the scope of IAS 39 are initially recognized at fair value plus directly attributable transaction costs, except for financial assets measured at fair value through profit or loss in respect of which transaction costs are carried to profit or loss.

A. Financial assets at fair value through profit or loss

The Group has financial assets at fair value through profit or loss comprising financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss.

Financial assets are classified as held for trading if they are acquired principally for the purpose of selling or repurchasing in the near term, if they form part of a portfolio of identified financial instruments that are managed together to earn short-term profits or if they are derivatives not designated as hedging instruments. Gains or losses on investments held for trading are recognized in the statement of income when incurred.

Embedded derivatives are separated from the host contract and accounted for separately if: ((a) the economic characteristics and risks of the embedded derivatives are not closely related to those of the host contract; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the combined instrument is not measured at fair value through profit or loss.

Derivatives, including separated embedded derivatives, are classified as held for trading unless they are designated as effective hedging instruments.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The Group assesses whether embedded derivatives are required to be separated from host contracts when the Group first becomes party to the contract. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

B. Loans and receivables

The Group has loans and receivables that are financial assets (non-derivative) with fixed or determinable payments that are not quoted in an active market. After initial recognition, loans and receivables are measured based at amortized cost using the effective interest method. Short-term credit (such as trade receivables and other receivables) is recognized according to its terms, usually at its nominal value.

C. Available-for-sale financial assets

The Group has available-for-sale financial assets that are non-derivative financial assets designated on initial recognition as available for sale or are not classified into one of the three other categories. After initial recognition, available-for-sale financial assets are measured at fair value. Gains or losses from fair value adjustments, except for exchange differences that relate to monetary debt instruments that are recognized as finance income or expense in profit or loss, are recognized in equity as other comprehensive income (loss) in the reserve for available-for-sale financial assets. When the investment is disposed of or in case of impairment, the amounts recorded in other comprehensive income (loss) are reclassified to the statement of income. Interest income on investments in debt instruments and dividends are recognized in the statement of income. Dividends received for investments in equity instruments are recognized in profit or loss on the date the entity's right to receive the dividend is established.

Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost.

D. Fair value

The fair value of investments that are actively traded in organized financial markets is determined by reference to market prices on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; discounted cash flows or other valuation models.

2. Financial liabilities

A. Financial liabilities measured at amortized cost

Loans and borrowings, debentures, the debt component in convertible debentures, structured bonds and other liabilities are initially recognized at fair value less directly attributable transaction costs (such as loan raising costs). After initial recognition, these liabilities are measured based on their terms at amortized cost using the effective interest method. Short-term borrowings (such as trade and other payables) are measured based on their terms, normally at face value. Gains and losses are recognized in profit or loss when the financial liability is derecognized as well as through the systematic amortization process.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

B. Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities classified as held for trading and financial liabilities designated upon initial recognition at fair value through profit or loss.

Liabilities in respect of short-selling are classified as financial liabilities measured at fair value through profit or loss. Therefore, these liabilities are initially recognized at fair value when the attributable transaction expenses are recognized in profit or loss. These liabilities are measured subsequent to initial recognition at fair value through profit or loss.

Derivatives, including separated embedded derivatives, are classified as held for trading unless they are designated as effective hedging instruments. In the event of a financial instrument that contains one or more embedded derivatives, the entire combined instrument shall be designated upon initial recognition as a financial liability at fair value through profit or loss.

The Group assesses whether embedded derivatives are required to be separated from host contracts when the Group first becomes party to the contract. Reassessment only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

3. **Offsetting financial instruments**

Financial assets and liabilities are offset and the net amount is presented in the balance sheet if there is a legally enforceable right to set off the recognized amounts and there is an intent to dispose of the asset and liability on a net basis or realize the asset and dispose of the liability simultaneously.

4. **Compound financial instruments**

Convertible debentures that are denominated in the issuing company's functional currency (NIS), which are not linked to an index or foreign currency and which contain both an equity component in respect of the conversion option and a liability component, are separated into the equity component (net of tax effect) and the liability component, and each component is presented separately less the respective transaction costs of each component. This separation is performed by first determining the carrying amount of the liability component based on the fair value of an equivalent non-convertible liability. The carrying amount of the equity component is the residual amount and is determined as the difference between the total proceeds received from the convertible debentures and the amount attributed to the liability component, as above, and, accordingly, presented in subsequent periods. Direct transaction costs are apportioned between the equity component (net of the tax effect) and the liability component based on the allocation of proceeds to the equity and liability components, as above.

After initial recognition, the liability component is classified as described above in respect of financial liabilities, at amortized cost, and presented in the balance sheet as a current or non-current liability based on the repayment dates in cash, even if the terms of the liability allow, at any time, repayment of the liability by issuing equity instruments of the issuing company.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

5. Issuance of a unit of securities

The issuance of a unit of securities involves the allocation of the proceeds received (before issuance expenses) to the components of the securities issued in the unit based on the following order: fair value is first determined for financial instruments measured at fair value in each period, then fair value is determined for other financial liabilities measured at amortized cost in each period. The allocated proceeds for equity instruments are determined at residual value. When the allocation of the consideration for components in the same level of hierarchy is based on relative fair value measurement, issuance costs are allocated to each component pro rata to the amounts determined for each component, net of any tax effect. After the allocation, each component is accounted for based on its classification (financial liability or equity instrument).

6. Derecognition of financial instruments

Financial assets

A financial asset is derecognized when the contractual rights to the cash flows from the financial asset expire or the Group has transferred its contractual rights to receive cash flows from the financial asset or assumes an obligation to pay the cash flows in full without material delay to a third party and has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A transaction involving factoring of accounts receivable and / or credit card vouchers is derecognized when the abovementioned conditions are met.

If the Company transfers its rights to receive cash flows from an asset and neither transfers nor retains substantially all the risks and rewards of the asset nor transfers control of the asset, a new asset is recognized to the extent of the Company's continuing involvement in the asset. When continuing involvement takes the form of guaranteeing the transferred asset, the extent of the continuing involvement is the lower of the original carrying amount of the asset and the maximum amount of consideration received that the Company could be required to repay.

Financial liabilities

A financial liability is derecognized when it is extinguished, that is when the obligation is discharged or cancelled or expires. A financial liability is extinguished when the debtor (the Group):

- Discharges the liability by paying in cash, other financial assets, goods or services
- Is legally released from the liability

Where an existing financial liability is exchanged with another liability from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is accounted for as an extinguishment of the original liability and the recognition of a new liability. The difference between the carrying amount of the above liabilities is recognized in the statement of income. If the exchange or modification is immaterial, it is accounted for as a change in the terms of the original liability, including adjustment of effective interest, and no gain or loss is recognized from the exchange. When determining whether an exchange transaction of a debt instrument constitutes material change, the Group takes into consideration quantitative and qualitative criteria, such as the exchange of a shekel debt instrument linked to the CPI to a debt instrument at fixed interest.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

7. Treasury shares

Company shares held by the Company and/or subsidiaries (including through exchange-traded funds) are recognized at cost and deducted from equity. Any profit or loss from purchase, sale, issue or cancellation of treasury shares is recognized directly in equity.

8. Put option granted to non-controlling shareholders

When the Group grants non-controlling interests a put option to sell part or all of their interests in a subsidiary during a certain period, on the date of grant, the non-controlling interests are classified as a financial liability. The Group recognizes the liability for the put option at fair value on the grant date and the holdings of the non-controlling interests are accounted for as if they are held by the Group.

In respect of business combinations that occurred through December 31, 2009, changes in the liability in subsequent periods (including changes that occurred after January 1, 2010), except for the unwinding of the discount, are recognized in goodwill.

If the option is exercised in subsequent periods, the proceeds from the exercise are treated as settlement of a liability. If the option expires, the liability is derecognized and an increase/decrease will be recognized in equity for transactions with holders of non-controlling interests and the relevant portion of the investment in the subsidiary will be treated as disposed of without loss of control.

9. Liability in respect of exchange-traded funds

The liability for exchange-traded funds (ETF) is a compound financial instrument that includes a host contract and an embedded derivative (index to which the ETF is linked). The host contract is recognized initially at fair value less transaction costs. In subsequent periods, the host contract is measured at amortized cost. Changes in the amortized cost of the host contract are recognized in profit or loss. The amortized cost is calculated using the effective interest method, taking into account the transaction costs, and with full reference to the period of exchange traded funds that constitute their expected useful life, inter alia, in view of the Group's ability to renew trading of any exchange-traded funds that were redeemed, at any time.

The embedded derivative with economic characteristics and risks that are not closely related to the economic characteristics and risks of the host contract is initially recognized at fair value and remeasured in subsequent periods at fair value. Changes in fair value are recognized in the statement of income.

According to IAS 39, the host contract and embedded derivative are accounted for separately and each is measured separately. IAS 39 does not require separate presentation of each of the components of the compound instrument. In accordance with IAS 39, if an instrument can be resold at any time for cash, the effect of separating an embedded derivative and the accounting treatment for each component is measurement of the hybrid instrument at the repayment amount at the balance sheet date.

In the Group's opinion, presentation of the components of the ETF together is the most appropriate presentation of the economic character of the liability for the ETF, since this reflects (before accounting for the issuance costs) the amount that the Group might be required to pay to index certificate holders, which may be redeemed at any time.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

10. The insurance subsidiaries resolved to designate the assets as follows:

A. Financial assets in investment portfolios of policies participating in investment profits:

These assets, which include marketable and non-marketable financial instruments are recognized at fair value through profit or loss, for the following reasons: These are portfolios under management, separate and identified, whose statement at fair value significantly reduces an accounting mismatch of reporting financial assets and financial liabilities at different bases of measurement. Furthermore, the management is based on fair value and the portfolio's performance is measured at fair value, in accordance with a documented risk management strategy. The information about the financial instruments is reported to the management (the relevant investments committee) internally at fair value.

B. Non-marketable financial assets that are not included in investment portfolios of investments earmarked to profit-participating policies (nostro), which do not include embedded derivatives or do not constitute derivatives:

These assets, which include designated debentures (Hetz life-linked agreements), other non-marketable debentures, commercial certificates, and loans and other receivables, are classified as loans and other receivables and recognized in the balance sheet under non-marketable debt assets.

Non-marketable shares are classified as available-for-sale financial assets.

C. Marketable financial assets which are not included in investment portfolios earmarked to profit-participating policies that do not include embedded derivatives or do not constitute derivatives (including investment funds):

These assets are classified as financial instruments available for sale.

D. Derivatives and financial instruments that include embedded derivatives requiring separation

These assets are assigned to the group of fair value through profit or loss (excluding derivatives designated as effective hedging instruments).

E. Financial assets and liabilities of certain liability certificates

Marketable and non-marketable financial assets and liabilities of liability certificates included in a portfolio measured as a whole by the Group at fair value, are stated at fair value.

L. Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that the following financial asset or group of financial assets is impaired.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

1. Financial assets carried at amortized cost

There is objective evidence of impairment of debt instruments and loans and receivables carried at amortized cost as a result of one or more events that had a negative effect on the estimated future cash flows after initial recognition. Evidence of impairment may include indications that the debtor is experiencing financial difficulties, including liquidity difficulty and default in interest or principal payments. The amount of the loss recorded in profit or loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred) discounted at the financial asset's original effective interest rate. If the financial asset has a variable interest rate, the discount rate is the current effective interest rate. The carrying amount of the asset is reduced through recording a provision. In subsequent periods, the amount of the impairment loss is reversed if the recovery of the asset can be related objectively to an event occurring after the impairment was recognized. The amount of the reversal, up to the amount of any previous impairment, is recorded in profit or loss.

2. Available-for-sale financial assets

For equity instruments classified as available-for-sale financial assets, the objective evidence includes a significant or prolonged decline in the fair value of the asset below its cost and calculation of changes in the technological, market, economic or legal environment in which the issuer of the instrument operates. The calculation of a significant or prolonged impairment depends on the circumstances at the end of each reporting period. The calculation considers historical volatility in fair value. Where there is evidence of impairment, the cumulative loss, which is recognized in other comprehensive income and measured as the difference between the acquisition cost (less any previous impairment losses) and the fair value, is reclassified from other comprehensive income and recognized as an impairment loss in profit or loss. In subsequent periods, reversal of impairment loss is not recognized in profit or loss but recognized as other comprehensive income.

For debt instruments classified as available-for-sale financial assets, objective evidence of impairment may arise as a result of one or more events that have a negative impact on the estimated future cash flows of the asset subsequent to the investment date. Evidence of impairment may include indications that the debtor is experiencing financial difficulties, including liquidity difficulty and default in interest or principal payments. Where there is evidence of impairment, the cumulative loss - measured as the difference between the acquisition cost (less principal payments, amortization using the effective interest method and previous impairment losses) and the fair value is reclassified from equity and recognized as an impairment loss in profit or loss. In a subsequent period, the amount of the impairment loss is reversed if the increase in fair value can be related objectively to an event occurring after the impairment was recognized. The amount of the reversal, up to the amount of any previous impairment, is recorded in profit or loss.

M. Derivative financial instruments

Sometimes the Group enters into contracts with derivative financial instruments such as forward currency contracts (forward) in respect of foreign currency and interest rate swaps (IRS) and transactions to fix gas prices and inventory prices in order to hedge its risks associated with foreign exchange rates, interest rate fluctuations and changes in the purchase or selling prices of gas and inventory. Such derivative financial instruments are initially recognized at fair value. After initial recognition, the derivatives are measured at fair value. Any gains or losses arising from changes in the fair values of derivatives that do not qualify for hedge accounting are carried directly to the statement of income.

The fair value of forward exchange contracts is based on the exchange rates for contracts with similar maturity dates. The fair value of IRS contracts and of transactions to fix gas and inventory prices are based on the market prices of similar instruments.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The fair value of non-traded financial instruments is determined using commonly used valuation techniques for similar financial components.

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which the Group wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. The hedge effectiveness is assessed at each balance sheet date.

Hedges which meet the criteria for hedge accounting are accounted for as follows:

Cash flow hedges

The effective portion of the gain or loss on the hedging instrument is recognized directly in equity as other comprehensive income (loss), while any ineffective portion is recognized immediately in the statement of income.

Amounts recognized as other comprehensive income (loss) are transferred to the statement of income when the hedged transaction affects profit or loss, such as when the hedged income or expense is recognized or when a forecast sale occurs. Where the hedged item is the cost of a non-financial asset or non-financial liability, this cost also includes the associated other comprehensive income (loss) reclassified from equity in the same period during which the asset or liability are recognized.

If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognized in other comprehensive income are transferred to the statement of income. If the hedging instrument expires or is sold, terminated or exercised, or if its designation as a hedge is revoked, amounts previously recognized in equity remain in equity until the forecast transaction or firm commitment occurs.

N. Leases

The tests for classifying leases as finance or operating leases depend on the substance of the agreements and are made at the inception of the lease in accordance with the principles below as set out in IAS 17.

1. Finance lease

Finance leases transfer to the Group substantially all the risks and benefits incidental to ownership of the leased asset. At the commencement of the lease term, the leased asset is measured at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. The liability for lease payments is presented at its present value and the lease payments are apportioned between finance charges and a reduction of the lease liability using the effective interest method.

After initial recognition, the leased asset is accounted for according to the accounting policy accepted for this type of asset.

2. Operating lease

Lease agreements are classified as an operating lease if they do not transfer substantially all the risks and benefits incidental to ownership of the leased asset. Initial direct costs incurred for the lease, which are not accounted for as investment property which are recognized in profit or loss, are added to the cost of the leased asset and recognized as an expense together with income from the lease. The lease payments are recognized as an income in profit or loss, on a straight-line basis over the lease term.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

O. Business combinations and goodwill

As from January 1, 2010, in view of the expansion of the definition of a "business" according to IFRS 3 (Revised), the Company also accounts for operations and assets that are not run as a business, provided the seller is capable of operating them as a business.

Business combinations are accounted for by applying the acquisition method. According to this method, the identifiable assets and liabilities of the acquired business are recognized and recorded at fair value at the acquisition date. The cost of the acquisition is the aggregate fair value of the assets transferred, liabilities incurred and equity interests issued by the acquirer on the date of acquisition.

In respect of business combinations that occurred on or after January 1, 2010, non-controlling interests are measured at fair value on the acquisition date or at the proportionate share of the non-controlling interests in the acquiree's net identifiable assets on the date of acquisition. The method is selected for each separate business combination.

In respect of business combinations that occurred through December 31, 2009, the non-controlling interests were measured at their proportionate share of the fair value of the acquiree's net identifiable assets.

The amendment to IFRS 3 (Revised) is applied retrospectively from the application date of IFRS 3 (Revised) and it limits the circumstances in which it is possible to choose the measurement of non-controlling interests based on their fair value on the date of acquisition or at the present ownership instruments' share in the recognized amounts of the acquiree's identifiable net assets. According to the amendment, this possibility is only available for components of non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the acquiree's net assets in the event of liquidation (usually shares). In contrast, for other components of non-controlling interests (such as options that represent equity instruments of the acquiree) no such choice is available, and they are measured at fair value on the acquisition date, unless another measurement basis is required by IFRS, such as IFRS 2.

For business combinations that occurred on or after January 1, 2010, direct costs related to the acquisition are recognized immediately as an expense in the statement of income.

For business combinations that occurred before December 31, 2009, these costs were recognized as part of the acquisition cost.

Any classification or designation made when recognizing assets and liabilities are assessed in accordance with the contractual terms, economic circumstances and pertinent conditions that exist at the acquisition date.

As from January 1, 2010, in a business combination achieved in stages, the acquirer remeasures its previously held equity interest in the acquiree at its acquisition date fair value and recognizes the resulting gain or loss, if any, including reversal of deferred amounts, in other comprehensive income. For business combinations that occurred before December 31, 2009, the Company elected to measure goodwill for each separate acquisition.

Goodwill is initially measured at cost which represents the excess of the acquisition consideration and the amount of non-controlling interests over the net identifiable assets acquired and liabilities assumed as measured on the acquisition date. If the resulting amount is negative, the acquisition is considered a bargain purchase and the acquirer recognizes the resulting gain in profit or loss on the acquisition date.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses and is not systematically amortized. For testing the impairment of goodwill, see section U.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

For business combinations that occur after January 1, 2010, contingent consideration is recognized at its fair value at the acquisition date and constitutes a financial asset or liability according to IAS 39. Subsequent changes in fair value of the contingent consideration are recognized in the statement of income. If the contingent consideration is classified as an equity instrument, it is measured at fair value on the acquisition date without subsequent measurement. In any event, if the changes are due to the temporary PPA differences in the measurement period, the changes are recognized as goodwill adjustments.

For business combinations occurring before December 31, 2009, contingent consideration was recognized on the acquisition date if the outcome of the contingency was probable and the amount could be measured reliably. Subsequent changes in the likelihood of the contingent consideration are accounted for prospectively as a change in estimate with a resulting adjustment to the acquisition cost and goodwill.

As from January 1, 2010, subsequent measurement of a deferred tax asset for acquired temporary differences which did not meet the recognition criteria at the measurement period is against profit or loss and not as adjustment to goodwill.

Upon the disposal of a subsidiary resulting in loss of control, the Company:

- Derecognizes the subsidiary's assets (including goodwill) and liabilities
- Derecognizes the carrying amount of the non-controlling interests
- Derecognizes the exchange differences that were charged to equity
- Recognizes the fair value of the consideration received
- Regarding loss of control on or after January 1, 2010, recognizes the fair value of any remaining investment
- Regarding loss of control up to December 31, 2009, the portion of the investment sold is derecognized with recognition of the resulting gain or loss and any remaining investment is accounted for either by the equity method (IAS 28) or as a financial asset (IAS 39).
- Regarding loss of control as from January 1, 2010, recognizes the components recognized in other comprehensive income (loss) on the same basis as would be required if the subsidiary had directly disposed of the related assets or liabilities. Accordingly, translation differences are recognized in profit or loss on the date of derecognition.
- Regarding loss of control through December 31, 2009, only the proportionate share that is disposed of is recognized.

Acquisitions of subsidiaries that are not business combinations

Upon the acquisition of subsidiaries and operations that do not constitute a business, the acquisition consideration is only allocated between the acquired business identifiable assets and liabilities based on their relative fair values on the acquisition date without attributing any amount to goodwill or to deferred taxes, whereby the non-controlling interest, if any, participates at its relative share of the fair value of the net identifiable assets on the acquisition date. Direct costs related to the acquisition are discounted as part of the acquisition consideration.

In the acquisition of non-controlling interests in subsidiaries, as above, up to December 31, 2009, the difference between the consideration paid and the relative non-controlling interest acquired on the date of acquisition is attributed to assets and liabilities as described above.

Upon the acquisition of non-controlling interests of subsidiaries, as above, that occurred starting from January 1, 2010, the accounting treatment is in accordance with section c above ("consolidated financial statements").

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

P. Investments accounted for according to the equity method

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies.

The investment in an associate is accounted for using the equity method. Under the equity accounting method, the investment in the associate is recorded in the balance sheet at cost and is subsequently adjusted to reflect the Group's share in the net assets, including the other comprehensive income (loss) of the associate. This does not include holdings of special purpose companies that issue and manage exchange-traded funds and by assets for performance based contracts of The Phoenix, which are stated at fair value in the statement of income.

The equity method is implemented up to the earlier of the date the Group loses significant influence or the investment is reclassified as an investment held for sale according to IFRS 5. When an investment in an associate previously classified as held for sale no longer meets the criteria for this classification, it is accounted for retrospectively using the equity method, from its classification as held for sale, with restatement of financial statements for prior periods.

Goodwill relating to the acquisition of an associate is initially measured as the difference between the acquisition cost and the Group's share in the net fair value of the associate's identifiable assets, liabilities and contingent liabilities. After initial recognition, goodwill is measured at cost and is not systematically amortized. Goodwill is examined for impairment as part of the investment in an associate as a whole.

If additional shares are acquired in equity-accounted investments, the Group calculates the purchase price allocation for each tranche separately. Upon a decrease in the equity interests in an associate while retaining significant influence in the associate, the Company realizes a relative portion of its investment in the associate and recognizes a gain or loss from the disposal, including the reclassification of the proportionate share of cumulative amounts previously recognized in other comprehensive income (loss) of the associate.

The Group's share of the operating results of the associate is presented in the statement of comprehensive income as "Group's share of earnings (losses) of associates" and other comprehensive income (loss) of the associate attributable to the Group is presented in other comprehensive income (loss) in the relevant item in equity. Profit or loss from transactions between the Group and the associate is eliminated according to the rate of holding in the associate.

Losses of associates in amounts which exceed their equity are recognized by the Company to the extent of its investment in the associates with the addition of any losses that the Company may incur as a result of a guarantee or other financial support provided in respect of these associates. For this purpose, the investment includes long-term receivables (such as loans granted) for which settlement is neither planned nor likely to occur in the foreseeable future.

The financial statements of the Company and its associates are prepared as of the same dates and periods. The accounting policy in the financial statements of the associates was applied consistently and uniformly with the policy applied in the financial statements of the Group.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

Q. Investment property

An investment property is property (land or a building or both) held by the owner (lessor under an operating lease) or by the lessee under a finance lease to earn rentals or for capital appreciation or both, rather than for use in the production or supply of goods or services, for administrative purposes, or for sale in the ordinary course of business.

Investment property is measured initially at cost, including costs directly attributable to the acquisition. After initial recognition, investment property is measured at fair value which reflects market conditions at the reporting date. Gains or losses arising from changes in the fair values of investment property are included in the statement of income when they arise. Investment property is not systematically depreciated.

The Group determines the fair value of an investment property on the basis of a valuation by an outside independent valuator who holds a recognized and relevant professional qualification.

R. Property, plant and equipment

Items of fixed assets are measured at cost with the addition of direct acquisition costs, less accumulated depreciation and impairment losses and excluding day-to-day servicing expenses. Cost includes spare parts and auxiliary equipment that can be used only in connection with the machinery and equipment.

The cost of self-constructed assets includes the cost of materials, direct labor and borrowing costs as well as any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management, and the present value of the expected cost item for decommissioning and restoring the site on which they are located (see below).

Depreciation is calculated on a straight-line basis over the useful life of the assets at annual rates as follows:

	%	Main %
Buildings	10-2	2.5
Machines, facilities and equipment	25-2.5	10
Motor vehicles	33-15	
Furniture and office equipment	33-5	
Refineries	7-2.5	5
Works of art	Without depreciation	
Leasehold improvements	Over the shorter of the lease term ,including the extension option held by the Group and intended to be exercised, and the expected life of the improvement.	

The cost of property, plant and equipment (primarily for gas exploration and oil refineries) includes the initial estimate of the cost of decommissioning the item and restoring the site on which it is located, for which the Group was obligated when the item was acquired or as a result of the use of the item during a particular period. The liability is first measured at fair value and changes in the liabilities deriving from passage of time are recognized in the statement of income. The residual value and the useful life of each asset are reviewed at least at each year-end and changes are accounted for prospectively as a change in an accounting estimate. See section U below for further details of impairment of property, plant and equipment.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The Group recognizes the costs of periodic maintenance on a fixed asset item (particularly refinery facilities) as part of the carrying amount of a fixed asset item, as incurred, when it is expected that economic benefits associated with the item will flow to the Group, and the cost of the item can be measured reliably. These costs are amortized over the period until the next maintenance (approximately four years). Ongoing maintenance costs are recognized in the statement of income as incurred.

Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognized. An asset is derecognized on disposal or when no further economic benefits are expected from its use. The gain or loss arising from derecognition of the asset (determined as the difference between the net disposal proceeds and the carrying amount in the financial statements) is included in profit or loss when the asset is derecognized.

S. Borrowing costs in respect of qualifying assets

A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale and includes fixed assets and inventories.

The Group capitalizes borrowing costs to qualifying assets.

The capitalization of borrowing costs commences when the activities to prepare the qualifying asset are in progress and ceases when substantially all the activities to prepare the qualifying asset for its intended use or sale are complete.

The amount of borrowing costs capitalized in the reporting period do not exceed over the borrowing costs that have been incurred in the reported period.

Borrowing costs include exchange differences arising from foreign currency borrowing to the extent that they are regarded as an adjustment to interest costs.

The capitalization of borrowing costs is suspended during long periods when development is discontinued.

T. Intangible assets

Separately acquired intangible assets are measured on initial recognition at cost with the addition of costs directly attributable to the acquisition. Intangible assets acquired in a business combination are included at the fair value at the acquisition date. After initial recognition, intangible assets are carried at their cost less any accumulated amortization and any accumulated impairment losses. Expenditures relating to internally generated intangible assets, excluding capitalized development costs, are recognized in the statement of income when incurred.

After initial recognition, intangible assets are carried at their cost less any accumulated amortization and any accumulated impairment losses.

According to management's assessment, intangible assets have a finite useful life. The assets are amortized over their useful life using the straight-line method and reviewed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least once a year. Changes in the expected useful life are accounted for as prospective changes in accounting estimates. The amortization charge on intangible assets with finite useful lives is recognized in the statement of income.

The length of the useful life of the intangible assets is as follows:

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

	<u>Years</u>
Marketing rights and customer relations	15-5
Software	10-3
Brands and trademarks	10-3
Franchises	138-10
Value of insurance portfolios	14-5
Non-competition agreements	15-5
Commission portfolios	10-2

Intangible assets with indefinite useful lives are not systematically amortized and are tested for impairment annually or whenever there is an indication that the intangible asset may be impaired. See also section 22. The useful life of these assets is reviewed annually to determine whether their indefinite life assessment continues to be supportable. If the events and circumstances do not continue to support the assessment, the change in the useful life assessment from indefinite to finite is accounted for prospectively as a change in accounting estimate and on that date the impairment of the asset is tested and it is amortized systematically over its useful economic life.

Gains or losses arising from derecognition of an intangible asset are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in profit or loss.

U. Impairment of non-financial assets

The Group evaluates the need to record an impairment of the carrying amount of non-financial assets whenever events or changes in circumstances indicate that the carrying amount is not recoverable. When the carrying amount of non-financial assets exceeds their recoverable amount, the assets are reduced to their recoverable amount. The recoverable amount is the higher of fair value less costs of sale and value in use. When measuring value in use, the expected future cash flows are discounted using a pre-tax discount rate that reflects the risks specific to the asset. The recoverable amount of an asset that does not generate independent cash flows is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in profit or loss.

An impairment loss of an asset, other than goodwill, is reversed only if there have been changes in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. Reversal of the loss is limited to the lower of the amount of previously recognized impairment of the asset (net of depreciation or amortization) or the recoverable amount of the asset. For an asset measured at cost, reversal of the loss is recognized in profit or loss.

When assessing the impairment of gas stations operated by a subsidiary in Israel, these stations are considered as a single cash generating unit, among others, due to the common customer base and the business inter-dependency of the various stations. Nevertheless, in cases where the subsidiary's management is of the opinion that certain stations do not contribute to the chain of gas stations, each of these stations is considered as a separate cash generating unit.

Gas stations operated by a subsidiary in Europe (Balkan countries and France) are tested for impairment as one cash generating unit for all gas stations in that country, since a significant part of the subsidiary's revenue in each country is generated by use of refueling cards, which the customer can use in any gas station in that country.

Gas stations operated by the US subsidiary for are tested for impairment in the relevant geographical area.

Other assets are each tested separately for impairment.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The following criteria are applied in assessing impairment of these specific assets:

1. Goodwill

The Group reviews goodwill impairment once a year or more frequently if events or changes in circumstances indicate that there is impairment.

Impairment is recognized for goodwill by assessing the recoverable amount of the cash-generating unit (or group of cash-generating units) to which the goodwill belongs. An impairment loss is recognized if the recoverable amount of the cash-generating unit (or group of cash-generating units) to which goodwill has been allocated is less than the carrying amount of the cash-generating unit (or group of cash-generating units). Impairment losses recognized for goodwill cannot be reversed in subsequent periods.

As from January 1, 2010, the highest possible level for allocating goodwill recognized in a business combination is an operating segment as defined in IFRS 8 – Operating Segments before aggregation for reporting purposes.

2. Investees accounted for according to the equity method

After implementing the equity accounting method, the Group determines whether it is necessary to recognize further loss for impairment of the investment in associates. The Group assesses at the end of each reporting period whether there is objective evidence that the investment in an associate has been impaired. Impairment is assessed in respect of the entire investment, including goodwill attributable to the associate. If there is objective evidence, as above, the amount of the loss is calculated as the difference between the recoverable amount of the investment in the associate and its carrying amount. The recoverable amount is the higher of value in use and fair value less costs to sell based on the estimated net cash flows to be generated by the associate. Impairment loss, as above, is not allocated specifically to goodwill that forms part of the investment and, accordingly, any reversal of that impairment loss is recognized to the extent that the recoverable amount of the investment subsequently increases. The loss, or its reversal, is recognized in profit or loss in the line item, "Group's share of earnings (losses) of companies and partnerships accounted for according to the equity method, net"

3. Intangible assets with indefinite useful life

The Group assesses goodwill for impairment annually, or more frequently if events or changes in circumstances indicate impairment.

V. Results of oil and gas exploration and development of proved reserves

Oil and gas investments and exploration are accounted for using the successful effort method, according to which:

1. Expenses incurred in the participation in geological and seismic exploration phase are recognized in the statement of income when they are incurred.
2. Investments in oil and gas drillings that are in the drilling stage for reservoirs that were not yet proven to produce oil or gas and that are yet to be classified as being non-commercial, are defined as exploration assets and the estimate is stated in the balance sheet at cost under investment in oil and gas assets.
3. Investments in oil and gas drillings, for reservoirs proved as dry and abandoned, or defined as non-commercial, are fully amortized from exploration and appraisal assets in the statement of comprehensive income.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

4. Investments for reservoirs that have a technical feasibility and commercial viability of oil or gas production (which are being appraised in a range of events and circumstances, mainly approval from the Commissioner of Petroleum Affairs that the reservoir is a commercial discovery and/or obtaining a lease from the Commissioner in the license area), are defined as oil and gas assets, are reclassified from exploration and appraisal assets to oil and gas assets, and stated in the balance sheet at cost. These oil and gas assets are amortized in the statement of comprehensive income on the basis of the production quantity compared to the total proven reserves in the oil or gas asset, according to an expert appraisal.
5. Costs accrued for development of the proved reserves of the Yam Tethys joint venture were designed to provide options for the extraction, handling, collection and storage of gas. These costs, which include engineering planning, development drillings, and acquisition and establishment of production facilities and pipes for the delivery of the gas onshore, are stated in the balance sheet at cost and amortized to the statement of income based on the production volume relative to the total proved reserves for the asset, as appraised by an expert.

Expenses entailed in the purchase of rights to licenses, titles and preliminary permits for oil and gas drilling, including increasing the Group's share in joint ventures, are accounted for as aforesaid.

The surplus cost from a business combination or acquisition of companies, partnerships and joint ventures that own such reserves, is allocated to investment in oil and gas reservoirs and amortized as described above. The surplus cost from licenses before start of production is not systematically amortized.

Oil and gas assets

1. The oil and gas assets item in the balance sheet includes costs accumulated for the partnership's proven oil and gas assets. These costs, which include costs for acquisition of rights in offshore areas, exploration drillings, engineering planning, development drilling, and acquisition and establishment of production facilities and pipelines for the delivery of the gas onshore and construction of a receiving terminal, are stated in the balance sheet at cost and amortized to the statement of comprehensive income according to the depletion method based on the actual production volume compared to the total proved, as appraised by an expert (see Note 7(A) below). The item also includes the costs accumulated for exploration and appraisal assets not yet proven.
2. **Measuring an asset and liability for decommission of assets**

The partnership recognized for the first time a liability together with an asset for its share in the liability to decommission assets, mainly the production platform at the end of its use. The liability was first measured at present value and the expenses arising from the passage of time are recognized in the statement of comprehensive income under finance. The asset was first measured at present value and is amortized over time in the statement of comprehensive income according to the useful life of the decommissioned asset. Changes in timing and in the amount of economic resources that are required to remove the liability and change in the discount rate are added or deducted from the asset in the current period together with a change in the liability (the discount rate at the balance sheet date is 6% per year).

W. Taxes on income

Taxes on income in the statement of income comprise current and deferred taxes. The tax results in respect of current or deferred taxes are carried to the statement of income except to the extent that the tax arises from items which are recognized directly in equity or in other comprehensive income. In such cases, the tax effect is also carried to the relevant item in equity or in other comprehensive income.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

1. Current taxes

The current tax liability is measured using the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date as well as adjustments required in connection with the tax liability in respect of previous years.

2. Deferred taxes

Deferred taxes are computed in respect of temporary differences between the carrying amounts in the financial statements and the amounts attributed for tax purposes, with a limited number of exceptions. Deferred taxes are measured at the tax rates that are expected to apply to the period when the taxes are reversed in profit or loss, comprehensive income or equity, based on tax laws that have been enacted or substantively enacted by the end of the reporting period. Deferred taxes in profit or loss represent the changes in the carrying amount of deferred tax balances during the reporting period, excluding changes attributable to items recognized in other comprehensive income or equity.

Taxes that would apply in the event of the disposal of investments in investees have not been taken into account in computing deferred taxes, as long as the disposal of the investments in investees is not probable in the foreseeable future. Also, deferred taxes that would apply in the event of distribution of earnings by investees as dividends have not been taken into account in computing deferred taxes, since the distribution of dividends does not involve an additional tax liability or since it is the Group's policy not to initiate distribution of dividends that triggers an additional tax liability.

All deferred tax assets and deferred tax liabilities are reported in the balance sheet as non-current assets and long-term liabilities, respectively. Deferred taxes are offset in the statement of financial position if there is a legally enforceable right to offset a current tax asset against a current tax liability and the deferred taxes relate to the same taxpayer and the same taxation authority.

Where there is uncertainty with respect to the existence of taxable income in the future, deferred taxes are not recognized as an asset in the financial statements.

X. Share-based payments

The Company's employees are entitled to remuneration in the form of share-based payment transactions as consideration for equity instruments ("equity-settled transactions") and to cash-settled benefits based on the increase in the Company's share price ("cash-settled transactions").

Equity-settled transactions

The cost of equity-settled transactions with employees is measured at the fair value of the equity instruments granted at grant date. The fair value is determined using a standard pricing model. In estimating fair value, the vesting conditions (consisting of service conditions and performance conditions other than market conditions) are not taken into account. The only conditions taken into account when estimating fair value are market conditions and non-vesting conditions. As for other service providers, transaction costs are measured at the fair value of the goods or services received in return for the equity instruments that were granted. When the fair value of the goods or services received in return for the equity instruments cannot be measured, they are measured at the fair value of the equity instruments that were granted.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The cost of equity-settled transactions is recognized in profit or loss, together with a corresponding increase in equity, during the period which the performance and/or service conditions are to be satisfied, ending on the date on which the relevant employees become fully entitled to the award ("the vesting period"). The cumulative expense recognized for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The expense or income recognized in profit or loss represents the movement in the cumulative expense recognized at the end of the reporting period.

No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether the market condition is satisfied, provided that all the other vesting conditions (service and/or performance) are satisfied.

If the Group modifies the conditions on which equity-instruments were granted, an additional expense is recognized for any modification that increases the total fair value of the share-based payment arrangement or is otherwise beneficial to the employee at the modification date.

If a grant of an equity instrument is cancelled, it is accounted for as if it had vested on the cancellation date, and any expense not yet recognized for the grant is recognized immediately. However, if a new grant replaces the cancelled grant and is identified as a replacement grant on the grant date, the cancelled and new grants are accounted for as a modification of the original grant, as described in the previous paragraph.

Cash-settled transactions

The cost of cash-settled transactions is measured at fair value on the grant date using a standard pricing model. The fair value is recognized as an expense over the vesting period and a corresponding liability is recognized. The liability is remeasured at each reporting date until settled at fair value with any changes in fair value recognized in the profit or loss.

Benefits that include the right of the employee or service provider to sell back to the Company or to Group companies its shares are accounted for as cash-settled transactions.

Y. Employee benefit liabilities

The Group has several employee benefit plans:

1. Short-term employee benefits

Short-term employee benefits include salaries, paid annual leave, paid sick leave, recreation and social security contributions and are recognized as expenses as the services are rendered. A liability in respect of a cash bonus or a profit-sharing plan is recognized when the Group has a legal or constructive obligation to make such payment as a result of past service rendered by an employee and a reliable estimate of the amount can be made.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

2. Post-employment benefits

The plans are normally financed by contributions to insurance companies and classified as defined contribution plans or as defined benefit plans.

The Group has defined contribution plans pursuant to Section 14 to the Severance Pay Law in Israel, under which the Group pays fixed contributions and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient amounts to pay all employee benefits relating to employee service in the current and prior periods. Contributions to the defined contribution plan in respect of severance pay or compensation are recognized as an expense when contributed simultaneously with receiving the employee's services and no additional provision is required in the financial statements.

Companies in the Group also operate a defined benefit plan in respect of severance pay pursuant to the Severance Pay Law in Israel. According to the Law, employees are entitled to severance pay upon dismissal or retirement. The liability for termination of employee-employer relation is measured using the projected unit credit method. The actuarial assumptions include future salary increases and rates of employee turnover based on the estimated timing of payment. The amounts are presented based on discounted expected future cash flows using a discount rate determined by reference to yields on Government bonds with a term that matches the estimated term of the benefit obligation.

In respect of its severance pay obligation to certain of its employees, the Company makes current deposits in pension funds and insurance companies ("the plan assets").

Actuarial gains and losses are recognized in profit or loss in the period in which they occur.

The liability for employee benefits presented in the balance sheet presents the present value of the defined benefit obligation less the fair value of the plan assets.

Z. Revenue recognition

Revenues are recognized in profit or loss when the revenues can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and the costs incurred or to be incurred in respect of the transaction can be measured reliably. Revenues are measured at the fair value of the consideration received less any trade discounts, volume rebates and returns.

The specific criteria for revenue recognition for the following types of revenues are:

1. Revenues from the sale of goods

Revenues from the sale of goods are recognized when all the significant risks and rewards of ownership of the goods have passed to the buyer and the seller no longer retains continuing managerial involvement. The delivery date is usually the date on which ownership passes.

2. Rental income

Rental income is recognized on a straight-line basis over the lease term. Where there is a fixed increase in rent over the term of the contract the aggregate amount of the increase is recognized as revenues on a straight-line basis only if there is certainty as to the collection of differences in rental fees in the future.

3. Revenues from production of fuels, storage and charter of tankers are recognized in profit or loss when the service is provided.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

4. Revenues from the rendering of services (including management fees)

Revenues from the rendering of services are recognized by reference to the stage of completion at the end of the reporting period. Under this method, revenues are recognized in the accounting periods in which the services are rendered. Where the contract outcome cannot be measured reliably, revenue is recognized only to the extent that the expenses incurred are recoverable.

5. Interest income

Interest income is recognized as it accrues using the effective interest method.

6. Revenues from royalties

Revenues from royalties are recognized as they accrue in accordance with the substance and terms of the relevant agreement.

7. Revenues from dividends

Revenues from dividends on investments not accounted for using the equity method are recognized when the right to receive the dividend is established.

8. Reporting gross or net revenues

When the Group acts as an agent or intermediary without bearing the risks and rewards associated with the transaction, its revenues are recognized on a net basis. However, in cases where the Group operates as a principal supplier and is exposed to the risks and rewards associated with the transaction, its revenues are presented on a gross basis.

9. Revenues from the sale of gas

Revenue from the sale of oil and gas is recognized when the customer receives the oil or gas.

10. Income from insurance businesses

A) Premiums

- 1) Premiums in life assurance and health insurance, including savings premiums and with the exception of intakes in respect of investment contracts, are recognized as revenues when the Group is entitled to receive such premiums.
Cancellations are recorded when the notification is received from the policyholder or when initiated by The Phoenix due to arrears in payments, subject to legal provisions. The policyholder's participation in profits is deducted from the premium.
- 2) General insurance premiums are accounted for as income based on monthly reports. Insurance premiums usually refer to an insurance period of one year. Gross income from premiums and changes in unearned premium are accounted for under earned premiums, gross.
In the motor act branch of insurance in Israel, the insurance comes into effect only after payment of the insurance premium, therefore the premium is accounted for on the date of payment.
Insurance premiums in respect of policies that come into effect after the balance sheet date or premiums in respect of policies for a period exceeding one year are recorded as a prepaid income.
Some of the premiums in Israel, primarily in the motor casco and comprehensive residential branches, include automatic renewals of policies due for renewal.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The income included in the financial statements is after cancellations requested by policyholders and net of cancellations and provisions due to non-payment of the premiums, subject to the law, and net of the policyholder's participation in profits, based on valid agreements.

B) Management fees and commissions

1) Management fees for performance based insurance contracts

Management fees include the following components:

For policies sold as of 1 January 2004 – fixed management fees only

For policies sold until December 31, 2003 – fixed and variable management fees

The management fees are computed in accordance with the Supervisor's directives on the basis of the yield and the accumulated saving of the policyholders in the profit-participating portfolio.

The fixed management fees are computed at fixed percentages of the accumulated saving and are recorded on a cumulative basis.

The variable management fees are computed as a percentage of the annual real profit (from January 1 to December 31) attributed to the policy, less the fixed management fees collected from that policy. Only positive variable management fees can be collected, net of negative amounts accumulated in the preceding years.

During each period, the variable management fees are recorded on a cumulative basis in accordance with the real monthly yield if it is positive. In months when the real yield is negative, the variable management fees are reduced to the amount of the cumulative variable management fees collected since the beginning of the year. Negative yield, for which a reduction of the management fees was not made during a current year, will be deducted for the purpose of computing the management fees from the positive yield in the subsequent year.

2) Management fees of non-insurance subsidiaries

Income from the management of pension funds and provident funds is recognized on the basis of the balances of the managed assets and on the basis of the receipts from the members.

Income from the management of mutual funds and income from the management of customer portfolios are recognized on the basis of the managed asset balance.

Income from general insurance commission in insurance agencies is recognized as incurred.

Income from life assurance commissions are recognized on the basis of the date of entitlement for payment of the commissions according to agreements with the insurance companies, net of provisions for refunds of commissions due to expected cancellations of insurance policies.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

3) Net investment income (losses) and other finance income

Interest income is recognized as it accrues using the effective interest method.

Revenues from dividends from investments not accounted for using the equity method are recognized when the right to receive the dividend is established.

Investment income includes the gains or losses realized in respect of available-for-sale financial assets. Gains and losses from the disposal of investments are calculated as the difference between the proceeds from the sale, net, and the initial or amortized cost and are recognized at the time of the sale.

Investment income includes gains or losses from revaluation of financial assets measured at fair value through profit or loss.

C) Recognition of revenues from underwriting and distribution and from brokerage fees

- 1) Revenues from underwriting and distribution - revenues from commission for underwriting and distribution are recognized when the issuance and distribution is carried out, after fulfilment of the terms in the agreement with the company and/or issuer.
- 2) Revenues from brokerage fees - revenues from commissions relating to transactions in securities are recognized on completion of the transactions.

10. Finance income and expense

Finance income comprises interest income on amounts invested (including available-for-sale financial assets), revenues from dividend, gains from sale of financial assets classified as available-for-sale, and changes in fair value of financial assets at fair value through profit or loss.

Changes in fair value of financial assets at fair value through profit or loss include interest and dividend income.

Finance expenses comprise interest expenses on liabilities measured at amortized cost, changes in the fair value of financial assets and financial liabilities at fair value through profit or loss and impairment losses of financial assets. Borrowing costs that are not capitalized to qualifying assets are recognized in profit or loss using the effective interest method.

Gains and losses on exchange differences are reported on a net basis.

11. Oil and gas profits levy

The levy for oil and gas profits is classified and presented in the same way as income tax.

12. Customer discounts

Current customer discounts are recognized in the financial statements when granted and are included in sales.

Customer discounts given at the end of the year and in respect of which the customer is not obligated to comply with certain targets, are recognized in the financial statements proportionately as the sales entitling the customer to the discounts are made.

Customer discounts for which the customer is required to meet certain targets, such as a minimum amount of annual purchases (either quantitative or monetary) or an increase in purchases compared to previous periods are recognized in the financial statements in proportion to the purchases made by the customer during the year that qualify for the target, provided that it is expected that the targets will be achieved and the amount of the discount can be reasonably estimated.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

AA. Cost of revenues and supplier discounts

Cost of sales includes expenses for loss, storage and conveyance of inventories to the end point of sale. Cost of sales also includes provisions for write-downs of inventories, inventory write offs and provisions for slow-moving inventories.

Discounts are deducted from cost of purchase when the conditions entitling to those discounts are satisfied. The portion of the discounts relating to that portion of the purchases that are in closing inventories are attributed to inventories and the balance reduces the cost of sales.

Supplier discounts received at the end of the year and in respect of which the Group is not obligated to comply with certain targets, are recognized in the financial statements proportionately as the purchases entitling the Group to the discounts.

Supplier discounts for which the Group is required to meet certain targets, such as a minimum amount of annual purchases (either quantitative or monetary) or an increase in purchases compared to previous periods are recognized in the financial statements in proportion to the purchases made by the Group during the year that qualify for the target, provided that it is expected that the targets will be achieved and the amount of the discount can be reasonably estimated.

BB. Earnings (loss) per share

Earnings (loss) per share are calculated by dividing the net income (loss) attributable to equity holders of the parent by the weighted number of ordinary shares outstanding during the period.

Basic earnings per share only include shares that were actually outstanding during the period.

Potential ordinary shares (convertible securities such as convertible debentures, warrants and employee options) are only included in the computation of diluted earnings per share when their conversion decreases earnings per share or increases loss per share from continuing operations. Further, potential ordinary shares that are converted during the period are included in diluted earnings per share only until the conversion date and from that date in basic earnings per share. The Company's share of earnings of investees is included based on the earnings per share of the investees multiplied by the number of shares held by the Company.

CC. Provisions

A provision in accordance with IAS 37 is recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the effect is material, the provisions are measured when discounting projected cash flows, using a pre-tax interest rate that reflects market expectations in respect of the unwinding of the discount, and, where appropriate, those risks specific to the liability.

1. Environmental liabilities

The Group's financial statements include a provision for expected expenses related to decontamination and remediation of environmental hazards. The provision is recorded when the management believes that it is probable that a liability has been created and the amount of the liability can be reasonably estimated. Environmental liabilities represent an estimate of the costs arising from examination and remediation of the contaminations created.

The management's assessment is based on internal and external estimates of the contaminations and the existing relevant remediation technology, and a review of applicable environmental regulations. Environmental liabilities accrue mostly no later than upon completion of the remedial review. The provision in respect of these liabilities is adjusted as additional information is obtained or the circumstances change. The costs of purchasing the equipment required for the current remediation of environmental hazards are recorded as property, plant and equipment.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

2. Legal claims

A provision for claims is recognized when the Group has a present, legal or constructive obligation as a result of a past event, it is more likely than not that an outflow of resources embodying economic benefits will be required by the Group to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the effect of the time value is material, a provision is measured at its present value. When assessing the need for recognition and measurement of the provisions, Group companies are assisted by legal counsels.

3. Onerous contracts

A provision for onerous contracts is recognized when the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received by the Group under it. The provision is measured at the lower of the present value of the anticipated cost of exiting from the contract and the present value of the net anticipated cost of fulfilling it.

4. Restructuring

A provision for restructuring is recognized when the conditions for recognition of the provision have been fulfilled and the Company has approved a detailed and formal restructuring plan for a business or for part of the business that is relevant to restructuring, to the location and the number of employees who will be affected by the change, and there is a reliable detailed estimate of the related costs and planned schedule. Also, there must be a valid expectation by the parties affected by the restructuring that the restructuring will be implemented or it has already commenced.

5. Contingent consideration in a business combination

The contingent consideration in a business combination is measured at fair value upon initial recognition. In subsequent periods, it is measured at the higher of:

- The amount initially recognized less, when appropriate, cumulative amortization
- The amount that would be recognized (if required) at the end of the reporting period in accordance with IAS 37

DD. Advertising expenses

Advertising expenses are recognized in profit or loss as incurred.

EE. Non-current assets or a disposal group held for sale and discontinued operations

Non-currents assets or a disposal group are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the assets must be available for immediate sale in their present condition, the Group must be committed to sell, there must be a program to locate a buyer and it is highly probable that a sale will be completed within one year from the date of classification. These assets are not depreciated and are presented separately in the balance sheet, at the lower of their carrying amount and fair value less costs to sell. If the carrying amount is higher than the fair value less costs to sell, an impairment loss is recognized for the assets (or disposal group) to the extent of the difference. Simultaneously, liabilities associated with these assets are presented separately in the balance sheet, in a similar manner. In addition, other comprehensive income (loss) is presented separately in the statement of changes in equity.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

As from January 1, 2010, when the parent decides to sell part of its interest in a subsidiary so that after the sale the parent retains a non-controlling interest (such as rights conferring significant influence), all the assets and liabilities attributed to the subsidiary are classified as held for sale and the relevant provisions of IFRS 5 are applicable, including presentation as discontinued operations.

As from January 1, 2010, the only the disclosures required in IFRS 5 are provided for non-current assets (or disposal groups) that are classified as held for sale or discontinued operations. Disclosures in other IFRSs apply to such assets only if they require specific disclosures in respect of those non-current assets or disposal groups.

A discontinued operation is an operation that either has been disposed of or is classified as held for sale and represents a separate major line of business or geographical area of operations. In addition to being classified in the balance sheet as above, the operating results and cash flows relating to the discontinued operation are presented separately in the statement of income and in the statement of cash flows with the comparative data including the segment information reclassified for that purpose.

FF Insurance contracts

IFRS 4 - Insurance Contracts allows the insurer to continue with the same accounting policy that was in effect prior to the transition date to IFRS for insurance contracts that it issues (including related acquisition costs and related intangible assets) and the reinsurance contracts that it acquires

In this context, it is noted that the accounting policy in general insurance business, applied by insurance subsidiaries in Israel (partially set by the Supervisor of Insurance in Israel) is substantially the same as that applied by insurance subsidiaries in other countries, with the exception of that stated in section (2) f (2) below and in Note 30(E).

1. Life assurance

A) Recognition of income – see section Z (10) above.

B) Liabilities for life assurance contracts

Liabilities for life assurance in Israel are computed according to the Supervisor's directives (regulations and circulars), generally accepted accounting principles and standard actuarial methods. The reserves are computed according to the relevant coverage data, such as the age of the policyholder, number of years of coverage, type of insurance and sum of insurance.

C) Liabilities for life assurance and the reinsurers' share therein are determined on the basis of annual actuarial assessments carried out by the appointed actuaries of the insurance subsidiaries.

Liabilities for CPI-linked life assurance contracts and CPI-linked investments used to cover these liabilities were included in the financial statements according to the most recently published CPI prior to the balance sheet date, including liabilities for life assurance contracts in respect of policies with semi-annual linkage.

D) Directives of the Supervisor of Insurance ("the Supervisor") regarding liabilities for annuities

Circulars issued by the Supervisor, regarding the method of calculating the liabilities for annuities in life assurance policies provide updated directives on how to calculate the provisions as a result of the improvement in life expectancy that requires monitoring the adequacy of the reserves in insurance policies that permit the receipt of an annuity, and their proper supplementation.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

Accordingly, The Phoenix Insurance immediately supplemented the liability, to the extent necessary, with respect to policies in which annuities are currently being paid or when the policyholder has reached retirement age or for a group of unprofitable policies. Regarding other policies, where profits are expected, the liability is supplemented alongside the receipt of the expected income, over the policy period.

E) Deferred acquisition costs

Deferred acquisition costs (DAC) of life assurance policies sold as from January 1, 1999 include commission for agents and acquisition supervisors and other expenses related to the acquisition of new policies, including part of the general and administrative expenses. The DAC is amortized at equal annual rates over the policy period but not over more than 15 years.

The DAC in respect of cancelled policies are written off at the time of cancellation or elimination.

Deferred acquisition costs of policies that were issued up to December 31, 1998 are computed by the actuaries of The Phoenix according to the "Zillmer deduction" method, based on a percentage of the premium or of the amount at risk according to the various insurance programs.

Pursuant to the directives of the Insurance Supervisor, the actuaries of The Phoenix assess the recoverability of the DAC in each reporting period. This assessment verifies that the liabilities for insurance policies, net of the DAC for policies sold since 1999 is sufficient, and that the policies are expected to generate future income to cover the DAC deduction and the insurance liabilities, operating expenses and commissions for those policies.

In addition, the actuaries of The Phoenix verify, in each year, the estimated period for receiving management fees for investment contracts, pension funds and provident funds to determine the amortization period of the DAC generated for them.

The assumptions used in this assessment, including assumptions regarding cancellations, operating expenses, yield on assets, mortality and illness rates, are determined by The Phoenix's actuaries every year on the basis of past experience and relevant current surveys.

Deferred acquisition costs for sale of pension plans

Direct acquisition costs (commissions to agents, acquisition supervisors and pension agents) that are directly attributable to acquisition of pension contracts, are recognized as deferred acquisition costs if they are separately identifiable and reliably measured and if their refund is expected, the direct acquisition costs represent the Company's right to receive management fees from pension funds. These results are amortized in equal annual rates over 10 years.

Liability adequacy testing for life assurance contracts

The Phoenix Insurance tests for liability adequacy for life assurance contracts. If the test indicates that the premiums received are insufficient to cover the expected claims, a special provision is recorded for the deficiency. Individual policies and collective policies are tested separately for groups of policies defined by the Supervisor.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

The assumptions used in these tests include assumptions regarding cancellations, operating expenses, yield from assets, mortality and illness rates, and are determined by the actuaries of The Phoenix Insurance every year on the basis of tests, experience and other relevant surveys. For collective policies, the test is according to the claims experience of the single collective and subject to statistical reliability of this experience.

F) Outstanding claims

Outstanding claims, net of the reinsurers' share therein, are computed on an individual case basis, according to the valuation of The Phoenix Insurance experts, based on the notifications regarding the insurance events and the sums insured.

The provisions for pension payments, annuities, long lasting payment claims for disability insurance, the direct and indirect expenses deriving from them, as well as the provisions for incurred but not yet reported claims (IBNR) are included under the liabilities for insurance contracts.

G) Investment contracts

Intakes in respect of investment contracts are not included in the item of earned premiums but are directly recorded under liabilities in respect of insurance contracts and investment contracts. Surrenders and maturities of these contracts are not included in the statement of income but are deducted directly from liabilities for insurance contracts and investment contracts.

In respect of these contracts, investment revenue, management fees collected from the policyholders, change in the liabilities and payments for insurance contracts for the share of the policyholders in investment revenue, commissions to agents, and general and administrative expenses are recognized in the statement of income.

H) Provision for participation in earnings of policyholders in group insurance

The provision is recognized under other payables. In addition, the change in the provision is offset by the income from the premium.

2. General insurance

A) Recognition of income – see section Z (10) above.

B) Payments and changes in liabilities in respect of insurance contracts, gross and residual, include settlement and direct handling costs of claims paid and outstanding claims that occurred during the reported period, as well as an adjustment of the provision for outstanding claims and their direct handling costs that were recorded in previous years.

C) Provisions for outstanding claims include provisions for indirect expenses to settle claims

D) Liabilities for insurance contracts and deferred acquisition costs

The reserve for unexpired risks and outstanding claims for insurance in Israel, included in liabilities for insurance contracts, and the reinsurers' share in the reserve and in the outstanding claims under reinsurance assets, and the deferred acquisition costs in general insurance, are computed in accordance with the Supervision of Insurance Business Regulations (Methods of Calculating Provisions for Future Claims in General Insurance), 1984, as amended, the Supervisor's directives in this respect and standard actuarial methods for computing outstanding claims, that are applied according to the actuaries' discretion.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

E) The liabilities section for insurance contracts is composed of liabilities for insurance contracts, as follows:

- 1) The unearned premium reserve reflects the insurance premium for the insurance period subsequent to the balance sheet date.
- 2) Provision for premium deficiency. The provision is recognized if the unearned premium (less deferred acquisition costs) does not cover the expected cost for insurance contracts. In the vehicle insurance, comprehensive residential and business branches, the provision is based on a model in the Insurance Business Regulations (Methods of Calculating Provisions for Future Claims in General Insurance), 1984 ("the calculation of reserves regulations").

F) Outstanding claims

The outstanding claims in the financial statements are computed as follows:

- 1) Outstanding claims and the reinsurers' share thereof are included on the basis of an actuarial valuation, except for the branches detailed in section 2 below. Indirect expenses to settle claims are included on the basis of an actuarial valuation.
- 2) In the following branches, the actuary determined that it is not possible to apply the actuary model due to the absence of statistical significance: engineering insurance, insurance of freight, marine hull and aircraft, and incoming business. These branches include outstanding claims based on the separate evaluation of each claim according to an opinion received from Company lawyers and experts of The Phoenix Insurance who handle the claims. The evaluations include a suitable provision for settlement and handling expenses not yet paid at the date of the financial statement and based on ceding companies for incoming business, with the addition of IBNR if necessary.
- 3) Excess of income over expenses

In insurance companies incorporated in Israel, for all businesses with long tail claims (branches in which it could be several years before the claim is settled), such as the liability and motor act branches, excess of income over expenses is calculated on a tri-annual cumulative basis (the excess).

The excess is comprised of premiums, acquisition costs and claims with the addition of yield at an annual rate of 3%, in real terms, all net of the reinsurers' share, for each insurance branch and the respective underwriting year. The excess accumulated until its release, from the beginning of the insurance, net of the unexpired risk reserve and net of outstanding claims calculated as aforesaid ("the accrual"), is included under liabilities for insurance contracts and any deficit is recognized as an expense.

In insurance subsidiaries in other countries, the accumulation method is not applied. The insurance reserves are based on standard actuarial methods.

G) Deferred acquisition costs

Deferred acquisition costs in general insurance include agents' commissions and part of the general and administrative expenses related to the issuance of policies, in respect of the unearned insurance premiums on retention. The acquisition costs are calculated for each branch separately, on the basis of the actual rates of expenses or according to standard rates, as a percentage of the unearned premium, at the lower of the two.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

- H) The insurance premiums item includes all the amounts paid by the borrowers in connection with property insurance policies through a mortgage bank. The amounts paid to a mortgage bank for expenses are recognized under the item commissions and other acquisition costs.
 - I) Claims recoveries and salvage are taken into consideration in the data-base by which the actuarial valuations of the outstanding claims are calculated.
 - J) Participation in income in group insurance, recorded on the basis of valid agreements, is deducted from the premiums.
3. Health insurance
- A) Recognition of income – see section Z (10) above.
 - B) Liabilities for health insurance contracts

Liabilities for health insurance contracts in Israel are computed according to the Supervisor's directives (regulations and circulars), generally accepted accounting principles and standard actuarial methods. The liabilities are computed according to the relevant coverage data, such as the age of the policyholder, number of years of coverage, type of insurance and sum of insurance.

Health insurance liabilities and the reinsurers' share therein are determined on the basis of actuarial assessments.
 - C) Outstanding claims

The provisions for long lasting payment claims with respect to long-term care insurance, the direct and indirect expenses deriving from them, as well as the provisions for incurred but not yet reported claims (IBNR) are included under the insurance reserves.
 - D) Provision for participation in earnings of policyholders in group insurance

The provision is recognized under other payables. In addition, the change in the provision is offset by the income from the premium.
 - E) The unexpired risk reserve, which is recognized under liabilities in respect of insurance contracts, includes, when necessary, a provision in respect of the anticipated loss (premium deficiency), which is computed on the basis of an actuarial valuation, as an estimated cash flow for the contract.
 - F) Deferred acquisition costs
 - 1) Deferred acquisition costs in health insurance include commissions for sales agents and supervisors and part of the general and administrative expenses related to the issuance of policies.
 - 2) In the health and hospitalization branch, deferred acquisition costs are amortized at equal rates over the period of the policy, but in no longer than six years. Deferred acquisition costs relating to cancelled policies are written off on the cancellation date.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

- 3) The appointed actuary assesses the recoverability of the DAC every year. The assessment verifies that the liabilities for insurance policies (policies sold in 2005 and for which the DAC is calculated), net of the DAC is adequate and that the policies are expected to generate future income to cover the DAC deduction, insurance liabilities, operating expenses and commissions for those policies. The assessment is on the product level.

The assumptions used in this assessment, which include assumptions regarding cancellations, operating expenses, yield on assets, mortality and illness rates, are determined by the actuaries every year on the basis of past experience and relevant current surveys.

FF. Foreign currency exchange rates and linkage

- Assets and liabilities in foreign currency, or linked to foreign currency, are included as per the valid representative exchange rate published by the Bank of Israel on the balance sheet date.
- The CPI-linked assets and liabilities are included as per the appropriate CPI for each linked asset or liability.

Exchange rates of the principal functional currencies and the CPI:

At	Euro representative exchange rate	USD representative exchange rate	December CPI
	NIS	NIS	Points (*)
December 31, 2011	4.938	3.821	216.3
December 31, 2010	4.738	3.549	211.7
December 31, 2009	5.442	3.775	206.2
December 31, 2008	5.297	3.802	198.4
Rate of change in the year ended:	%	%	%
December 31, 2011	4.22	7.7	2.1
December 31, 2010	(12.9)	(5.9)	2.7
December 31, 2009	2.7	(0.7)	3.9

*) CPI on average basis 1993 = 100

HH Presentation of the statement of comprehensive income

The Company elected to present comprehensive income in two statements: a statement of income and a statement of comprehensive income, which include, as well as the profit from the statement of income, all the items recognized in other comprehensive income.

II Changes in other comprehensive income items

The Group presents the changes between the opening and the closing balances of each other comprehensive income component in the statement of changes in equity.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

JJ Disclosure of new IFRSs in the period prior to their adoption

IAS 1 – Presentation of Financial Statements

In June 2011, the IASB published an amendment to IAS 1 ("the amendment"). The amendment revises the way other comprehensive income is presented. According to the amendment, components that may be reclassified to profit or loss in the future (for example, for derecognition or settlement) would be presented separately from those that would never be reclassified to profit or loss.

The amendment is effective retrospectively for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

The Company estimates that the amendment is not expected to have a material effect on the financial statements.

IAS 12 - Income Taxes

The amendment to IAS 12 ("the amendment") applies to investment property measured at fair value. According to the amendment, the deferred tax asset/liability in respect of such property should be measured based on the presumption that the carrying amount of the property will be recovered in full through sale (and not through use). However, if the investment property is depreciable and is held within a business model with the objective of recovering substantially all of the underlying economic benefits through use and not sale, the Company should apply the regular guidelines of IAS 12 (namely, deferred taxes are measured based on the expected recovery of the property as determined by management - through sale or use).

The amendment supersedes the provisions of SIC 21 that require separation of the land component and the building component of investment property measured at fair value in order to calculate the deferred tax.

The amendment is effective retrospectively commencing from the financial statements for annual periods beginning on January 1, 2012. Earlier application is permitted.

The Company estimates that the amendment is not expected to have a material effect on the financial statements.

IAS 19 – Employee Benefits (Revised)

In June 2011, the IASB published IAS 19 (Revised) ("the standard"). The main amendments in the standard are as follows:

- Actuarial gains and losses will be recognized in other comprehensive income only and not in profit or loss.
- The 'corridor' method, which allowed deferral of actuarial gains and losses, is eliminated.
- The return on plan assets will be recognized in profit or loss based on the rate used to discount the obligations for employee benefits, regardless of the actual composition of the investment portfolio.
- The distinction between short-term and long-term employee benefits will be based on the expected settlement date and not on the date the employee's rights to the benefit is established.
- The cost of past services arising from changes in the plan will be recognized immediately.

The standard is effective retrospectively for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

The Company is evaluating the effect of the new standard, but at this stage, is unable to assess the effect on the financial statements.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

IAS 32 -Financial Instruments: IFRS 7 - Financial Instruments: Disclosure

In December 2011, the IASB issued amendments to IAS 32 - Offsetting Financial Assets and Financial liabilities ("the amendments to IAS 32"). The amendments to IAS 32 clarify the meaning of "currently has a legally enforceable right to set off" ("the right to set off"). According to the amendments to IAS 32, rights of set-off must not only be legally enforceable in the normal course of business, but must also be enforceable in the event of bankruptcy or insolvency of one of the counterparties. The amendments to IAS 32 also clarify that of offset must not be contingent on a future event or periods of time in which they will not apply, or may be removed by a future event.

At the same time, in December 2011, the IASB issued amendments to IFRS 7 - Offsetting Financial Assets and Financial liabilities ("the amendments to IFRS 7"). The amendments to IFRS 7 require the Company to disclose information about rights of set-off and related arrangements (such as collateral agreements), about the composition of the offset amounts and amounts subject to arrangements that allow offsetting but do not meet all the offsetting criteria in IAS 32.

The amendments to IAS 32 will be applied retrospectively in financial statements for annual periods beginning on or after January 1, 2014. Earlier application is permitted with disclosure and with the disclosure required under the amendments to IFRS 7 as set out above. The amendments to IFRS 7 will be applied retrospectively in financial statements for annual periods beginning on or after January 1, 2013.

The Company believes that the amendments to IAS 32 are not expected to have a material effect on the financial statements. The disclosures required according to the amendments to IFRS 7 will be included in the Company's financial statements.

IFRS 7 - Financial Instruments: Disclosure

The amendment to IFRS 7 ("the amendment") introduces new and expanded disclosure requirements regarding derecognition of financial assets and disclosure requirements in cases where there is unusual transfer activity near the end of a reporting period. The objective of the amendment is to assist users of financial statements to assess the risks to which the Company may remain exposed from transfers of financial assets and the effect of these risks on the Company's financial position. The amendment is designed to enhance the reporting transparency of transactions involving asset transfers, specifically securitization of financial assets. The amendment is applied prospectively for accounting periods beginning on January 1, 2012. Earlier application is permitted.

The relevant disclosures will be included in the Company's financial statements.

IFRS 9 – Financial Instruments:

1. In November 2009, the IASB issued IFRS 9 – Financial Instruments, the first part of Phase 1 of a project to replace IAS 39 – Financial Instruments: Recognition and Measurement. IFRS 9 ("the standard") focuses mainly on the classification and measurement of financial assets and it applies to all financial assets within the scope of IAS 39.

According to IFRS 9, upon initial recognition, all the financial assets (including hybrid contracts with financial asset hosts) will be measured at fair value. In subsequent periods, debt instruments should be measured at amortized cost if both of the following conditions are met:

- The asset is held within a business model whose objective is to hold assets in order to collect the contractual cash flows.
- The contractual terms of the financial asset give rise, on specified dates, to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

Notwithstanding the aforesaid, upon initial recognition, the Company may designate a debt instrument that meets both of the abovementioned conditions as measured at fair value through profit or loss if this designation eliminates or significantly reduces a measurement or recognition inconsistency ("accounting mismatch") that would have otherwise arisen.

Subsequent measurement of all other debt instruments and financial assets should be at fair value.

Financial assets that are equity instruments should be measured in subsequent periods at fair value and the changes recognized in profit or loss or in other comprehensive income, in accordance with the election by the Company on an instrument-by-instrument basis (amounts recognized in other comprehensive income cannot be subsequently transferred to profit or loss). Nevertheless, if equity instruments are held for trading, they should be measured at fair value through profit or loss. This election is final and irrevocable. When an entity changes its business model for managing financial assets it shall reclassify all affected financial assets. In all other circumstances, reclassification of financial instruments is not permitted.

The standard is effective commencing from January 1, 2015. Earlier application is permitted. Upon initial application, the standard should be applied retrospectively with appropriate disclosure or with restatement of comparative figures, subject to the reliefs set out in the standard.

2. In October 2010, amendments to the standard were issued regarding derecognition and financial liabilities. According to those amendments, the provisions of IAS 39 will continue to apply to derecognition and to financial liabilities for which the fair value option has not been elected (designated as measured at fair value through profit or loss); that is, the classification and measurement provisions of IAS 39 will continue to apply to financial liabilities held for trading and financial liabilities measured at amortized cost.

The changes arising from these amendments affect the measurement of a liability for which the fair value option had been chosen. Pursuant to the amendments, the amount of the adjustment to the liability's fair value that is attributable to changes in credit risk should be presented in other comprehensive income. All other fair value adjustments should be presented in profit or loss. If presenting the fair value adjustment of the liability arising from changes in credit risk in other comprehensive income creates an accounting mismatch in profit or loss, then that adjustment should also be presented in profit or loss rather than in other comprehensive income.

Furthermore, according to the amendments, derivative liabilities in respect of certain unquoted equity instruments can no longer be measured at cost but rather only at fair value,

The amendments are effective commencing from January 1, 2015. Earlier application is permitted provided that the Company also adopts the provisions of the standard regarding the classification and measurement of financial assets (the assets phase.) Upon initial application, the amendments should be applied retrospectively, with appropriate disclosure or with restatement of comparative figures, subject to the reliefs set out in the amendments.

The Company is evaluating the effect of the new standard but at this stage, is unable to assess the effect, if any, on the financial statements.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

IFRS 10, IFRS 11, IFRS 12, IFRS 13 - Consolidated Financial Statements, Joint Arrangements, Disclosure of Interests in Other Entities and Fair Value Measurement

In May 2011, The IASB issued four new standards: IFRS 10 – Consolidated Financial Statements; IFRS 11 – Joint Arrangements; IFRS 12 – Disclosure of Interests in Other Entities and IFRS 13 – Fair Value Measurement ("the new standards"); and amendments to standards: IAS 27R (Revised 2011) – Separate Financial Statements and IAS 28R (Revised 2011) – Investments in Associates and Joint Ventures.

The new standards are effective retrospectively for annual periods beginning on or after January 1, 2013. Earlier application is permitted, but only if the new standards are early-adopted together (except for the disclosure requirements according to IFRS 12, which may be applied separately). The standards include transition guidelines with exemptions for initial application.

The main provisions of the standards and their expected effect on the Company are described below:

IFRS 10 – Consolidated Financial Statements

IFRS 10 replaces IAS 27 for accounting of consolidated financial statements, and provides guidelines for accounting of structured entities, which were previously within the scope of SIC 12, Consolidation – Special Purpose Entities.

IFRS 10 does not contain changes to consolidation requirements, however it includes a new definition for control as the basis for consolidation and contains a single model for consolidation. According to IFRS 10, control requires power over an investee and exposure or a right to variable returns from an investee. Power is the ability to affect and direct the investee's activities, which has a significant effect on the investor's returns.

According to IFRS 10, when assessing control, potential voting rights are considered only if they are exercisable, whereas according to IAS 27 prior to the amendment, potential voting rights are considered only if they are currently exercisable, and the management's intentions and the financial ability to exercise these rights are not considered.

In addition, according to IFRS 10, an investor has control even if it owns less than the majority of the voting rights in the investee (effective control), while according to IAS 27, there are two models for consolidation: de facto control and legal control.

IFRS 10 will be applied retrospectively in financial statements for annual periods beginning on or after January 1, 2013.

The Company is assessing the effect of the new standard on the financial statements, however at this stage, it is unable to assess the effect.

IAS 27R – Separate Financial Statements

IAS 27R ("the amendment") replaces IAS 27 and addresses separate financial statements only. The current guidelines for separate financial statements remain unchanged according to the revised amendment.

IFRS 11 – Joint Arrangements

IFRS 11 supersedes IAS 31 – Interests in Joint Ventures and SIC 13 – Jointly Controlled Entities: Non-Monetary Contributions by Venturers.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

IFRS 11 establishes accounting principles for joint arrangements of which two or more parties have joint control.

IFRS 11 classifies joint arrangements in two categories:

- Joint ventures, where the parties to the arrangement have joint control of the rights to the net assets of the joint venture. According to IFRS 11, joint ventures are accounted for using the equity method only, whereas according to IAS 31, jointly controlled entities can be accounted for using the proportionate consolidation method or the equity method.
- Joint operations, where the parties to the arrangement have joint control of the rights to the assets and obligations for the liabilities, relating to the joint operations. According to IFRS 11, the entity will recognize the assets, liabilities, revenues and expenses of the joint operations based on its proportionate share of this activity, as determined in the joint arrangement, the same as the requirements in current accounting principles.

IFRS 11 will be applied retrospectively in financial statements for annual periods beginning on or after January 1, 2013.

The Company believes that the effect of IFRS 11 on the financial statements is not expected to be material. It is noted that the Group accounts for jointly-controlled entities according to the equity method, under IAS 31.

IAS 28R – Investments in Associates

IAS 28R replaces IAS 28. The main changes compared to IAS 28 relate to equity accounting of investments in joint ventures, following publication of IFRS 11 and the transition from proportionate consolidation to equity accounting for these investments. According to IAS 28 (Revised), for disposal of an investment in an associate or a joint transaction, including part thereof, the provisions of IFRS 5 should be applied for the part that fulfills the requirements for classification as held for sale, and for the remaining part, the equity method continues to be applied until the date of actual disposal. In addition, for an investment in an associate that becomes an investment in a joint venture and vice versa, the equity method continues to be applied and the remaining investment is not remeasured.

IFRS 28 (Revised) will be applied retrospectively in financial statements for annual periods beginning on or after January 1, 2013. Earlier application is permitted, however if the Company elects early application, it must apply IFRS 10, IFRS 11, IFRS 12 and IAS 27R (2011) as one package.

The Company believes that the effect of IFRS 28 (Revised) on the financial statements is not expected to be material.

IFRS 12 – Disclosure of Interests in Other Entities

IFRS 12 establishes the disclosure requirements for investees, including subsidiaries, joint ventures, associates and structured entities. IFRS 12 expands the disclosure requirements for the judgments and assumptions applied by management in determining whether the entity has control, joint control or significant influence over an investee, and determines the type of joint arrangement. IFRS 12 also establishes disclosure requirements for significant investees.

The appropriate disclosures will be included in the Company's financial statements with initial application of the standard.

Notes to the Consolidated Financial Statements

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)

IFRS 13 – Fair Value Measurement

IFRS 13 establishes guidelines for fair value measurement, when this measurement is required according to international standards. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. IFRS 13 also defines characteristics of market participants and states that fair value is based on the assumptions that market participants would use. According to IFRS 13, fair value measurement assumes a transaction taking place in the principal market for the asset or liability, or in the absence of a principal market, in the most advantageous market.

IFRS 13 requires maximizing the use of observable inputs compared to the use of unobservable inputs. IFRS 13 established a fair value hierarchy according to the inputs used to determine fair value:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2: Inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly
- Level 3: Inputs that are not based on observable market data (unobservable inputs) (assessment without using observable market inputs).

IFRS 13 establishes disclosure requirements.

The disclosures and measurement of assets and liabilities according to IFRS 13 are required prospectively only after initial application, from the financial statements for annual periods commencing on or after January 1, 2013. Earlier application is permitted. These new disclosures do not apply to the comparative figures.

The appropriate disclosures will be included in the Company's financial statements with initial application of the standard.

The Company believes that the effect of IFRS 13 on the financial statements is not expected to be material.

NOTE 3 – CASH AND CASH EQUIVALENTS

	Interest rate Annual Weighted *	December 31	
		2011	2010
		NIS million	
A. <u>Cash balances and deposits available for immediate withdrawal</u>			
NIS	2.72	369	395
Foreign currency	2.27	1,589	1,231
		1,958	1,626
B. <u>Short-term deposits</u>			
NIS	2.90	991	1,427
Foreign currency	2.29	661	390
		1,652	1,817
		3,610	3,443

*) December 31, 2011

Notes to the Consolidated Financial Statements

NOTE 4 – PERFORMANCE-BASED CASH AND CASH EQUIVALENTS IN INSURANCE COMPANIES

	December 31	
	2011	2010
	NIS million	
Cash balances and deposits available for immediate withdrawal (1)	609	214
Short-term deposits (2)	667	393
	<u>1,276</u>	<u>607</u>

- (1) At December 31, 2011, cash in banks bears current interest at a weighted annual rate of 2.79% based on interest rates for daily deposits (2010, 1.72%).
- (2) Short-term bank deposits in banks are for periods of between one week and three months. At December 31, 2011, deposits bear weighted annual interest at a rate of 3.05%. (2010, 2%).

NOTE 5 – SHORT-TERM INVESTMENTS OF THE FINANCE SECTOR (MAINLY EXCHANGE-TRADED FUNDS AND DEPOSITS)

	December 31	
	2011	2010
	NIS million	
A. <u>Financial assets measured at fair value through profit or loss (1)</u>		
Marketable securities	90	99
Non-marketable securities		
Debentures	5	148
Assets held by special purpose entities that issue exchange-traded funds and deposits	8,744	13,380
	<u>8,839</u>	<u>13,627</u>
B. <u>Credit for acquisition of securities</u>		
Open accounts	190	97
Less allowance for doubtful accounts	(6)	(5)
Receivables, net	<u>184</u>	<u>92</u>
C. <u>Designated deposits:</u>		
NIS	6,838	1,993
In USD	2,333	1,446
Other	1,241	1,088
	<u>10,412</u>	<u>4,527</u>
	<u>19,435</u>	<u>18,246</u>

- (1) Financial assets, other than assets used as back-up assets held by special purpose entities that issue exchange-traded funds and deposit, are classified as held for trading and, therefore, are recognized at fair value through profit or loss. Assets held by special purpose entities that issue exchange-traded funds and deposit are designated by the Group at initial recognition at fair value through profit or loss.

Notes to the Consolidated Financial Statements

NOTE 6 – OTHER SHORT-TERM INVESTMENTS

	December 31	
	2011	2010
	NIS million	
<u>Financial assets held for trading and measured at fair value through profit or loss</u>		
Shares	43	72
Government debentures	420	551
	463	623
<u>Available-for-sale financial assets</u>		
Shares	15	45
Government debentures	36	127
	51	172
<u>Bank deposits (1)</u>	201	213
	715	1,008

NOTE 7 – TRADE RECEIVABLES

	December 31	
	2011	2010
	NIS million	
Open accounts	3,815	3,077
Checks receivable	473	67
	4,288	3,144
Less allowance for doubtful accounts	106	108
Trade receivables, net	4,182	3,036

Trade receivables do not bear interest. At December 31, 2011, the average credit term for customers in Israel and the United States is 55, 77 and 10 days, respectively. Impaired debts are accounted for through recording an allowance for doubtful accounts.

Changes the allowance for doubtful accounts:

	NIS million
<u>Balance as of January 1, 2010</u>	100
Provision for the year	20
Doubtful accounts written off	(7)
Exchange differences on translation of foreign operations	(5)
<u>Balance as of January 1, 2011</u>	108
Provision for the year	12
Doubtful accounts written off	(15)
Exchange differences on translation of foreign operations	1
<u>Balance as of December 31, 2011</u>	106

Notes to the Consolidated Financial Statements

NOTE 7 – TRADE RECEIVABLES (CONTD.)

Aging analysis of gross trade receivables balance as of the balance sheet date:

	Trade receivables not yet past due	Trade receivables past due with collection in arrears of					
		Up to 90 days	91-180 days	181-270 days	271-365 days	Over 1 year	Total
		NIS million					
<u>December 31, 2011</u>	3,750	358	41	10	3	126	4,288
Less allowance for doubtful accounts							106
<u>December 31, 2011</u>							4,182
<u>December 31, 2010</u>	2,851	142	44	3	2	102	3,144
Less allowance for doubtful accounts							108
<u>December 31, 2010</u>							3,036

NOTE 8 – INSURANCE PREMIUM RECEIVABLE

A. Composition:

	December 31	
	2011	2010
NIS million		
Premium receivables (b)	971	938
Less allowance for doubtful accounts	10	6
Total premium receivable	<u>961</u>	<u>932</u>

B. Aging:

	December 31	
	2011	2010
NIS million		
Premium receivable past due, but not impaired	810	744
Past due *):		
Less than 90 days	93	113
90-180 days	27	16
More than 180 days	<u>28</u>	<u>51</u>
Total premium receivable past due, but not impaired	148	180
Impaired premium receivable	13	14
Less allowance for doubtful accounts	10	6
Premium receivables, net	<u>961</u>	<u>932</u>

*) Primarily past due receivables in life assurance. These receivables are largely secured by the maturity value of the policy.

Notes to the Consolidated Financial Statements

NOTE 9 – OTHER RECEIVABLES

	December 31	
	2011	2010
	NIS million	
Prepaid expenses, advances to suppliers and revenues receivable	279	215
Related parties – current balances	41	39
Receivables for acquisition of operations	-	99
Current maturities of long-term debts and loans	31	33
Institutions	125	59
Dividend receivable	-	51
Financial derivatives	15	2
Insurance companies and insurance agents	58	47
Customer deposits held in trust	30	66
Receivables for joint ventures (1)	331	77
Other receivables (2)	302	200
	<u>1,212</u>	<u>888</u>

- (1) At the balance sheet date, the balance in respect of transfer of moneys by Avner Oil Exploration – Limited Partnership and Delek Drilling – Limited Partnership to Noble, from joint venture activities: Michal Matan, Ratio Yam, Ruth, Alon and Yam Tethys to finance the partnership's share in repaying liabilities for the joint venture.
- (2) Including receivables of NIS 150 million for disposal of an investment in available for sale financial assets

NOTE 10 – INVENTORIES

	December 31	
	2011	2010
	NIS million	
Fuel products in gas stations and facilities	824	615
Inventory of consumables in gas stations	185	163
Oil and distillates in the refinery	1,807	354
Other	225	141
	<u>3,041</u>	<u>1,273</u>

Notes to the Consolidated Financial Statements

NOTE 11 – FINANCIAL INVESTMENTS OF INSURANCE COMPANIES

A. Composition:

	December 31	
	2011	2010
	NIS million	
Financial investments for performance based contracts (1)	19,714	19,986
Other financial investments (2)	16,416	15,233
	36,130	35,219

1. Financial investments for performance based contracts

	December 31	
	2011	2010
	NIS million	
Marketable debt assets	7,282	7,332
Non-marketable debt assets	3,895	3,936
Shares	4,200	4,683
Other financial investments	4,337	4,035
	19,714	19,986

Fair value hierarchy of financial assets classified in accordance with IFRS 7

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
	NIS million			
Marketable debt assets	7,282	-	-	7,282
Non-marketable debt assets	-	3,765	130	3,895
Shares	4,109	-	91	4,200
Other	2,176	201	1,960	4,337
Total	13,567	3,966	2,181	19,714

	December 31, 2010			
	Level 1	Level 2	Level 3	Total
	NIS million			
Marketable debt assets	7,332	-	-	7,332
Non-marketable debt assets	-	3,826	110	3,936
Shares	4,594	-	89	4,683
Other	2,668	458	909	4,035
Total	14,594	4,284	1,108	19,986

Notes to the Consolidated Financial Statements

NOTE 11 – FINANCIAL INVESTMENTS OF INSURANCE COMPANIES (CONTD.)

Changes in level-3 financial assets measured at fair value

	Financial assets measured at fair value through profit or loss			
	Non-marketable debt assets	Shares	Other financial investments	Total
	NIS million			
Balance as of January 1, 2011	110	89	909	1,108
Total gains (losses) recognized in profit or loss	(51)	-	3	(48)
Acquisitions	-	2	1,193	1,195
Redemptions	(19)	-	(145)	(164)
Transfer to level 3	90	-	-	90
Balance as of December 31, 2011	130	91	1,960	2,181
Total gains (losses) for the period included in profit or loss for assets held at December 31, 2011	(51)	-	3	(48)

2. Other financial investments

	December 31, 2011			
	At fair value through profit or loss	Available-for-sale financial assets	Loans and receivables	Total
	NIS million			
Marketable bonds ©	129	4,563	-	4,692
Non-marketable bonds (D)	-	1,896	8,445	10,341
Shares (E)	13	476	-	489
Other (F)	299	596	-	894
Total	440	7,531	8,445	16,416

	December 31, 2010			
	At fair value through profit or loss	Available-for-sale financial assets	Loans and receivables	Total
	NIS million			
Marketable bonds ©	50	4,443	-	4,493
Non-marketable bonds (D)	-	1,417	8,112	9,529
Shares (E)	14	569	-	583
Other (F)	261	367	-	628
Total	325	6,796	8,112	15,233

Notes to the Consolidated Financial Statements

NOTE 11 – FINANCIAL INVESTMENTS OF INSURANCE COMPANIES (CONTD.)**B. Financial investments in insurance companies as presented in the balance sheet:**

	December 31	
	2011	2010
	NIS million	
Current assets	1,717	1,660
Non-current assets	34,413	33,559
	<u>36,130</u>	<u>35,219</u>

C. Marketable bonds in other financial investments

	December 31	
	2011	2010
	NIS million	
Government bonds or government-guaranteed bonds	3,026	3,092
Other non-marketable bonds	1,665	1,399
Other marketable bonds	1	2
	<u>4,692</u>	<u>4,493</u>
Impairment recognized in profit or loss (cumulative)	<u>22</u>	<u>17</u>

D. Non-marketable bonds in other financial investments

	Carrying amount		Fair value	
	2011	2010	2011	2010
	NIS million			
Government bonds or government-guaranteed bonds	5,385	5,260	6,526	6,379
Other non-marketable bonds	4,956	4,269	5,094	4,473
Total non-marketable bonds	<u>10,341</u>	<u>9,529</u>	<u>11,620</u>	<u>10,852</u>
Impairment recognized in profit or loss (cumulative)	<u>80</u>	<u>43</u>	-	

E. Shares in other financial investments

	December 31	
	2011	2010
	NIS million	
Marketable shares	463	556
Non-marketable shares	26	27
Total shares	<u>489</u>	<u>583</u>
Impairment recognized in profit or loss (cumulative)	<u>-</u>	<u>24</u>

Notes to the Consolidated Financial Statements

NOTE 11 – FINANCIAL INVESTMENTS OF INSURANCE COMPANIES (CONTD.)

F. Other financial investments

	December 31	
	2011	2010
	NIS million	
Marketable financial investments	652	455
Non-marketable financial investments	242	173
	894	628
Impairment recognized in profit or loss (cumulative)	67	66

Other financial investments include mainly investments in exchange-traded funds, mutual funds, investment funds, financial derivatives, future contracts, options and structured products.

G. Disclosure of other financial investments measured at fair value

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
	NIS million			
Marketable debt assets	4,692	-	-	4,692
Non-marketable debt assets	-	1,896	-	1,896
Shares	463	-	26	489
Other	652	30	212	894
Total	5,807	1,926	238	7,971

	December 31, 2010			
	Level 1	Level 2	Level 3	Total
	NIS million			
Marketable debt assets	4,493	-	-	4,493
Non-marketable debt assets	-	1,417	-	1,417
Shares	556	-	27	583
Other	455	64	109	628
Total	5,504	1,481	136	7,121

Notes to the Consolidated Financial Statements

NOTE 11 – FINANCIAL INVESTMENTS OF INSURANCE COMPANIES (CONTD.)

Movement in assets measured at fair value on level 3

	Year ended December 31, 2011		
	Shares	Investments Financial Other	Total
		NIS million	
Balance as of January 1, 2011	27	109	136
			-
Total profits and losses:			-
In profit or loss	-	22	22
Other comprehensive income	(1)	19	18
	(1)	41	40
Movement:			
Purchases	3	86	89
Sales	(3)	-	(3)
Deposits	-	(24)	(24)
	-	62	62
	26	212	238
Total gains included in profit or loss for assets held at December 31, 2011	3	29	31

Movement in assets measured at fair value on level 3

	Year ended December 31, 2010		
	Shares	Investments Financial Other	Total
		NIS million	
Balance as of January 1, 2010	42	135	177
Total profits and losses:			
In profit or loss	-	13	13
Other comprehensive income	1	4	5
	1	17	18
Movement:			
Purchases	6	20	26
Sales	(22)	(6)	(28)
Deposits	-	(57)	(57)
	(16)	(43)	(59)
	27	109	136
Total gains (losses) included in profit or loss for assets held at December 31, 2010	3	(3)	-

Notes to the Consolidated Financial Statements

NOTE 11 – FINANCIAL INVESTMENTS OF INSURANCE COMPANIES (CONTD.)

H. Interest rates used for determining fair value in Israel

The fair value of non-marketable financial assets measured at fair value through profit or loss, and the fair value of non-marketable financial assets for which information is provided for disclosure purposes only, are determined by discounting estimated future cash flows. The discount rates are based on the yields of government bonds and margins of corporate debentures as reported on the TASE plus a premium for non-marketable. The interest rates used for discounting are determined by a company that provides interest rate quotations in relation to different risk ratings.

NOTE 12 – LONG-TERM LOANS, DEPOSITS AND RECEIVABLES

A. Composition:

	Interest rate Annual (1)	December 31	
		2011	2010
		NIS million	
	%		
Loans			
CPI-linked (2)	7.0	82	86
USD-linked or -denominated	6.3	59	9
Unlinked	6.0	50	82
		191	177
Less - current maturities		31	30
		160	147
Fuel Administration, long term (3)		252	235
Long-term trade receivables		40	43
Deposits and limited securities		80	51
Other		226	113
		758	589

(1) Balance as of December 31, 2011

(2) At December 31, 2011, includes NIS 11 million to interested parties (in 2010, NIS 11 million). See also Note 45.

(3) The balance is in respect of fuel inventory purchased by Delek Israel for the Fuel Administration. Considering the financial characteristics of the agreement with the Fuel Administration regarding the inventory, the balance in respect of this inventory is recognized as a receivable and not as inventory. The debt of the Fuel Administration for this inventory is linked to the dollar exchange rate and bears interest at Libor + 0.75% up to December 31, 2007. As from January 1, 2008, following the agreement with the Fuel Administration, the interest rate was adjusted to Libor + 1.5%-3.3%. The repayment date for the debt principal has not yet been set (the interest is paid on an ongoing basis). At December 31, 2011, the interest rate is 3%.

Notes to the Consolidated Financial Statements

NOTE 12 – LONG-TERM LOANS, DEPOSITS AND RECEIVABLES (CONTD.)**B. Maturities of loans**

	December 31 2011
	NIS million
First year – current maturities	31
Second year	18
Third year	14
Fourth year	60
Fifth year	9
Sixth year and onwards	59
	<u>191</u>

C. See Note 33 for liens.**NOTE 13 – INVESTMENTS IN OTHER FINANCIAL ASSETS**

	December 31	
	2011	2010
	NIS million	
Investment in available-for-sale financial assets		
Marketable shares (1)	477	2,172
Non-marketable shares (2)	5	328
Marketable debentures	3	-
	<u>485</u>	<u>2,500</u>
Investments in other financial assets at fair value through profit or loss		
Marketable shares	15	27
	<u>500</u>	<u>2,527</u>

1. Investment in available-for-sale financial assets - marketable shares

- A) In August 2009, the Company's board of directors resolved to approve an investment of USD 218 million to purchase shares in the US company, Noble Energy Inc. ("Noble"), which is traded on the NYSE (2% of Noble's share capital). In July 2010, the Company's board of directors resolved to increase the investment in Noble shares in an additional amount that will not exceed 1% of the share capital of Noble. In August 2010, the Company's board of directors resolved to increase the limit of the investment in Noble up to a total holding of 4% of the share capital of Noble.

In 2011, the Group sold Noble shares. The pre-tax profit created for the Group from the sale of Noble shares amounted to NIS 397 million in 2011 (in 2010 – NIS 38 million).

Notes to the Consolidated Financial Statements

NOTE 13 – INVESTMENTS IN OTHER FINANCIAL ASSETS

To finance the acquisition of Noble shares, in 2009, the Group entered into an agreement with a foreign bank for a non-recourse loan of USD 120 million. The Group pledged Noble shares in favor of the foreign bank as collateral for the loan. In November 2010 the loan was increased and was replaced with a new loan, for the acquisition of up to 5,244,000 Noble shares, representing 3%, which will not exceed USD 230 million, for repayment by November 2013. The Group has undertaken to maintain, during the loan period, a ratio of 55% between the value of the collateral and the outstanding debt. If the ratio between the outstanding debt and the value of the collateral exceeds 66% (subject to changes under certain circumstances), the Group is required to act immediately to maintain the ratio of 55% between the balance of the outstanding debt and the value of the collateral. The Group calculates the value of the collateral and outstanding debt at the end of each trading day. The Group calculates the outstanding debt and value of total holdings and measures the ratio between the two. The Group is entitled to draw dividends distributed for the pledged shares, subject to compliance with the required collateral-debt ratio. Moreover, the agreement includes provisions for immediate forced repayment, including in the event of extreme change in the trading volume of Noble shares, suspension of trading or a sharp fall in Noble's share price. The interest for the utilized loan is annual Libor interest plus 1.57%, repayable annually. At December 31, 2011, NIS 30 million of the loan was utilized.

At December 31, 2011 the investment in Noble amounts to NIS 64 million. The positive balance of the capital reserve (before tax) reflecting gains from unrealized appreciation amounts to NIS 12 million.

- B. In 2011, the Group included expenses of NIS 165 million for impairment of certain financial assets classified as available for sale (before the effect of tax). At December 31, 2011, the balance of the marketable shares included in the investment in available-for-sale financial assets amounts to NIS 413 million.
- 2) Delek US Holdings ("Delek US") held 34.6% of the shares in Lion Oil Company ("Lion"). Most of the remaining shares in Lion are held by a third party who is the controlling shareholder. From the date of acquisition (July 2007) through September 30, 2008, the investment in Lion was presented using the equity method. In the fourth quarter of 2008, Delek US assessed the accounting treatment and concluded that it does not have significant influence over Lion because, among other reasons, Delek US is unable to influence decisions made by the board of directors of Lion and because it does not have access to necessary financial information about Lion. Therefore, as from the fourth quarter of 2008, the investment in Lion is treated as an available-for-sale asset. The change in the accounting treatment is after receiving the approval of the US Securities and Exchange Commission (SEC).

In 2010, Delek US recognized impairment of USD 60 million for the investment, based on a transaction for the acquisition of a further 53.7% of Lion shares. At December 31, 2010, the balance of the investment in Lion amounts to USD 71.6 million. At December 31, 2011 and after acquisition of all Lion shares, the financial statements of Lion are consolidated in the financial statements of the Group, and are no longer stated under investment in available-for-sale financial assets. See Note 14(I) below.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS**A. Composition:**

	Associates	
	December 31	
	2011	2010
	NIS million	
Shares	2,301	2,895
Loans – capital notes	374	939
	2,675	3,834
Less - provision for impairment	342	33
	2,333	3,801

- (1) Most of the increase in the provision during the year is due to provisions for impairment of the investment in Delek Automotive Systems Ltd. and Delek Real Estate Ltd. For further information see sections N(3) and F, respectively.

B. Condensed information from the financial statements of associates

	December 31	
	2011	2010
	NIS million	
Group share of net assets of associates, based on percentage of interest held as of the balance sheet date (including surplus cost):		
Current assets	4,891	4,643
Non-current assets	3,557	5,130
Assets in the insurance and financial sectors	2,965	2,740
Current liabilities	(4,700)	(4,735)
Long-term liabilities	(1,818)	(2,659)
Liabilities in the insurance and financial sectors	(2,594)	(2,224)
Net assets	2,301	2,895

	Year ended		
	December 31		
	2011	2010	2009
	NIS million		
Group share of results of associates based on percentage of interest held during the period			
Revenues	5,606	4,804	2,578
Net income (loss) *)	(223)	156	91

*) After adjustments for fair value differences

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)**C. Condensed financial information of an associate**

The Group owns 50% of the shares of IDE Technologies Ltd. ("IDE"). The Group's investment in IDE is accounted for using the equity method. The amount included in the statement of income in 2010 for the Group's investment in IDE is more than 10% of the net profit and it is expected that the profit for the Group's investment in IDE will exceed 10% of the net profit in 2012. Accordingly, the Company included condensed information about IDE for each reporting period (USD millions):

	December 31	
	2011	2010
	USD millions	
Current assets	303	183
Non-current assets	536	395
Current liabilities	151	100
Non-current liabilities	468	302
Holders of non-controlling interests	16	-
Equity attributable to equity holders of the parent	204	176

	December 31		
	2011	2010	2009
	USD millions		
Revenues	353	195	377
Gross profit	82	53	96
Operating income	50	26	68
Finance income, net	9	14	12
Net income attributable to equity holders of the parent	40	32	71

At December 31, 2011, the balance of goodwill attributable to the investment in IDE is NIS 46 million.

For the deferred tax liability for the investment in IDE, see Note 42(E).

D. Investments in shares listed for trading on the TASE:

	December 31, 2011		December 31, 2010	
	Carrying amount	Market value	Carrying amount	Market value
	NIS million			
Subsidiaries (1)	10,657	19,845	5,479	15,978
Partnerships and associates (2)	1,081	846	2,253	6,743

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)**1. Composition of the investment in shares of subsidiaries listed for trading on the TASE**

	December 31, 2011		December 31, 2010	
	Carrying amount	Market value	Carrying amount	Market value
	NIS million			
Delek US Holdings Inc.	1,646	1,732	1,086	1,027
The Phoenix Holdings Ltd.	1,876	1,391	1,964	1,731
Delek - The Israel Fuel Corporation Ltd.	936	560	810	1,180
Delek Drilling – Limited Partnership	711	4,529	491	5,476
Delek Energy Systems Ltd.	114	6,777	(52)	5,594
Avner Oil Exploration - Limited Partnership *)	4,054	4,054	-	-
Cohen Development and Industrial Buildings Ltd. *)	283	198	-	-
Gadot Biochemical Industries Ltd. **)	-	-	119	79
Excellence Investments Ltd.	1,037	604	1,061	891
	<u>10,657</u>	<u>19,845</u>	<u>5,479</u>	<u>15,978</u>

*) On December 28, 2011, the Company acquired the investment in Cohen Development and Industrial Buildings Ltd. As a result, and in view of the acquisition of and control in the general partner Avner Oil Exploration – Limited Partnership, the investment in the partnership was consolidated for the first time (see also Note section M(6) below).

**) As from August 2011, the shares of Gadot Biochemical Industries Ltd. are no longer listed on the TASE.

2. Composition of the investment in associates listed for trading on the TASE

	December 31, 2011		December 31, 2010	
	Carrying amount	Market value	Carrying amount	Market value
	NIS million			
Avner Oil Exploration - Limited Partnership *)	-	-	828	5,000
Delek Automotive Systems Ltd.	970	691	1,316	1,551
Mehadrin Ltd.	168	151	177	172
Delek Real Estate Ltd.	(57)	4	(68)	20
	<u>1,081</u>	<u>846</u>	<u>2,253</u>	<u>6,743</u>

*) At December 31, 2011, the investment in Avner Partnership was consolidated for the first time. For further information, see also section M(6) below)

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)**E. Additional information about an associate held directly by the Company**

	<u>Country of incorporation</u>	<u>Company's interest in equity and voting rights %</u>	<u>Amounts provided by the Company to an associate</u>		<u>Balance of investment in an associate and loans provided</u>
			<u>Loans</u>	<u>Guarantees NIS million</u>	
2011					
Delek Real Estate Ltd. **)	Israel	4.99%	239	60	21
	<u>Country of incorporation</u>	<u>Company's interest in equity and voting rights %</u>	<u>Amounts provided by the Company to an associate</u>		<u>Balance of investment in an associate and loans provided</u>
			<u>Loans</u>	<u>Guarantees NIS million</u>	
2010					
Delek Real Estate Ltd. *)	Israel	4.99%	361	58	271

*) See section G below

F. Subsidiaries**1. Additional information about subsidiaries held directly by the Company**

	<u>Country of incorporation</u>	<u>Company's interest in equity and voting rights %</u>	<u>Amounts provided by the Company to a subsidiary</u>		<u>Investment in a subsidiary (accounted for according to the equity method)</u>
			<u>Loans and capital notes</u>	<u>Guarantees NIS million</u>	
2011					
Delek Investments and Properties Ltd. *)	Israel	100	2,949	8	6,073
Delek Sea Maagan 2011 Ltd.	Israel	100	51	-	-
Delek Petroleum Ltd.	Israel	100	2,239	-	1,992
			<u>5,239</u>	<u>8</u>	<u>8,065</u>
2010					
Delek Investments and Properties Ltd.	Israel	100	3,561	12	3,526
Delek Petroleum Ltd.	Israel	100	1,384	-	1,311
			<u>4,945</u>	<u>12</u>	<u>4,837</u>

*) In February 2012, a merger of Delek Investments and Properties Ltd. and the Company was approved, pursuant to section 103 of the Income Tax Ordinance. According to the approval, all the operations of Delek Investments and Properties Ltd. will be transferred to the Company.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

2. Dividends from subsidiaries

In 2011, Delek Investments distributed a dividend of NIS 350 million (in 2010, NIS 300 million).

Dividends received at headquarter companies from their investees:

Investee	Year ended December 31		
	2011	2010	2009
	NIS million		
Delek Automotive Systems Ltd.	74	245	92
Delek US Holdings Inc.	49	21	22
Delek - The Israel Fuel Corporation Ltd.	8	21	21
The Phoenix Holdings Ltd.	28	-	-
Delek Drilling – Limited Partnership	-	-	2
Avner Oil Exploration - Limited Partnership	-	-	4
Republic Companies Inc.	15	36	-
IDE Technologies Ltd.	18	20	-
	192	343	141

Principal changes in investees

G. Investment in Delek Real Estate Ltd.

- In October 2008, the Company's board of directors resolved to distribute all or most of its shares in Delek Real Estate Ltd. ("Delek Real Estate") to the Company's shareholders, subject to receiving the required approvals by virtue of the obligations and covenants of the Company and Delek Real Estate towards third parties.

On March 31, 2009, after receiving these approvals, the board of directors resolved to distribute most of Delek Real Estate shares held by the Company as a dividend to the equity holders of the parent. The record date was April 20, 2009 and the distribution date was May 3, 2009. After the distribution, the Group owns approximately 5% of Delek Real Estate's issued and paid up share capital. Accordingly, the Company no longer consolidates the operations of Delek Real Estate in its financial statements and includes them in accordance with the equity method.

The results of Delek Real Estate operations up to the date of distribution are presented separately in the statement of income under profit (loss) from discontinued operations.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

The table below presents information on the results of operations attributable to the discontinued operations.

	Year ended December 31 2009 *)
	NIS million
Revenues	406
Cost of revenues	118
Gross profit	288
Appreciation of investment property, net	3
Selling and marketing expenses	2
General and administrative expenses	45
Other revenue, net	2
Operating income	246
Finance income	54
Finance expenses	251
	49
Group's share in earnings of associates and partnerships, net	3
Profit before income tax	52
Taxes on income	35
Net income	17

*) The information relates to the operating results of Delek Real Estate up to the date of deconsolidation.

The table below presents information on the comprehensive income attributable to discontinued operations.

	Year ended December 31 2009 *)
	NIS million
Gain for available-for-sale financial assets	1
Loss from cash flow hedges	(63)
Adjustments for translation of financial statements of foreign operations	268
Company's share of other comprehensive loss of associates	(8)
Other comprehensive income from discontinued operations	198

*) The information relates to the operating results of Delek Real Estate up to the date of deconsolidation.

The statement of income and the statement of comprehensive income, the data for discontinued operations and other comprehensive income from discontinued operations for 2009 include also data for Delek Automotive Systems Ltd. which was presented as a discontinued operation in those years. See also section C below.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

Following the distribution of Delek Real Estate shares, the equity of the Group attributed to equity holders of the parent was reduced by the amount of the investment distributed, including the related tax effects (the total amount is NIS 171 million).

In connection with the distribution of the shares of Delek Real Estate as a dividend in kind, the Company entered into an agreement with a bank, according to which, among others, the bank cancelled the lien on the shares of Delek Real Estate. In addition, the Company undertook that when Delek Real Estate repays any part of the loans provided by the Company to Delek Real Estate for Roadchef (principal of NIS 280 million), the Company will acquire from the bank, in an amount equal to the repayment part of the rights in the debt that Delek Real Estate owed the bank, up to a total of NIS 150 million. The bank will sell the debt to the Company without transferring any of the rights of the bank to the collateral that was or will be provided in its favor to secure the debt. The Company is entitled to record a lien on all the assets securing the debt, subject to a number of conditions. To guarantee the liabilities of the Company towards the bank, the Company assigned, by way of a first lien in favor of the bank, all its rights in accordance with the loan agreements of Delek Real Estate for Roadchef.

In January 2012, in accordance with these liabilities and view of the acquisition of 75% of Roadchef shares (see section L below), the Company acquired Delek Real Estate's debt to the bank of NIS 150 million. The loan bears interest at a rate of prime 0.25% and is repayable in January 2018. The Company received a bank loan of NIS 150 million at the same terms as the acquired debt of Delek Real Estate. According to IAS 39, the acquired loans were initially measured at fair value, taking into account market interest for similar loans. To secure repayment to the Company of Delek Real Estate's loan of NIS 150 million, Delek Real Estate undertook to pledge its rights in the Hof Carmel project as a second ranking lien. In addition, as part of the acquisition of Roadchef shares, the Company provided credit of NIS 75 million to Delek Real Estate. The debt bears annual interest at a rate of 1% above the Company's funding cost. The loan is repayable in January 2018.

At December 31, 2011, the balance of the loans and guarantees provided by the Company and its subsidiaries to Delek Real Estate amounted to NIS 331 million (not including investments in profit-sharing insurance policies and exchange-traded funds through debt instruments of Delek Real Estate).

Delek Real Estate announced the suspension of principal and interest payments to all its creditors (except for principal and interest payments to insured creditors using proceeds from assets pledged to those creditors), therefore interest was not paid to the Company as well. As from the second quarter of 2011, there is a going concern qualification in the financial statements of Delek Real Estate. In view of the financial position of Delek Real Estate and further to its reports, there is significant doubt as to whether Delek Real Estate will be able to meet its liabilities and continue as a going concern.

Under these assumptions, the Company assessed the balance of Delek Real Estate's debt and in the reporting period and recognized an additional provision of NIS 104 million for impairment (including its share in the losses of Delek Real Estate), including the loans of NIS 21 million provided to Delek Real Estate (the balance of the principal and interest amounts to NIS 239 million).

In addition, at the reporting date, Delek Real Estate has a debt for loans provided by The Phoenix and its subsidiaries amounting to NIS 66 million (52% of the debt is from funds from policies guaranteeing insurance yields and 48% of the debt is from nostro funds). According to the repayment dates that were defined, an amount of NIS 45 million (principal and interest) was set for repayment in August 2011. In November 2011, NIS 5 million was paid on account of the debt of Delek Real Estate and The Phoenix. The Phoenix has collateral equal to the balance of the loan principal, therefore no provision was included in the financial statements of The Phoenix.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

Further to the meetings of the Investment Committee, Audit Committee and Board of Directors of The Phoenix, it was decided, subject to approval of the general meeting, to suspend the decision of whether to extend the dates of the payments due by Delek Real Estate in August 2011, until clarifications are received regarding Delek Real Estate and its creditors. Approval of the general meeting was received on September 21, 2011.

2. On December 3, 2009, the Securities Authority searched the offices of Delek Real Estate, in respect of the assets belonging to subsidiaries of Delek Real Estate outside of Israel.

On January 2, 2010, Delek Real Estate reported that, to the best of its knowledge, the matters under investigation by the Securities Authority are in respect of the following:

- Evaluation of the accounting treatment of Delek Real Estate's investments in Hilton and Marriot hotels
- Valuation of a foreign company owning parking lots in the UK, leased to NCP Ltd., as presented in the financial statements of Delek Real Estate in 2007-2009
- Evaluation of the agreement of a foreign subsidiary of Delek Real Estate with a third party in respect of the operation of Roadchef properties

On August 31, 2010, the Securities Authority announced that it had completed the investigation of Delek Real Estate and sent the investigative material to the prosecution, which will decide how to proceed. The Securities Authority also claims that the results of the investigation include suspicions, which refer mainly to classification and valuation of Roadchef in the Company's financial statements and the valuation of a second tier subsidiary of Delek Real Estate that owns parking lots in the UK.

On September 16, 2010, Delek Real Estate received notice from the District Attorney's Office in Tel Aviv (Taxation and Economy) pursuant to section 60(A) of the Criminal Procedure Law [Consolidated Version], 1982, regarding the transfer of the investigative material to the prosecution.

Subsequent to the balance sheet date, on January 25, 2012, Delek Real Estate received notice from the District Attorney in Tel Aviv (Taxation and Economy) that Delek Real Estate will be indicted for the following offenses, subject to a hearing:

- A) Two offenses under section 415 of the Penal Law, 1977 ("the Penal Law") and three offenses under section 53(a)(4) of the Securities Law, 1968 ("the Securities Law"). These offenses refer to Delek Real Estate and two former directors for alleged acts in 2008. In brief, District Attorney claims that the two former officers allegedly acted in contravention of the law and through misrepresentations to change the accounting classification of the holding in Roadchef (see section L below) in the financial statements of Delek Real Estate from property, plant and equipment to investment property in the Company's quarterly statements in the first three quarters of 2008.
- B) An offense under section 415 of the Penal Law and an offense under section 53(a)(2) of the Securities Law. These offenses are attributed to the Company, a former officer in the Company and a former officer in a subsidiary, in respect of their alleged acts in 2009. In brief, District Attorney claims that the two former officers allegedly acted in contravention of the law and through misrepresentations to change the accounting classification of the holding in Roadchef (see section L below) in the financial statements of Delek Real Estate from property, plant and equipment to investment property in the Company's quarterly statements in the first three quarters of 2008.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

According to the District Attorney's notice, before filing an indictment in these matters, Delek Real Estate will have the right to present their position against the allegations. The hearing is set for May, 2012. Delek Real Estate is assessing the notice together with its legal counsel.

The Company's management believes that this will not affect the Company's financial statements. However, Delek Real Estate is unable to estimate the outcome of the hearing and the implications of the outcome of the hearing and indictment, in respect of the previous accounting treatment of these issues.

Up to May 2009, Delek Real Estate was a subsidiary of the Group. As from this date (the date Delek Real Estate shares were distributed as a dividend in kind), the Group owns 5% of the shares of Delek Real Estate, and the investment is accounted for using the equity method. Any investigation of the financial statements of Delek Real Estate could affect the Group's financial statements for the relevant reporting periods.

3. See Note 32(A)(9) below for information about the claim against a controlling shareholder in the Company, the Company and officers in Delek Estate and a motion for certification of a class action.
4. See section L below for information about the acquisition of 75% of the shares in Delek Motorways Services from Delek Real Estate.
5. In May 2010, Delek Real Estate completed a rights issue for the acquisition of 114,698,115 shares for NIS 126 million. The Group exercised the entire quantity of rights that it was offered and acquired Delek Real Estate shares for NIS 6 million. The Group's interests in Delek Real Estate subsequent to the acquisition remained unchanged.
6. In February 2011, Delek Real Estate completed a rights issue for the acquisition of 86,154,310 shares for USD 60 million. The Group exercised the entire quantity of rights that it was offered for NIS 3 million. The Group's interests in Delek Real Estate subsequent to the acquisition remained unchanged (5%).

H. Insurance and finance operations

1. Acquisition of Excellence shares

In April 2006, The Phoenix Investments, a wholly owned subsidiary of the Company ("The Phoenix Investments") completed the acquisition of 40% of Excellence shares for NIS 322.5 million.

Under the agreement, The Phoenix Investments has a call option exercisable from January 1, 2009, and the sellers have a put option exercisable from February 1, 2009 for the sale of an additional 40.88% to The Phoenix Investments. The agreement also sets out adjustments to profit and equity to be included in calculation of the consideration.

The agreement was amended in June 2009 ("the new agreement"). According to the new agreement, The Phoenix Investments will acquire 40.88% of the issued share capital of Excellence, in five lots from 2009 to 2013. The first lot is 20.44% of the issued share capital of Excellence. The second to fifth lots are 5.11% of the issued share capital of Excellence. The total consideration for the shares will be between NIS 620 million and a maximum of NIS 730 million, linked to the CPI for March 2009.

According to the new agreement, up to the reporting date, The Phoenix acquired the first, second and third lots for NIS 342.7 million, NIS 105 million, and NIS 97 million, respectively. The fourth lot is expected to be acquired in April 2012.

The consideration for the fourth and fifth lots will not exceed NIS 90 million, linked to the CPI of March 2009.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

The Phoenix Investments may accelerate the purchase of Excellence shares at any time and the sellers may accelerate the purchase of the shares that are outstanding on the acceleration date, in the circumstances set out in the agreement.

The Company guaranteed all the undertakings of The Phoenix Investments for an unlimited amount, in accordance with the terms of the new agreement.

In 2009 and 2010, The Phoenix Investments completed a number of transactions for the acquisition of Excellence shares, traded on the TASE and in off-floor transactions, for a total consideration of NIS 47.3 million and NIS 28 million, respectively.

At December 31, 2011, The Phoenix owns 78.43% of the issued and paid up share capital of Excellence. The share of The Phoenix in the equity of Excellence, including outstanding shares that can be accelerated, amounts to 88.65%, at the balance sheet date.

The Phoenix Investments carried out periodic impairment assessment of the goodwill attributable to its investment in Excellence at December 31, 2011, the balance of which at this date amounted to NIS 560 million. To assess the recoverability of the goodwill, the recoverable amount of the cash-generating units to which the goodwill was assigned was assessed separately (pension and financial services). The recoverable amount of the provident fund and financial services unit is calculated on the basis of a valuation by an external independent assessor and on the projected representative operating cash flow multiplier method, which is similar to the discounted cash flow method. According to this assessment, the pension unit requires amortization of NIS 118 million for goodwill, mainly due to erosion of management fees. In respect of the financial services unit, based on the valuation, the recoverable amount of the unit exceeds its carrying amount. For further information see Note 20 below.

2. The Phoenix holds 5% of Linchfield Limited ("Linchfield"), which is accounted for according to the equity method due to the other holdings of the controlling shareholder. In the reporting period, Linchfield recognized an impairment loss on investment property. The share of The Phoenix in the loss amounted to NIS 49 million and was recognized in the statement of income under the Group's share in earnings of subsidiaries and associate partnerships, net.
3. In January 2011, the Company acquired an additional 528,438 shares of The Phoenix of NIS 1 par value each on the TASE for NIS 7 million. Subsequent to the acquisition, the Group owns 55.55% of The Phoenix.
4. In April 2011, Barak Capital Ltd. ("Barak Capital"), which is owned 48% by the Group, completed a sale of all of its shares in its associate, Index Teudot Sal Ltd., to DS Apex Holdings Ltd. for NIS 35 million. The estimated pre-tax gain for Barak Capital is NIS 34 million, which is recognized in the statement of income under the Group's share in income of associate companies and partnerships, net (the Group's share in this profit is NIS 16 million).
5. As set out in Note 2(C), the Group eliminates the revaluation to market value of securities of Group companies (shares and debentures), held by SPCs that issue and manage ETFs and which are held for profit-sharing policies in insurance companies. Conversely, these holdings are accounted for in accordance with generally accepted accounting principles for the acquisition (sale) of treasury shares, acquisition (sale) of other shares of subsidiaries and intercompany holdings of debentures.

The effect of the accounting treatment on the net profit for 2011 attributable to equity holders of the parent amounted to a gain of NIS 17 million (in 2010, a loss of NIS 7 million and in 2009, a loss of NIS 25 million).

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

6. In the reporting period, severe weather, including tornadoes, hit some areas in the United States, (mainly in the Southern United States), causing damage in states where the subsidiary Republic Companies Inc. ("Republic") operates, as well as other damage caused by fires (mainly in Texas). The loss incurred by Republic for the weather-related damage amounts to USD 65 million (before the effect of tax and after reinsurance) (in 2010, USD 23 million).
7. For information about the impairment of goodwill arising upon acquisition of Republic, see Note 20(B)(3) below.
8. In 2011, due to the negative returns, The Phoenix did not charge variable management fees for participating policies. At December 31, 2011, the estimated management fees that will not be collected due to the negative returns until positive returns are achieved amounted to NIS 279 million. At the end of February 2011, this amount was NIS 199 million.

I. Fuel operations in the United States

- 1) On November 20, 2008, a fire broke out at Delek US refinery in Tyler, Texas. Two employees died of injuries sustained in the fire. The refinery was shut down to enable a thorough investigation of the circumstances of the event and the extent of the damages. The fire caused damage in two of the refinery's operating units. As well as repairing the damage, it was decided to carry out periodic renovation and work to improve facilities. In May 2009, the refinery restarted operations.

In 2009, Delek US received USD 116 million (NIS 465 million) from the insurance company, including USD 64.1 million (NIS 257 million) for loss of profits and USD 51.9 million (NIS 208 million) for property damage, which was recorded in the financial statements, net of expenditures incurred in the amount of USD 11.6 million (NIS 46 million). Net gain of NIS 419 million was recorded in the statement of income for 2009 in the line item, other income (expenses).

In 2010, Delek US received USD 17 million (NIS 64 million) from the insurance company, including USD 12.8 million (NIS 49 million) for loss of profits and USD 4.2 million (NIS 15 million) for damage to property, which was recorded in the financial statements less costs in the amount of USD 0.2 million (NIS 0.8 million). Net income was recorded in the statement of income under compensation from an insurance company. The receipts in the second quarter of 2010 constitute the completion of the accounting with the insurance company for damages caused by the fire. In 2009-2010, the receipts from the insurance company amounted to USD 141.4 million (NIS 562 million).

- 2) On April 29, 2011, Delek US completed the acquisition of 53.7% of the share capital of Lion. Following the transaction, Delek US owns 88.3% of the share capital of Lion.

Delek US acquired the sellers interests in Lion according to the following outline:

- 1) The sellers received a cash payment of USD 80.2 million (after working capital adjustments)
- 2) Delek US issued 3,292,844 of its shares, valued at USD 44.3 million, to the sellers (the number of shares was based on the average closing price of Delek US shares for the ten trading days preceding the completion date of the transaction).
- 3) Lion issued a USD 50 million note payable to the sellers and guaranteed by Delek US. The note bears annual interest at a rate of 4% (paid quarterly) and is payable in five equal annual payments of the principal as from the end of the second year after its issue.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

- 4) Lion transferred its interests in an oil pipeline (valued at USD 50 million) and its entire asphalt inventory against repayment of Lion's debt to the sellers.

In addition, Delek US participated in the refinancing of Lion's net working capital, which was previously partially financed by the sellers.

The acquisition was partially financed by an owners loan of USD 40 million provided by Delek Petroleum Ltd. (a wholly-owned subsidiary of the Company, hereinafter: "Delek Petroleum") to Delek US. The loan principal will be repaid in six equal payments of USD 6 million each, on June 30th of each year from 2012 through 2017 and a final payment of USD 4 million on December 31, 2017. The loan principal bears annual interest at a rate of 7.25%, which will be paid in quarterly installments.

Subsequent to the issue of these shares, Delek Petroleum's holding in Delek US decreased from 72.4% to 68.3%. Consequently, in the second quarter of 2011, the Group recognized an increase of NIS 41 million in reserves from transactions with non-controlling interests.

According to IFRS 3 (revised) regarding acquisition of control in stages, Delek US accounted for its previous investment in Lion (which was previously accounted for as an available-for-sale financial asset) as if disposed of at the date control was established, while Delek US acquired 88.3% of the shares in Lion at fair value. As a result, Delek US recognized a gain of USD 12.9 (approximately NIS 44 million).

Delek US temporarily attributed the consideration for acquisition of the assets and liabilities of Lion at the acquisition date as follows:

	USD millions	NIS million
Current assets	244	829
Property, plant and equipment	312	1,058
Long term loans and debit balances	5	17
Other intangible assets	11	38
Current liabilities	(251)	(854)
Note payable to the sellers	(50)	(170)
Other long-term liabilities	(30)	(100)
	241	818
Holders of non-controlling interests	(25)	(86)
	216	732

The acquisition cost includes:

	USD millions
Cash paid	80
Shares issued to sellers	44
*) Contingent consideration	7
Value of prior investment in Lion	85
	216

- *) The fair value of the contingent consideration is based on payments to the sellers for future sales of asphalt inventory.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

As from the acquisition date, Delek US fully consolidates the financial statements of Lion. Lion's revenues and costs for the period from the acquisition date through to December 31, 2011 are as follows:

	From the acquisition date through to December 31, 2011	
	Unaudited	
	USD millions	NIS million
Revenues	2,090	7,492
Cost of revenues	1,996	7,155
Other costs (including financing)	79	284
Net income	15	53

In October 2011, Delek US acquired the remaining shares from holders of non-controlling interests for USD 13 million, paid in cash.

As a result, Delek US recognized an increase of USD 17 million (approximately NIS 62 million) in equity in capital reserve from transactions with holders of non-controlling interests (the Group's share is NIS 42 million).

In December 2011, Delek US acquired 100% of the participating units of Paline Pipeline Company, which owns and operates a crude oil pipeline in the United States. The consideration for the acquisition amounted to USD 50 million, which will be repaid over three years. Of this, an amount of USD 25 million was paid in cash and the balance is a loan from the seller, repayable over three years.

J. Fuel operations in Europe

On October 1, 2010, Delek Europe BV, owned 80% by the Delek Petroleum and 20% by Delek Israel ("DEBV") finalized a transaction to acquire the fuel marketing operations of BP France SA ("BP") in France, including 410 gas stations, 300 convenience stores and interests in three terminals. Ownership of the assets was transferred to a subsidiary.

The consideration for the transaction was set at EUR 170 million before working capital adjustments. The acquisition agreement included a mechanism for working capital adjustment to the acquisition cost. According to BP, working capital adjustments at the time of the transaction amounted to EUR 60 million and the compensation that was transferred amounted to EUR 230 million. In March 2011, an agreement between DEBV and BP stipulated that working capital adjustments will be reduced to EUR 39 million, reflecting a total consideration of EUR 209 million for the transaction (BP received EUR 21 million in April 2011).

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

In the third quarter of 2011, DEBV completed the final attribution of the acquisition consideration. The temporary purchase price allocation of excess acquisition cost is as follows:

	Temporary attribution	Final attribution
	EUR million	
Current assets	81	81
Property, plant and equipment	134	134
Investment in investees and long-term receivables	9	11
Customer relations (amortized over 10 years)	26	23
Goodwill	37	31
Current liabilities	(47)	(47)
Non-current liabilities	(31)	(24)
	<u>209</u>	<u>209</u>

K. Fuel in Israel

1. In June 2009, Delek Petroleum sold 6.51% of Delek Israel shares for NIS 95 million. As a result, the Group's holdings in Delek Israel declined to 79.17%. The gain on this sale amounted to NIS 31 million (before income taxes).
2. In July 2011, Delek Petroleum issued a full tender offer for all the outstanding shares of Delek Israel for NIS 101 per share.

On August 4, 2011, Delek Petroleum announced the results of the tender offer, which was only partially accepted. According to the results, Delek Petroleum acquired 1,099,699 ordinary shares of Delek Israel from offerers that submitted notices of acceptance, representing 9.69% of the issued and paid up share capital and voting rights of Delek Israel. Subsequent to the acquisition, Delek Petroleum owns 9,861,473 ordinary shares representing 86.90% of the issued and paid up share capital and the voting rights in Delek Israel. The consideration for the acquisition amounted to NIS 111 million. As a result of the acquisition, in 2011, Delek Petroleum recorded a decrease of NIS 7 million in capital under capital reserve from transactions with non-controlling interests.

3. On August 31, 2011, the Ministry of Energy and Water published the Order for Supervision of Prices of Goods and Services (Maximum Prices at Gas Stations) (Amendment), 2011, signed by the Minister of Energy and Water and the Minister of Finance ("the 2011 Supervision Order"). According to the 2011 Supervision Order, as from September 1, 2011, the marketing margin for self-service 95 octane gasoline will be NIS 589 per thousand liters and the extra fee for full service will be NIS 173 per thousand liters.

The total reduction in the marketing margin and ORL gate price according to the 2011 Supervision Order is NIS 162 per thousand liters.

The 2011 Supervision Order includes changes in the method for adjusting an item in the marketing margin and the extra fee for full service.

On September 19, 2011, the Supreme Court sitting as the High Court of Justice heard the petition of Delek Israel and other fuel companies and ruled that the marketing margin should be reviewed, mainly to allow Delek Israel and the other fuel companies to submit the updated information that was presented at the hearing. The schedule for implementing the High Court ruling is as follows:

Within one week from the date of the hearing, the Fuel Administration will issue new requirements for updated information.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

Within two weeks from receiving the requirements of the Fuel Administration, Delek Israel and the other fuel companies involved in the petition will submit updated information and an oral hearing will be held on this basis.

Within three months from the date of the oral hearing, a new decision will be made regarding the marketing margin and the State will notify the High Court of Justice of the new decision within one week of making the decision. Delek Israel and the other fuel companies may respond within one more week.

In this context, it is noted that the petition of Delek Israel and the other fuel companies to receive a temporary injunction against the Order for Supervision of Prices of Goods and Services (Maximum Prices at Gas Stations), 2002 ("the Supervision Order") was dismissed and the Supervision Order remains in effect until otherwise ruled.

The reduction of the marketing margin (if there is no change in view of the petition by Delek Israel and the fuel companies), may have a material adverse effect on the business of Delek Israel and its operating results. It is noted that the extent of the effect depends on the steps that Delek Israel takes to mitigate the financial effect of the reduction of the marketing margin.

4. See also Note 17(A) for further information about assessment of impairment of fuel property, plant and equipment by Delek Israel.

L. Delek Motorway Services UK

At December 31, 2010, the Group held 25% of the share capital of Delek Motorway Services UK ("DMS") through Delek Petroleum. The balance of the shares of DMS was held indirectly by Delek Real Estate (a company owned and controlled by the controlling shareholder of the Company). DMS holds the entire share capital of a UK company (MSA), which owns Roadchef Ltd. DMS holds the entire share capital of a UK company (MSA), which owns Roadchef Ltd. Roadchef owns 19 service stations in the UK, operating under the Roadchef brand (the group of companies is referred to hereunder as Roadchef).

In November 2008, Delek Petroleum and Delek Real Estate decided to dispose of their investment in Roadchef. Therefore, as from that date, the investment in Roadchef is presented as a held for sale asset.

In 2009, and up to February 2010, selling activities were undertaken during which potential buyers evaluated the investment and offers to purchase the investment were received. In 2009, based, among others, on the offers received during the selling process and based on the impairment of assets included in the financial statements of Roadchef, the Group reduced its investment in Roadchef by NIS 74 million, which was included in other income (expenses), net.

Further to the aforesaid, in February 2010, due to the stagnation in negotiations with a potential buyer, the managements of Delek Real Estate and Delek Petroleum concluded that there is a significantly lower likelihood of selling the asset at the asking price and that a sale under the requested terms is no longer highly probable. Therefore, and in accordance with IAS 28 – Investments in Associates, as from the first quarter of 2010, the investment in Roadchef was accounted for retrospectively according to the equity method.

As a result of the aforesaid, the investment in Roadchef at December 31, 2009 was reclassified from available-for-sale assets to investments in companies and investees, and other expenses of NIS 75 million in 2009 was reclassified from other income (expenses) to finance income and to the Company's share in the profits of partnerships and investees, net. The effect of the aforesaid on the Group's capital reserve as a result is not significant.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

On November 24, 2010, and further to the negotiations between the Company and Delek Real Estate Ltd., the audit committee and board of directors of the Company approved an agreement to purchase the interests (75%) of Delek Belron International Ltd. ("Delek Belron"), a wholly owned subsidiary of Delek Real Estate, in companies owning Roadchef.

On January 10, 2011, the general meeting of the Company and Delek Real Estate approved the transaction. On January 19, 2011, the board of directors of Delek Petroleum approved the transfer of ownership in Roadchef from Delek Belron to Delek Petroleum, instead of the Company. The transaction was completed on January 24, 2011.

The transaction is in NIS, equivalent to GBP 86.25 million (NIS 497 million) at the closing date of the transaction, reflecting a value of GBP 115 million for Roadchef (NIS 663 million). The Company paid Delek Petroleum the consideration by offsetting Delek Real Estate's debt to the Company of NIS 394 million and a cash payment of NIS 104 million.

Although this is a business combination under common control as the transaction has an economic nature from the aspect of Delek Petroleum, the transaction is accounted for as a business combination achieved in stages according to the acquisition method established in the revised IFRS 3. Accordingly, and based on the notional approach in the revised IFRS 3, Delek Petroleum remeasured its previously-held investment in Roadchef as if disposed of at the date control was established, while Delek Petroleum acquired 100% of the shares in Roadchef at fair value.

As a result, equity attributable to the Company's shareholders increased by NIS 22 million and the profit from the notional disposal of the prior investment in Roadchef, considering the sale of capital reserves deferred to other comprehensive income in the past, amounted to insignificant sums.

Delek Petroleum attributed the acquisition consideration for the assets and liabilities of Roadchef at the acquisition date as follows:

	GBP millions	NIS million
Current assets	12	68
Property, plant and equipment	60	347
Goodwill	142	822
Agreements (amortized on a straight-line basis over 19-22 years)	47	271
Licenses and user rights (amortized on a straight-line basis over 21-138 years)	76	438
Current liabilities	(41)	(235)
Debentures	(155)	(891)
Long-term loans from banks	(5)	(29)
Other long-term liabilities	(5)	(29)
Deferred tax reserve	(16)	(99)
	<u>115</u>	<u>663</u>

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

As from the acquisition date, Delek Petroleum fully consolidates the financial statements of Roadchef. Roadchef's revenues and costs for the period from the acquisition date through to December 31, 2011 are as follows:

	From the acquisition date through to December 31, 2011	
	Unaudited	
	GBP millions	NIS millions
Revenues	202	1,157
Cost of revenues	(190)	(1,087)
Other costs (including financing)	(16)	(93)
Net income (loss)	(4)	(23)

See section G below for information about the Israel Securities Authority's investigation of the assets belonging to Delek Real Estate's foreign subsidiaries, including the operation of Roadchef's assets.

Subsequent to the transaction, Delek Petroleum owns 100% of the share capital of Roadchef.

M. Oil and gas exploration and production

1. In June 2010, Delek Investments sold 31,696 of the shares of Delek Energy Systems Ltd. ("DES") shares for NIS 33 million. The difference between the consideration received and the increase in non-controlling interests amounted to NIS 32 million (before income tax) and was included in the consolidated statements of changes in equity under exercise and issue of shares to non-controlling interests. At December 31, 2010, Delek Investments held 78.9% of the share capital of DES.

In 2011, the Group acquired 47,560 additional shares in DES on the TASE for NIS 65 million, representing 0.94% of the equity of DES. The difference between the consideration paid and the value of the acquired equity amounted to NIS 64 million and was recognized directly in capital reserve from transactions with non-controlling interests. Subsequent to the acquisition, the Company and Delek Investments and Properties Ltd. (a subsidiary wholly-owned by the Company, hereinafter: "Delek Investments") hold 79.87% of the equity of DES.

2. In 2010, DES and Delek Investments acquired on the TASE 7,592,482 participating units in Delek Drilling for NIS 87 million. The difference between the consideration paid and the value of the acquired equity amounted to NIS 78 million and was recognized directly in capital reserve from transactions with non-controlling interests. On December 31, 2010, the holdings of DES and Delek Investments in Delek Drilling amounted to 62.73% and 7.78%, respectively.

In 2011, the Group acquired 6,748,486 additional participating units in Delek Drilling on the TASE for NIS 89 million, representing 1.23% of the equity of Delek Drilling. The difference between the consideration paid and the value of the acquired equity amounted to NIS 81 million and was recognized directly in capital reserve from transactions with holders of non-controlling interests. Subsequent to the acquisition, the Company and Delek Investments owned 9.02% of the equity of Delek Drilling (in addition to 62.7% of the equity of Delek Drilling owned by DES).

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

3. In 2010, DES and Delek Investments acquired an additional 50,237,819 participating units in Avner on the TASE for NIS 94 million. At December 31, 2010, the holdings of DES and Delek Investments in Avner amounted to 47.42% and 13.71%, respectively. The excess cost arising from the acquisitions were attributed to oil and gas assets.

In 2011, the Group acquired 24,487,075 additional participating units in Avner on the TASE for NIS 59 million, representing 0.73% of the equity of Avner. Subsequent to this acquisition, the Company and Delek Investments owned together 14.44% of the partnership's equity. The excess cost of acquisition over the fair value amounted to NIS 53 million, attributable to investments in oil and gas exploration and production.

4. On August 2, 2011, the Group issued a shelf offering memorandum by way of a full exchange tender offer and specifications for a tender offer, (which was updated on August 25, 2011) to acquire 1,009,910 ordinary shares of NIS 1 par value each of DES ("the tender offer"). According to the tender offer, the Group offered to acquire the offered shares from the offerors for 1,009,910 units each comprising (a) 36 participating units of NIS 1 par value in Delek Drilling and (b) 472 participating units of NIS 0.01 par value in Avner. On September 11, 2011, a notice of acceptance was submitted, according to which the Group acquired 353,988 shares of DES for 12,743,568 participating units of NIS 1 par value in Delek Drilling and 167,082,336 participating units of NIS 0.01 par value in Avner. Subsequent to the acquisition, the Company and Delek Investments held 86.92%, 6.7% and 9.4% in DES, Delek Drilling and Avner, respectively (in addition, DES held 62.73% in Delek Drilling and 47.48% in Avner).

Additionally, in October 2011, the Company acquired 23,275 shares of DES for 837,900 participating units of NIS 1 par value each in Delek Drilling and 10,869,425 participating units of NIS 0.01 par value each in Avner.

Following the decrease in the effective holding in Avner, in the reporting period, the Group recorded a gain of NIS 67 million (before the effect of tax) (representing the difference between the quoted price prior to the acceptance date and the carrying amount of the exercised participating units of Avner, after elimination of the relative share in the gain attributable to the Group's remaining indirect holding in Avner). The gain was recognized in gain (loss) from the disposal of investments in investees, net.

In addition, in the reporting year, the Group recognized NIS 164 million against capital reserve (credit) for transactions with controlling shareholders following acquisition of Delek Energy shares and an indirect increase in the holdings in DES.

Subsequently, the Group and Delek Investments hold 87.4%, 6.533% and 9.107% in DES, Delek Drilling and Avner, respectively (in addition, DES holds 62.7% in Delek Drilling and 46.6% in Avner).

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

5. On October 18, 2011, DES signed an agreement with the former CEO of DES ("the CEO"), after receiving the approval of the audit committee and board of directors of DES. The agreement sets out terms for termination of the CEO's employment at DES (as from this date, the CEO serves in his position as senior officer in the Group) and for exercise of his options ("the agreement"). The CEO will continue to serve as chairman of the subsidiary Delek Drilling Management (1993) Ltd. and as CEO of Avner Oil and Gas Ltd.

The main points of the agreement between DES and the CEO are as follows:

The CEO held 184,475 options exercisable for DES shares by the earlier of June 1, 2014 or 120 days from termination of his employment ("the CEO's options" and "the options agreement", respectively). The following terms were determined:

- A) 55,343 of the CEO's options will be exercised in a cashless exercise, according to which the CEO is entitled to a cash payment of NIS 53.528 million (before tax) from DES, reflecting the benefit component in the options at the quoted price of DES shares at the end of trading on October 18, 2011, meaning NIS 1,323 per share. In November 2011, DES paid the consideration for these options to the CEO in cash.
- B) 55,342 of the CEO's options will be exercised in a cashless exercise, according to which he is entitled to 39,488 DES shares, reflecting the benefit component in the options at the quoted price of DES shares at the end of trading on October 18, 2011, meaning NIS 1,323 per share. In November 2011, these shares were issued in the name of the trustee for the CEO (after exercising the options for DES shares, the Group holds 86.7% of the share capital of DES).
- C) The expiry date for 73,790 of the CEO options will be changed and the options will be exercisable for DES shares by November 1, 2012. In view of the agreement signed with the CEO, another 73,790 options to which the CEO was entitled were forfeited and as a result, income of NIS 6 million was recognized in the statement of income under general and administrative expenses.

The CEO will be entitled to sell to DES all or part of the DES shares that he exercised ("the put option") for the average price of DES shares on the TASE during the 30 days preceding the notification date of the sale of shares to DES, provided notification of exercise is given prior to November 1, 2012. The option agreement and/or the aforesaid does not prevent and/or restrict the CEO in any way from selling his DES shares to any third party. According to the valuation received by DES for the put options, based on the Black and Scholes model and the share price at the balance sheet date, the Group included a liability of NIS 150 million for the right to acquire the shares and recognized NIS 123 million from transactions with non-controlling interests in capital reserve (credit) (before the effect of tax).

For revaluation of the put option, the Group recognized general and administrative expenses of NIS 22 million.

For the derivative suit filed against DES, the former CEO and seven directors in DES, see Note 32(A)(9).

6. On December 28, 2011, the Company completed the acquisition of 51.76% of the share capital of Cohen Development and Industrial Buildings Ltd. ("Cohen Development"), which engages, inter alia, in oil and gas exploration and production, for NIS 274 million. The oil and gas exploration and development operations of Cohen Development are carried out through a jointly-owned company held by Cohen Development at a rate of 50%, Avner Oil and Gas Ltd. ("Avner"), which is the general partner in the limited partnership Avner Oil Exploration ("the Avner Partnership") and the balance is held by DES.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

Cohen Development is entitled to royalties from the Avner Partnership at the rate set out below, from each share of the partnership in the oil, gas or any other materials of value produced and used from the oil assets in which the partnership has or will have an interest. Overriding royalties to Cohen Development are at a rate of 2.75% of the Noa and Ashkelon leases and 2.875% of the other leases and licenses held by the Avner Partnership and other oil assets in which the Avner Partnership will have rights in the future.

The sellers also have a call option to buy participating units in Delek Drilling and Avner partnerships from the Company (according to a mix to be decided by the Company) in a quantity reflecting a total value of NIS 150 million (to calculate the price of the units, a formula has been determined which includes the weighted average of the rates of the participating units on the date the agreement is signed and the transaction completed). The option is granted in two lots: the first lot (a quantity reflecting a value of NIS 75 million) is given for up to 6 months from the date of completion, and the second lot (a quantity reflecting a value of NIS 75 million) is given for up to 12 months from the date of completion. The Company included a liability of NIS 14 million for the option in its financial statements at fair value.

A consideration of NIS 274 million was paid on the date of completion and the sellers provided the Company with loans of NIS 75 million, without linkage and interest. The loans were included in the financial statements at fair value in the amount of NIS 70 million and are recognized under credit from banks and others.

The loans will be repaid to the sellers as follows:

- NIS 37.5 million will be paid when the first lot is exercised.
- The remaining NIS 37.5 million will be paid when the second lot is exercised.

A formula has been determined to set off the consideration at the exercise prices and interest. As collateral for the payments of the loans, the Group pledged participating units of Delek Drilling with a value of NIS 112.5 million in favor of the sellers. The pledge will be adjusted from time to time, such that the value of the pledged units on the assessment date and according to the price of the relevant participating units on the TASE at that date will be equal to 150% of the balance of the unpaid consideration.

Taking into account the fair value of the option and the loan as aforesaid, the total consideration for acquisition of control in Cohen Development amounted to NIS 283 million.

Following the transaction for acquisition of control in Cohen Development, the Company became the controlling shareholder in Avner (by virtue of the holdings of DES in Avner and the holdings of Cohen Development in Avner). Achieving control in the general partner gives the Company the ability to manage and control the Avner Partnership. It is noted that immediately prior to completing the transaction, the Group held (in concatenation) 50.3% of the participating units of the Avner Partnership and accounted for this investment in its financial statements by the equity method, due to the joint control in Avner immediately prior to the transaction. As a result of achieving control for the first time in Avner and therefore indirectly also in Avner Partnership, the Company consolidated the financial statements of the Avner Partnership as from the completion date, instead of presenting it by the equity method. In view of the acquisition of control in Cohen Development, and indirect acquisition of control in Avner Partnership, the Company recognized, according to IFRS 3 (Revised) regarding acquisition of control in stages, a gain of NIS 3.683 billion, of which an amount of NIS 3.283 million is attributable to the equity holders of the parent, arising from revaluation of the previous investment in Avner Partnership at fair value, based on the TASE price of Avner Partnership when the transaction was completed, and which was included in the statement of income for 2011 under gain (loss) from disposal of investments in a partnership and investees, net.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

In addition, the Company employed an independent assessor to allocate the acquisition cost (which also includes the fair value of the holding in the participation units of Avner at the date of acquisition of control) to the identifiable assets and liabilities of Avner Partnership and Cohen Development. The surplus fair value of the carrying amount was NIS 8 billion (including the share attributable to holders of non-controlling interests) and is mainly attributable, temporarily, to oil and gas assets and production, without attribution of the deferred tax reserve for the surplus cost. The Company will amortize this surplus cost over the period, as determined in the allocation, in view of the expected production period of the reservoirs, thereby reducing its part in the future operating results of Avner Partnership and Cohen Development

N. Automotive operations

- On September 15, 2010, an agreement was signed between Delek Investments and a company controlled by Gil Agmon, who serves as CEO of Delek Automotive Systems Ltd. ("Delek Automotive") and who is a shareholder in the company. According to the agreement, Delek Investments will sell to Gil Agmon 22% of the share capital of Delek Automotive that it owns, for NIS 1 billion. Finalization of the transaction was subject to the following: preconditions: Approval from the manufacturers of Mazda and Ford cars to transfer control in Delek Automotive to Gil Agmon and approval from the banks. Prior to finalization of the transaction, Delek Investments owned 55% of the share capital of Delek Automotive.

Gil Agmon undertook (unilaterally) towards the Group that as long as Delek Investments maintains more than 20% of the share capital of Delek Automotive, he will act to appoint two directors recommended by the Group and as long as Delek Investments owns more than 15%, he will act to appoint one director recommended by the Group. Pursuant to the Articles of Incorporation of Delek Automotive, up to ten directors can be appointed at Delek Automotive (including independent directors).

The transaction was completed on October 20, 2010. After finalization of the transaction, Gil Agmon owns 38% of the share capital of Delek Automotive and the Group owns 33% of the share capital of Delek Automotive. As from this date, the Group is no longer the exclusive controlling shareholder of Delek Investments, therefore the Group no longer consolidates Delek Automotive in its financial statements. Pursuant to IAS 27 (revised), Consolidated and Separate Financial Statements, the Group recognized the remaining investment in Delek Automotive at fair value at the date of loss of control and as from this date, the balance of the investment in Delek Automotive is accounted for on an equity basis. The profit generated for the Group from the sale of the shares and revaluation of the remaining shares to their market value as set out above, amounted to NIS 2 billion (before income tax). Of this amount, NIS 1.1 billion is attributable to revaluation of the outstanding shares and will be recognized in assets and liabilities of Delek Automotive as follows:

	NIS million	Amortization period (years)
Inventory	27	0.3
Property, plant and equipment	33	45
Concession	679	30
Goodwill	549	
Deferred taxes	(139)	According to the relevant assets and liabilities
Share-based payment	(14)	
	<u>1,135</u>	

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

Following the sale of Delek Automotive shares, as described above, the results of Delek Automotive up to the date of the sale (including the gain generated for the Company from the sale of shares and revaluation of the remaining investment) were presented separately in the statement of income under profit from discontinued operations, with reclassification of comparative figures.

The table below presents information on the results of operations attributable to the discontinued operations.

	Year ended December 31	
	2010 *)	2009
	NIS million	
Revenues	3,363	4,744
Cost of revenues	2,865	4,218
Gross profit	498	526
Selling and marketing expenses	30	41
General and administrative expenses	22	28
Other revenue	-	-
Operating income	446	457
Finance income	50	125
Finance expenses	79	16
Profit before income tax	417	566
Taxes on income	102	132
Net income	315	434
Gain from disposal of an investment, net	1,824	-
	2,139	434
Attributable to:		
Equity holders of the parent	1,995	250
Non-controlling interests	144	184
	2,139	434

*) The information for 2010 relates to the operating results of Delek Automotive up to the date of deconsolidation.

The amounts of other comprehensive income and capital reserves for discontinued operations are insignificant.

The statement of income and the statement of comprehensive income, the data for discontinued operations and other comprehensive income from discontinued operations for 2009 include also data for Delek Real Estate, which was presented as a discontinued operation in those years. See also Note 14G(1).

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

2. On December 13, 2011, Delek Motors Ltd. (a wholly-owned subsidiary of Delek Automotive, hereinafter: "Delek Motors") completed the acquisition of Kamor Motors Ltd. ("Kamor") for a total consideration of NIS 235 million. The excess cost on acquisition is mainly attributed to franchise and goodwill.

Kamor Motors imports and sells BMW cars, four-wheel drives, motorcycles, accessories and spare parts in Israel.

3. In view of indications of impairment of the Group's investment in Delek Automotive, the Company received a valuation of NIS 970 million for the recoverable amount from an independent assessor, estimating the value in use of the Group's investment in Delek Automotive at December 31, 2011 (based on discounting the cash flow, at a discount rate of 11%, assuming that the representative cash flow applicable from the sixth year will increase by 3% per year) In view of the difference between the value of the investment in Delek Automotive in the Group's financial statements and its recoverable amount, the Group included a provision of NIS 250 million in its financial statements for impairment of its investment in Delek Automotive, which was recognized in the Group's share in gains (losses) of companies and partnerships accounted for at equity.

O. Gadot Biochemical Industries Ltd.

1. In April 2010, Gadot Biochemical Industries Ltd. ("Gadot") completed a rights issue for the acquisition of 3,971,226 shares for USD 10 million (approximately NIS 40 million). The Group exercised the entire quantity of rights that it was offered for USD 6 million (approximately NIS 23 million).
2. In May 2011, Gadot completed a rights issue for the acquisition of 3,303,464 shares for USD 4.5 million. The Group exercised the entire quantity of rights that it was offered for USD 3.5 million. The difference between the consideration paid and the value of the acquired equity amounted to insignificant sums and was recognized directly in capital reserve from transactions with non-controlling interests.
3. On August 30, 2011, Delek Investments issued a full tender offer for Gadot shares. On September 14, 2011, Delek Investments announced the results of the tender offer, according to which Delek Investments acquired 1,891,003 shares from the offerers, representing 10.27% of the issued and paid up share capital and voting rights of Gadot. The tender offer includes the conditions for a forced sale according to section 337(a) of the Companies Law, 1999. Subsequent to the acquisitions, Delek Investments holds 76.37% of the issued share capital of Gadot and Oil Refineries Ltd. holds 23.63% of the issued share capital of Gadot. Gadot shares were delisted from the TASE, however Gadot debentures continue to trade on the TASE.
4. For further information about the provision for impairment of property, plant and equipment recognized by Gadot in its financial statements, see Note 17 below.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)**P. Share-based payment in companies****1. Expense recognized in the financial statements**

The expense recognized in the financial statements for services received from employees is presented in the table below:

	Year ended December 31		
	2011	2010	2009
	NIS million		
Equity-settled share-based payment plans	24	28	31
Cash-settled share-based payment plans	56	33	23
Total recognized expense from share-based payments	80	61	54

2. Additional information:

Company	No. of outstanding options	Vested options	Exercise price per share	Type of plan settlement	Average no. of years remaining until exercise
December 31, 2011					
Delek USA	4,993,329	1,248,354	USD 8.68-14.22	Shares	5.5
Delek Israel	653,955	305,346	NIS 144-162	Shares	2.5
Delek Europe Holdings	750	630	NIS 5.579-6.458	Shares/cash	Immediate
DEBV	45,000	-	EUR 231-274	Shares	3.5
DES	313,610	228,751	NIS 349.96-468.99	Shares/cash	4.8
The Phoenix	8,138,896	4,438,940	NIS 7.78-20.58	Shares	1.4

For information about the phantom options plan for managers and officers in the Company, see Note 45H(4).

3. Principal share-based payment plans of the Group companies during the reporting period**A) Delek Europe**

- (1) According to the employment agreement of the new CEO of DEBV, from March 2011, it was agreed in principle to grant 45,000 options exercisable for DEBV shares (a holding rate of 2.5%, fully diluted). The options will vest in four lots over five years. The exercise price will be based on the normalized EBITDA of DEBV in 2010, multiplied by 8.25 less external debt and owners loans (including notional interest). At the approval date of the financial statements, the final options plan is yet to be approved and signed.

In accordance with the principles of the plan, the value of the benefit was estimated at EUR 3.3 million (NIS 16 million). In the period ended December 31, 2011, expenses of EUR 966 thousand (approximately NIS 5 million) were recognized for this plan under general and administrative expenses.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)

- (2) According to the employment agreement of the former CEO of Delek Europe Holdings Ltd. ("Delek Europe"), who also served as chairman of the board of directors ("the CEO"), which was signed in December 2008, the CEO was granted 750 options exercisable for Delek Europe shares (2.5% fully diluted). The exercise price was based on the value of Delek Europe in the amount of NIS 167 million. If Delek Europe, Delek Benelux ("Benelux") (a company wholly-owned by DEBV), DEBV or another related party issue securities on any stock exchange, the CEO will be entitled to convert his allocated shares to shares of the issuing company while maintaining the benefit component. The options are exercisable on six annual dates as from June 2007. It was further agreed that the CEO will have the option to sell his shares to Delek Europe provided Delek Europe shares are not issued to the public, therefore the grant of the options was accounted for as a liability grant.

On September 18, 2011, the CEO of Delek Europe announced his resignation from Delek Europe. The CEO remained in his position until December 15, 2011.

At December 31, 2011, 630 options were unvested. The fair value of the plan is estimated at NIS 17.7 million. In the reporting period, the Company adjusted the value of the options in the amount of NIS 10.6 million and these expenses were included in the statement of income under administrative and general expenses. The CEO of Delek Europe informed Delek Europe that he wishes to sell Delek Europe his unexercised options (five lots out of the six lots that were originally granted) and the parties are acting according to the agreement to determine the consideration, if any, for these options.

According to the employment agreement of the former CEO of Benelux, the CEO was granted 45,000 options exercisable for Benelux shares (2.5% at full dilution). The exercise price was based on Delek Europe's value of EUR 129 million. The options are exercisable on seven annual dates as from April 2008. It was further agreed that the CEO of Benelux will have the option of selling his shares to Benelux provided Benelux shares are not issued to the public, accordingly, the grant of the options was accounted for as a liability grant.

In February 2011, the former CEO of Benelux announced his resignation. According to the former CEO's employment agreement regarding the options that were granted to him in the past, valuations were performed for Benelux to adjust the value of the vested options paid to the CEO of Benelux. As a result, in the reporting period, Benelux adjusted the value of the options by another EUR 3.8 million (approximately NIS 19 million) (before the effect of income tax). These expenses were included in the statement of income under general and administrative expenses.

Notes to the Consolidated Financial Statements

NOTE 14 – BUSINESS COMBINATIONS AND INVESTMENTS IN INVESTEE COMPANIES AND PARTNERSHIPS (CONTD.)**B. DES**

- (1) On August 14, 2011, the board of directors of Delek Drilling Management (1993) Ltd. ("the general partner") approved the employment terms of Yossi Abu as CEO of the general partner, effective from April 1, 2011.

On August 23, 2011, the audit committee and the board of directors of the Company approved the terms of his employment. In addition, at that date, approval was received to grant the CEO 1,486,620 phantom units at the value of the underlying asset (the partnership's participating units) amounting to NIS 15 million, at the average closing price of the participating units in the 30 trading days preceding the date the agreement was signed. The phantom units will vest in three equal lots on different dates (3 years, 4 years and 5 years from the date the agreement was signed). The exercise price is NIS 11.12 unlinked for the first lot, plus 5% for each lot as from the second lot. The economic value of phantom units, according to a valuation of an external assessor, amounts to NIS 10.2 million, at December 31, 2011 (the fair value of the phantom units was estimated using the Merton method, based on the Black and Scholes formula) and based on the following assumptions:

Share price (NIS)	14.05
Exercise price (NIS)	11.12-12.26
Standard deviation (%)	44.6 - 45.6
Risk-free interest (%)	3.4-3.5

In addition, approval was received to place a guarantee in favor of a bank that will provide a loan of NIS 12 million to the CEO of the general partner to acquire the partnership's participation units ("the loan"). The loan period is 5 years and 3 months from the date it is provided or 90 after termination of employment (or termination of services), whichever is earlier. The bank may only redeem part of the proceeds of the sale of the participation units acquired by Yossi Abu (non-recourse terms).

The participation units will serve as collateral for the loan. One year after his appointment, the CEO of the general partner may sell half of the participation units he purchased, and two years after his employment, he may sell the balance of the participation units that he purchased. According to a valuation of an external assessor, at December 31, 2011, the value of the guarantee amounts to NIS 5.4 million (the fair value of the guarantee was estimated using the binomial method).

In 2011, the amount of expenses for the plan recognized in the statement of income amounted to NIS 2.4 million.

- 2) For details of the options granted to the former CEO of DES, see Note 14(M)(7) above.

- Q.** At December 31, 2011, the Company, Delek Investments and Delek Petroleum have no liens on the shares of investees, other than a lien of 159,000 DES shares (representing 3% of its share capital) registered by Delek Investments and a lien on Roadchef shares registered by Delek Petroleum in favor of banks in Israel as collateral for the Company's liabilities.

Notes to the Consolidated Financial Statements

NOTE 15 – INVESTMENT PROPERTY

A. Composition and change

	2011	2010
	NIS million	
Balance as of January 1	384	356
Purchases (including consolidation)	153	28
Exchange differences on translation of foreign operations	-	(15)
Transfer from property, plant and equipment	-	21
Sales	(1)	-
Deconsolidation	-	(34)
Adjustment to fair value	24	28
Balance as of December 31	560	384

- B. Investment property is presented according to fair value on the basis of valuations of external, independent assessors having the requisite qualifications and experience in the location and type of property being assessed. The fair value is based, in part, on recent market transactions in properties and locations similar to those of the properties owned by Group companies, and based on estimated future cash flows from the property. In estimating cash flows, current leases are taken into consideration and discount rates are used which reflect market estimates of uncertainties with regard to the future amount and timing of the cash flows. In calculating the fair value, assessors have used discount rates between 7%-9%. In calculating the fair value of investment property, assessors take into account similar transactions for similar assets in similar places. At December 31, 2011, an amount of NIS 317 million is in respect of performance based assets (2010, NIS 212 million).

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION

A. Composition and change

	Exploration and evaluation assets	Oil and gas production assets	Total
	NIS million		
Cost			
Balance as of January 1, 2010	32	1,761	1,793
Additions during the year			
Investments	82	411	493
Disposals	(6)	(2)	(8)
Exchange differences on translation of foreign operations	(5)	(118)	(123)
Balance as of January 1, 2011	103	2,052	2,155
Additions during the year			
Investments	351	778	1,129
Disposals	(21)	(668)	(689)
Exchange differences on translation of foreign operations	24	136	160
Balance as of December 31, 2011	457	2,298	2,755
Accumulated depreciation, depletion and amortization			
Balance as of January 1, 2010	-	461	461
Additions in 2010	8	130	138
Impairment	8	57	65
Exchange differences on translation of foreign operations	(1)	(31)	(32)
Balance as of January 1, 2011	15	617	632
Disposals	(9)	(171)	(180)
Additions in 2011	-	199	199
Exchange differences on translation of foreign operations	-	38	38
Balance as of December 31, 2011	6	683	689
Amortized cost at December 31, 2011	451	1,615	2,066
Company consolidated for the first time (*)			9,397
Amortized cost at December 31, 2011			11,463
Depreciated cost at December 31, 2010	88	1,435	1,523

*) Final allocation of the different assets, including deferred taxes, has not been made. For further information, see Note 14(M)(6).

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

B. Offshore drilling in the Yam Tethys project

1. The Yam Tethys project is an oil and gas exploration and production project on the continental shelf of the State of Israel. This project includes a number of offshore drillings, some of which resulted in material gas discoveries and production commenced in 2004 (see section 2 below).

At the date of approval of the financial statements, the following companies own rights in the Yam Tethys project:

	%
Noble Energy Mediterranean Ltd ("Noble" *)	47.059
Delek Drilling – Limited Partnership	25.5
Avner Oil Exploration - Limited Partnership	23
Delek Investments	4.441
	100

*) Noble is the drilling operator of the project ("the operator" or "Noble").

2. Additional information about the Yam Tethys project:

- A) In 1999-2001, the joint venture carried out offshore drillings at the Noa lease (Noa and Noa South I) and at the Ashkelon lease (Mari 1, Mari 2 and Mari 3), where two gas reservoirs were discovered (Noa and Mari gas reservoirs).
- B) On February 18, 2004, natural gas started to flow from the Mari gas reservoir to Israel Electric Corporation Ltd. ("IEC"), pursuant to the agreement with IEC. Gas is delivered to IEC at the Eshkol, Reading, Gezer, Hagit and Zafit power stations. See section G below for additional information about the gas supply agreements with other customers.
- C) The partners in the joint venture approved an agreement between Noble and foreign suppliers for the acquisition of a compression system, which, together with the drillings in the project, will increase production capacity from the Mari gas field, in view of the decrease in pressure at the Mari reservoir, in order to meet the requirements of the Yam Tethys project customers and which may also comprise part of the natural gas delivery system at the Mari gas field (if and to the extent that such shall be decided upon).

In the reporting period, installation of the compression system was completed, which, together with the drillings in the project, will increase production capacity from the Mari gas field, in view of the decrease in pressure at the Mari reservoir, in order to meet the requirements of the Yam Tethys project customers. This system may also comprise part of the natural gas delivery system at the Mari gas field (if and to the extent that such shall be decided upon). The compression system started to operate in the second half of 2011 at a total investment (100% of the rights) of USD 84 million.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

E) Gas reserves in the Mari reservoirs

According to reports received from Netherland Swell & Associates Inc. ("NSAI"), an engineering consulting company that provides estimates of oil and gas reserves, the natural gas reserves (in BCM) in the Mari B field are as follows:

	<u>BCM</u>
Proved gas reserves at the Mari reservoir	
Balance as of December 31, 2008	16.3
Gas sold in 2009	(2.9)
Gas sold in 2010	(3.3)
Gas sold in 2011	<u>(4.3)</u>
Balance as of December 31, 2011	<u>5.8</u>
Proved + probable gas reserves at the Mari reservoir	
Balance as of December 31, 2011	<u>6.5</u>

F) Development of the Noa field

On June 12, 2011, the Commissioner of Petroleum Affairs approved the development of the northern part of the Noa field by the Yam Tethys project operator ("Noa North"). In addition, the Commissioner limited the total quantity of gas produced to the amount in the Noa North reservoir, which the operator estimates at 1.2 BCM, to prevent allegations of gas production from other parts of the reservoir extending beyond the lease area.

On July 31, 2011, the partnerships in the Noa lease approved the budget and development plan for the Noa North reservoir in the Noa Lease, according to the outline presented by the project operator, Noble Energy Mediterranean Ltd. ("Noble").

Development of the Noa North reservoir will provide additional supply of natural gas to the Israeli market, mainly to customers that have signed agreements with the consolidated partnership for the supply of natural gas, until gas supply commences.

Tamar project

The development plan includes mainly drilling of two diagonal production wells with subsea completions, Noa 2 and Noa 3, to a total vertical depth of 1,880 m (including a water depth of 800 m). Noble estimates that both wells have a production capacity of 100 MMcf/d of natural gas. The natural gas will flow through a pipeline to the Mari-B production platform for processing, and then through the existing 30-in pipeline to the Yam Tethys reception terminal at Ashdod.

On October 2, 2011, Noble informed the partners that the Noa 2 and Noa 3 production wells that were drilled from the end of July 2011 by the Noble Homer Ferrington rig, have been successfully completed. According to Noble, development of the Noa North reservoir should be completed in September 2012 at a total development cost (for 100% of the rights) of USD 212 million. Of this amount, USD 75 million has been invested up to the balance sheet date. The estimates and information regarding development of the Noa field are based on information received from the operator and are as yet uncertain, as yet uncertain, and are expected to be adjusted as additional information is gathered as the result of a range of factors connected to natural gas exploration and production projects.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

According to a report prepared by NSAI in accordance with the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), at December 31, 2011, the quantity of natural gas reserves in the Noa field classified as reserves approved for development, amounts to 1 BCM. In addition, according to the NSAI report, the quantity of contingent reserves in the Noa field, for which there is no approved development plan at this stage, is between 0.6 BCM (low estimate) and BCM 1.8 (high estimate).

These estimates of the natural gas reserves in the Mari and Noa reservoirs and the contingent resources in the Noa lease are the professional assessments and assumptions only of NSAI, which are as yet uncertain. The estimates are expected to be adjusted as additional information is gathered and/or as a result of a range of factors related to oil and gas exploration and production projects, including as a result of continued analysis of the drilling findings.

Subsequent to the balance sheet date, on January 24, 2012, Delek Drilling and Avner ("the partnerships") announced that recently, there has been a reduction in supply of natural gas from the Mari B reservoir ("the reservoir"), and according to updated estimates of Noble, the project operator, there will be a further reduction in the capacity and scope of supply from the reservoir.

As a result, the Yam Tethys project partners are assessing the techno-economic implications of the reduced supply, as well as the methods of operation that are available to stem the reduced supply and moderate its consequences, while maintaining the serviceability of the Yam Tethys project production system. The reduction in supply is expected to have an adverse effect on the financial results of the Company and its partnerships, however at this stage, the Company and its partnerships are unable to estimate, at a high level of certainty, the scope of the effect. In the reporting year, the partnerships recognized a provision of USD 10 million, net, less royalties, for the losses for the effect of the reduction in supply. The Yam Tethys project partners are negotiating with the authorities and with the project customers, with the aim of minimizing the effect of the reduced supply on their operations. From information submitted to the partnership by Noble, and as a result of the assessment and analysis performed by Noble itself and through third parties, it arises that production from the Mari B reservoir led to a constant reduction of pressure in the reservoir, which resulted in the sinking of soil layers above the reservoir. Sinking of the soil layers resulted in damage and loss of production capacity in some of the production wells, alongside penetration of water to other production wells, impairing production capacity. It is noted that the production platform at the Yam Tethys project is planned from an engineering and technical aspect to allow for sinking, mainly due to sinking of the soil layers above the reservoir and below the production platform, and at this stage, sinking of the soil layers caused the production platform to sink within permitted levels according to the engineering and technical planning performed in advance.

Subsequent to the balance sheet date, on March 4, 2012, the Yam Tethys partners announced their decision to participate in exploration drilling at the Pinnacles 1 satellite reservoir. The exploration drilling will appraise the presence of natural gas in the target layers. If natural gas is discovered in a quantity that is sufficient for development of the satellite reservoirs, the drilling will be completed as a production drilling as part of the combined development of the satellite reservoirs and the Noa reservoir. The total drilling budget is USD 30 million (for 100% of the rights). If natural gas is discovered in the target layers in a quantity that is sufficient for development of the satellite reservoirs, the drilling will be completed as a production drilling and the total development budget of the satellite reservoirs (including the drilling and exploration budget, completion of the drilling as a production well and costs involved in connecting it to the production facilities of the Yam Tethys project), is USD 100 million.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

C. Michal and Matan joint venture (Tamar and Dalit leases)

1. The Michal Matan joint venture is an oil and gas exploration project in the area of the Tamar and Dalit leases, 50-100 km west of the Haifa coast. At the date of approval of the financial statements, the following companies own rights in the project:

	%
Noble *)	36
Delek Drilling	15.625
Avner	15.625
Isramco Negev 2 Limited Partnership	28.75
Dor Gas Exploration Limited Partnership	4
	100

*) Noble is the operator of the joint venture

2. Tamar 1 and Tamar 2 drillings

A. Development of the Tamar natural gas field

In 2009, two offshore drillings at the Tamar 1 well and the Tamar 2 appraisal drilling were completed, with a significant gas discovery. On December 3, 2009, the Commissioner granted the I/12 Tamar lease to the holders of the 308/Matan license, for exploration and production of oil and natural gas in the license area.

In August 2010, the Ministry of Energy and Water approved the project partners' development of the Tamar gas field as a dual pipeline to deliver natural gas from the field to a platform that will be constructed next to the Yam Tethys platform and from there, through the existing pipeline to the Yam Tethys receiving terminal in Ashdod, which will be expanded to receive the gas.

The Petroleum Commissioner asked the project operator for a reservoir development plan, including the arrangements between the partners in the Tamar lease and the relevant holders of rights in the Ashkelon lease regarding the pipeline and receiving terminals and onshore handling facilities, including storage arrangements. At the publication date of these financial statements, the parties signed the arrangement.

The Tamar project partners approved the development plan of the project, at an estimated cost (100%) of USD 3.06 billion. At this stage, the development costs are estimates only, received from the operator, and there is no certainty as to the actual costs. In addition, the partners estimate, based on information received from Noble, that supply of natural gas from the project will begin in the first half of 2013.

In view of the estimates of costs in the development budget of the Tamar project, the partnerships are required to raise significant amounts to finance its share.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

On April 10, 2011, development drilling commenced at the Tamar project. According to the plan submitted to the project partners by the drilling operator, the project operator, the Tamar 6, Tamar 5, Tamar 4 and Tamar 3 wells were drilled to an initial depth of 2,500 m (including water depth). In the second stage, these drillings were continued, with the aim of reaching a final depth of 5,200 meters. In the third stage, the wells will be prepared for production, followed by the Tamar 2 well, originally drilled in 2009 as an exploratory well for the Tamar 1 discovery. The schedule for this plan is one year.

At the publication date of the financial statements, the rig has completed drilling works at the Tamar 2, 3, 4, 5 and 6 development wells.

At December 31, 2011, the total investments for development of the Tamar natural gas field amounted to USD 1,543.7 million (100% of the rights).

B. Estimated natural gas reserves in the Tamar gas field

According to the report prepared by NSAI in July 2011, based on the Petroleum Resources Management System (PRMS), at June 30, 2011, the natural gas reserves in the Tamar field are classified as reserves approved for development and are as follows: Proved reserves: 195 BCM Proved and probable reserves: 275 BCM.

The estimates of the natural gas reserves in the Tamar lease are partially based on geological, geophysical and other information received from the drillings and from operations in the lease. These estimates are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. The estimates for actual quantities of natural gas produced may be different from these estimates and assumptions, partly due to technical and operational conditions and/or regulatory changes and/or the supply and demand conditions in the natural gas market and/or actual performance of the reservoir. The estimates and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production.

3. **Dalit drilling**

In 2009, the Dalit offshore well was drilled 50 km off the coast of Israel and a commercial discovery was declared. On December 3, 2009, the Commissioner granted the I/13 Dalit lease to the holders of the 308/Michal license, for exploration and production of oil and natural gas in the license area.

According a report received from NSAI, NSAI believes that the Dalit formation is separated into a number of fault blocks and that it is possible that the blocks that are not connected to the main block of the Dalit 1 drilling will not have the same quality as that discovered in the main block. Accordingly, NSAI has classified part of the gas resources in the Dalit lease as contingent resources and part as prospective resources. According to the report, the amount of contingent reserves in the Dalit lease at December 31, 2011 is between 6.1 BCM (low estimate) and 9.5 BCM (high estimate).

These estimates of the contingent resources in the Dalit lease are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. The estimates are expected to be adjusted as additional information is gathered and/or as a result of a range of factors related to oil and gas exploration and production projects, including as a result of continued analysis of the drilling findings.

The total investment for the Dalit drilling at December 31, 2011 amounted to USD 56.8 million.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

D. Ratio Yam joint venture

1. The Ratio Yam project is a joint venture for oil and gas exploration. At December 31, 2011, the following companies own rights in the project:

	%
Noble *)	39.66
Avner	22.67
Delek Drilling	22.67
Ratio Yam - Oil and Gas Exploration	15.00
	100

*) Noble is the operator of the joint venture

2. Leviathan 1 well

In October 2010, drilling started at Leviathan 1 ("the well") in the Rachel license.

The well is 135 km west of Haifa and 47 km south west of the Tamar discovery at a water depth of 1,634 m. Drilling of three targets was planned (see below) to a final depth of 7,200 km (including water depth) and is expected to take about five months.

On December 29, 2010, the partners announced a significant gas discovery at the well. The well reached a depth of 5,170 m (including water depth) to the bottom of the main target (NG10 prospect) and a series of tests were carried out, including electrical logs and coring from the target layers, for the purpose of further analysis.

According to a report received from NSAI, the amount of contingent reserves in the Leviathan discovery at December 31, 2011, which is classified as development pending, is between 362 BCM (low estimate) and 600 BCM (high estimate).

After the partners approve the development plan, which includes a reasonable expectation for the sale of natural gas, the contingent resources will be classified as proved reserves, probable reserves and possible reserves.

These estimates of the contingent resources in the Leviathan discovery are the professional estimates and assumptions only of NSAI and there can be no certainty in respect of them. The estimates are expected to be adjusted as additional information is gathered and/or as a result of a range of factors related to oil and gas exploration and production projects, including as a result of continued analysis of the drilling findings.

The total investment for the Leviathan 1 drilling at December 31, 2011 amounted to USD 197.1 million (100%).

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

3. Leviathan 1 well - secondary layers

In January 2011, the drilling rig started continuation drillings towards the lower layers (secondary lower Oligocene layers and lower Cretaceous layer).

On April 3, 2011, Noble informed the project partners that it had temporarily suspended drilling to the secondary layers at the Leviathan 1 well due to technical operational problems related to wear on the wellbore casing, which prevents further work and because equipment and materials, which are unavailable in Israel, are required to repair the malfunction and continue drilling. Following the aforesaid, the drilling rig has moved to the Tamar project for development drilling.

Subsequent to the balance sheet date, on January 14, 2012, the partners announced that after the operator acquired the equipment and materials required to continue drilling, another drilling rig reached the drill site at Leviathan. The rig will begin drilling work into the deeper targets.

The Leviathan 1 well is expected to reach a final depth of 7,400 m (including the water depth). However, it is noted that according to Noble, since drilling has not yet been performed to these depths in the Levant Basin, reaching the final drilling depth depends on technical feasibility and it is uncertain whether the data during the drilling works will allow drilling to the final planned depth. Drilling is expected to continue for three months. In the first stage, the existing well will be drilled (which was plugged with cement and other materials and abandoned to ensure its preservation) and the worn wellbore casing will be insulated by installing another pipe (tieback). This stage is expected to continue for one month. In the second stage, drilling will be deepened to the final depth. This stage is expected to continue for two months, at a total cost (100%) of USD 215 million (including drilling works up to April 2011). The cost of the continuation of drilling (100%), representing part of the total cost, is USD 45 million (not including production tests, to the extent that a decision is made to perform them).

4. Leviathan 2 appraisal well

On March 9, 2011, the partners approved the Leviathan 2 appraisal well. The Leviathan field covers a vast area of 325 square km, therefore at least two appraisal wells are required to continue the appraisal of the natural gas reserves in the main target layers (NG10) in the Leviathan field. Accordingly, it was decided to drill the Leviathan 2 appraisal well in the Amit license, 14 km from the Leviathan 1 discovery well at a total depth of 5,400 m (including water depth of 1,700 m).

The Pride North America drilling rig ("the rig") started drilling on March 20, 2011. Drilling is expected to continue for three months at a total cost (100%) of USD 70 million, not including production tests.

On May 15, 2011 the project partners announced that Noble (the drilling operator) has decided to end drilling at the Leviathan 2 well and to drill an alternate appraisal well ("Leviathan 3") nearby, as described below.

The Leviathan 2 well reached a depth of 4,570 meters, hundreds of meters above the target layers (NG10). During the drilling process, the operator identified water flowing behind the wellbore casing to the seabed. The operator estimates that sand layer from which the water is flowing has no geological impact on the target layers (NG10) and this does not affect the estimated amount of contingent resources in the Leviathan discovery. The operator monitored the water flow and found no indications of hydrocarbons. Due to the potential damage to the technical completeness and stability of the drilling systems, which was intended as a production drilling, the operator has concluded that the well is unsuitable for continued drilling at this location and has suspended drilling operations. In view of the aforesaid, Delek Drilling recognized its share of the drilling costs (less indemnification received from the insurance company), in the net amount of USD 6.5 million, in the statement of income.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

On August 1, 2011, at the request of the Petroleum Commissioner, the Group submitted a number of alternatives for the abandonment plan of the Leviathan 2 well if the flow of water does not stop and furnished an unconditional bank guarantee of USD 30 million (100%), valid until June 30, 2012.

The operator is assessing these alternatives and reviewing the parameters required to plan and select the target for plugging and the required equipment. Assessment of the flow of water will take several months, and then Petroleum Commissioner will determine what action the partnership is required to take, if any, to plug the well.

The partnership's management believes, based on the assessment of its professional advisors, that at this preliminary stage there is still insufficient information to select the suitable technology for abandonment and since it is possible that the abandonment plan may not be implemented, the costs of abandoning the well cannot be reliably estimated.

It is noted that the partnerships have control of well insurance, to cover control of well expenses, including redrilling up to a liability level of USD 200 million (100%) per case.

The participants are working with the insurers to receive indemnity under the policy. In 2011, Delek Drilling received USD 5.9 million (after deductibles), representing part of the insurance indemnification.

5. Leviathan 3 appraisal well

On June 26, 2011, the Leviathan project operator informed the project partners that on June 24, 2011, the PNA started drilling at Leviathan 3 after the Leviathan 2 wells were abandoned. The drilling is in the Amit license area located 4.4 km from the Leviathan 2 drilling (and 9.6 km from the Leviathan 1 discovery drilling).

On September 5, 2011, the partners announced, based on information received from Noble, that the Leviathan 3 assessment drilling had reached a depth of 2,600 m (2,700 m above the target layer) and drilling at the Leviathan 3 well was suspended due to continuous technical problems in the blowout preventer and auxiliary equipment in the Pride North America rig, which is performing the drilling. Following the aforesaid, the Pride North America rig left the drilling area and the Sedco Express rig completed drilling at Leviathan 3. The Leviathan 3 well is expected to be completed as one of the producing wells in the Leviathan field.

On December 14, 2011, the partners announced that according to Noble, the Leviathan 3 appraisal drilling had been completed and natural gas had been discovered in the appraisal drilling. At December 31, 2011, the total cost of the Leviathan 3 appraisal drilling amounted to USD 129.5 million (of which, the share of the consolidated partnership is USD 29.4 million).

6. Dolphin 1 well in the Hanna license

On August 29, 2011, the Sedco Express rig started drilling the Dolphin 1 well. The Dolphin 1 well is 11 km west of the Haifa coast at a depth of 1,560 meters.

The main target of the Dolphin 1 drilling is the gas prospect in the lower Miocene and upper Oligocene layers (which match the layers identified in the Tamar sands, called 10NG) at a total depth of 6,000 meters (including water depth).

On December 18, 2011, the partners reported that according to information received from Noble, natural gas had been discovered in the upper target sand layers. Noble carried out various tests and gathered information during the drilling, including electric and other logs, analysis of rock samples, chemical analyses of the natural gas and measurement of pressure in the reservoir, the results of which, as provided by the operator, satisfied the partners that there was natural gas at the drilling site. Noble also informed the partners that, in its opinion, the quantity of natural gas discovered at the drilling site justifies an analysis and evaluation of the overall quantities of natural gas in the reservoir, and an analysis and evaluation of the quantities of natural gas that can be produced commercially. Accordingly, the Dolphin 1 well is a natural gas discovery.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

At December 31, 2011, the total cost of the Dolphin 1 drilling amounted to USD 56.7 million (100%).

Subsequent to the balance sheet date, on February 12, 2012, the consolidated partnerships announced that according to a report from NSAI, prepared in accordance with the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS) ("the contingent resource report"), the quantity of contingent natural gas resources at the Dolphin reservoir, at December 31, 2011, which are classified as development on hold) is between 1.05 BCM (low estimate) and 5.03 (high estimate).

According to the resources report, the contingent resources are in an undeveloped location, therefore the appraisal is based on the estimated volume of the reservoir and the recovery efficiencies, with an analogy to reservoirs with similar geological characteristics and properties. The resources are contingent on approval of the development plan for the Dolphin project and demonstration of economic feasibility for the project.

The consolidated partnership announced that it will explore different options for commercializing the natural gas in the Dolphin 1 reservoir, as part of the assessment of the options for integrating the reservoir's development plan with development plans of adjacent fields, which may allow such joint development.

The consolidated partnership further announced that at this stage, it is unable to determine an estimated timetable for the formulation and/or implementation of a development plan for the Dolphin 1 reservoir, pending completion of an examination of possible development plans of adjacent fields and the option of integrating the development plan for the Dolphin 1 reservoir.

It is noted that development of the Dolphin 1 reservoir might be integrated with the development plan for the Leviathan reservoir, located 30 km northwest of the Dolphin 1 reservoir, or it may be integrated as part of a future stage in the development of the Tamar reservoir, located approximately 30 km northeast of the Dolphin 1 reservoir.

It is emphasized that each alternative of a development plan has different timetables and construction and operation costs, therefore until the development plan for the Dolphin 1 reservoir is assessed and prepared, the timetables and development budget for the reservoir cannot be estimated.

The estimates of NSAI regarding the contingent resources in the Dolphin 1 reservoir are the professional evaluations and assumptions only of NSAI in respect of which there is no certainty. The evaluations and assumptions may be updated if additional information becomes available and/or as the result of a range of factors related to oil and natural gas exploration and production projects, including due to continued analysis of the drilling findings and due to operational and/or market and/or regulatory conditions.

7. Tanin 1 well in the 364/Alon A license

On August 30, 2011, the partners decided to approve an exploratory drilling at the Tanin 1 well in the 364/Alon A license area. The approval was received on the basis of the recommendation of the operator, Noble, as presented to the license partners. The Tanin 1 well is 120 km northwest of the Haifa coast at a depth of 1,770 meters. The total drilling budget (two stages, not including production tests) is estimated at USD 50 million.

The main target of the Tanin 1 drilling is the gas prospect in the lower Miocene and upper Oligocene layers (which match the layers identified in the Tamar sands, called 10NG) at a total depth of 5,472 meters (including water depth). The decision whether and how to perform future production tests will be determined on the basis of the drilling findings. The presence of natural gas in the target layers could lead to drilling a number of additional wells in the license area.

In December 2011, drilling started at Tanin 1. On February 5, 2012, subsequent to the balance sheet date, the partners announced that according to information received from Noble, the Tanin 1 well has reached a final depth of 5,500 m (including the depth of the water). The partners concluded that significant indicators of natural gas were discovered in the well, according to reports from Noble, based on tests carried out during the drilling.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

Subsequent to the balance sheet date, on February 7, 2012, the partners announced that Noble had carried out tests, including logging while drilling, which included electrical and gamma ray tests, as well as initial analyses of the composition of the natural gas and the rock samples from the reservoir. The results, as provided by the operator, satisfied the partnerships of the existence of natural gas at the drilling site.

The operator informed the partnerships that, in its opinion, the quantity of natural gas discovered at the drilling site justifies an analysis and evaluation of the overall quantities of natural gas in the reservoir, and an analysis and evaluation of the quantities of natural gas that can be produced commercially. At December 31, 2011, the consolidated partnership recognized an investment of USD 9.8 million for its participation in the drilling costs.

8. Aphrodite well in Block 12 in Cyprus

Subsequent to the balance sheet date, on March 6, 2012, the partnerships announced that according to information received from Noble, the operator of the A-1 exploration drilling (Aphrodite), which the operator carried out at the end of December 2011 to a depth of 5,137 m (including the depth of the water), natural gas was discovered.

According to a report prepared by NSAI in accordance with the guidelines set out in the Petroleum Resources Management System approved by the Society of Petroleum Engineers (SPE-PRMS), the quantity of contingent reserves in the Aphrodite reservoir at January 31, 2012, which is classified as development pending, is between 14 BCM (low estimate) and 82 BCM (high estimate).

These estimates of the contingent resources in Block 12 are the professional evaluations and assumptions only of NSAI and there can be no certainty in respect of them. The estimates are expected to be adjusted as additional information is gathered and/or as a result of a range of factors related to oil and gas exploration and production projects, including as a result of continued analysis of the drilling findings.

At December 31, 2011, the share of Avner Partnership and Delek Drilling in the drilling costs amounts to USD 30 million.

E. Oil exploration and production in the United States

1. On February 14, 2011 a transaction was signed and completed for the sale of part of the oil and gas assets of Delek Energy Systems US, in Texas USA ("the assets"), which include oil wells producing about 100 barrels of oil net per day (less royalties), for USD 11 million in cash (in the fourth quarter of 2010). According to the agreement, the operating results of these assets as from January 1, 2011 will be transferred to the acquiring company.
2. On February 15, 2011, an agreement was signed for the sale of an additional part of the oil and gas assets of Delek Energy Systems US ("the agreement"). Most of the assets in the agreement are in Texas, Oklahoma and New Mexico, and include oil wells producing (as of the fourth quarter of 2010) about 250 barrels of oil net per day (less royalties) ("the assets"). According to the agreement, assets and the operating results of these assets as from January 1, 2011 will be transferred to the acquiring company. The transaction was completed on March 25, 2011 for a total consideration of USD 31.3 million.
3. On May 11, 2011, DES announced that it had signed an agreement to sell a significant part of the oil and gas assets in the United States, owned indirectly by its subsidiary, DES US ("the agreement"). According to the agreement, as from January 1, 2011, the assets and the operating results of these assets will be transferred to the acquiring company. On June 9, 2011, the transaction was completed for a cash payment of USD 120 million. It is noted that of this consideration, USD 95 million was used to repay a loan used to acquire assets.

DES recognized a profit of NIS 72 million from these transactions (taking into account disposal of capital reserve amounting to NIS 15 million for translation differences and transaction expenses) included in the statement of income under other revenues (expenses), net.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

F. Principal financing agreements investments in oil and gas developments

Bridge loan to finance the share of the limited partnerships in the development costs of the Tamar project

In June 2010, the partnerships signed a bridge loan agreement ("the financing agreement") through special purpose companies (see below) with Barclays Bank Plc and HSBC Bank Plc (hereinafter together: "the financing banks"). Under the financing agreement, each partnership will receive a non-recourse loan of up to USD 190 million ("the loan"), to finance the share of each partnership in the development costs in the Tamar field ("the Tamar project"). Concurrently with the financing agreement signed by the partnerships, financing agreements with the same terms were signed between the financing banks and Dor Gas Exploration Limited Partnership ("Dor Gas") (for a loan of USD 50 million), to finance the share of Dor Gas in part of the development costs of the Tamar project.

The loan is for the period until the agreement is signed for long-term non-recourse project finance to fully finance the partnerships' share in the Tamar project development costs ("the project finance") or for 18 months, whichever is earlier with an option for extension to a total of 24 months under certain terms. In December 2011, the loan was extended for an additional six months, until June 2012.

The loan will be repaid in one single payment at the end of the loan period. The partnerships intend to take steps to raise financing for the project before the finance agreement expires, such that the project finance will repay the loan. The partnerships may repay the loan prematurely, subject to the terms set out in the finance agreement.

The loan is in dollars and bears variable annual interest calculated at LIBOR for three months plus a maximum of 4% if the loan is not extended beyond 18 months. (not including fees). The funds of the loan are transferred to each partnership on a current basis, in accordance with the payment requirements issued by the operator to the partners for development costs of the Tamar project (cash calls) and to finance the loan costs.

To receive the loan, the partnerships set up special purpose companies. As collateral for repayment of loan, each partnership pledged its rights in the assets related to the Tamar project. The main points are as follows: The rights in the Tamar and Dalit leases ("the leases"), the rights in the JOA of the Tamar project, the rights in any future agreements for the sale of natural gas from the Tamar project, shares in the SPC and accompanying agreements of the Tamar project (such as insurance policies and equipment). The loan is a non-recourse loan and the lenders have no right of recourse to the Partnership's assets that were not pledged in their favor.

These pledges are subject to royalty rights of the state and other entities that are entitled to receive royalties from the Partnerships (including interested parties). To establish legal certainty regarding priority of claim in the event of insolvency of the Limited Partnership, the financing agreements prescribe, based on the banks' requirements, that the leases will be pledged as collateral for the right to royalties in favor of the entities entitled to royalties for the term of the financing agreement.

The financing agreement establishes a mechanism that allows each partnership, under certain conditions, to raise an additional amount of up to USD 100 million, using the same collateral and subject to approval of the majority of the lenders.

As is standard in this type of financing, the partnerships have undertaken standard covenants, including the following main commitments: Restrictions on taking additional loans (other than non-recourse loans, loans from related parties and loans of up to USD 20 million); compliance with liquidity tests; compliance with the reservoir to debt ratio; restrictions on the change in operations; restrictions on the transfer of control in the partnerships; restrictions on signing contracts that may adversely affect the partnerships' ability to raise project financing; maintaining the pledged assets and avoiding breach or change of conditions of the material agreements, including agreements not to vote in accordance with the JOA in a way that may adversely affect the ability of the partnership to raise the project financing (including with respect to replacing the operator); purchase of insurance in accordance with the JOA; conditions for the purchase of additional rights in the Tamar project; and restrictions on approval of sole risk operations in the Tamar project.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

As customary in financing transactions of this nature, the financing agreement defined events of default, which if occur (subject to recovery periods set out in the financing agreement) confer on the financing banks the right to call for immediate repayment of the loan, including the following main events: failure to pay amounts owed to lenders; breach of covenants; breach of representations; insolvency events; occurrence of events that may have a material adverse effect on the ability of the partnerships to fulfill their material obligations in respect of the financing agreement or the Tamar project, events that may have a material adverse effect on their assets or main businesses or the financial condition of the partnerships or events that could have a material adverse effect on their ability to raise the project financing; cancellation or inability to receive material approval required for the Tamar project; meeting of additional milestones set according to agreed deadlines (project development; gas sales agreement with IEC; planning approval for establishment of the gas receiving terminal; availability of drilling rigs for development drilling); and a continuing force majeure event in connection with the Tamar project.

Parallel to signing the financing agreement, the partnerships appointed the financing banks as exclusive consultants and organizers for project financing, and granted them exclusive participation rights according to certain conditions set out in any of the partnerships' hedge transactions and the right of refusal for financial services and other consulting services provided to the partnerships in respect of the Tamar project.

On December 22, 2011, the loan period set out in the original bridge loan agreement was extended for another six months, up to June 24, 2012 or until the signing of the long-term non-recourse project finance agreement to finance the share of the partnerships in the development costs of the Tamar project ("the project finance"), whichever is earlier ("the extension of the bridge loan agreement"). Extension of the bridge loan agreement was based on an extension option, provided by the original bridge loan agreement and under terms set out therein, which included the adjusted interest rate, such that 18 months after the first withdrawal from the bridge loan (February 12, 2012), the interest rate will be adjusted to a rate based on the three month Libor plus a margin of 5.75%. The loan will be repaid in one payment on the last date of the extended bridge loan agreement. The partnerships intend to take steps to secure project financing before the end of the extension period of the bridge loan agreement, such that the project financing will be used to repay the loan. The partnerships have the right to an early repayment of the loan, subject to the terms set out in the original bridge loan agreement.

Signing of the loan agreement by the Israeli partners in the Yam Tethys project

On June 9, 2011, the partnerships announced that they had signed a loan agreement ("the loan agreement") with a syndicate of banks headed by Morgan Stanley & Co. International Plc ("the financing banks"). Under the financing agreement, each partnership will receive a non-recourse loan of up to USD 109 million ("the loan"). The loan will be used to finance the share of the partnerships in the operating costs for their oil rights. Concurrently, financing agreements with the same terms were signed between the financing banks and Delek Investments and Properties Ltd. for a loan of USD 23 million.

The loan is for up to three years, depending on the rate of gas sales. If the sales exceed the amount set in the basic model appended to the loan agreement, part of the surplus proceeds can be used for early repayment of the loan. The partnership may repay the loan prematurely at any time and at no charge.

The dollar-denominated loan bears an annual variable interest rate of three-month Libor plus a margin of 2.75%. The loan will be repaid starting from October 2011 in eleven unequal quarterly payments based on the repayment schedule set by the parties, and depending on the forecast for gas sales set in the basic model. In addition, when the loan is received, the partnership will pay a one-time fee of 2% of the loan as set out in the financing agreement.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

To receive the loan, the partnerships set up special purpose companies. According to the financing agreement, the loan will be issued to the special purpose companies and will be issued back-to-back to the partnerships. To secure repayment of the loan, each partnership will place a lien on its rights to the assets related to the Mari reservoir in the Ashkelon lease, primarily: its rights in the Ashkelon lease, in the shares of Yam Tethys Ltd., in the JOA in the Ashkelon lease, including its rights in the project equipment and facilities, in agreements for sale of natural gas signed by the partners in the Ashkelon lease, the shares of the special purpose company and the assets and agreements related to the project (such as insurance policies). The loan is a non-recourse loan and the lenders have no right of recourse against the partnership's assets that have not been pledged in their favor.

The partnerships have accepted standard covenants, including the following main commitments: compliance with a ratio of debt service for the remaining the loan period, a commitment to pay all taxes and levies owed by the partnership, the partnership's compliance with commitments under agreements to sell gas and the JOA, which were pledged, compliance with safety requirements, the partnership's commitment to function as a partnership in accordance with the laws of the State of Israel, restrictions structural changes in the partnership, restrictions on changes in agreements for the gas sales and the JOA, protection of pledged assets, and refraining from any breach or change of any of the significant terms of agreements,

The financing agreement sets out standard events of default, which if they materialize (subject to remedial periods as provided by the financing agreement) the financing banks may call for immediate repayment of the loan. The breach events include the following main events: nonpayment of amounts due to lenders; breach of covenants; breach of representations; insolvency events; events that could have a material adverse effect on the ability of the limited partnerships to fulfill their material obligations in respect of the financing agreement or the pledged agreements for sale of gas, events that could have a material adverse effect on their assets or main businesses or the financial position of the partnership.

The partnerships applied to the Tax Authority for an exemption from withholding tax for foreign lenders. If the exemption is not received, the partnerships will gross up withholding tax according to the domiciles of the foreign lenders when the interest is paid.

On June 1, 2011, the Tax Authority permitted the loan for each partnership.

On September 27, 2011, the second amount of USD 83 million was withdrawn after approval was received to record the liens. At the end of October 2011, USD 40 million was repaid on account of the loan. In addition, subsequent to the balance sheet date, at the end of January 2012, USD 16.8 million was repaid on account of the loan.

Loan agreement from a bank

On December 22, 2011, the partnerships announced a loan agreement ("the loan agreement") had been signed between the partnership and HSBC Bank Plc ("the financing bank"). Under the financing agreement, each partnership will receive a non-recourse loan of USD 250 million ("the loan"). The loan funds will be used for investments in the Leviathan project, the Tamar development, limited investments in other oil properties of the partnerships and payment of various loan-related expenses ("the use of the loan").

The loan is made available in two facilities, as follows:

Facility A amounting to USD 75 million, which will be available for withdrawal after the fulfillment of a number of preconditions (primarily, the approval of the Commissioner of Petroleum Affairs for a lien on the licenses, as set out below) and repayment 24 months after signing the agreement. Subsequent to the balance sheet date, in March 2012, and after fulfillment of the conditions set out above, the first withdrawal was approved. Up to the publication date of these financial statements, USD 60.9 million has been received on account of the first withdrawal.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

Facility B amounting to USD 175 million, which will be available for withdrawal when closing the entire Tamar project financing, and repayment of the bridge loan (provided to the partnerships for the Tamar project), no later than June 24, 2012, with repayment 24 months after the first withdrawal from Facility B, and no later than June 24, 2014. The partnerships may repay the loan prematurely, subject to the terms set out in the finance agreement, without premature repayment fees.

The loan is in dollars and bears variable annual interest calculated at Libor for three months plus a margin of between 3.5% and 4.5% (not including fees).

To receive the loan, the partnerships set up special purpose companies. In accordance with the financing agreement, the loan to the special purpose companies will be a back-to-back loan. To secure repayment of the loan, each partnership will place a lien on its rights to the assets related to the Leviathan project, primarily: its rights in the Amit and Rachel licenses ("the licenses"), in the JOA of the Leviathan project, in the shares of the special purpose company and the assets and agreements related to the Leviathan project (such as insurance policies). The loan is a non-recourse loan and the lenders have no right of recourse against the partnerships' assets that were not pledged in their favor. These pledges are subject to royalty rights of the state and other entities that are entitled to receive royalties from the partnerships (including interested parties). To establish legal certainty regarding priority of claim in the event of insolvency of the partnerships, the financing agreements prescribe, based on the bank's requirements, that the licensees will be pledged as collateral for the right to royalties in favor of the entities entitled to royalties for the term of the financing agreement.

The partnerships have accepted standard covenants, including the following main commitments: Restrictions on taking additional loans (other than non-recourse loans, loans from related parties and loans of up to USD 20 million); compliance with the reservoir to debt ratio; restrictions on the change in operations; restrictions on the transfer of control in the partnership; restrictions on signing contracts that may have a material adverse effect; maintaining the pledged assets and avoiding breach or change of conditions of the material agreements, including agreements not to vote in accordance with the JOA in a way that may adversely affect the ability of each partnership to fulfill their material obligations in respect of the financing agreement; purchase of insurance in accordance with the JOA; conditions for the purchase of additional rights in the Leviathan project; and restrictions on approval of sole risk operations in the Leviathan project.

As is standard in financing transactions of this nature, the financing agreement defined events of default, which if occur (subject to recovery periods set out in the financing agreement) confer on the financing bank the right to call for immediate repayment of the loan, including the following main events: non-payment of amounts due to the lenders; breach of covenants; breach of representations; insolvency events; events that could have a material adverse effect on the ability of the partnerships to fulfill their material obligations in respect of the financing agreement or the Leviathan project, a material adverse effect on the main assets or businesses or the financial position of the partnerships, events that could affect the partnerships' ability to sell the Leviathan project in a way that will allow it to repay the loan when due; cancellation or inability to obtain significant approval required for the Leviathan project; and repeated force majeure relating to the Leviathan project.

When signing the financing agreement, the partnerships appointed the financing bank as sole consultant and coordinator of the long-term loan (which will replace, inter alia, the loan which is the subject of this report) and granted it the right to provide various services (whether alone or with the cooperation of other banks) in respect of the Leviathan project.

The partnership has applied to the Tax Authority for permission to receive the loan and if necessary, will ask for an exemption from withholding tax for the foreign lenders. If the exemption is not received, the partnership will gross up withholding tax according to the domiciles of the foreign lenders, if relevant, when the interest is paid.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

Subsequent to the balance sheet date, on February 27, 2012, the partnerships received notice from the Petroleum Commissioner that by virtue of his powers under section 76 of the Petroleum Law, 1952 and after consulting with the Petroleum Council, he has decided to approve the partnerships' application to place a lien on the partnerships' rights, in accordance with the licenses for oil and natural gas exploration and production, in favor of the financing bank, as collateral for the loan provided to a wholly-owned company of the partnership, for the partnership's operations under the Rachel and/or Amit rights and in accordance with the lien agreement attached to the lien request. Each partnership may also use the loan to finance investments in the Yam Tethys project: drilling at the satellite reservoir of the Mari B reservoir in the I/10 Ashkelon lease ("the Pinnacles"), to the extent that the partnerships decide to drill and development of the Noa North field in the I/7 Noa license and to finance their operations under the I/12 Tamar lease. The Commissioner's approval is subject to the conditions and clarifications determined, including that after fulfillment of the conditions for the first withdrawal of the loan funds under the project finance in the Tamar project, no further funds will be withdrawn from the loan for which the licenses were pledged for the investment in the Tamar development, other than in the event of an unforeseeable deviation from the establishment budget of the Tamar project and after receiving approval from the Commissioner.

G. Principal natural gas supply agreements

Yam Tethys project

At the balance sheet date, the partners in the Yam Tethys project entered into agreements for the supply of natural gas in a total estimated quantity of 30.1 BCM. Up to December 31, 2011, 21.5 BCM of this amount has been supplied.

1. Agreements with Israel Electric Corporation for the supply of natural gas

On June 25, 2002, an agreement was signed with the Israel Electric Corporation Ltd. ("the IEC") for the supply of natural gas to IEC ("the agreement").

Under the terms of the agreement, the Yam Tethys group will supply the IEC with natural gas for 11 years (up to 2014) or until the Yam Tethys group supplies the IEC with natural gas in a total volume of 18 BCM, the earlier of the two. The agreement includes provisions and commitments for numerous issues, including: The commitment of the IEC to pay for a minimum annual quantity even if it does not consume that quantity, accounting arrangements, penalties for breach of the commitments (including for failure to meet timetables or non-supply of gas), force majeure, guarantees and collateral for the IEC, limitations on assigning the agreement, contract law, and settling disputes.

The contracted price for the gas is denominated in USD per energy unit (BTU) and is linked to a basket of fuels and to the US Producer Price Index according to the mechanism in the agreement, including minimum and maximum prices. On February 18, 2004, the joint venture began supplying natural gas to IEC facilities.

On August 6, 2009, the joint venture partners and the IEC signed a memorandum of understanding for the sale of additional quantities of natural gas. Under these agreements, the joint venture will supply an additional annual volume of 1 BCM of gas for the next five years (a total of 5 BCM). The price for gas purchased under the memorandum of principles is higher than the price at which IEC purchases natural gas under the agreement for supply of natural gas of 2002.

The parties reached an agreement regarding distribution of the additional quantity of gas supplied according to the MOU out of the entire quantity of gas supplied to IEC in the period commencing from July 1, 2009.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

2. Other agreements

At December 31, 2011, the partners in the Yam Tethys group have entered into agreements for the supply of natural gas to several parties (including Delek Ashkelon, (a subsidiary), Paz Ashdod Refinery, Hadera Paper Ltd., Dead Sea Works and Oil Refineries Ltd.) for periods ranging between 5 and 15 years totaling 9.8 BCM and at an estimated financial scope of between USD 830 and USD 900 million. Actual revenue will be affected by a number of conditions, as set out in the agreements.

Tamar project

1. Agreements with Israel Electric Corporation for the supply of natural gas

Subsequent to the balance sheet date, on March 14, 2012, an agreement for the supply of natural gas was signed between the partners in the Tamar lease ("the sellers" and "the Tamar project", respectively), and the Israel Electric Corporation Ltd. ("IEC"). The main points of the agreement are described below ("the supply agreement")

In the agreement IEC has undertaken to purchase a minimum quantity from the sellers, as set out below, and no more than the total contracted quantity of 78 BCM ("the total contracted quantity"). According to the agreement the IEC has an option, which can be exercised until April 2, 2013, to increase the total contracted quantity purchased from the Tamar project to 99 BCM ("the option"). It is noted that if the option is exercised, the sellers will be required to increase the supply capacity of the handling and transport system of the Tamar project, subject, inter alia to receiving the authorizations required by law.

According to the supply agreement, IEC is expected to purchase a minimum quantity (take or pay) of 42.5 BCM of natural gas from the Tamar project or a minimum quantity (take or pay) of 5 BCM per year if IEC exercises the option (subject to adjustments based on the gas sales of the Tamar project partners and the electricity production of IEC).

The period of the supply agreement will start when gas starts to flow from the Tamar project and will end after 15 years, or at the date that IEC purchases the total contracted quantity, whichever is the earlier. IEC is entitled to extend the agreement period by up to two additional years, if by the of end 15 years after gas starts to flow from the Tamar project IEC has not purchased the total contracted quantity, as described above.

The agreement sets two dates for adjusting the price (according to the formula set out in the agreement): 8 years and 11 years after gas starts to flow from the Tamar project. At the first adjustment date (after 8 years) the adjustment to the price will be up to 25% (increase or reduction), and at the second adjustment date the adjustment will be up to 10% (increase or reduction).

The price of gas in the agreement will be set according to a formula that includes a base price and linkage, based mainly on the US Consumer Price Index for all Urban Consumers (CPI-U).

The Tamar project partners estimate (based on the formula, estimates of the US CPI-U and a forecast of IEC's gas consumption when signing the agreement) that the cumulative revenues from the sale of natural gas to IEC (relative to 100% of the rights in the Tamar project) are likely to amount to USD 14 billion if the option is not exercised, and USD 23 billion if the option is exercised. It is clarified that the actual revenues will be derived, inter alia, from the actual gas quantities purchased by IEC, exercise of the option and the exercise date (if exercised), and from the price of gas calculated in accordance with the above formula.

The agreement includes several preconditions, the main ones being obtaining approval from the Antitrust Authority, the Public Services Authority - Electricity, and the Government Companies Authority.

The above estimates of the financial amounts included in the agreement, the quantity of natural gas purchased, and date supply starts under the agreement are forward looking information for which there can be no certainty that it will materialize, in whole or in part, and it might materialize in a different manner, due to various factors including non-fulfillment of the preconditions, in whole or in part, changes in the quantity, rate and timing of natural gas consumption by IEC, exercise of the option by IEC and exercise date (if exercised), the price of gas in accordance with the formula in the supply agreement, and linkage to the US CPI-U.

Notes to the Consolidated Financial Statements

NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION (CONTD.)

2. Additional letters of intent

At December 31, 2011, the Tamar project partners have agreements for the supply of natural gas to a number of entities (including Dalia Power Energies Ltd., Ramat Negev Energy Ltd. and Ashdod Energy Ltd., Hadera Paper Ltd. and Mashav Initiating and Development Ltd.) for up to 17 years in a total scope of between 83 BCM and 104 BCM and an estimated financial scope of between USD 14 billion and USD 23 billion. Actual revenue will be affected by a number of conditions, as set out in the agreements.

3. Memorandum of understanding with Daewoo Shipbuilding and Marine Engineering Co. and D&H Solutions AS Ltd.

On November 22, 2011, the Tamar and Dalit project partners signed the memorandum of understanding with Daewoo Shipbuilding and Marine Engineering Co. and D&H Solutions AS Ltd., the main points being:

The memorandum of understanding refers to the assessment of an agreement for the Tamar partners to sell natural gas to the acquirers from the Tamar project for liquefaction to liquid natural gas (LNG) and to export it to South Korea and/or other countries to be agreed upon by the parties. The acquirers intend to liquefy the natural gas using a floating liquefied natural gas facility ("the FLNG") to be constructed and financed by the acquirers and positioned in the Tamar and/or Dalit gas field and from there, to be transported in special tankers to target markets.

In accordance with the memorandum of understanding, in the first stage, which is expected to continue for three months, the initial front-end engineering design (pre-FEED) will begin to define the parameters required for the detailed plan. After this stage (if the Tamar partners and the FLNG partners so decide), the second stage of the detailed front end engineering design (FEED) will begin, which is expected to continue for nine months. After this stage and subject to a decision on the final investment (if the Tamar partners and the FLNG partners so decide), construction of the FLNG facility in Korea, development drillings and construction of a special production system at the Tamar and/or Dalit gas field will begin. This stage is expected to continue for three or four years. Together with the detailed engineering planning, the parties intend to negotiate for an agreement for the supply of natural gas by the Tamar partners to the FLNG for 15 to 20 years, in quantities required to produce 2-3 million tons per annum (MTPA) of LNG, meaning estimated annual gas sales of between 3 BCM and 4.5 BCM.

The price that the acquirers will pay for natural gas is expected to be a factor of LNG selling prices by the acquirers and the expected costs of liquefaction and transportation. According to indications and certain assumptions provided by the acquirers, including current LNG prices, and based on the price of USD 100 per barrel of oil, it is expected that the Tamar partners will be paid between USD 7 and USD 9 per MMBtu of natural gas. Actual revenue will be a factor of a range of considerations, including those described above and the prices of fuels when supplied.

The memorandum of understanding further noted that each Tamar partner may participate in the construction of the FLNG facility in a scope and under the conditions to be agreed between the parties.

It is clarified that supply of gas to the FLNG is not expected to have an adverse effect on the supply capacity of the Tamar reservoir to the Israeli market and is expected to be supplied through a dedicated production system which will include development of new wells for this purpose.

It is further emphasized that this is a memorandum of understanding only and development through the FLNG, including the actual supply of gas, is subject to engineering and economic feasibility studies as well as negotiations for a series of contracts, including a binding contract for the sale of gas, and obtaining all the approvals required by law.

Notes to the Consolidated Financial Statements

**NOTE 16 – INVESTMENTS IN OIL AND GAS EXPLORATION AND PRODUCTION
(CONTD.)****4. Royalties to the State and others**

The Commissioner of Petroleum Affairs in the Energy and Waters informed the Yam Tethys joint venture that the State has decided not to take the royalties it is entitled to (in kind) from gas discoveries, but rather to take the market value of the royalties per well in US dollars.

The method for calculating the royalties due to the State was agreed according to the Commissioner of Petroleum Affairs' announcement on July 19, 2004 and a summary of a discussion held with the Commissioner. According to the agreements, the financial statements include royalty payments to the State, representing 11.3% (in 2010, 11.2%) of the gross sales of the joint transaction. The method for calculating the royalties is used also to calculate the market value per well of the super royalties paid to the companies in the Group and to others.

5. See Note 42(A)(2) for information about approval of the recommendations of the Sheshinski committee in respect of taxation of petroleum profits.

Notes to the Consolidated Financial Statements

NOTE 17 – PROPERTY, PLANT AND EQUIPMENT

A. Composition and movement:

2011

	Leasehold improve- ments	Machinery, facilities and equipment	Computers, furniture and office equipment	Pumps, tanks and station equipment	Refineries	Works of art	Vehicles	Total
	NIS million							
Balance as of January 1, 2011	4,693	557	668	2,637	1,722	74	89	10,440
Additions during the year	467	15	125	288	85	-	11	991
Exchange differences on translation of foreign operations	122	53	8	90	169	-	1	443
Additions for companies and a partnership consolidated for the first time	379	-	126	3	1,335	-	5	1,848
Disposals during the year	(68)	(1)	(8)	(111)	-	-	(11)	(199)
Balance as of December 31, 2011	5,593	624	919	2,907	3,311	74	95	13,523
<u>Accumulated depreciation</u>								
Balance as of January 1, 2011	804	197	456	1,126	277	-	57	2,917
Additions during the year	187	27	88	212	163	-	10	687
Exchange differences on translation of foreign operations	18	17	4	31	25	-	1	96
Disposals during the year	(32)	-	(3)	(82)	-	-	(8)	(125)
Balance as of December 31, 2011	977	241	545	1,287	465	-	60	3,575
<u>Amortized cost at December 31, 2011</u>	4,616	383	374	1,620	2,846	74	35	9,948
Less - provision for impairment (1)	127	176	2	30	-	2	1	338
<u>Reduced cost at December 31, 2011</u>	4,489	207	372	1,590	2,846	72	34	9,610

Notes to the Consolidated Financial Statements

NOTE 17 – PROPERTY, PLANT AND EQUIPMENT (CONTD.)

2010

	Leasehold improve- ments	Machinery, facilities and equipment	Computers, furniture and office equipment	Pumps, tanks and station equipment	Refineries	Works of art	Vehicles	Total
	NIS million							
Balance as of January 1, 2010	4,377	573	654	2,440	1,729	76	102	9,951
Additions during the year	340	14	47	123	159	-	12	695
Exchange differences on translation of foreign operations	(148)	(30)	(8)	(158)	(109)	-	-	(453)
Additions for a company consolidated for the first time	484	-	3	306	-	-	-	793
Deconsolidation	(264)	-	(26)	-	-	-	(7)	(297)
Reclassified to investment property	(22)	-	-	-	-	-	-	(22)
Assets held for sale	(6)	-	-	(14)	-	-	-	(20)
Disposals during the year	(68)	-	(2)	(60)	(57)	(2)	(18)	(207)
Balance as of December 31, 2010	4,693	557	668	2,637	1,722	74	89	10,440
<u>Accumulated depreciation</u>	-	-	-	-	-	-	-	-
Balance as of January 1, 2010	773	186	426	1,022	222	-	72	2,701
Additions during the year	125	24	55	176	131	-	9	520
Exchange differences on translation of foreign operations	(19)	(13)	(5)	(37)	(19)	-	(2)	(95)
Deconsolidation	(50)	-	(18)	-	-	-	(5)	(73)
Reclassified to investment property	(3)	-	-	(12)	-	-	-	(15)
Assets held for sale	(2)	-	-	-	-	-	-	(2)
Disposals during the year	(20)	-	(2)	(23)	(57)	-	(17)	(119)
Additions for a company consolidated for the first time	-	-	-	-	-	-	-	-
Balance as of December 31, 2010	804	197	456	1,126	277	-	57	2,917
<u>Depreciated cost at December 31, 2010</u>	3,889	360	212	1,511	1,445	74	32	7,523
Less - provision for impairment	17	-	-	30	-	2	-	49
<u>Depreciated cost at December 31, 2010</u>	3,872	360	212	1,481	1,445	72	32	7,474

Notes to the Consolidated Financial Statements

NOTE 17 – PROPERTY, PLANT AND EQUIPMENT (CONTD.)

- (1) Gadot has invested great effort in an attempt to bring the plant in China to profitability and has provided the subsidiary in China with significant financial resources, administrative support and support in planning and operating its facilities. However, the company in China is suffering from sustained losses, mainly due to a sharp rise in prices of raw materials (mainly cassava) and energy against expectations taken into account in the initial business plan, failure to find alternative production sources, levies imposed on citric acid manufacturers in China after construction of the plant began, and difficulty in raising funds to finance ongoing operations. In addition, at the end of 2011, there was a significant decrease in selling prices of citric acid. In view of the aforesaid and due to the significant finances that are required to continue operations in China, the limited finances available to the company and the difficulty in obtaining credit in China to finance this activity, the Company's board of directors resolved to significantly reduce activity at the plant in China and to consider how to continue operations in China, including disposal of the operations or discontinuation of the operations. In view of the aforesaid, the financial statements of Gadot as of December 31, 2011 include an assessment of the recoverable amount of the plant's assets in China at fair value less selling costs (disposal value) and not according to the value in use as in the past. Accordingly, Gadot included a provision of USD 61.1 million (NIS 239 million) in its financial statements for impairment of most of the subsidiary's assets in China, according to the assessment of Gadot's management that the recoverable amount on disposal of this operation is negligible.

Additionally, in view of indications of impairment, Gadot received a valuation from an independent assessor for the recoverable amount of property, plant and equipment assets in Israel. The recoverable amount in Israel was based on the value in use, calculated according to the cash-generating unit which is an operating segment of Gadot. The value in use of the cash-generating units in Israel was calculated according to the present value of expected cash flows. The discount rate used to determine the value in use is 17.54%.

Based on these assumptions, the value in use of property, plant and equipment attributable to the fructose unit amounts to USD 34 million compared to the carrying amount (including working capital) of USD 47 million. Accordingly, the value in use of fructose unit assets is USD 13 million (NIS 51 million) less than their carrying amount. As a result, the Group included a provision for impairment of property, plant and equipment in this amount.

Additionally, based on these assumptions, the value in use of property, plant and equipment attributable to the citric acid and salts unit amounts to USD 36 million compared to the carrying amount (including working capital) of USD 22 million. Accordingly, the management of Gadot believes that no provision is required for impairment of property, plant and equipment.

Impairment of USD 76 million (approximately NIS 290 million) was recognized in the statement of income under other expenses.

- (2) Delek Israel is assessing impairment for most of its gas stations as one cash-generating unit. At December 31, 2011, in view of the decrease in the marketing margin in Israel and the fact that the market value of Delek Israel's shares on the TASE at that date is significantly lower than its equity, Delek Israel assessed the recoverable amount of the gas stations, which have a carrying amount of NIS 1.009 billion (including working capital attributable to the gas stations). The recoverable amount determined by an independent assessor was based on the value in use of the gas stations.

When determining the recoverable amount, Delek Israel used the following key assumptions:

- The pre-tax discount rate was 10.4% (after tax, 8.1%).
- The forecasted cash flows took into account annual growth of 3% in the next five years, followed by annual growth of 1.5%.

Since the recoverable amount of the unit exceeds the carrying amount of the gas stations, a provision for impairment of the gas stations is not required.

B. See Note 33 for liens.

Notes to the Consolidated Financial Statements

NOTE 18 – DEFERRED ACQUISITION COSTS IN INSURANCE COMPANIES**A. Composition:**

	December 31	
	2011	2010
	NIS million	
Life assurance and long-term savings	720	680
Health insurance	140	116
General insurance	329	318
	<u>1,189</u>	<u>1,114</u>

Stated in the balance sheet as follows:

	December 31	
	2011	2010
	NIS million	
Current assets	428	393
Non-current assets	761	721
	<u>1,189</u>	<u>1,114</u>

B. Change in deferred acquisition costs in life assurance and long-term savings and health insurance.

	Life assurance and long-term saving	Health
	NIS million	
Balance as of January 1, 2010	642	106
Additions		
Acquisition commissions	118	20
Other acquisition costs	72	15
Total additions	190	35
Current write off	(75)	(19)
Write-off for cancellations	(77)	(6)
Balance as of January 1, 2011	680	116
Additions		
Acquisition commissions	118	33
Other acquisition costs	74	25
Total additions	192	58
Current write off	(83)	(27)
Write-off for cancellations	(69)	(7)
Balance as of December 31, 2011	<u>720</u>	<u>140</u>

Notes to the Consolidated Financial Statements

NOTE 19 – STRUCTURED BONDS

At December 31, 2011, the balance of structured bonds amounted to NIS 736 million.

The structured bonds were issued through special purpose companies that engage exclusively in issuing bonds and handling assets mortgaged in favor of the bond holders ("Heharim companies"). The issuing companies are special purpose companies ("SPC"), which were set up for the sole purpose of issuing bonds and these companies may not engage in any other commercial activity. The SPC acquires non-marketable structured bonds ("notes") from the proceeds of the issuance, which constitute the sole source of repayment of the liabilities of the Heharim companies (non-recourse liabilities).

At December 31, 2010, there are nine series of structured bonds: two are listed on the TASE, two for which trading was suspended and 11 were issued in private offerings. The bonds (except for Keshet and part of the Matbeot Olam – World Currencies series), which are traded on the TASE, have been rated by Standard & Poor's Maalot at ilAAA.

The fair value of the notes backing up the marketable structured bonds at December 31, 2011, based on the market price of the marketable bond at the balance sheet date is NIS 226 million.

NOTE 20 – GOODWILL AND OTHER INTANGIBLE ASSETS

A. Composition:

	Goodwill	Marketing, rights, brands, franchises and customer portfolios	Software	Value of insurance portfolios	Licenses and concessions	Other	Total
	NIS million						
Balance as of January 1, 2010	3,242	808	493	412	-	37	4,992
Deconsolidation	(15)	-	-	-	-	-	(15)
Additions	23	53	130	3	-	-	209
Companies consolidated for the first time	166	125	-	-	-	-	291
Impairment	(111)	-	-	-	-	-	(111)
Amortization recognized during the year	-	(86)	(88)	(41)	-	(8)	(223)
Exchange differences on translation of foreign operations	(132)	(81)	-	(7)	-	(3)	(223)
Balance as of January 1, 2011	3,173	819	535	367	-	26	4,920
Additions	4	64	196	-	-	59	323
Companies consolidated for the first time	866	270	-	-	438	-	1,574
Impairment	(338)	-	-	(21)	-	-	(359)
Amortization recognized during the year	-	(110)	(103)	(51)	-	-	(264)
Adjustment for contingent consideration	(68)	-	-	-	-	-	(68)
Exchange differences on translation of foreign operations	70	32	1	5	9	12	129
Balance as of December 31, 2011	<u>3,707</u>	<u>1,075</u>	<u>629</u>	<u>300</u>	<u>447</u>	<u>89</u>	<u>6,247</u>

Notes to the Consolidated Financial Statements

NOTE 20 – GOODWILL AND OTHER INTANGIBLE ASSETS (CONTD.)**B. Impairment of goodwill and intangible assets with a defined useful life**

To assess impairment of goodwill and intangible assets with a defined useful life, goodwill and the value of insurance portfolios were attributed to business sectors, as follows:

	Goodwill		Value of insurance portfolios	
	December 31			
	2011	2010	2011	2010
	NIS million			
Insurance and finance in Israel 1)	1,136	1,481	268	311
Fuel in Israel (2)	327	327	-	-
Insurance abroad (3)	192	374	32	56
Gas stations and convenience stores in the USA (4)	222	223	-	-
Gas stations and convenience stores in Europe (5)	730	697	-	-
Delek Motorways Services UK	840	-	-	-
Other segments	260	71	-	-
Total	3,707	3,173	300	367

1. (a) At December 31, 2011, the Company has surplus cost attributable to goodwill of NIS 311 million and the value of the insurance portfolios of NIS 268 million created by acquisition of control of Phoenix in 2006. Examination of impairment of goodwill and value of insurance portfolios is based, among others, on the assessment of an independent external assessor. In the valuation, part of the goodwill and value of insurance portfolios for life assurance and general insurance activity were attributed to cash-producing units. The goodwill that cannot be attributed specifically was examined on the level of the entire sector consistently with the allocation at the acquisition date.

The recoverable amount of the life assurance unit is calculated on the basis of the embedded value, using the discount rate reflecting the level of risk in the relevant cash flows. Calculating the embedded value is based on discounting the future cash flows arising from the life assurance portfolio less the cost of capital required and with the Company's equity after a number of adjustments. In addition, the valuation took into account the value of new businesses (VNB).

The recoverable amount of general insurance is based on the value of use calculated by discounting the expected future cash flows using the discount rates that reflect the risk level of the operation.

The carrying amount (including surplus cost and goodwill) of the life assurance unit, general insurance unit and unattributable goodwill amounts to NIS 1.086 billion, NIS 119 million and NIS 240 million, respectively. The recoverable amount of the life assurance unit and general insurance unit amounts to NIS 1.407 billion and NIS 769 million, respectively. In view of the aforesaid, the Company concluded that at December 31, 2011, goodwill and the value of the insurance portfolios were not impaired.

Notes to the Consolidated Financial Statements

NOTE 20 – GOODWILL AND OTHER INTANGIBLE ASSETS (CONTD.)

- (b) Goodwill amounting to NIS 560 million was attributed to acquisition of Excellence in the financial statements of The Phoenix, after provision for impairment of NIS 110 million in the financial statement of The Phoenix, which was attributed to the provident unit. See Note 14H(1).

Goodwill amounting to NIS 150 million was attributed to operations of insurance agencies and financial consultation with a recoverable amount based on individual valuations for the various agencies, calculated according to the projected cash-flow method, which is the basis for determining that the recoverable amount of the goodwill of each of the agencies exceeds its carrying amount, therefore, impairment of the agencies is not required.

A total of NIS 260 million is attributed to goodwill for acquisition of Prisma Investment House Ltd. in 2009. Excellence evaluates the contingent consideration periodically. The adjustment to the contingent consideration arising from the passage of time is recognized in the statement of income. The balance of the adjustment is recognized in goodwill. According to the assessment of an independent external valuator, a provision for impairment of goodwill is not required.

2. The balance attributable to fuel storage and distribution in Israel amounts to NIS 327 million at December 31, 2011 (at December 31, 2010, NIS 327 million). The recoverable amount of the fuel storage and distribution unit was based on discounting the future cash flows expected to be received. To determine the recoverable amount, the pre-tax discount rate used was 8.8% and the cash flow forecasts took into account annual growth of 2% in 2013-2011 and 1.5% through the remainder of the discounting period. According to the assessment of an independent external assessor, a provision for impairment is not required for goodwill.
3. In 2011, the Group examined the recoverable amount of goodwill and other intangible assets of Republic based on the weighted discounted expected future cash flow method and comparison with benchmark companies in the sector. When calculating the future discounted cash flow, discount rates were used that reflect the risk level of 14.3% of the growth rate in net premiums earned as from 2015 at a rate of 3%. Following the examination, in the reporting year, the Group recognized impairment of USD 230 million.

In 2010, the Group examined the recoverable amount of goodwill of Republic based on the discounted expected future cash flow method and comparison with benchmark companies in the sector, taking discount rates that reflect the level of risk of the operations (13%). Following the examination, in 2010, the Group recognized impairment of USD 57 million.

4. The balance attributable to gas stations and convenience stores in the USA amounts to NIS 222 million at December 31, 2011 (at December 31, 2010, NIS 223 million). The recoverable amount is based on various valuation techniques, including multiples and discounted future cash flows. In 2011, an impairment of USD 2.2 million (NIS 8 million) was recognized for goodwill.
5. At December 31, 2011, goodwill attributable to gas stations and convenience stores in Europe amounts to NIS 730 million (at December 31, 2010, NIS 697 million). Impairment was based on the value in use of various cash-generating units, using the following parameters: discount rate of 8.36%, inflation rate of 1.5%, and representative predicted cash flows for five years including annual growth of 1-3%. In 2011, impairment was not recognized for this goodwill (all changes compared to the prior year arise from exchange differences).
6. At December 31, 2011, goodwill attributable to motorway service stations in the UK amounts to NIS 840 million. Impairment was based on the value in use of various cash-generating units, using the following parameters: discount rate of 9% and representative predicted cash flows for six years including annual growth of 0.5-3%. Accordingly, a provision for impairment was not recognized for this goodwill in the reporting year.

Notes to the Consolidated Financial Statements

NOTE 21 – SHORT-TERM CREDIT FROM BANKS AND OTHERS**A. Composition:**

	Interest rate	December 31	
	annual (1)	2011	2010
	%	NIS million	
From banks			
Foreign currency			
US dollar or dollar linked	5.5	1,933	558
EUR	2.1	289	247
Pound Sterling	4.1	199	-
Other	6.67	5	47
		<u>2,426</u>	<u>852</u>
NIS			
CPI linked	5.7	506	320
Unlinked	4.8	525	943
		<u>1,031</u>	<u>1,263</u>
From others			
Unlinked		70	-
		<u>70</u>	<u>-</u>
Current maturities of other debentures		1,414	1,245
Current maturities of debentures convertible to Company shares (2)		252	-
Current maturities of long-term loans		1,262	698
		<u>2,928</u>	<u>1,943</u>
		<u>6,455</u>	<u>4,058</u>

(1) Most of the loans bear interest at a variable rate. The rate presented is a weighted average at December 31, 2011.

(2) For further information, see Note 26.

B. See Note 25(C) for compliance with financial covenants.**C. See Note 33 for collateral.**

Notes to the Consolidated Financial Statements

NOTE 22 – TRADE PAYABLES

	December 31	
	2011	2010
	NIS million	
Mainly open accounts		
Foreign currency or linked thereto	4,518	2,158
NIS	240	185
	<u>4,758</u>	<u>2,343</u>

The trade payables are non-interest bearing and are normally settled in less than 30 days.

- *) On April 29, 2011, Delek US entered into a three-year agreement with a third party (J. Aron) to acquire and sell inventory following the acquisition of control in Lion. According to the agreement, which expires on April 29, 2014, Lion will purchase inventory of distillates from J. Aron on an ongoing basis. When the agreement expires, Delek US will purchase the remaining inventory from J. Aron at the market prices prevailing at that time. Since the financing agreement for purchasing the inventory does not comply with the guidelines of IAS 18 for recognizing revenue, Delek US recognized proceeds of USD 243 million (approximately NIS 824 million) as a liability included under liabilities to trade and other payables.

At the balance sheet date, the liability for this agreement is USD 299 million (NIS 1.142 billion).

NOTE 23 – OTHER PAYABLES

	December 31	
	2011	2010
	NIS million	
Institutions	1,544	1,276
Prepaid income and expenses payable	421	298
Advance payments from customers	9	10
Salaries and incidentals	209	197
Liability for share-based payment	174	-
Related parties	32	9
Payables for joint ventures in oil and gas	696	220
Interest to be paid	387	265
Deferred purchase costs for reinsurance	34	32
Insurance companies and insurance agents	184	180
Liabilities to insurance agents	229	179
Liability for acquisition of shares of a subsidiary from non-controlling interests	163	177
Deposits from tenants	513	422
Others and accrued expenses	654	545
	<u>5,249</u>	<u>3,810</u>

Notes to the Consolidated Financial Statements

NOTE 24 – EXCHANGE-TRADED FUNDS AND DEPOSIT

	December 31	
	2011	2010
	NIS million	
Exchange-traded funds and deposit (1)	18,471	17,256
Current maturities of structured bonds	-	359
Liability for short sale of securities	491	312
	<u>18,962</u>	<u>17,927</u>

(1) Details of exchange-traded funds

- A. Excellence owns special purpose companies (“SPCs”) that issue exchange traded funds and deposits listed on the TASE. In this context, Excellence issues exchange-traded funds (“ETFs”) that track share, commodity and sector indexes, reverse certificates for share indexes and covered warrants for indexes and commodities (“the certificates”). The issuing companies are SPCs that were set up to issue ETFs, commodity certificates and reverse certificates, and other securities approved by the board of directors of the TASE.

ETFs were issued by companies that exclusively issue ETFs and handle assets pledged in favor of the debenture holders. The certificates accurately track an index and are convertible into shares or at a financial value according to the reference index determined for that certificate. The certificates are backed by underlying assets that produce the yields of various share and goods indexes. Of the proceeds of the issuance, the companies deposit sums in accounts (banks or financial institutes) and underlying assets and/or financial instruments and derivatives that will be acquired to fulfill their obligations towards the debenture holders. The rights of the debenture holders will be exercised out of the net proceeds received from the companies from the pledged assets. Up to December 31, 2011, 134 certificates were issued.

- B. Deposit certificates were issued by companies that engage exclusively in issuing deposit certificates and handling assets that are pledged in favor of the deposit holders. Deposit certificates are linked (principal and interest) to the rate of exchange for a variety of currencies against the Israeli shekel and they bear interest. Each of the deposit certificate companies is an SPC which was set up for the sole purpose of issuing deposit certificates and these companies may not engage in any other commercial activity. The companies make bank deposits from the proceeds of the issuance to secure their liabilities towards the holders of the deposit certificates. The rights of the companies in the backup deposits are the sole source of repayment for obligations to the holders of the certificates of deposit. The certificates of deposit are rated at different ratings from AA- AAA+. The rating is based, among others, on the rating of the banks in which the deposits are placed. Up to December 31, 2011, seven deposit certificates were issued.

Notes to the Consolidated Financial Statements

NOTE 24 – EXCHANGE-TRADED FUNDS AND DEPOSIT (CONTD.)

C. Composition of the exchange-traded funds

	December 31	
	2011	2010
	NIS million	
Host contract *)	14,280	14,057
Embedded derivative **)	4,191	3,199
	<u>18,471</u>	<u>17,256</u>

(*) Measured at amortized cost

**) Measured at fair value through profit or loss

D. Additional details about the composition of assets and liabilities of SPCs as of December 31, 2011

	Israel share indexes	Sector share indexes	Foreign share indexes	Commodity indexes NIS million	Exchange rates	Debenture indexes	Other
Backed up assets, net *)	7,927	132	4,251	514	211	5,855	24
Certificates	7,880	131	4,208	512	202	5,837	21
	<u>47</u>	<u>1</u>	<u>43</u>	<u>2</u>	<u>9</u>	<u>18</u>	<u>3</u>

*) Less credit and credit balances and less liabilities for options for short sale of securities

NOTE 25 – LOANS FROM BANKS AND OTHERS

A. **Composition and terms:**

	Annual interest rate (1)	December 31	
		2011	2010
		NIS million	
	%		
Loans from banks:			
USD or USD-linked	4.5	2,413	2,434
GBP		48	-
Euro or euro-linked	4.0	1,912	1,607
Linked to the CPI	5.2	334	565
Unlinked	4.1	688	128
Other currencies	6.1	72	182
		<u>5,467</u>	<u>4,916</u>
Loans from others	6.0	126	36
		<u>5,593</u>	<u>4,952</u>
Less - current maturities		<u>(1,262)</u>	<u>(698)</u>
		<u>4,331</u>	<u>4,254</u>

(1) Most of the loans bear interest at a variable rate. The rate presented is a weighted average at December 31, 2011.

Notes to the Consolidated Financial Statements

NOTE 25 – LOANS FROM BANKS AND OTHERS (CONTD.)

B. Settlement dates:

	December 31 2011 NIS million
First year – current maturities	1,262
Second year	1,231
Third year	85
Fourth year	579
Fifth year	269
Sixth year and onwards	2,167
	5,593

C. Additional details

1. In December 2009, the Company and Delek Investments entered into an agreement with a bank for a loan, the balance of which amounts to NIS 600 million at December 31, 2011. Pursuant to the agreement, the financial covenants determined in prior agreements were annulled and new covenants were established, as follows:

- The Company and Delek Investments have undertaken that the total guarantees that they will provide, as defined in the loan agreement will not exceed NIS 1.5 billion.
- The Group and Delek Investments are required to maintain certain financial ratios derived from the market value of their assets in relation to the total liabilities of the companies.

The Company undertook that the total dividends to be declared will not exceed a certain percentage of the net profit attributable to the Company's shareholders.

At December 31, 2011, the Company is in compliance with these financial covenants.

2. In respect of loans from banks and others, the balance of which amounts to NIS 9 billion at December 31, 2011, certain subsidiaries have undertaken to meet certain financial covenants, mainly in respect of the amount of their equity, the ratio of credit to balance sheet total, the ratio of equity to balance sheet total, the financial debt and debt coverage. As the balance sheet date, certain subsidiaries are not in compliance with the financial covenants set out above, therefore an amount of NIS 340 million is stated under short-term liabilities. In addition, some of the companies undertook towards the banks that as long as the loans are not repaid in full, they will refrain from distributing a dividend exceeding a specific percentage of their net earnings.
3. See Note 13(1) for financing of acquisition of Noble shares.

D. See Note 33 for other collateral.

Notes to the Consolidated Financial Statements

NOTE 26 – DEBENTURES CONVERTIBLE INTO COMPANY SHARES

On April 26, 2010, the Company issued 255,378,000 par value Debentures (Series DD) (“the Debentures”). The debentures are payable in one payment on October 31, 2012 and bear annual interest of 4.1%, payable twice a year on April 30 and October 31, 2012. The debentures are unlinked (principal and interest). The debentures are convertible into ordinary shares of NIS 1 par value each of the Company, such that as from their listing on the TASE through to October 15, 2012, each NIS 1,225 par value debenture will be convertible into one ordinary share of NIS 1 par value of the Company, subject to adjustments for distribution of a dividend and so on. According to IAS 32 – Financial Instruments: Presentation, the consideration for the convertible debentures was split such that in the first stage, the value of the liability was defined, based on the value of similar liabilities without a conversion right and the proceeds attributed to the equity component was set as a residual value. The proceeds of the issuance amounted to NIS 253 million (after offsetting issuance expenses of NIS 2 million). Of this amount, NIS 247 million (net of issuance expenses) was attributed to the liability component of the debentures and the other NIS 7 million (net of issuance expenses) was attributed to the conversion options and recognized directly in the Company's equity. The effective interest for the debt component is 5.8% per year. At December 31, 2011, the balance of the convertible debentures was presented under short-term credit from banks and others.

NOTE 27 – OTHER DEBENTURES

A. Composition:

	Effective weighted interest	Weighted interest rate	December 31	
		December 31, 2011	2011	2010
	%	%	NIS million	
CPI-linked debentures				
Debentures issued by the Company	5.1	5.0	5,408	5,547
Debentures issued by subsidiaries *)	5.2	5.1	4,309	4,681
Unlinked debentures				
issued by the Company	7.7	7.9	2,255	1,808
Unlinked debentures issued by subsidiaries	5.8	5.8	1,044	810
Debentures linked to GBP issued by subsidiaries	7.5	7.5	861	-
Debentures linked to the US dollar, issued by subsidiaries	6.3	6.1	778	516
			14,655	13,362
Less - current maturities			(1,414)	(1,245)
			13,241	12,117

Notes to the Consolidated Financial Statements

NOTE 27 – OTHER DEBENTURES (CONTD.)

B. Additional details about issuances in 2011

1. In July 2011, the Company issued 178,503 units. Each unit comprises the following: NIS1,000 par value Debentures (Series O) and five Warrants (Series 16), exercisable for NIS 100 par value Debentures (Series O) by September 6, 2011. These debentures and option warrants are listed for trading. The Company issued a total of NIS 178,503,000 par value Debentures (Series O) and 892,515 Warrants (Series 16). The debentures are repayable in three equal payments, on October 18 of each of the years 2015 to 2017. The debentures bear annual interest at a rate of 8.5%, payable twice a year on April 18 and October 18 each year. The consideration of the issuance amounted to NIS 184 million (after offsetting issuance expenses of NIS 2 million). The amounts attributable to the option warrants are insignificant. The effective annual interest rate of the debentures is 8.3%.

The Company also issued 262,340 units, as follows: NIS 1,000 par value Debentures (Series R) and five Warrants (Series 17), exercisable for NIS 100 par value Debentures (Series R) by September 6, 2011. These debentures and option warrants are listed for trading. The Company issued a total of NIS 262,340,000 par value Debentures (Series R) and 1,311,700 Warrants (Series 17). The debentures are linked to the CPI and are payable in six equal annual payments on October 31 of each of the years 2016 and 2017 and 2019 to 2022. The debentures bear fixed annual interest at a rate of 6.1%, payable twice a year on April 30 and October 31 each year. The consideration of the issuance amounted to NIS 285 million (gross) (issuance expenses amounted to NIS 2 million). The amounts attributable to the option warrants are insignificant. The effective annual interest rate of the debentures is 5.9%.

2. In November 2011, the Company issued NIS 258 million par value Debentures (Series O) in a private placement. Debentures (Series O) are listed for trading and are repayable in three equal payments, on October 18 of each of the years 2015 to 2017. The debentures bear annual interest at a rate of 8.5%, payable twice a year on April 18 and October 18 each year. The consideration for the issuance amounted to NIS 261 million (issuance expenses amounted to insignificant sums).

C. **Repayment dates subsequent to the balance sheet date:**

	December 31
	2011
	NIS million
First year (current maturities)	1,414
Second year	1,609
Third year	1,483
Fourth year	1,516
Fifth year	1,776
Sixth year and onwards	6,857
	14,655

D. **See 33 below for information about collateral.**

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS

A. Financial risk factors

The Group's activities expose it to various financial risks, such as market risk (including currency risk, CPI risk, interest risk, and price risk), credit risk and liquidity risk. The Group's comprehensive risk management plan focuses on measures to minimize possible negative effects on the financial performance of the Group. The Group uses derivative financial instruments to hedge against exposure to certain risks.

See section E below for financial risks of insurance companies.

1. Exchange rate risk

The Group is exposed to exchange rate risk due to exposure to various currencies, such as the dollar, euro, and sterling. The exchange rate risk is due to future commercial transactions (including purchase of goods in foreign currency), recognized assets and liabilities denominated in foreign currency other than the functional currency of the Company and net investments in foreign operations.

The Group companies enter into transactions involving derivative financial instruments, from time to time, such as forward transactions and options to hedge their exposure to exchange rate fluctuation.

As of the balance sheet date, subsidiaries were involved in the following open transactions:

	<u>Scope of transactions</u> <u>NIS millions</u>
<u>Agreements for forward transactions</u>	
Purchase of dollar for shekel	728
<u>Foreign currency options purchased</u>	
Purchase of dollar for euro	84
<u>Foreign currency options written</u>	
Purchase of shekel for dollar	32
	<u>844</u>

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

The fair value of the transactions and their carrying amount at December 31, 2011 reflect a net liability of NIS 9 million.

Most of the transactions are for a period of up to one year, and are not recognized as hedging transactions for accounting purposes.

Risk factor	Gain (loss) from the change			
	2011		2010	
	Increase of 5%	Decrease of 5%	Increase of 5%	Decrease of 5%
	NIS million			
NIS/USD exchange rate	11	(11)	63	(63)
NIS/other currency exchange rate	1	(1)	2	(2)
Foreign currency/foreign currency exchange rates	5	(5)	(27)	27

2. CPI risk

The Group has bank loans and debentures linked to changes in the CPI. In addition, the Group has provided loans that are linked to changes in the CPI.

A subsidiary entered into a transaction for the acquisition of 900 million index units for NIS 939 million. In addition, the subsidiary entered into transactions for the sale of 100 million index units for NIS 103 million. The fair value at the balance sheet date reflects a liability of NIS 4 million.

An increase of 2% in the CPI will result in a loss of NIS 196 million (in 2010, NIS 121 million) and a decrease of 2% in the CPI will lead to a similar profit.

3. Credit risk

The Group holds cash and cash equivalents, short- and long-term investments and other financial instruments in various financial institutions in Israel and abroad on the highest level.

Group revenues are composed of large number of customers. Trade receivables include a limited number of customers that generally have a significant debt balance. The Group has no collateral for most of the trade receivables and loans.

The subsidiaries assess trade receivables regularly and the financial statements include provisions for doubtful accounts which properly reflect, in the estimate of the subsidiaries, the loss in debts for which collection is uncertain.

See section E below for information about credit risk in the insurance sector.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

4. Liquidity risk

The table below presents the repayment dates of the Group's financial liabilities in accordance with the contractual terms, undiscounted.

December 31, 2011

	<u>Up to 1 year</u>	<u>1-2 years</u>	<u>2-3 years</u>	<u>3-4 years</u>	<u>4-5 years</u>	<u>Over 5 years</u>	<u>Total</u>
	<u>NIS million</u>						
Short-term credit	3,269	-	-	-	-	-	3,269
Long-term loans from banks	1,171	1,103	423	631	900	1,593	5,821
Trade payables	4,690	-	-	-	-	-	4,690
Tax and other payables	3,321	-	-	-	-	-	3,321
Other debentures	1,767	2,039	1,966	2,003	1,878	6,475	16,128
Debentures convertible into Company shares	266	-	-	-	-	-	266
Guarantees for associates	209	-	-	-	-	-	209
Derivative instruments	29	19	14	14	14	-	90
	<u>14,722</u>	<u>3,161</u>	<u>2,403</u>	<u>2,648</u>	<u>2,792</u>	<u>8,068</u>	<u>33,794</u>

December 31, 2010

	<u>Up to 1 year</u>	<u>1-2 years</u>	<u>2-3 years</u>	<u>3-4 years</u>	<u>4-5 years</u>	<u>Over 5 years</u>	<u>Total</u>
	<u>NIS millions</u>						
Short-term credit	1,710	-	-	-	-	-	1,710
Long-term loans from banks	847	658	772	301	744	2,015	5,337
Trade payables	2,277	-	-	-	-	-	2,277
Tax and other payables	3,890	-	-	-	-	-	3,890
Other debentures	1,491	1,893	1,782	1,648	1,530	6,217	14,561
Debentures convertible into Company shares	10	266	-	-	-	-	276
Derivative instruments	36	27	47	13	-	-	123
	<u>10,261</u>	<u>2,844</u>	<u>2,601</u>	<u>1,962</u>	<u>2,274</u>	<u>8,232</u>	<u>28,174</u>

5. Interest rate risk

The Company and its investees have shekel loans at variable interest, therefore the Group is exposed to changes in interest rates in Israeli banks. Some of the Group companies took loans at variable interest at foreign interest rates, therefore they are exposed to changes in interest rates in those countries. Changes in interest rates in Israel and the USA could have an adverse effect on the yields of the convertible securities portfolios of insurance companies held by subsidiaries, which provide collateral for insurance liabilities.

The table below describes the impact on pre-tax profit and on equity (if there is no effect on pre-tax profit), following possible changes in market interest rates in respect of financial instruments bearing interest at a variable rate.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

<u>Risk factor</u>	Effect on earnings (loss)		Effect on capital	
	2011		2011	
	Increase of 0.5%	Decrease of 0.5%	Increase of 0.5%	Decrease of 0.5%
	NIS million			
USD interest	(62)	57	-	-
EUR interest	(4)	4	10	(11)

The Group companies carry out interest rate swap transactions to reduce exposure. The open transactions at the date of the balance sheet are as follows:

Delek Benelux entered into a number of interest rate swap transactions. At December 31, 2011, the transactions amount to EUR 142 million, for which Delek Benelux pays average effective interest of 2.84% (in 2010, 2.72%).

These swap transactions are partially accounted for as accounting hedge transactions. The fair value of the transactions at December 31, 2011 reflects a liability of EUR 21.1 million.

In the reporting period, Delek US entered into interest swap transactions for USD 160 million (NIS 594 million), which mature in 2015. These transactions were not accounted for as an accounting hedge in the financial statements. In the reporting period, finance expenses of USD 4.2 million (approximately NIS 15 million) were included in the financial statements.

In addition, Delek US enters into forward contracts for the purchase of fuels and future contracts to fix the purchase price of crude oil and the selling price of the fuel distillates inventory.

6. Price risk

The Group has investments in marketable financial instruments on the TASE, shares and debentures, classified as available-for-sale and financial assets measured at fair value through profit or loss, and other financial instruments, for which the Group is exposed to changes in fair value based on the market price on the TASE.

For the impact of the price risk on insurance subsidiaries in Israel, see section E below.

The table below presents the impact of possible changes on market prices of securities on pre-tax profit and on capital (with the exception of insurance subsidiaries in Israel).

<u>Risk factor</u>	Effect on earnings (loss)				Effect on capital			
	2011		2010		2011		2010	
	Price increase of 10%	Price decrease of 10%	Price increase of 10%	Price decrease of 10%	Price increase of 10%	Price decrease of 10%	Price increase of 10%	Price decrease of 10%
	NIS million							
Share security price	47	(47)	80	(80)	250	(250)	199	(199)

*) Assuming there is no impairment of available-for-sale securities

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

7. Transactions of oil, fuels and gas prices

The table below presents the impact of possible changes in the prices of oil, fuels and gas on pre-tax profit:

<u>Risk factor</u>	Gain (loss) from the change			
	2011		2010	
	Price increase of 20%	Price decrease of 20%	Price increase of 20%	Price decrease of 20%
	NIS million			
Oil and fuel price	472	(472)	167	(167)

8. Main assumptions used in calculation of sensitivity tests

The changes selected in the relevant risk variables were based on management assessments of the reasonable changes that are likely to occur in these risk variables.

The Company performed sensitivity tests for the main market risk factors that might affect the operating results or financial position. The sensitivity analyses present the profit or loss and/or change in equity (before tax) for each financial instrument in respect of the relevant risk variable for each reporting date. Risk factors are tested on the basis of the significance of the exposure of the operating results or financial position of each risk factor in relation to the functional currency and assuming that all the other variables are constant.

The risk is not exposed to interest risk in loans at fixed interest. For loans at fixed interest, the sensitivity test for interest risk will only be performed on the variable component in the interest. Sensitivity tests for marketable investments with a quoted market price (TASE price) were based on possible changes in these market prices.

Sensitivity tests for options were generally based on the Black and Scholes model.

B. Fair value

The table below describes the balance in the financial statements and the fair value of groups of financial instruments, presented in the financial statements, not on the basis of fair value.

	Carrying amount		Fair value	
	December 31		December 31	
	2011	2010	2011	2010
	NIS million			
<u>Financial liabilities</u>				
Long-term loans	5,210	3,108	4,593	2,899
Convertible debentures	252	248	254	265
Debentures	11,702	10,669	11,225	11,043
Total	17,164	14,025	16,072	14,207

The carrying amount of financial instruments such as cash and cash equivalents, short-term investments, trade receivables, other receivables, loans to associates, long-term loans extended, borrowings from banks and others, liabilities to trade payables and other payables is equal to or approximates their fair value.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

C. Classification of financial instruments according to fair value level

The financial instruments presented in the statements at fair value are classified into groups with similar characteristics. The fair value level set out below is determined according to the inputs used to determine fair value:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities
 Level 2: Inputs other than quoted prices included within Level 1 that are observable, either directly or indirectly
 Level 3: Inputs that are not based on observable market data (unobservable inputs) (assessment without using observable market inputs).

Financial assets measured at fair value

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
	<u>NIS million</u>		
<u>December 31, 2011</u>			
Financial assets at fair value through profit or loss			
Shares	58	-	-
Debentures	315	-	-
Marketable forward contracts	4	14	-
Foreign currency forward contracts	1	7	-
Available-for-sale financial assets:			
Shares	3	-	80
Debentures	412	-	-

Financial liabilities measured at fair value

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
	<u>NIS million</u>		
<u>December 31, 2011</u>			
Financial liabilities at fair value through profit or loss			
Embedded derivatives	-	-	1
Liabilities for share-based payment	-	151	-
Other liabilities	-	1	-
Foreign currency forward contracts	-	4	-
Interest forward contracts	-	125	-
Marketable forward contracts	-	5	-

Level 3 financial assets

	<u>Available-for-sale financial assets</u>
	<u>NIS million</u>
<u>Balance as of January 1, 2011</u>	328
Total profit recognized in other comprehensive income	4
Dispositions in the year	(243)
Exchange differences on translation of foreign operations	9
<u>Balance as of December 31, 2011</u>	<u>80</u>

In 2011, there were no transfers between the different fair value levels.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

D. Linkage of monetary balances

	December 31, 2011																
	Israeli currency		Foreign currency					Monetary items of foreign operations									
	Unlinked	CPI-linked	USD	JPY	EUR	Other currency	Fair value	Performance-based	USD	CAD	GBP	EUR	Other currency	Non-monetary	ETFs	Total	
Cash and cash equivalents	1,436	-	424	4		5		-	1,227	-	9	505				3,610	
Performance-based cash and cash equivalents in companies	-	-	-	-	-	-	-	1,276	-	-	-	-	-	-	-	1,276	
Short-term investments in the financial sector	-	80	-	-	-	-	-	-	-	-	-	-	-	15	19,340	19,435	
Short-term investments in insurance companies	-	-	-	-	-	-	-	1,404	313	-	-	-	-	-	-	1,717	
Other short-term investments	-	-	201	-	-	-	412	-	102	-	-	-	-	-	-	715	
Financial derivatives	-	-	-	-	-	-	15	-	-	-	-	-	-	-	-	15	
Trade receivables	1,641	-	158	1	-	4	-	-	1,172	-	32	1,174	-	-	-	4,182	
Insurance premium receivable	-	-	-	-	-	-	-	584	377	-	-	-	-	-	-	961	
Other receivables	263	9	349	-	1	8	-	201	299	-	9	54	-	-	4	1,197	
Current tax assets	-	-	-	-	-	-	-	61	9	-	-	18	-	-	-	88	
Reinsurance assets	-	-	-	-	-	-	-	459	1,457	-	-	-	-	-	-	1,916	
Inventories	-	-	-	-	-	-	-	-	136	-	-	-	-	2,905	-	3,041	
Deferred acquisition costs in insurance companies	-	-	-	-	-	-	-	269	159	-	-	-	-	-	-	428	
Financial investments of insurance companies	-	-	-	-	-	-	-	32,666	1,747	-	-	-	-	-	-	34,413	
Long-term loans, deposits and receivables	74	79	324	-	-	-	20	5	186	-	-	49	-	-	21	758	
Investments in other financial assets	-	-	-	-	-	-	500	-	-	-	-	-	-	-	-	500	
Investments in associates and partnerships	89	133	-	-	-	-	-	164	-	-	-	7	-	1,940	-	2,333	
Investment property	-	-	-	-	-	-	-	481	5	-	-	-	-	74	-	560	
Investments in oil and gas exploration and production	-	-	-	-	-	-	-	-	1,902	-	-	-	-	9,561	-	11,463	
Reinsurance assets	-	-	-	-	-	-	-	899	759	-	-	-	-	-	-	1,658	
Property, plant and equipment, net	-	-	-	-	-	-	-	326	219	-	-	-	-	9,065	-	9,610	
Deferred acquisition costs in insurance companies	-	-	-	-	-	-	-	761	-	-	-	-	-	-	-	761	
Structured bonds	-	-	-	-	-	-	-	-	-	-	-	-	-		736	736	
Goodwill	-	-	-	-	-	-	-	798	232	-	-	-	-	2,677	-	3,707	
Other intangible assets, net	-	-	-	-	-	-	-	-	70	-	-	-	-	2,470	-	2,540	
Deferred taxes	-	-	-	-	-	-	-	10	106	-	-	-	-	164	-	280	
Total assets	3,503	301	1,456	5	1	17	947	40,364	10,477	-	50	1,807	-	28,871	20,101	107,900	

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

	December 31, 2011																
	Israeli currency		Foreign currency					Monetary items of foreign operations									
	Unlinked	CPI-linked	USD	JPY	EUR	Other currency	Fair value	Performance-based	USD	CAD	GBP	EUR	Other currency	Non-monetary	ETFs	Total	
Liabilities																	
Interest bearing loans and borrowings	1,878	865	1,379	-	-	-	-	-	1,800	-	244	289	-	-	-	6,455	
Trade payables	216	-	584	-	1	2	-	-	3,230	-	64	662	-	-	-	4,758	
Other payables	697	780	358	-	-	-	191	818	1,031	-	81	1,292	-	1	-	5,249	
Exchange-traded funds and deposit	-	-	-	-	-	-	-	-	-	-	-	-	-	-	18,962	18,962	
Tax liabilities	11	5	-	-	-	-	-	4	-	-	-	10	-	-	-	30	
Financial derivatives	-	-	-	-	-	-	7	-	-	-	-	8	-	-	-	15	
Insurance reserves and outstanding claims	-	-	-	-	-	-	-	3,507	-	-	-	-	-	-	-	6,032	
Loans from banks and others	518	510	120	-	-	-	-	-	2,525	-	-	-	-	-	-	4,331	
Other debentures	3,167	6,800	175	-	-	-	-	1,836	1,199	-	70	1,914	-	-	-	13,241	
Structured bonds				-	-	-	-	-	445	-	818	-	-	-	-	735	
Financial derivatives		-	-	-	-	-	-	-	-	-	-	102	-	-	735	102	
Liabilities for employee benefits, net	6	-	-	-	-	-	-	115	94	-	-	-	-	59	-	274	
Insurance reserves and outstanding claims	-	-	-	-	-	-	-	32,983	1,215	-	-	-	-	-	-	34,198	
Provisions and other liabilities	16	194	67	-	-	-	-	210	285	-	-	246	-	2	-	1,020	
Deferred taxes	-	-	-	-	-	-	-	181	3	-	-	-	-	1,224	-	1,408	
Total liabilities	6,508	9,154	2,683	-	1	2	198	39,654	11,827	-	1,277	4,523	-	1,286	19,697	96,810	
Equity balance, net	(3,005)	(8,853)	(1,227)	5	-	15	749	710	(1,350)	-	(1,227)	(2,716)	-	27,585	404	11,090	

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

E. Market risks in insurance companies

Revenue from investments arising from performance based portfolios and nostro portfolios have a material impact on the Company's profits. The extent of the impact on profits depends on the characteristics of the insurance liabilities (nostro and profit participating) and the conditions of the management fees in products for which the relevant reserve is held.

1. Performance based contracts

In profit participating policies issued from 2004 onwards, all yields from investments are allocated to the policyholders and the insurer is eligible to fixed management fees at the rate of 1-2%, depending on the track. For these products, the impact of the yields on the profits of the insurance company is reduced to exposure derived from the total scope of the reserve from which the insurer's management fees are derived.

In profit participating policies issued up until December 31, 2003, the yield from the investment is allocated to the policyholders and the insurer is eligible to fixed management fees at the rate of 0.6% of the accruals and variable management fees of 15% of the real profit achieved after deducting the fixed management fees. In these products, in addition to the exposure derived from the amount of the accumulation, there is an impact on the Company's profits as a result of the rate of the variable management fees derived in accordance with the real yields allocated to the policyholders.

In pension and provident funds business, yields from investments (net of fixed management fees) are allocated to the members. Therefore, the impact of the results of the investment on the profits of the company managing the pension or provident funds is based on the total scope of the accrued amount from which the management fees for the management company is derived.

Regarding the assets and liabilities for these products, the insurance company does not have direct exposure for changes in interest, fair value of investments or the CPI. The effect of the financial results on the insurance company's profits is reduced to exposure derived from variable management fees based on yields recognized for policyholders, which applies only to policies issued before 2004, and from all the liabilities on which the insurer's fixed management fees are based for all the performance-based products.

In view of the aforesaid, the sensitivity tests and maturity dates of the liabilities set forth below do not include performance based contracts.

Below is a sensitivity test for performance based contracts and the effect of any change in yield on profit (loss).

Any change of 1% in the real yield on the investments according to performance-based contracts for policies issued up to 2004, with liabilities of NIS 16.4 billion in their respect as of December 31, 2011, affects management fees in the amount of NIS 25 million and fixed management fees in the amount of NIS 1 million. The effect of the change on policies issued from 2004 onwards is not material.

When the yield of these contracts is negative, the Company does not collect management fees and is not able to collect them until a positive yield is achieved that will cover the accrued negative yield. Therefore, the change of 1% in the real yield will not be reflected in the statements of income, except to the extent of the amount of the remaining debt to be covered.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

2. Sensitivity tests relating to market risks for non-performance based contracts

The tables below describe the sensitivity tests presenting the change in profit (loss) and equity for the financial assets, the financial liabilities and the liabilities for insurance and investment contracts for the relevant risk variable as of each reporting date, assuming that all the other variables are fixed. These sensitivity tests do not include, as mentioned, the impact of performance based contracts as described above. The changes in the variables are in relation to the carrying amount of the assets and liabilities. In addition, it was assumed that the changes do not reflect permanent impairment of assets stated at reduced cost or available-for-sale assets, therefore, in the sensitivity tests, impairment losses were not included for these assets.

The sensitivity tests reflect direct impacts only, without secondary impacts.

It is noted that the sensitivities are not linear, hence larger or smaller changes in relation to the changes described below are not necessarily simple extrapolation of the impact of the changes.

At December 31, 2010 (The Phoenix)

	Interest rates (1)		Investment in equity instruments		Change in CPI		Change in foreign currency exchange rate	
	+1%	-1%	+10%	-10%	+1%	-1%	+10%	-10%
	NIS million							
Profit (loss)	30	(34)	9	(9)	(20)	20	(87)	87
Comprehensive income (loss) (3)	(65)	61	78	(78)	(20)	20	(49)	49

As of December 31, 2010 (The Phoenix)

	Change in interest rate		Investment in equity instruments		Change in CPI		Change in exchange rate USD 1	
	+ 1%	- 1%	+ 10%	- 10%	+ 1%	- 1%	+ 10%	- 10%
	NIS million							
Profit (loss)	32	(25)	6	(6)	(26)	26	(37)	37
Comprehensive income (loss) (3)	(68)	75	54	(54)	(26)	26	(8)	8

- (1) The sensitivity analysis to change in interest refers to fixed interest instruments and variable interest instruments. For instruments at fixed interest, the exposure is for the carrying amount of the instrument and for variable interest instruments the exposure is for cash flows from the instrument. The Company performs adequacy tests for yield-guaranteed life assurance reserves against the value of the portfolio. The sensitivity to a decrease in the interest rate of 1% from the value of the reduction in the value of the portfolio against this reserves in the amount of NIS 81 million, net of tax.
- (2) Investment in instruments that have no fixed cash flow, or the Company has no information about this cash flow (according to IFRS 7, this does not include investments in associates).
- (3) The sensitivity analysis for comprehensive income (loss) also reflects the effect of profit (loss) for the period.
- (4) In the sensitivity test for the CPI and currency, non-monetary items were also taken into account, according to the directives of the Supervisor.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

3. Liquidity risk

Liquidity risk is the risk that the Company will be required to dispose of its assets at an inferior price in order to meet its liabilities.

- A) The Phoenix is exposed to risks arising from uncertainty regarding the date the Company will be required to pay claims and other benefits to policyholders in respect of the scope of finances that will be available at that date. However, a significant part of its insurance liabilities in the life assurance sector are not exposed to liquidity risk due to the nature of the insurance contracts as described below.
- B) It is noted, however, that a possible unexpected requirement to raise funds in a short time could require significant disposal of assets within a short time, at prices that do not necessarily reflect their market value.
- C) Performance-based contracts in life assurance: In accordance with the conditions of the contracts, the policyholders are entitled to receive the value of the investments, and no more. Therefore, if the value of the investments falls for any reason, there will be a corresponding decrease in the level of the Company's liabilities.
- D) Non-performance based contracts in life assurance: 34% of the life assurance portfolio is for non-performance based contracts, however they guarantee an agreed yield. These contracts are mainly hedged by designated bonds (Hetz (life linked bonds) issued by the Bank of Israel. The Company may exercise these bonds when these policies are called for redemption.
- E) The Phoenix's liquidity risk is mainly due to the assets balance that are not designated bonds and are not against performance based contracts. These assets represent 59% only (NIS 38 billion) out of all the assets of The Phoenix.
Out of the aforementioned balance of assets, NIS 5 billion are marketable assets that can be sold immediately. NIS 20 billion are held against holders of benchmark certificates, exchange traded funds, reverse certificates, complex certificates and certificates of deposit. In accordance with the investment directives, the Company is required to hold liquid assets (government bonds or cash and cash equivalents) amounting to at least 15% of the required capital.

4. Management of assets and liabilities

The tables below summarize the estimated maturity dates of the Company's non-discounted insurance and financial liabilities. As the amounts are not discounted, there is no correlation between them and the balance of the insurance and financial liabilities in the balance sheet.

The estimated maturity dates of the life assurance and health insurance liabilities are included in the tables as follows:

Savings: contractual maturity dates, in other words, retirement age, without assumed cancellations, and assuming the savings will be withdrawn as a lump-sum and not as an annuity.

Annuity for payment, disability income insurance for payment, and long term care for payment – based on an actuarial estimate.

Other – reported under "Without a defined maturity date".

The estimated payment dates of gross general insurance liabilities are based on an actuarial estimate that assigns an estimated date to the total undiscounted liabilities according to claim payment experience.

Total liabilities include provisions for expected deviations and an unearned premium reserve less deferred acquisition cost.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

The maturity dates of financial liabilities and liabilities for investment contracts were included on the basis of the contractual maturity dates. In contracts in which the other party has the right to choose the date for payment of the amount, the liability is included on the basis of the earliest date that the Company can be asked to pay the liability.

Liabilities for life assurance and health insurance contracts (The Phoenix)

	<u>Up to 1 year</u>	<u>1-5 years</u>	<u>5-10 years</u>	<u>10-15 years</u>	<u>More than 15 years</u>	<u>No defined repayment date</u>	<u>Total</u>
	<u>NIS million</u>						
December 31, 2011	1,759	3,728	3,162	1,373	1,489	627	12,138
December 31, 2010	1,606	3,222	3,250	1,390	1,709	588	11,765

*) Not including performance based contracts

Liabilities for general insurance contracts **) (The Phoenix)

	<u>1-3 years</u>	<u>3-5 years</u>	<u>More than 5 years</u>	<u>No defined repayment date</u>	<u>Total</u>
	<u>NIS million</u>				
December 31, 2011	2,691	787	919	300	4,697
December 31, 2010	2,628	770	894	254	4,546

Financial liabilities and liabilities for investment contracts

	<u>Up to 1 year</u>	<u>1-5 years</u>	<u>5-10 years</u>	<u>10-15 years</u>	<u>More than 15 years</u>	<u>Total</u>
	<u>NIS million</u>					
December 31, 2011						
Financial liabilities	1,339	1,225	1,293	216	-	4,073
Liabilities for investment contracts	2	8	1	1	-	12
Liabilities for performance based investment contracts	418	-	-	-	-	418
Liability for contingent consideration and provision for payment for the option to acquire an investee	164	195	38	-	-	397
At December 31, 2010:						
Financial liabilities	1,580	1,176	1,486	216	-	4,458
Liabilities for investment contracts	4	8	4	-	-	16
Liabilities for performance based investment contracts	390	-	-	-	-	390
Liability for contingent consideration and provision for payment for the option to acquire an investee	130	328	130	-	-	588

*) Liabilities up to one year include NIS 418 million (December 31, 2009, NIS 390 million) repayable on demand. These liabilities were classified as repayable up to one year, even though the actual repayment dates could be later.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

5. Credit risks - Debt assets by rating

Debt assets of insurance companies in Israel

	Local rating *)				
	December 31, 2011				
	A or higher	A to BBB	Lower than BBB NIS million	Unrated	Total
<u>Marketable debt assets</u>					
Government bonds	3,195	-	-	-	3,195
Corporate debentures	911	701	8	20	1,640
Total marketable debt assets in Israel	4,106	701	8	20	4,835
<u>Non-marketable debt assets</u>					
Government bonds	5,286	-	-	-	5,286
Corporate debentures	561	597	27	5	1,190
Deposits in banks and institutions	850	1	-	-	851
Other debt assets according to securities:					
Mortgages	-	-	-	74	74
Loans on policies	127	-	-	-	127
Loans pledged by real estate	-	100	-	-	100
Other securities	260	386	6	30	682
Unsecured	19	-	121	49	189
Total non-marketable debt assets in Israel	7,103	1,084	154	158	8,499
Total debt assets in Israel	11,209	1,785	162	178	13,334
Of which – debt assets with internal rating	483	794	135	-	1,412

*) Each rating includes all the ranges, for example: A includes A- to A+.

Debt assets abroad

	International rating *)				
	December 31, 2011				
	A or higher	A to BBB	Lower than BBB	Unrated	Total
	NIS million				
<u>Debt assets abroad</u>					
Government bonds	7	8	-	6	21
Corporate debentures	-	15	1	10	26
Total marketable debt assets abroad	7	23	1	16	47
<u>Non-marketable debt assets</u>					
Mortgages	-	-	-	-	-
Loans pledged by real estate	-	-	17	3	20
Loans in other securities	-	-	-	19	19
Total unmarketable debt assets abroad	-	-	17	22	39
Total debt assets abroad	7	23	18	38	86
Of which – debt assets with internal rating	-	-	18	-	18

*) Each rating includes all the ranges, for example: A includes A- to A+.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

Debt assets of insurance companies in Israel

	Local rating *)				
	December 31, 2010				
	A or higher	A to BBB	Lower than BBB	Unrated	Total
	NIS million				
<u>Marketable debt assets</u>					
Government bonds	3,164	-	-	-	3,164
Corporate debentures	894	654	12	16	1,576
Total marketable debt assets in Israel	4,058	654	12	16	4,740
<u>Non-marketable debt assets</u>					
Government bonds	5,155	-	-	-	5,155
Corporate debentures	446	605	36	-	1,087
Deposits in banks and institutions	917	22	-	-	939
Other debt assets according to securities:					
Mortgages	-	-	-	80	80
Loans on policies	-	-	-	119	119
Loans pledged by real estate	-	19	-	-	19
Other securities	277	200	3	34	514
Unsecured	-	-	127	57	184
Total non-marketable debt assets in Israel	6,795	846	166	290	8,097
Total debt assets in Israel	10,853	1,500	178	306	12,837
Of which – debt assets with internal rating	359	308	27	-	694

*) Each rating includes all the ranges, for example: A includes A- to A+.

Debt assets abroad

	International rating *)				
	December 31, 2010				
	A or higher	A to BBB	Lower than BBB	Unrated	Total
	NIS million				
<u>Debt assets abroad</u>					
Corporate debentures	6	14	8	1	28
Total marketable debt assets abroad	6	14	8	1	28
<u>Non-marketable debt assets</u>					
Mortgages	-	6	-	-	6
Loans pledged by real estate	-	22	16	-	38
Loans in other securities	-	3	-	-	3
Total unmarketable debt assets abroad	-	31	16	-	47
Total debt assets abroad	6	45	24	1	76
Of which – debt assets with internal rating	-	32	16	-	48

*) Each rating includes all the ranges, for example: A includes A- to A+.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

Credit risks for other assets (in Israel)

	Local rating *)			
	December 31, 2011			
	A or higher	A to BBB	Lower than BBB	Total
	NIS million			
Loans to associates	-	-	-	187
Other receivables, other than balances from reinsurers	-	-	-	234
Deferred tax assets	-	-	-	28
Other financial investments	237	4	10	305
Cash and cash equivalents	1,136	-	-	1,136

*) Each rating includes all the ranges, for example: A includes A- to A+.

	Local rating *)			
	December 31, 2010			
	AA or higher	A to BBB	Lower than BBB	Total
	NIS million			
Loans to associates	-	-	-	187
Other receivables, other than balances from reinsurers	-	-	-	308
Deferred tax assets	-	-	-	23
Other financial investments	115	12	2	172
Cash and cash equivalents	1,092	-	-	1,092

*) Each rating includes all the ranges, for example: A includes A- to A+.

Credit risks for non-equity instruments (in Israel)

	Local rating *)			
	December 31, 2011			
	AA or higher	A to BBB	Lower than BBB	Total
	NIS million			
Unused credit facilities	40	-	-	40

	Local rating *)			
	December 31, 2010			
	A or higher	A to BBB	Lower than BBB	Total
	NIS million			
Unused credit facilities	-	-	-	-

*) Each rating includes all the ranges, for example: A includes A- to A+.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

Credit risks for other assets (in other countries)

	International rating *)			
	December 31, 2011			
	A or higher	A to BBB	Lower than BBB	Unrated
	NIS million			
Other financial investments	314	7	-	112
	433			

	International rating *)			
	December 31, 2010			
	AA or higher	A to BBB	Lower than BBB	Unrated
	NIS million			
Other financial investments	222	5	-	81
	308			

*) Each rating includes all the ranges, for example: A includes A- to A+.

Debt assets of insurance companies abroad

	International rating			
	December 31, 2011			
	A or higher	A to BBB	Lower than BBB	Unrated
	NIS million			
Marketable debt assets	-	-	-	-
Government bonds	100	-	-	-
Corporate debentures	1,590	70	137	-
Total marketable debt assets abroad	1,690	70	137	-
Non-marketable government bonds	-	-	-	-
Total debt assets abroad	1,690	70	137	-

Debt assets of insurance companies abroad

	International rating			
	December 31, 2010			
	AA or higher	A to BBB	Lower than BBB	Unrated
	NIS million			
Marketable debt assets	106	-	-	-
Government bonds	1,054	82	156	21
Corporate debentures	-	-	-	-
Total marketable debt assets abroad	1,160	82	156	21
Non-marketable government bonds	-	-	-	-
Total debt assets abroad	1,160	82	156	21

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)**6. Exposure to credit risks of reinsurers**

The insurance companies insure some of their business affairs with reinsurance, mainly through reinsurers abroad. However, reinsurance does not exempt the direct insurers of their liability towards the policyholders according to the insurance policies.

The insurance companies are exposed to risks due to uncertainty regarding the ability of the reinsurers to pay their share of the liabilities for insurance contracts (reinsurance assets) and their liabilities for claims paid. This exposure is managed by ongoing monitoring of the situation of the reinsurer in the global market and compliance with its financial obligations.

The Phoenix is exposed to credit risk to a single reinsurer, due to the structure of the reinsurance market and the limited number of reinsurers with an adequate rating.

According to the directives of the Commissioner, the board of directors of The Phoenix determines, once a year, the maximum exposure for reinsurers, based on international rating. The Phoenix manages these exposures by individual evaluation of each of the reinsurers. In addition, the exposures of The Phoenix are dispersed amount different reinsurers, generally reinsurers with high international rating.

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

December 31, 2011:

In the financial statements of insurance companies in Israel

<u>Name of reinsurer</u>	Total premiums for reinsurers in 2011	Debit (credit) balance, net	Reinsurance assets					Total exposure	Debts in arrears	
			Life assurance *)	Health insurance	Property insurance	Liability insurance	Reinsurer deposits		6-12 months	More than one year
			NIS million							
AA or higher										
Munich Reinsurance Co AG	114	3	20	141	26	59	117	131	-	-
Swiss Reinsurance Co,	79	1	91	21	45	123	69	212		
General Reinsurance AG	79	4	29	111	-	47	29	164	-	-
Other	77	3	4	-	69	69	26	120	-	-
Total	349	11	144	273	140	298	241	627	-	-
A										
Lloyd's	57	(17)	-	-	25	82	-	90	-	-
Other	248	(7)	9	-	197	144	78	265	-	-
Total	305	(24)	9	-	222	226	78	355	-	-
BBB	-	-	-	-	-	-	-	-	-	-
Lower than BBB or unrated	1	(1)	1	-	3	41	-	44	1	-
Total	655	(14)	154	273	365	565	319	1,026	1	-

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

December 31, 2011:

In the financial statements of insurance companies abroad

	Total reinsurance premiums in 2011	Current credit net balances	Reserves for unexpired risks	Outstanding claims		Reinsurer deposits	Total exposure (a)	Current debts in arrears included in open balances 6-12 months
				Assets	Liabilities			
				NIS million				
<u>A- and above</u>								
Hartford Fire Insurance Co.	650	-	332	23	325	-	684	-
Others	722	(84)	229	157	818	-	1,116	-
	1,372	(84)	561	180	1,143	-	1,800	-
<u>B and above</u>	134	(57)	50	-	191	-	187	-
<u>Unrated</u>	15	-	-	1	1	-	1	-
<u>Total</u>	1,521	(141)	611	181	1,335	-	1,988	-

(A) The total exposure to reinsurers is the share of reinsurers in insurance reserves and outstanding claims, net of deposits and net of the amount of the credit notes received from the reinsurer to secure their liabilities, plus (less) the net current debit (credit) balance.

(B) The rating was determined by the rating company AM Best.

(C) Republic received credit notes in the amount of NIS 653 million from reinsurers to secure their liabilities

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

In the financial statements of insurance companies in Israel

Name of reinsurer	Total premiums for reinsurers in 2010	Debit (credit) balance, net	Reinsurance assets					Total exposure	Debts in arrears	
			Life assurance *)	Health insurance	Property insurance	Liability insurance	Reinsurer deposits		6-12 months	More than one year
			NIS million							
AA or higher										
GEN RE	82	(3)	28	161	-	-	25	160	-	-
Munich Reinsurance Co AG	108	(11)	19	142	20	148	92	226	-	-
Other	50	1	2	-	46	70	13	107	-	-
Total	240	(13)	49	303	66	218	130	493	-	-
A										
Swiss Reinsurance Co	94	(1)	95	29	52	120	77	217	-	-
Other	290	6	8	-	217	216	71	376	1	-
Total	384	5	103	29	269	336	148	593	1	-
BBB	-	-	1	-	-	-	-	1	-	-
Lower than BBB or unrated	12	(2)	-	-	13	54	3	62	-	-
Total	636	(10)	153	332	348	608	281	1,149	1	-

Notes to the Consolidated Financial Statements

NOTE 28 – FINANCIAL INSTRUMENTS (CONTD.)

December 31, 2010

In the financial statements of insurance companies abroad

	Total reinsurance premiums in 2010	Current credit net balances	Reserves for unexpired risks	Outstanding claims		Reinsurer deposits	Total exposure (a)	Current debts in arrears included in open balances 6-12 months
				Assets	Liabilities			
				NIS million				
<u>A- and above</u>								
Hartford Fire Insurance Co.	657	-	319	25	330	-	678	-
Others	838	(39)	245	138	784	-	1,129	-
	1,495	(39)	564	163	1,114	-	1,807	-
<u>B and above</u>	185	(53)	89	2	117	-	156	-
<u>Unrated</u>	4	4	2	1	2	-	7	-
<u>Total</u>	1,684	(88)	655	166	1,233	-	1,970	-

(A) The total exposure to reinsurers is the share of reinsurers in insurance reserves and outstanding claims, net of deposits and net of the amount of the credit notes received from the reinsurer to secure their liabilities, plus (less) the net current debit (credit) balance.

(B) The rating was determined by the rating company AM Best.

(C) Republic received credit notes in the amount of NIS 580 million from reinsurers to secure their liabilities

Notes to the Consolidated Financial Statements

NOTE 29 – ASSETS AND LIABILITIES FOR EMPLOYEE BENEFITS

Post-employment benefits

Labor laws and the Severance Pay Law in Israel requires the Group companies to pay compensation to employees if they are dismissed or when they retire or to make routine deposits in defined deposit plans under section 14 of the Severance Pay Law, as described below. The liability of the Group companies for this is recognized as a post-employment benefit. The liability of the Group companies for employee benefits is based on the valid labor agreement and the employee's salary, which generate the right for compensation.

Post-employment benefits are usually financed by deposits classified as a defined benefit plan or as a specific deposit plan as described below.

Defined deposit plan

The provisions of section 14 of the Severance Pay Law, 1963 ("the Severance Law") apply to part of the compensation payments, according to which the Group's routine deposits in the pension fund and/or insurance policies exempt it from any other liability towards the employees.

Defined benefit plan

The Group has a defined benefit plan for severance pay under the Severance Pay Law. By law, employees are entitled to compensation if they are dismissed or on demand. The liability for severance is based on the actuarial method.

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS

A. Liabilities for insurance contracts and investment contracts

Non-performance based insurance contracts and investment contracts

	December 31					
	2011	2010	2011	2010	2011	2010
	Gross		Reinsurance		Residual	
			NIS million			
Life assurance and long-term saving						
Insurance contracts	9,150	8,668	103	101	9,047	8,567
Investment contracts	9	12	-	-	9	12
Net of amounts deposited in the Company as part of a defined benefit plan for Group employees	(20)	(22)	-	-	(20)	(22)
Total life assurance and long-term saving	9,139	8,658	103	101	9,036	8,557
Insurance contracts included in the health insurance sector	1,158	1,135	262	321	896	814
Insurance contracts included in the general insurance sector	8,477	8,009	3,026	3,107	5,451	4,902
Total liabilities for non-performance based insurance contracts and investment contracts	18,774	17,802	3,391	3,529	15,383	14,273

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)Performance based insurance contracts and investment contracts

	December 31					
	2011	2010	2011	2010	2011	2010
	Gross		Reinsurance		Residual	
	NIS million					
Life assurance and long-term saving						
Insurance contracts	20,924	20,546	51	52	20,873	20,494
Investment contracts	418	390	-	-	418	390
Net of amounts deposited in the Company as part of a defined benefit plan for Group employees	(66)	(67)	-	-	(66)	(67)
Total life assurance and long-term saving	21,276	20,869	51	52	21,225	20,817
Insurance contracts included in the health insurance sector	181	181	11	11	170	170
Total liability for field defendant insurance contracts and investment contracts	21,457	21,050	62	63	21,395	20,987

B. Liabilities for insurance contracts included in the general insurance sector, by category:

	December 31					
	2011	2010	2011	2010	2011	2010
	Gross		Reinsurance		Residual	
	NIS million					
<u>In Israel</u>						
Compulsory motor insurance	3,709	3,661	565	609	3,144	3,052
Property and other branches	1,027	926	365	348	662	578
Total liabilities for insurance contracts in the general insurance sector	4,736	4,587	930	957	3,806	3,630
Deferred acquisition costs:						
Compulsory motor insurance	42	39	8	6	35	34
Property and other branches	128	114	26	26	102	88
Total	170	153	34	32	137	122
Liabilities for general insurance contracts net of deferred acquisition costs:						
Compulsory motor insurance and liabilities (C1)	3,667	3,622	558	603	3,109	3,018
Property and other branches	899	812	339	322	560	490
Total liabilities for general insurance contracts net of deferred acquisition costs:	4,566	4,434	897	925	3,669	3,508

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

	December 31					
	2011	2010	2011	2010	2011	2010
	Gross		Reinsurance		Residual	
			NIS million			
<u>Abroad</u>						
Total liabilities for insurance contracts in the general insurance sector	1,311	1,434	578	646	733	788
Provisions for outstanding claims						
Motor	790	807	585	659	205	148
Property	263	193	142	122	121	71
Liability	1,377	1,047	791	622	586	425
Total provisions for outstanding claims	2,430	2,047	1,518	1,403	912	644
Total	3,741	3,481	2,096	2,049	1,645	1,432

C. Change in liabilities for insurance contracts included in the general insurance sector, net of deferred acquisition costs:

In Israel

1. Compulsory motor insurance

	December 31					
	2011	2010	2011	2010	2011	2010
	Gross		Reinsurance		Residual	
			NIS million			
Balance at the beginning of the year	3,621	3,455	603	589	3,018	2,866
Cumulative cost of claims for the current underwriting year	550	543	44	40	506	503
Change in carrying amount at the beginning of the year due to linkage to the CPI and investment gains according to the discounting assumption	80	69	10	10	70	59
Change in cumulative cost of claims for prior underwriting years	(172)	(61)	(59)	(46)	(113)	(15)
Total change in cumulative cost of claims	458	551	(5)	4	463	547
Payments to settle claims during the year						
For the current underwriting year	(7)	(8)	(1)	-	(6)	(8)
For prior underwriting years	(450)	(445)	(65)	(49)	(385)	(396)
Total payments for the year	(457)	(453)	(66)	(49)	(391)	(404)
Other	45	68	26	59	19	9
Balance at the end of the year	3,667	3,621	558	603	3,109	3,018

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

1. Opening and closing balances include outstanding claims, provision for short premium, unearned premium reserve, net of deferred acquisition costs.
2. Cost of cumulative claims (ultimate) is the balance of the outstanding claims (non-cumulative), provision to premium deficiency, unearned premium reserve net of deferred acquisition costs with the addition of the total claims payments including direct and indirect expenses to settle claims.
3. The payments include indirect expenses to settle claims (administrative and general recorded in the claims) in relation to the underwriting years.
4. The cumulative cost of claims is adjusted according to the model in view of actual development of the claims.
5. The change in the estimated cumulative cost of the claim for prior underwriting years in 2010 and 2011 is mainly due to motor property.
6. The decrease in gross payments and reinsurance in 2010 is due to compulsory motor insurance.

2. Property and other branches

	December 31					
	2011	2010	2011	2010	2011	2010
	Gross		Reinsurance		Residual	
	NIS million					
Balance at the beginning of the year	812	788	323	295	489	493
Aggregate cost of claims for the reporting year	846	752	223	204	623	548
Change in the aggregate cost of claims for events prior to the reporting year	14	(48)	14	(14)	-	(34)
Payments to settle claims during the year	(598)	(501)	(149)	(88)	(449)	(413)
For events prior to the reporting year	(221)	(195)	(86)	(74)	(135)	(121)
Total payments	(819)	(696)	(235)	(162)	(584)	(534)
Changes in provisions for net unearned premiums from deferred acquisition costs	46	16	14	-	32	16
Balance at the end of the year	899	812	339	323	560	489

1. Opening and closing balances include outstanding claims, provision for short premium, unearned premium reserve, net of deferred acquisition costs.
2. The cumulative cost of claims for events in the reporting year includes the balance of outstanding claims at the end of the reporting year with the addition of total claims payments in the reporting period, including direct and indirect expenses to settle claims.
3. Underwriting payments to settle claims during the year include payments for events prior to the reporting year with the addition of the change in the balance of outstanding claims for events prior to the reporting year.
4. The liabilities for payments to settle claims include direct and indirect expenses to settle claims (general and administrative recorded in the claims) attributed to the damage years.
5. The gross increase in 2011 is mainly due to the engineering branch. The decrease in 2010 is mainly due to a decrease in estimates of the claims in the motor property and property loss branches. The increase in reinsurance in 2011 is mainly due to the engineering branch. The decrease in 2010 is mainly due to the property loss branch.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

Abroad

	December 31					
	2011	2010	2011	2010	2011	2010
	Gross		Reinsurance		Residual	
	NIS million					
Total liabilities for insurance contracts in the general insurance sector at year end	1,311	1,434	578	646	733	788
<u>Change in provisions for claims</u>						
Balance at the beginning of the year	2,047	2,430	1,403	1,518	644	912
Cumulative cost of claims for the current underwriting year	1,957	1,909	1,029	1,251	928	658
Change in estimated cost of claims for prior underwriting years	202	134	52	102	150	32
Total change in cumulative cost of claims	2,159	2,043	1,081	1,353	1,078	690
Payments to settle claims during the years						
For the current underwriting year	1,013	916	472	546	541	370
For prior underwriting years	935	893	602	537	333	356
Total payments for the period	1,948	1,809	1,074	1,083	874	726
Effect of changes in the exchange rate for foreign operations	172	(617)	108	(385)	64	(232)
	2,430	2,047	1,518	1,403	912	644
Balance at the end of the year	3,741	3,481	2,096	2,049	1,645	1,432

D. Liabilities for insurance contracts are presented in the balance sheet as follows:

	December 31	
	2011	2010
	NIS million	
Current liabilities	6,032	5,478
Long-term liabilities	34,198	33,375
	40,230	38,853

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

E. Insurance risks

Insurance risk, including:

Underwriting risk: The risk of using incorrect prices due to deficiencies in the underwriting process and due to the gap between the risk when pricing and establishing the premium and the actual occurrence so that the collected premiums are insufficient for covering future claims and expenses. The gaps may arise from accidental changes in business results and from changes in the cost of the average claim and/or the incidence of the claims as a result of various factors.

Reserve risks: The risk of an incorrect assessment of the insurance liabilities which might cause the actuarial reserves to be inadequate for covering all the liabilities and claims. The actuarial models according to which the Company assesses its insurance liabilities are based on the fact that the pattern of the behavior of past claims represents forward looking information. The Company's exposure is comprised of the following risks:

1. Model risk – the risk of choosing an incorrect model for pricing and/or assessing the insurance liabilities
2. Parameter risk – the risk of using incorrect parameters, including the risk that the amount paid for settling the Company's insurance liabilities or that the date of settlement of the insurance liabilities is different than expected

Catastrophe risk: The exposure to a single catastrophe such as natural disaster, war, terror, natural damages or earthquake that will result in significant damage. The material catastrophe to which the Company is exposed in Israel is earthquake and in the United States hurricanes and storms.

The amount of the expected maximum loss in general insurance business in Israel, due to exposure to a single catastrophic event or cumulative damage for a particularly large event with maximum possible loss (MPL) of 2.1% is NIS 5.237 billion gross and NIS 65 million on retention and NIS 25 million plus the cost of reinstatement of the coverage

The gross probable maximum loss (PML) for Republic from natural disasters for 50 years is USD 176.5 million, for 100 years is USD 260.7 million and for 200 years is USD 399.3 million (net amounts, after reinsurance, are USD 20 million, USD 20 million and USD 119.3 million, respectively).

In life assurance business there is a capital requirement against damage for a particularly large event (catastrophe) at a rate of 0.17% and the amount of the risk for death.

Collapse of reinsurers, change in capacity and tariffs of reinsurers: Insurance companies use reinsurers to hedge against insurance risks or to share them with reinsurers. The collapse of reinsurers, change in reinsurance contracts and tariffs might impair the Company's ability to pay insurers or limit their ability to provide insurance. In the insurance sector abroad, the Republic Group issues policies on behalf of insurance companies and takes out reinsurance cover of those insurance companies. These companies bear the risk in this sector, however should they fail to meet their undertakings towards Republic Group, Republic could be liable, without it receiving indemnification.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

1. Insurance risk in life assurance and health insurance contracts

General

Following is a description of the various insurance products and the assumptions used to calculate their respective liabilities based on product type.

According to the Commissioner's directives, the insurance liabilities are calculated by an actuary pursuant to standard actuarial methods and consistently with the previous year. The liabilities are computed according to the relevant coverage data, such as age and gender of policyholder, term of insurance, date of commencement of insurance, type of insurance, periodic premium and amount of insurance.

Actuarial methods used to calculate the insurance liabilities

(1) Adif and investment tracks insurance programs

Adif and investment track insurance programs consist of an identified savings component. The basic and main reserve is in the amount of the accumulated savings plus the yield according to the policy's terms as follows:

- Principal linked to an the investment portfolio (performance based contracts)
- Principal linked to the CPI plus a fixed guaranteed interest or credited by a guaranteed yield against adjusted assets (performance based contracts)

In respect of insurance components that are attached to these policies (such as occupational disability, death and long term care) the insurance liability is calculated separately as set out below.

(2) Insurance programs such as endowment (traditional)

Endowment and similar insurance programs include a savings component in the event that the policyholder is still alive at the end of the term of a program with an insurance component of death risk during the period of the program. In respect of these products, the insurance liability is calculated for each covered aspect as a discounting of the cash flows in respect of the anticipated claims, including payment at the end of the period, net of future anticipated premiums. This calculation is based on assumptions according to which the products were priced and/or on assumption based on the claims experience, including the interest rates ("tariff interest"), mortality or morbidity tables. The calculation is according to the net premium reserve method, which does not include the component that was loaded on the premium tariff for covering the commissions and expenses, in the anticipated flow of receipts and on the other hand it does not deduct the anticipated expenses and commissions. The reserve in respect of performance based traditional products based on the actual yield achieved less management fees.

- (3) Liabilities for pensions are calculated according to anticipated life expectancy on the basis of the updated mortality tables that are constructed in accordance with information published by the Ministry of Finance in the Supervisor's circular.
- (4) Liabilities in respect of annuities paid for life in respect of valid policies (paid and settled) which have not yet reached the stage of realization of annuity or the policyholder has reached retirement age and the actual payment did not yet begin, are calculated according to the probability of annuity withdrawal and in accordance with the anticipated life expectancy on the basis of the updated mortality tables, taking into consideration the anticipated profits from the policies until the policyholders reach retirement age in accordance with the Supervisor's circulars. If the guaranteed annuity coefficients of the policies are higher, the required increase is also higher.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

- (5) Life assurance programs include pure risk products (such as diseases and hospitalization, long term care, dread diseases, and disability) sold as independent policies or attached to policies with a basic program such as Adif, investment track or traditional. An actuarial liability is calculated in respect of some of these programs. The calculation is according to the gross premium reserve method which includes all the premium components in the anticipated flow of receipts and deducts the liability cost and the anticipated expenses and commissions. Negative provisions were not offset by positive provisions. Some of the plans used the net reserve premium method, described above. For the other plans, the insurance liability is calculated at IBNR (claims incurred but not yet reported).
- (6) In respect of continuous claims in payment, in long term care and occupational disability insurance, the insurance liability is calculated according to the duration of the anticipated payment, and it is discounted according to the tariff interest rate of the product.
- (7) Liabilities for outstanding claims in life assurance and health insurance are calculated on the basis of the experience of the Company.
- (8) Liabilities for claims incurred but not yet reported (IBNR) in life assurance and health insurance are calculated on the basis of the experience of the Company.
- (9) Insurance liabilities in respect of collective insurance consist of a liability in respect of unearned premium, provision for participation in profits, IBNR reserve (claims incurred but not yet reported), reserve for continuity and provision for future losses, if necessary.
- (10) For collective life, health and long-term care insurance, including dental and sick leave insurance, the actuarial liability is calculated on the basis of the experience of the individual collective. This liability includes reference to the insurance companies.

Major assumptions used in the calculation of insurance liabilities

(1) Discount rate

For endowment and similar insurance programs (traditional) see section (E)(1)(2) above). For pure risk products with fixed premium, the interest used for discounting is as follows:

- In insurance policies that are mainly backed by designated debentures, tariff interest is at a rate of 3% to 5%;
- For performance based products issued in 1991 onwards, tariff interest is at a rate of 2.5%, linked. In accordance with the terms of the policy, changes in interest are carried to policyholders.
- The discounting rate could change as a result of material changes in the long-term interest rate in the market.

(2) Morbidity and mortality rates

- A) The mortality rates used in the calculation of insurance liabilities for death of policyholders prior to attaining the age of retirement (namely excluding the mortality of policyholders who receive retirement pensions and those receiving monthly compensation for disability or long term care) are generally the same as the rates used to determine the tariff.
- B) The liability for life annuity payments is based on updated mortality tables. Increase in the mortality rate assumption, due to increase in actual mortality rate to a level exceeding the existing assumption, will result in an increase of insurance liabilities for mortality of policyholders prior to attaining the age of retirement and decrease in liability for annuities payable for life.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

It is noted that there has been a reverse trend of increase in the life expectancy and decrease in mortality rate in the last decades. The mortality assumption used in the calculation of the liability for annuity takes into account assumptions for future increase in life expectancy.

- C. The morbidity rates relate to the prevalence of claims for mortality from serious diseases, occupational disability, long term care, operations and hospitalization and disability from accident. These rates are based on the Company's experience or researches of reinsurers. In areas of long term care and disability, the period for paying annuities is determined according to the company's experience or researches of reinsurers.

As long as the morbidity rate assumption increases, the insurance liability will grow in respect of morbidity rate from serious diseases, disability, long term care, operations and hospitalization.

(3) Pension rates

Life assurance policies, including savings component, were maintained for funds deposited until 2008 in two tracks: capital track and annuity track. In certain policies, the policyholder may select the track upon retirement. Since the insurance liability is different in each of these tracks, the company is required to determine the rate of policies in which the policyholder selects the pension track. This rate is based on the supervision guidelines with adjustment to the Company's experience. As from 2008, all plans are for pension.

(4) Cancellation rates

The cancellation rates affect the insurance liabilities in respect of part of the health insurances and the annuities paid for life during the period before beginning the payments. The cancellation of insurance contracts can be due to the cancellation of policies initiated by the company due to discontinuation of the premium payments or surrenders of policies at the policyholders' request. The assumptions regarding the cancellation rates are based on the company's experience and they are based on the type of product, the life span of the product and sales trends.

(5) Continuity rates

There are health insurances and collective long-term care insurances in which the policyholders are entitled to continue to be insured under the same conditions, even if the collective contract is not renewed. In respect of this option of the policyholders, the company has a liability that is based on assumptions regarding the continuity rates of the collective insurances and the continuity rates of the contracts with the policyholders after the collective contract expires.

If there is a higher probability that the collective contract will not be renewed (a higher continuity rate) the insurance liability will also increase, since the insurance will continue under the previous conditions, without adjusting the underwriting to the change in the policyholders' state of health.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

(6) Sensitivity analysis in life assurance

December 31, 2011

	Cancellations (repayments, settlements and deductions)		Morbidity rate		Mortality rate	
	+10%	-10%	+10%	-10%	+10%	-10%
	NIS million					
Profit or loss and comprehensive income (equity)	2	(7)	(68)	33	21	(8)

December 31, 2010

	Cancellations (repayments, settlements and deductions)		Morbidity rate		Mortality rate	
	+10%	-10%	+10%	-10%	+10%	-10%
	NIS million					
Profit or loss and comprehensive income (equity)	10	(11)	(68)	55	50	(59)

2. Insurance risk in general insurance contractsSummary of the main insurance branches

The Company in Israel underwrites general insurance contracts, mainly compulsory motor insurance, liability, motor casco and property. The Company abroad underwrites mainly property, motor and liability insurance, both private and commercial.

Compulsory motor insurance in Israel covers the policyholder and driver for any liability that they might incur, in accordance with the Road Accidents Victims Compensation Law, 1975, due to bodily injury to the driver, passengers or pedestrians injured by the vehicle. Compulsory motor insurance claims are long tail, in other words, it could be several years before the claim is settled. In foreign consolidated insurance companies, compensation for bodily injury policies in motor insurance is limited to the amount set out in the policy,

Liability insurance is designed to cover the policyholders' liability for damage that he may cause to a third party. The main types of insurance are third party liability insurance, employer liability insurance and other liability insurances such as professional liability, product liability and director and officeholder liability. The time of filing the claims and settlement is affected by a number of factors such as the type of coverage, the policy terms and legislation and legal precedents. Compulsory motor insurance claims are generally long tail, in other words, it could be several years before the claim is settled.

Policies that insure against motor vehicle damage and third party motor property damage grant the policyholder coverage for property damage. The coverage is generally limited to the value of the vehicle that was damaged. The premium for motor vehicle property insurance requires approval of the general policy by the Supervisor of insurance and is an actuarial rate and partially differential (which is not uniform for all insured parties and is adjusted for risk). The premium is based on a number of parameters, those related to the vehicle of the policyholder (such as type of vehicle and year of manufacture), and those related to the nature of the policyholder (such as the age of the driver and claims history).

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

Underwriting is partly through the actual tariff, and partly through a system of procedures which are intended to check the claims history of the policyholder including presentation of proof of "no-claims" from the previous insurer for the last three years, proof of updated protection, which are integrated automatically when issuing the policies.

In most cases, motor vehicle property insurance policies are issued for one year. In most cases, claims for these policies are made close to the time that the insurance incident occurs.

Property insurance provides policyholders with coverage for physical damage to their property. The main risks covered by property insurance are risks of fire, explosion, break-in, earthquake and damage by natural forces. Property insurance sometimes includes coverage for loss of profits following physical damage to the property. Property insurance is an important part of residential, merchant, engineering, and cargo (maritime, land, air) insurance policies. In most cases, claims against these policies are settled close to the date of the insurance event.

The insurance company abroad, taking into account the geographic area in which it operates, is exposed to risk due to disasters, including hurricanes, hail storms, tornadoes and fire, such as hurricane Ike and Gustav in September 2008, and Katarina and Rita in August and September 2005. In addition, in 2008, wind, hail and tornadoes caused record damages. It is difficult to foresee the occurrences of these events with statistical accuracy or to estimate the extent of the damage that may be caused. The scope of losses from the disasters depends on various factors, including the exposure of the policyholders in the area of the event, scope of reinsurance and increase in premiums, and unexpected changes in insurance coverage due to regulatory or legal procedures following catastrophe.

Principles for calculating actuarial valuations in general insurance

General

A) Liabilities in respect of general insurance contracts include the following main components:

- Provision for unearned premium
- Premium deficiency
- Outstanding claims
- Less deferred acquisition costs:

The provision for unearned premium and excess of income over expenses is calculated independently of any assumptions and accordingly, is not exposed to the reserve risk. For the manner in which these provisions are calculated, see Note 2 above.

B) According to the Supervisor's directives, the outstanding claims are calculated by an actuary, according to standard actuarial methods and consistently with the previous year. The selection of the appropriate actuarial method for each branch of insurance and for each year of occurrence/underwriting, is based on the compatibility of the method to the branch and sometimes there is a combination of methods. The valuations are primarily based on past experience of the development of claim payments and/or development of the amount of the payments and specific estimates. The valuations include assumptions regarding the average cost of claim, cost of handling the claims and frequency of the claims. Additional assumptions may address changes in interest rates, exchange rates and timing of payments. Payment of claims includes direct and indirect expenses of settlement less claims recoveries and deductible.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

- C) The use of actuarial methods that are based on the development of the claims is mainly adequate when there is stable and sufficient information regarding the payment of the claims and/or the specific valuations in order to estimate the total expected cost of claims. When the available information in handling the claims is insufficient, sometimes the actuary uses a computation which weighs between the known estimate (in the company and/or the branch) such as LR and the actual development of the claims. Greater weight is given to the valuation based on experience as time passes and additional information is accumulated for the claims.
- D) Quality valuations and judgments are also taken into account as to the degree that past trends will not continue in the future. For example: due to a one time event, internal changes such as change in the portfolio mix, underwriting policy and handling procedures of claims and in respect of external factors such as legal ruling and legislation. If the above changes were not fully reflected in past experience, the actuary updates the models and/or makes specific provisions on the basis of statistical and/or legal estimates, as appropriate.
- E) In several large claims with non-statistical profile, the reserve (in gross and on retention) is determined on the basis of the opinion of the company's experts and in accordance with the recommendations of their legal advisors.
- F) The reinsurers share of the outstanding claims is calculated according to the type of agreement (proportionate or unproportionate), actual claims experience and the premium that was transferred to the reinsurers
- G) The evaluation of the outstanding claims for the Company's share of the pool in incoming transactions and joint insurance received from other insurance companies (leading insurers) was based on a calculation made by the pool or by the leading insurers or by the Company.

Actuarial methods in main insurance branches:

A) Motor property

In the motor property branch, the liabilities are calculated on the basis of the development of payments and/or development of outstanding claims model (link ratio / chain ladder), with reference to the types of coverage, such as comprehensive, third party, types of vehicles, such as 4-ton and over 4-ton and types of damage, such as accident, theft and natural disasters.

For recent months of damage, which are not mature, use was also made in the averages method in determining the cost of claim per policy.

There are separate estimates of the claims department in the following cases:

- Old claims
- Claims for car theft and natural damages

The individual estimates take into account the deductibles.

Subrogation and remnants are taken into consideration and the actuarial model takes into account the development of all the payments (positive and negative). In addition, there is a model for estimating the amount of the expected subrogation.

A provision was calculated for indirect expenses for settling claims.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

B) Compulsory motor insurance

In the motor property branch, the liabilities are calculated on the basis of the development of payments and/or development of outstanding claims model (link ratio / chain ladder). For later underwriting years, the cost of claims is based on the LR rate and the payments development model and/or outstanding claims development model (Bornhuetter-Ferguson). The tail of the development is calculated on the basis of the Sherman model.

There are separate estimates of the claims department in the following cases:

- Old claims
- Particularly large claims

The outstanding claims are estimated separately on the gross level and on the reinsurance level.

The share of the reinsurer in excess for the last three underwriting years is based the percent of the reinsurance premium, taking into account known claims for these years. For claims that occurred in a prior period, the estimate is according to the actual claim.

Estimates for facultative reinsurance are made in a separate model (gross and retention).

The individual estimates take into account the deductibles.

Subrogation and remnants are taken into consideration and the actuarial model takes into account the development of all the payments (positive and negative).

A provision was calculated for indirect expenses for settling claims.

The valuation of the outstanding claims for the Company's share of the pool is based on the calculation made by the Association of Insurance Companies in Israel ("the pool").

C) Property and other branches

In the property and other branches, liabilities are calculated on the basis of the payments development model and outstanding claims development model (link ratio / chain ladder). For periods that are not mature, use was also made in the averages method in determining the cost of claim per policy.

There are separate estimates of the claims department in the following cases:

- Old claims
- Claims for car theft and natural damages

The outstanding claims are estimated separately on the gross level and on the reinsurance level.

The share of the reinsurer in claims for excess is estimated according to the actual claims.

Estimates for facultative reinsurance are made in a separate model to claims in branches in which the share of the reinsurer is material.

The individual estimates take into account the deductibles.

Subrogation and remnants are taken into consideration and the actuarial model takes into account the development of all the payments (positive and negative).

A provision was calculated for indirect expenses for settling claims.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

D) Branches in which actuarial assessment is not made

Engineering insurance, insurance of freight, marine hull and aircraft, and incoming business include outstanding claims on the basis of a separate evaluation of each claim according to an opinion received from Company lawyers and experts who handle the claims and ceding companies for incoming business, with the addition of IBNR if necessary.

Assumptions and essential models for determining insurance liabilities in general insurance:

Chain ladder/link ratio

These methods are based on the development of historical claims (such as development of payments and/or development of amount of payments, and valuations of the individual claims and development of the number of claims), in order to value the anticipated development of existing and future claims. The use of these methods are mainly suitable after a sufficient period since the event occurred or the policy is underwritten, when there is enough information from the existing claims in order to evaluate the total anticipated claims. The difference between the methods is due to the method for calculation of the average development (simple or weighted average). In branches with highly diverse claims, as well as the average development coefficient, the standard deviation of the development coefficients is calculated.

Bornhuetter-Ferguson (BF) -

This method combines early estimates known in the company or branch, and an additional estimate based on the claims themselves. The early estimates utilize premiums and loss ratio for evaluating the total claims. The second estimate utilizes actual claims experience based on other methods (such as chain ladder). The combined claims valuation weighs the two estimates, while greater weight is given to the valuation based on the claims experience as time passes and additional information is accumulated for the claims. This method is mainly used when there is insufficient information.

The averages -

At times, as in the Bornhuetter-Ferguson method, when the claims history in the last periods is insufficient, the historical average method is utilized. In this model, the claims cost is determined based on the average cost of the claim per policy for earlier years and the number of policies in the later years. Another method for calculation is the multiplication of the cost of the historical claim for the policy and the number of policies in the relevant period.

Sherman model -

This is a mathematic model used to adjust non-linear distribution with development coefficients calculated using chain ladder/link ratio models. Through the distribution, it is possible to calculate the development coefficients for prior periods for which information is not available (development tail).

The main assumptions taken into consideration in the actuarial valuation:

- (A) Outstanding claims in the compulsory motor insurance and liability branches were discounted at the lower of annual interest at a rate of 3% or a risk-free interest rate.

An increment was included for the risk margin (standard deviation) in the base of the reserve in the compulsory motor insurance and liability branches.

Notes to the Consolidated Financial Statements

NOTE 30 – LIABILITIES FOR INSURANCE CONTRACTS (CONTD.)

- (B) In foreign insurance companies, outstanding claims were not discounted and no increment was included for risk margin (standard deviation).
- (C) The basic assumption for each calculation method is that the historical behavior of the claims reflects the future behavior.
- (D) When analyzing development of payments, insurance companies in Israel add a claims tail according to the Sherman model.

NOTE 31 – PROVISIONS AND OTHER LIABILITIES

	December 31	
	2011	2010
	NIS million	
Liability for remediation of environmental hazards (1)	161	108
Costs for divestiture of assets	142	66
Prepaid revenue	37	50
Liability for acquisition of shares of a subsidiary from non-controlling interests (2)	195	350
Deposits from reinsurers	206	181
Other	279	153
	<u>1,020</u>	<u>908</u>

(1) The balance in the financial statements represents the estimation of the Group companies regarding liabilities for environmental quality in respect of pollution discovered in a number of gas stations in Israel and abroad, and in respect of potential pollution at Pi Gilot terminals and refineries. See also Note 2.

(2) See Note 14H.

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS

A. Contingent liabilities

There are contingent claims, including application for certification as class action suits, against certain investees for significant sums that might reach billions of shekels. In some cases, it is not possible to assess their outcome at this stage, and therefore no provision was recorded in the financial statements.

Details of the material claims filed against the Group companies are provided below (claims against Group companies that were closed up to the approval date of the financial statements, without material effect on the statements, were not included in this disclosure):

1. **Contingent claims against Delek Israel**

- A) On December 7, 2011, an application for certification of a class action suit was filed against Delek Israel. According to the motion for certification, Delek Israel acted in contravention of the law by not granting a discount of 30 agorot under a sales campaign for self-service customers. The total amount of the claim is NIS 18.5 million.
In addition, the plaintiffs are seeking additional legal remedies.

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that in view of the preliminary stage of the proceeding, the outcome of the motion cannot be assessed at this stage.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

- B) On September 5, 2011, an application for certification of a class action was filed against Delek Israel. According to the motion for certification, as from October 1, 2006, customers purchasing diesel fuel with a fuel card and/or through the Dalkan refueling system pay more per liter of diesel fuel than customers who do not have an agreement with Delek Israel. The total amount of the claim is NIS 65 million. The grounds for the motion are breach of agreement, misleading information, an act of bad faith and unjust enrichment. On January 15, 2012, Delek Israel submitted a response to the motion for certification and asked to dismiss the motion.

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that there is less than a 50% chance that the motion will be accepted, therefore a provision was not included in the financial statements.

- C) On August 28, 2011 a motion for certification of a class action suit was filed against Delek Israel and other fuel companies. According to the motion, the fuel companies attributed expenses unrelated to the sale of gasoline to the marketing margin, which is part of the maximum price of 95 and 96 octane gasoline, in contravention of the law and while misleading the regulator. The total claim amounts to NIS 1 billion. The share of Delek Israel is NIS 21.4%. The grounds for the motion are by virtue of the Torts Ordinance, Supervision Order, Consumer Protection Law and unjust enrichment.

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that in view of the preliminary stage of the proceeding, the outcome of the motion cannot be assessed at this stage.

- D) In August 2011, an application for certification as a class action suit was filed against Delek Israel. The plaintiffs are customers using the Dalkan (automatic refueling system) to purchase diesel fuel. The plaintiffs contend that according to the series of agreements between them and Delek Israel, they were charged a higher price for diesel fuel, compared to the price paid by random customers (who are not Dalkan customers) and accordingly, they are entitled to receive a refund for the excess charge from Delek Israel, as well as the other members of the group they represent (customers using the Dalkan to purchase diesel fuel Dalkan in the seven years preceding the motion for certification). The plaintiffs estimate the amount of the claim at NIS 181 million for amounts that the group members were allegedly charged in contravention of the law. The plaintiffs are also seeking additional legal remedies.

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that there is less than a 50% chance that the motion will be accepted, therefore a provision was not included in the financial statements.

- E) On December 23, 2010 a motion for certification of a class action suit was filed against Delek Israel and other fuel companies. According to the motion for certification, the fuel companies are in violation of the provisions of sections 2-4 of the Consumer Protection Law, 1981, by misleading the public regarding the nature, amount and quality of fuels that they sell, among other things and by failing to inform consumers that they sell the fuels at the temperature of the environment, while when purchased, calculation is according to a temperature of 15 degrees Celsius and therefore the consumers are sold an inferior product. The plaintiffs contend that by doing so, the fuel companies received, in contravention of the law, moneys for a product that was sold by misleading the consumers and unjustly enriched themselves contrary to the provisions in section 1 of the Unjust Enrichment Law, 1979. The plaintiffs are asking the court to place the amount of the claim against Delek Israel at NIS 106 million. On January 1, 2012, Delek Israel submitted a response to the motion for certification and asked to dismiss the motion.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that there is less than a 50% chance that the motion will be accepted, therefore a provision was not included in the financial statements.

- E) On October 3, 2010, a motion for certification of a class action suit was filed against Delek Israel and other fuel companies. The applicants claim that the series of agreements between each respondent and some of its station owners, including retail and property agreements, constitute a restrictive arrangement that prevents station owners from entering into agreements with other entities, preventing price competition. The amount of the claim against all the respondents is NIS 1.2 billion.
On February 27, 2012, Delek Israel submitted a response to the motion for certification and asked to dismiss the motion.

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that in view of the preliminary stage of the proceeding, the outcome of the motion cannot be assessed at this stage.

- G) In November 2006, three motions for certification of class action suits were filed against Delek Israel, third parties and also against the former deputy CEO of Delek Israel. The applicants claim that Delek Israel, together with the other defendants, acted, inter alia, in a fraudulent, misleading and negligent manner and violated their statutory duty. The motions and claims were filed following an investigation by the Israel Police concerning the dilution of fuels at several gas stations marketing Delek Israel fuels and in view of possible damages that may have been incurred as a result of this. The motions amount to NIS 1.4 billion.

In all of these proceedings, Delek Israel filed motions for summary dismissal, motions to try all three proceedings before the same judge and motions to extend the deadline for the submission of a response to the motion for approval until after the hearing on the summary dismissal. The court granted the motion to try the proceedings before the same judge.

In the third quarter of 2007, one motion, in the amount of NIS 90 million, was stricken off by consent and the court ordered the combination of the two remaining motions into one. Following combination of the two motions, the amount of the motion for certification of a class action suit was reduced from NIS 1.4 billion to NIS 554 million. Furthermore, the former deputy CEO of Delek Israel was removed from the petition. The applicants filed a motion for a continuance in the proceedings in the motion for certification as a class action until receipt of a peremptory decision against the other defendants (but not against Delek Israel) in a criminal proceeding instituted against them. The court allowed a continuance in the proceedings until a decision is made in a criminal proceeding. Delek Israel filed a motion for leave to appeal the decision for a continuance in the proceedings and in August 2009, the court denied the motion for leave to appeal and upheld the stay of proceedings. At October 2011, the criminal ruling has been given, however the proceedings have yet to resume.

The management of Delek Israel estimates, based on the opinion of its legal counsel, that until the applicants submit a response to Delek Israel's response to the motion for certification as a class action suit, the chances of the motion cannot be assessed and therefore no provision was made for them in the financial statements.

- H) In October 2009, a claim and application for its certification as a class action suit was filed against Delek Israel and against other fuel companies ("the defendants"). According to the claim and application for certification, when refueling at automatic pumps, the pumps start working immediately after entering the payment means, before fuel starts to flow from the pump, and the fuel meter starts to run together with the payment meter. The applicant alleges that in this way, tens of agurot are charged for fuel that has not been supplied and consumed when refueling at an automatic fuel pump at Delek Israel stations.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

The applicant is claiming declaratory relief, ordering Delek Israel to stop collecting these amounts and to refund any overpayment that was allegedly charged by Delek Israel. The total claim amounts to NIS 124.3 million. The proportionate share of Delek Israel in this amount is NIS 42.4 million.

The management of Delek Israel believes, based, among other things, on the opinion of its legal counsel, that there is more than a 50% chance that the class action will be certified, however the amount payable by the Delek Israel, if the claim or class action is approved is not material and the outcome is not expected to have a material effect on the financial statements.

- I) In December 2010, the Ministry of Environmental Protection filed an indictment against Delek Israel and former managers and officers.

The indictment refers to several alleged omissions in contravention of the Water Regulations (Prevention of Water Pollution (Fuel Stations), 1997, including failure to carry out sealing tests, failure to submit sealing test results to the Petroleum Commissioner, failure to report a fuel leak and failure to treat an unsealed facility.

A list of 72 prosecution witnesses was attached to the indictment.

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that in view of the preliminary stage of the proceeding, the outcome of the motion cannot be assessed at this stage.

- J) On January 10, 2011, a motion for certification of a class action suit was filed against Delek Israel and other fuel companies. According to the motion for certification, the fuel companies violated statutory duty according to the Torts Ordinance (New Version), 1968 and the provisions of the Water Law, 1959 and its subsequent regulations, for failure to prevent leakage from containers and pipelines. The damage claimed is non-monetary, infringement on the autonomy of the individual by involuntary exposure to polluted water with a health risk and the amount claimed from each company is NIS 200 million. On January 22, 2012, Delek Israel submitted a response to the motion for certification.

The management of Delek Israel estimates, based, inter alia, on the opinion of its legal counsel, that there is less than a 50% chance that the motion will be accepted, therefore a provision was not included in the financial statements.

- K) On March 8, 2011, a motion for certification of a class action suit was filed against a wholly-owned subsidiary partnership of Delek Israel ("the partnership").

The plaintiffs contend that the acts of partnership were negligent, in breach of statutory duty, caused private and public nuisance according to the Civil Wrongs Ordinance (New Version), 1968, and were in breach of the provisions of the Prevention of Nuisances Law, 1961, on the grounds that between September 2008 and October 28, 2009, Delek Pi Giliot stored 850 cubic meters of heating liquid at the Jerusalem terminal, which emitted odor fumes containing substances that are suspected of endangering public health, and exposed the group members (civilians who were in the Har Nof neighborhood in Jerusalem at this time), to polluted air and a pungent odor that impaired their quality of life, convenience, welfare and health.

Monetary damages are being claimed for impairment of property in the area and non-monetary damages are being claimed for the alleged exposure to air pollution and the pungent odor. The amount being claimed from the partnership is NIS 700 million.

The management of Delek Israel believes, based, inter alia, on the opinion of its legal counsel, that due to the preliminary stage of the proceedings, is not possible to assess the outcome of the motion, although the parties are negotiating for a settlement and it is highly likely that the case will be concluded with the payment of an amount that is not significant for Delek Israel.

For further information see the financial statements of Delek Israel that are available to the public.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

2. Contingent claims against Delek Europe

A number of legal claims were filed against DEBV in the course of regular business, in a cumulative amount of EUR 14 million (approximately NIS 69 million). The management of DEBV estimates that it is unlikely that the claim will be approved, therefore a provision was not included in the financial statements.

3. Contingent claims against Delek US

- A) Further to the contents of Note 14 regarding the fire at the refinery, the circumstances of the event are being investigated by a number of entities, including an internal investigation by Delek US, the department for occupational safety and health, the US Chemical Safety and Hazard Investigation Board and the US Environmental Protection Agency. In May 2009, the department of occupational safety and health completed the investigation and issued a notice estimating a fine of USD 0.2 million. Delek US is appealing this notice and does not believe that the result will have a material effect on its business. Delek US is unable to accurately assess the results of the other examinations, including possible fines or other enforcement activities, however it estimates that the existing procedures will not have a material adverse effect on its operations.
- B) A subsidiary in the USA, Delek Refining Inc. ("Delek Refining"), is subject to the provisions of the law, regulations, licenses and environmental supervision set by the competent authorities in its field of business at the federal, state and local levels. These provisions pertain to Delek Refining's entire activity, both in the field of refining and of the fuel products that it produces, and in the field of transportation (the oil pipe). The environmental legislation is complex, and is constantly changed and updated.

The main legislation for environmental control relevant to operations of Delek Refining refers to the quality of air, liquid, solid and toxic waste and to the prevention of ground and groundwater contamination.

The environmental authorities in the United States conducted two investigations against the former owners of the refinery and the pipeline, following the discovery of contaminants in the soil and in the underground water in the area of the refinery and the pipeline. The remediation and purification processes of the contaminants have yet to be completed.

As part of the acquisition of the refinery and the oil pipe, Delek Refining assumed the liability for the existing contaminants, in respect of which the investigation and the remediation and purification processes are still ongoing, as well as the liabilities imposed on the previous owners in respect of the contaminants, the provision included in the financial statements of Delek US as of December 31, 2011 amounts to USD 12.6 million (NIS 45 million). Delek Refining is not entitled to indemnification by the former owners in respect of environmental damages known to it at the acquisition date, however it is entitled to a limited (in amount and time) indemnification in respect of costs that it may incur in the future due to the discovery of environmental damages that were caused prior to its of the refinery, but were unknown at the time. The Company estimates the indemnification at USD 1.4 million (approximately NIS 5 million).

It is further noted that Delek Refining acquired an environmental insurance policy that covers certain environmental damages that may be discovered in the future.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

4. Contingent claims against The Phoenix and its investees

The Phoenix has general exposure, which cannot be estimated or quantified, partly due to the complexity of the services provided by The Phoenix to its policyholders and members. The complexity of these arrangements includes potential for claims of interpretations and other due to differences in information between The Phoenix and the other parties to the insurance contracts referring to a range of commercial and regulatory terms. It is impossible to predict the types of claims that will arise in this area, and the exposure arising from these and other claims in respect of the insurance contracts, through the hearings mechanism set out in the Class Actions Law.

In recent years, there has been a significant increase in the scope of motions for certification as class action suits against The Phoenix and the number of claims certified as class actions. This is part of the general increase in motions for certification as class action suits in general, including against companies operating in the same sector as The Phoenix, mainly due to the Class Actions Law, 2006. This significantly increases the potential exposure of The Phoenix to losses if the class actions against the Company and/or the subsidiaries are accepted.

Motions for certification as class actions are filed in accordance with the Class Actions Law, 2006 ("the Class Actions Law"). The procedure for motions for certification of class actions are divided into two main stages: The first stage is the hearing of the motion for certification of a class action ("the motion for certification" or the "certification stage", respectively). If the motion for certification is summarily dismissed, the hearing stage on the level of the class action is concluded. A ruling in the certification stage may be appealed at the court of appeal. In the second stage, if the motion for certification is accepted, the class action will be heard ("the stage of certification of a class action"). The ruling at the stage of certification of a class action can be appealed at the court of appeal. The Class Actions Law includes specific arrangements for settlements, in the approval stage and in the certification of a class action stage, and arrangements for withdrawal of the plaintiff from the motion for certification or from the class action.

In respect of the motions for certification of a class action as described in sections A-E below, the management of The Phoenix believes, based, inter alia, on the opinion of its legal counsel, that it is more likely than not that the statements of defense of The Phoenix and/or subsidiaries of The Phoenix will be accepted and the motion for certification as a class action suit is more likely than not to be rejected, and are not covered by a provision in the financial statements. Provisions were included in the financial statements to cover the exposure estimated by the Company or the subsidiary for motions for certification as class action suits in which it is more likely that the Company's statement of defense will be dismissed.

The management of The Phoenix believes, based, inter alia, on the opinion of its legal counsel, that the provisions made in the financial statements to cover the exposure estimated by The Phoenix and/or its subsidiaries are appropriate.

Following is a description of certain motions for certification of class actions:

- A) On December 19, 2006 a claim was filed with the District Court of Tel Aviv against Phoenix Insurance, accompanied by a motion to approve the lawsuit as a class action suit, which Phoenix Insurance received on December 25, 2006
The lawsuit and the motion to approve it as a class action suit involves a matter that falls in frame of the "disability by accident" annex that is added, at the policyholder's request, to the life assurance policy (the appendix).

The remedy requested by the plaintiff is that Phoenix be required to pay the difference between the compensation due under the policy, according to the plaintiff, and the actual compensation paid, for the entire class.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

The plaintiff's own damages were set at approximately NIS 77 thousand, whereas for the entire class the plaintiff does not have at his disposal data allowing calculation of the total damage.

On December 5, 2007, the Attorney General announced his decision to hear the case, by virtue of the authority conferred upon him, after seeing that the "right of the State of Israel or public interest could be affected by or are involved in the proceedings". On May 1, 2008, the Attorney General's position was received, supporting the position of the Insurance Supervisor, which is the basis for the claim.

On January 11, 2009, subsequent to the hearing and written summations, the court ruled to certify the claim as a class action suit. On March 8, 2009, The Phoenix Insurance filed a motion to appeal the certification of a class action at the Supreme Court ("the motion to appeal". In accordance with the court ruling, the plaintiffs submitted a response to the motion to appeal. On May 19 the Attorney General's opinion of the motion to appeal was received. At the same time, The Phoenix Insurance filed a motion at the district court to postpone the continuation of investigation of the claim at the district court until the Supreme Court rules on the motion to appeal. The district court dismissed this motion. The Phoenix Insurance filed a motion to appeal this ruling at the Supreme Court (the additional motion to appeal) and at the same time, the Phoenix Insurance petitioned the district court to postpone the continuation of investigation of the claim until the ruling on the other motion to appeal. The district court dismissed this motion as well.

The Phoenix Insurance petitioned the Supreme Court to hand down a ruling for the other motion to appeal and to postpone the publication date of the notice in the newspaper and the date for filing a statement of defense.

The Supreme Court ruled that at this time, and until another ruling is handed down, it is not required to publish a notice in the newspaper about certification of the class action and to file statements of defense in the class action. It was further ruled that the motion to appeal requires a response. The respondents filed a response. On this background and at the request of the parties, the hearing of the class action at the district court was postponed until the Supreme Court rules on the motion to appeal.

On January 6, 2011, the Supreme Court heard both motions to appeal. The parties are waiting for the ruling.

- B) On October 19, 2004 a claim was filed against The Phoenix Insurance, accompanied by a motion to approve the claim as a class action suit. The claim involves the payment of motor insurance benefits in "total loss" cases. The plaintiffs claim that in total loss cases, Phoenix Insurance does not pay the full insurance benefits that allegedly correspond to the car's full list price, but rather deducts from the value of the vehicle various amounts in respect of special variables associated with the vehicle price-list, that may affect its value. The plaintiffs argue that in so doing without notifying the policyholders when quoting the price of the insurance policy or when entering into the insurance contract, Phoenix Insurance allegedly misleads all policy holders and is in breach of statutory duty in view of the relevant guidelines of the Insurance Supervisor. The plaintiffs set the claim amount at approximately NIS 41 million.

On January 14, 2010, the district court accepted the application for certification as a class action suit. The Phoenix appealed this ruling.

In a ruling handed down on September 12, 2011, the motion to appeal filed by The Phoenix Insurance against the ruling to certify the class action was dismissed, stating that contentions of The Phoenix Insurance will be kept for an appeal (if filed) on the ruling of the claim. On September 15, 2011, The Phoenix Insurance informed the district court of the Supreme Court ruling. On September 15, 2011, the district court ordered the Attorney General to update the court, within 30 days, of the progress of the Supervisor of Insurance in the preparation of an outline to return the moneys to the policyholders, which is also expected to apply to the group members in this claim, and when receiving the update, the timetable for continuation of the case will be set.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

On December 29, 2011, the Supervisor of Insurance notified the court that the Supervisor is continuing to review the outline for refunding the moneys, therefore the Supervisor wishes to submit an update immediately prior to the date of the hearing set for May 2012. The court accepted the request and on December 29, 2011, ordered that the Supervisor submits his position by the second half of April 2012.

- C) On January 3, 2008, a statement of claim and motion for a certification as a class action suit were filed with the District Court in Tel Aviv against The Phoenix Insurance and other insurance companies, arguing that management fees were collected from the policyholder in profit-sharing life assurance policies in contravention of the law. The lawsuit was filed by four plaintiffs and on behalf of every person who is or was insured by one or more of the defendant insurance companies, under a combined profit-sharing life assurance policy type, issued between 1992 and 2003 (inclusive) ("the group").

The plaintiffs argue that the defendant insurance companies collected management fees in profit-sharing life insurance policies contrary to the instructions of Regulation 6A to the Insurance Businesses Supervision Regulations (Terms in Insurance Contracts), 1981 ("The Supervision Regulations") and contrary to the instructions of the Insurance Supervisor.

As argued, the defendant insurance companies acted in contravention of the law in two aspects (or at least in one of them):

- (a) They collected regular monthly management fees exceeding 0.05% until 2004 (inclusive), apart from 2002.
- (b) They collected the variable fees monthly and not at the end of the year, thus allegedly depriving the policyholders of the proceeds for the variable management fees, collected throughout the year.

The lawsuit against Phoenix Insurance refers to the second argument only.

The personal damage incurred, as argued by one of the plaintiffs who was insured by The Phoenix Insurance in respect of each insurance year, amounts to NIS 13.22, and the total personal damage of all plaintiffs (each one in respect of each insurance year) allegedly amounts to NIS 32.21.

The total damage incurred as argued by the entire group was estimated by the plaintiffs at a nominal amount of about NIS 244 million of which the plaintiffs attribute NIS 40 million to The Phoenix Insurance.

The plaintiffs request the court to order the reimbursement of the excess management fees that were allegedly collected unlawfully, or the reimbursement of the monthly proceeds allegedly lost by each member of the group. The plaintiffs also move for a mandatory injunction that will instruct the plaintiffs to change their mode of operation.

The grounds argued in the lawsuit are as follows: (a) misleading and false presentation; (b) breach of the provisions of the Supervision on Financial Services (Insurance) Law – 1981, the supervision regulations and the circulars of the Insurance Supervisor; (c) lack of good faith; (d) unjust enrichment.

The claim is in the stage of legal proceedings and the continuation of the hearing of this case was set for the end of March 2012.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

- D) On July 5, 2011, a claim and motion for certification as a class action suit was filed against The Phoenix Insurance at the Central District Court, under the Class Actions Law, 2006 ("the claim").

The claim refers to alleged overcharging, in contravention of the law, of credit fees by the defendant from its policyholders, while breaching the provisions of the law and misleading the policyholders.

The group that the plaintiffs seeks to represent is all the policyholders and/or beneficiaries insured by the defendant in general insurance policies, and who paid the defendant excess credit fees and/or collection fees and/or arrangement fees, in contravention of the law and/or with deviation from the interest rates presented to the policyholders, as from May 1, 1984 ("the group").

The amount of the plaintiff's personal claim is estimated at NIS 31.60.

The plaintiffs estimate that the class action suit amounts to NIS 393.

The alleged grounds of the claim are, inter alia, violation of the Control of Financial Services Law (Insurance), 1981 and the subsequent regulations, breach of the agreement and misleading information, breach of statutory duty, breach of duty of good faith in negotiations for a contract and in fulfilling a contract, unjust enrichment and negligence.

The remedies sought by the plaintiffs are, inter alia, to order the defendant to return to the plaintiffs, and to any plaintiff included in the class action group, the moneys that were allegedly collected in contravention of the law, plus linkage differences and interest by law, and plus special interest as set out in the Insurance Contract Law, from the date of each payment through to the date the amounts were actually returned; to award compensation for the group or the public, for the yields on the surplus moneys allegedly collected; to order the defendant to immediately stop overcharging the policyholders for credit fees and/or arrangement fees and/or addition to the policy issued from the date of the petition onwards, and to stop collecting credit fees and/or arrangement fees and/or collection fees for any existing policy or addition to an existing policy for which the excess credit fees were calculated.

The Phoenix Insurance has yet to respond to the motion for certification of a class action. The preliminary hearing is set for April 17, 2012.

- E. On April 7, 2011, a claim and motion for certification of a class action suit was filed against The Phoenix Insurance at the Tel Aviv-Jaffa District Court, under the Class Actions Law, 2006 ("the claim").

The plaintiff contends that the defendant prevents and/or delays transfer of moneys under insurance policies to policyholders and/or beneficiaries and/or third parties in liability insurance, and to members of the provident funds, pension funds and savings plans offered by the defendant, by directing its customers and/or third parties to lift invalid attachments that remained registered in the defendant's register in contravention of the law. This also refers to attachments on pension benefits, which had not yet been formulated on the attachment date, and which cannot be attached according to section 26 of the Severance Pay Law and section 25(b) of the Control of Financial Services Law (Provident Funds), 2005.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

The group that the plaintiff seeks to represent is defined as any person who was entitled, during the seven years preceding the date of filing of this lawsuit, to receive from the defendant insurance benefits and/or moneys that were set aside for or related to any type of insurance policy ("the moneys") and for which the defendant delays and/or delayed moneys, claiming that it has an attachment order as a third party in the name of that person, while that person had no insurance contract with the defendant or any legally attachable property that is held by the defendant, at the date the attachment orders are registered in the defendant's registers and/or within three months after this date or at another date set in the attachment order and/or when the attachment is invalid for any reason ("the group").

The amount of the plaintiff's personal claim is NIS 7,763.

The plaintiff estimates that the general damage caused to the entire group is NIS 5.791 billion.

The grounds for the claim include alleged unjust enrichment, breach of statutory duties, breach of agreement, misleading conduct, breach of fiduciary duty and negligence.

The remedies sought by the plaintiff include to declare that the defendant breached its duties; to order the defendant to refrain from delaying the transfer of funds to the group members, for attachments that are not legally valid, which are still registered in the defendant's registers; to order the defendant to inform those that are about to enter into an agreement with it in an insurance contract and/or third parties that submit claims by virtue of liability insurance, that it was sent attachment orders in their name and that by virtue of these orders, it cannot fulfill its liabilities under the law and/or the agreement and to pay them the moneys, and to order the defendant to compensate the group members, and to refund their moneys that are delayed in contravention of the law, plus linkage differences and interest by law, according to section 28(A) of the Insurance Contract Law, and to return the gains that the defendant produced and/or the commission and management fees that it collected for these moneys.

On November 24, 2011, The Phoenix Insurance filed its response to the motion for certification of a class action and the applicant filed its response to this response. In addition, the applicant filed its response to the motion of The Phoenix Insurance to dismiss its response to the response of The Phoenix to the motion to dismiss ("the motion to dismiss". The Phoenix Insurance filed its response to the response of the applicant to the motion to dismiss. The pre-trial hearing was set for May 1, 2012.

Notes to the Consolidated Financial Statements

**NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS
(CONTD.)**

The following table summarizes the amounts in the claims described above and in other claims filed against The Phoenix and its investees. It is clarified that the amount claimed is not necessarily quantification of the estimated amount of exposure by The Phoenix and/or subsidiaries, as these are estimates by the plaintiffs whose cases will be deliberated in the legal proceedings. It is further clarified that the table below does not include proceedings that have been concluded, including proceedings for which a settlement has been agreed upon.

Class	Number of claims	Amount claimed (NIS millions)
Claims certified as class actions:		
Amount attributable to The Phoenix	4	521
The amount of the claim was not noted	1	-
Contingent motions for certification as class actions:		
Amount attributable to The Phoenix	15	7,448
Claims attributable to several companies without attribution of a specific amount to The Phoenix	2	330
The amount of the claim was not noted	2	-
Other material claims	2	56

The amount of the total provision of class actions, legal proceedings and others, filed against The Phoenix as described above amounts to NIS 62 million (December 31, 2010, NIS 44 million).

For further information, see the statements of The Phoenix that are available to the public.

5. Contingent claims against Gadot

Several law suits amounting to several hundred million shekels have been filed against Gadot and others, for bodily injury and damage to property with regard to Gadot's activity in the Kishon River area (for details, see Gadot's financial statements, which are available to the public).

In some of these cases, there are serious factual disputes and there are many facts that need to be decided and are unknown to Gadot. Moreover, the aforementioned proceedings are very complex and problematic since, among other reasons, most of the suits pertain to ongoing events that occurred over decades, in which a very large number of entities are involved, including the State and local authorities, therefore it is not possible to assess the responsibility and the share of any one entity involved in the suits. It is also scientifically difficult to determine the degree of causal connection between the discharge of industrial wastewater and the damages alleged by the plaintiffs.

6. In September 2007, a claim was filed against Yam Tethys Ltd. (a company owned by the partners in the Yam Tethys project) and others defendants (the State of Israel, Natural Gas Authority, Israel Natural Gas Lines Ltd. and Israel Electric Corporation Ltd.) at the Tel Aviv district court by trawling fishermen for damages allegedly incurred as a result of a reduction in the areas in which they can trawl following the construction of the gas rig and pipeline. The amount of the claim is NIS 35 million.

On May 11, 2010, the first pre-trial hearing was held, after arbitration of the case failed. Dates for the hearing were set for November 2012. The plaintiff is required to submit evidence no later than 60 days prior to the date set for the evidentiary hearing and the defendants are required to submit their evidence no later than 30 days prior to the date set for the evidentiary hearing.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

In view of the information available to the legal counsel of Yam Tethys Ltd., given the fact that the claim mainly refers to part of the pipeline unrelated to Yam Tethys Ltd., and that the plaintiffs do not indicate concrete financial damage caused to them, it is more likely than not that the claim will be dismissed and in any event, even if all or part of the claim is accepted, it is likely that the part of Yam Tethys will be relatively small.

7. A number of claims have been filed against Group companies, deriving from the course of regular business. The Group's management estimates that, based on the assessment of the management of the companies, the provisions that were made for these claims, beyond the existing insurance coverage, are sufficient.
8. On January 31, 2012, a motion for certification as a derivative suit was filed against DES, the former CEO of DES ("the CEO") and seven directors in DES.
In the motion, the applicant contends that DES undertook to effect a distribution that is not permitted, according to the definition of this term in the Companies Law, in favor of the CEO, and that cancellation of the undertaking to effect the distribution will benefit DES by NIS 20 million. Further information: According to the motion, in October-November 2011, DES approved an arrangement for the termination of the CEO's employment. According to the arrangement, inter alia, the CEO will have the option to demand that DES acquires his shares of DES (the shares that the CEO will receive after exercising the options allotted to him). According to the applicant, this option constitutes a "distribution" according to the definition of this term in section 1 of the Companies Law, 1999, and as such, it is required to comply with the earnings test set out in section 302(a) of the Law: the distribution will only be effected out of the profits of the Company. According to the applicant, the undertaking to acquire the CEO's shares did not comply with the earnings test, since at the time of the undertaking, DES had a surplus of NIS 16 million only for distribution, while the cost of the undertaking amounted to NIS 150 million. According to the motion, the value of the benefit in the undertaking to the CEO amounts to NIS 20 million. The applicant claims that when approving the arrangement for termination of the CEO's employment, the directors in DES breached their duty of care towards the Company. In view of the aforesaid, the applicant petitioned to order the cancellation of the put options granted to the CEO and the distribution that DES effected. In respect of the directors, the court is asked to determine that "they breached their duty of care towards DES by permitting the prohibited distribution.

In view of the preliminary stage of the case, DES is unable to assess the outcome of this claim. The management of DES believes that the distribution is permitted and if the CEO requires DES to acquire the shares he holds in DES, the acquisition will be in compliance with the law.

9. On November 28, 2011, a statement of claim and motion for certification of a class action suit was filed at the economic division of the Tel Aviv district court ("the motion"), against the controlling shareholder of the Company, the Company and former and serving officers in Delek Real Estate, including the Company's board of directors, the CEO and legal counsel. ("the Respondents"). Delek Real Estate is not included in the statement of claim. In the motion, the applicant claims that the shareholders of Delek Real Estate incurred damage due to the alleged acts and omissions of the respondents in the Company. The damage claimed in the statement of claim is NIS 720 million. The management of the Company believes, based on the opinion of its legal counsel, that at this preliminary stage, it is not possible to assess the outcome and risks of the claim.

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

B. Guarantees

At December 31, 2011, the following guarantees are in place:

	NIS million
Guarantees for associates (1) (2) (3) (5)	209
Guarantees for others (4) (5)	191
	400

- (1) Including guarantees of NIS 61 million in favor of Delek Real Estate. See also Note 14(G)(1).
- (2) Including guarantees of NIS 87 million in favor of IDE for construction and operation of desalination plants
- (3) The Company provided a guarantee of USD 18 million (NIS 61 million) in favor of Israel Electric Corporation Ltd. ("IEC"), according to the share of Delek Investments, Delek Drilling and Avner, guaranteed by IEC, according to its commitment pursuant to the natural gas supply agreement of 2002. The guarantee is valid until July 1, 2012.
- (4) DES provided a guarantee for the indemnification liabilities to buyers of oil and gas assets, which were exercised up to an amount of USD 12 million for the period up to December 31, 2018.
- (5) The Company is the guarantor for the liabilities of subsidiaries towards banks and third parties. The liabilities for the guarantees amounted to NIS 494 million at December 31, 2011 (including NIS 174 million for wholly-owned companies).

C. Agreements

1. At December 31, 2011, Delek Petroleum has the following agreements with third parties, for the rent and lease of stations, facilities and buildings:

	NIS million
First year	477
Second year through the fifth year	1,300
More than five years	2,121
	3,898

In addition, Delek Petroleum and its subsidiaries have entered into agreements for the purchase of fuel products (delivery in January-December 2012) amounting to NIS 5,016 million. A subsidiary in the United States has agreements with suppliers for purchasing fuels for defined periods that include commitments to purchase minimum amounts with a penalty for non-compliance with these amounts

2. See Note 16 for agreements in respect of investments in oil and gas exploration.
3. The Phoenix Insurance has agreements for the acquisition of investment property at December 31, 2011 amounting to NIS 62 million, of which NIS 18 million is for performance-based contracts (at December 31, 2010, NIS 152 million, of which NIS 105 million is for performance-based contracts).
4. The Phoenix Insurance, a subsidiary, has obligations for future investments in venture capital and investment funds amounting to NIS 616 million at December 31, 2011, of which NIS 539 million is for performance-based contracts (at December 31, 2010, NIS 775 million, of which NIS 705 million is for performance-based contracts).

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

5. A subsidiary that is a member of the TASE clearing house ("the clearing house") is responsible, together with the other clearing house members for any loss caused due to non-payment of any amount that the clearing house member owes and has not paid, or securities that a clearing house member should have transferred and did not transfer. The responsibility of each clearing house member is at the rate of the financial turnover of that TASE member compared to the financial turnover of the operations of all clearing house members on the TASE in the twelve months preceding the month in which the event occurred.
In 2002, the board of directors of the TASE resolved to establish a clearing house risk fund to secure the Company's liabilities to the clearing house. The share of each fund member will be determined according to its proportionate share on the TASE based on the average daily clearing house turnover. Accordingly, Excellence deposited its share, amounting to NIS 26 million at December 31, 2011 (NIS 26 million at December 31, 2010) in the TASE risk account. Excellence holds this amount through marketable securities.
6. In April 2009, United Mizrahi Bank Ltd. and The Phoenix Provident signed an agreement according to which the bank will provide Provident with management services member accounts in the provident fund for monthly management fees at a rate of 0.1% per year at a value of the assets of the funds managed by The Phoenix Provident ("the operating agreement"). The operating fees will be calculated on the basis of an assets report as of the end of the charging month for a period from January 2009. The agreement was assigned to The Phoenix Management in 2010. In February 2012, the operating agreement was extended until December 31, 2012. The parties are negotiating to extend the operating agreement for an additional period and to revise the operating fees. As from March 1, 2012, operating fees are expected to be 0.05% only.
7. A subsidiary of Excellence signed a number of agreements to manage member accounts in provident funds with a number of banks. The agreements were signed for different periods and for different management fees, generally at a rate of 0.1% of the total assets of the provident funds. The amount of management fees paid to the subsidiary in 2011 amounted to NIS 14 million.
8. The Phoenix Insurance Agency Ltd. ("The Phoenix Agency"), a subsidiary of The Phoenix, owns 70% of the capital and voting rights (directly and indirectly) in Agam Leaderim (Israel) Insurance Agency (2003) Ltd., which is one of Israel's largest leading agencies for life assurance and long-term savings products and financial products. According to the shareholders agreement of September 2005 between The Phoenix Agency and two individuals who are shareholders in The Phoenix Agency and who serve as CEOs in The Phoenix Agency ("the founders"), each founder was given a put option up to November 8, 2014 and The Phoenix Agency was given a call option to acquire from the founders the shares of The Phoenix Agency up to November 8, 2014, according to the provisions in the agreement. Transfer of the shares in The Phoenix Agency is subject to the right of first refusal to other parties to acquire the shares.

9. Leases

A. Leases for which the Company is a lessee in an operating leases

The Phoenix has lease agreements for vehicles. The leases are for an average of three years, without an option to extend the contract. Minimum future lease payments for operating lease contracts that cannot be cancelled at December 31, 2011 are as follows:

	NIS million
Up to 1 year	4
1-5 years	3
	<u>7</u>

Notes to the Consolidated Financial Statements

NOTE 32 – CONTINGENT LIABILITIES, GUARANTEES AND COMMITMENTS (CONTD.)

B. Leases in which the Company is the lessor

The Phoenix leases a number of commercial buildings (investment property) to external institutions. The lease agreements are for variable periods that cannot be cancelled, with rental fees linked to the CPI. Renewal of the leases at the end of their term is subject to the consent of the Company and the lessors.

Minimum future lease payments for lease contracts that cannot be cancelled at December 31, 2011:

	NIS million
Up to 1 year	56
1-5 years	221
More than five years	72
	349

D. Indemnification and insurance of officers

1. The Group has undertaken to indemnify all entitled officers of the Group for any action taken in virtue of their service as officers in the Group in the past, present and future. The Group has undertaken to indemnify all entitled officers of the Group for any action taken in virtue of their service as officers in the Group in the past, present and future.
2. The Group has decided to exempt officers of the Group from their liability under the duty of care toward the Group pursuant to chapter three, part six of the Companies Law – 1999.
3. The Company has insured the liability of officers for a total liability limit of USD 100 million.

NOTE 33 – LIENS

- A. To secure loans from banks, debentures and other institutes, amounting to NIS 10 billion at December 31, 2011, collateral was provided as follows:
 - The Company and its subsidiaries recorded fixed and floating liens on their non-current and current assets, including on inventories, specific deposits, the right to trade receivables, certain oil and gas assets, the right to receive overriding royalties, specific liens on certain shares of investees and participating units and mortgages on all the companies' rights in properties in respect of which credit was granted.
 - Subsidiaries have undertaken to meet certain conditions, including to refrain from recording a lien in favor of others without the prior agreement of the lending corporations
 - See Note 24(C) for undertakings to meet financial covenants.
- B. See Note 16 for liens in respect of investments in oil and gas assets.

Notes to the Consolidated Financial Statements

NOTE 34 – CAPITAL

A. Composition:

	December 31, 2011		December 31, 2010	
	Registered	Issued and paid up	Registered	Issued and paid up
	Number of shares			
Ordinary shares of NIS 1 par value each	15,000,000	11,723,669	15,000,000	11,723,669

The shares are listed on the TASE.

- B.** In January 2009, the Company acquired 5,504 of its shares on the TASE for NIS 0.75 million. In addition, in July 2009, the Company acquired an additional 5,459 shares for NIS 2 million. Subsequent to the acquisition, the number of dormant shares amounted to 346,407 ordinary shares. In addition, Delek Investments acquired 22,462 Company shares for NIS 10 million.

At December 31, 2010, the Company holds 346,407 dormant shares and Delek Investments holds 22,462 Company shares.

- C.** In May 2009, NIS 1,120,169 par value debentures of the Group were converted into 3,890 Group shares.
- D.** In 2010, special purpose companies issuing ETFs acquired Group shares in a net amount of NIS 11 million.
At December 31, 2010, SPCs own 69,555 ordinary shares of the Company.

In 2011, special purpose companies issuing ETFs acquired Group shares in a net amount of NIS 10 million.

At December 31, 2010, SPCs own 79,706 ordinary shares of the Company.

- E.** In April 2010, the Company issued 255,378,000 par value debentures (Series DD) exercisable into ordinary shares of NIS 1 par value each. See Note 26.
- F.** In September 2011, Delek Investments acquired 18,354 shares of the Company on the TASE for NIS 10 million, which are presented as treasury shares in the Company's equity. Subsequent to the acquisition, Delek Investments holds 40,816 ordinary shares of the Company. The Company also holds 346,407 of its shares. See section B above.

- G.** Unexercised option warrants at the reporting date:

	Balance of option warrants at December 31, 2011	Exercise supplement at December 31, 2011 NIS	Exercisable
Series 6 *)	260,000	798.9387	Up to September 9, 2013
Convertible options – Debentures (Series DD) *)	240,365	1,068.4608	Up to October 15, 2012
	<u>500,365</u>		

*) The exercise addition and conversion price are unlinked and subject to adjustments.

- G.** In February-March 2010, 33,416 Series 5 option warrants were exercised into 33,416 ordinary shares of the Company for NIS 16.3 million. Following the exercise, the Company's equity increased by NIS 29 million, reflecting the additional exercise and recognition of the value of the liability shortly before the exercise into capital. Subsequent to the exercise, the issued and paid up share capital amounted to 11,723,669 ordinary shares of the Company of NIS 1 par value each. The balance of Series 5 options expired in March 2010.

Notes to the Consolidated Financial Statements

NOTE 34 – CAPITAL (CONTD.)

H. Dividends

1. On March 24, 2010, the Group declared the distribution of a dividend to its shareholders totaling NIS 100 million (NIS 8.79 per share). The dividend was paid in April 2010.
2. On May 31, 2010, the Group declared the distribution of a dividend to its shareholders totaling NIS 150 million (NIS 13.18 per share). The dividend was paid in June 2010.
3. On July 26, 2010, the Group declared the distribution of a dividend to its shareholders totaling NIS 120 million (NIS 10.54 per share). The dividend was paid in August 2010.
4. On September 21, 2010, the Group declared the distribution of a dividend to its shareholders totaling NIS 90 million (NIS 7.9 per share). The dividend was paid in October 2010.
5. On November 30, 2010, the Group declared the distribution of a dividend to its shareholders totaling NIS 500 million (NIS 43.94 per share). The dividend was paid in December 2010.
6. On March 31, 2011, the Group declared the distribution of a dividend to its shareholders totaling NIS 200 million (NIS 17.58 per share). The dividend was paid in April 2011.
7. On May 30, 2011, the Group announced the distribution of a dividend to its shareholders totaling NIS 105 million (NIS 9.23 per share). The dividend was paid in June 2011.
8. On August 31, 2011, the Group announced the distribution of a dividend to its shareholders totaling NIS 100 million (NIS 8.8 per share). The dividend was paid in September 2011.
9. On November 29, 2011, the Group announced the distribution of a dividend to its shareholders totaling NIS 100 million (NIS 8.8 per share). The dividend was paid in December 2011.
10. On March 29, 2012, the Group announced the distribution of a dividend to its shareholders totaling NIS 120 million.

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER

- A. The information below regarding the required and existing equity of The Phoenix Insurance is in accordance with Control of Financial Services Regulations (Insurance) (Minimum Equity Required of an Insurer) 1998 (Amendment), 2004 ("the Capital Regulations") and the guidelines of the Supervisor.

	December 31 2011	2010 NIS million
Minimum capital		
Amount required at the balance sheet date according to the Capital Regulations and Supervisor's directives (b)	2,441	1,982
Actual amount calculated in accordance with the Capital Regulations		
Tier 1 capital	1,823	1,847
Hybrid tier 2 capital	670	397
Subordinated tier 2 capital	545	710
Total actual amount calculated in accordance with the capital regulations	3,038	2,954
Excess	597	972
Apart from the general requirements in the Companies Law, distribution of a dividend from excess capital in insurance companies is also subject to liquidity requirements and compliance with the investment regulations. In this matter, the amount of the investment in investees, against which it is mandatory to place excess capital under the Commissioner's guidelines, therefore constituting non-distributable excess	330	299

Notes to the Consolidated Financial Statements

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER (CONTD.)

	December 31	
	2011	2010
	NIS million	
(a) The required amount includes capital requirements for:		
General insurance/initial capital	430	414
Long-term care insurance	44	42
Exceptional risks in life assurance	224	205
Deferred acquisition costs in life assurance and health insurance	755	700
Requirements for guaranteed yield plans	-	-
Unrecognized assets as defined in the Capital Regulations	67	87
Investments in consolidated insurance companies and management companies	91	68
Investment and other assets	559	552
Catastrophe risks in general insurance	80	55
Operating risks	191	170
Total amount required under the amended Capital Regulations (b)	2,441	2,293
Less the difference required for completion up to December 31, 2011 (b)	-	(311)
	2,441	1,982

- (b) In November 2009, an amendment was published to the Control of Financial Services Regulations (Minimum Capital Required from an Insurer) (Amendment), 2009 ("the amendment").

According to the amendment, by the publication date of the financial statements, an insurer is required to increase its capital for the difference between the capital required pursuant to the regulations, before and after the amendment ("the difference"). The difference will be calculated at each reporting date. The capital will be increased at the dates and rates set out below:

- Up to the publication date of the financial statements as of December 31, 2009, at least 30% of the difference
- Up to the publication date of the financial statements as of December 31, 2010, at least 60% of the difference
- Up to December 31, 2011, the entire difference will be paid.

The amendment includes, in addition to the existing capital requirements, capital requirements for the following categories:

- A. Operational risks
- B. Market and credit risks, as a percentage of the assets, based on the extent of the risk typical of the various assets.
- C. Catastrophe risks in general insurance
- D. Capital requirements for guarantees

In addition, capital requirements were expanded for the following categories:

- A. Plans guaranteeing life assurance yields against which or against some of which there are no earmarked debentures.
- B. Capital requirements for the insurer's holding in management companies of provident funds and pension funds.

In addition, the exemptions were granted for the following instances:

Notes to the Consolidated Financial Statements

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER (CONTD.)

- Calculation of the capital required for information system development expenses, subject to the Supervisor's approval
- Deduction of the reserve for tax created for unrecognized assets held contrary to the investment regulations or contrary to the Commissioner's instructions.
- It was determined that the Supervisor may allow, subject to terms that he defines, a reduction of the capital requirements of 35% of the original difference, for acquisition of provident fund operations or a provident fund management company, for an insurer whose equity deficit is due to a capital requirement in this amount only.

In the amendment, the definition of basic capital was deleted, definitions of Tier 1 and Tier 2 capital were changed and a definition for Tier 3 capital was added. The definitions of Tier 2 and Tier 3 capital are subject to the conditions and rates determined by the Supervisor.

In continuation and according to the Supervisor's intention to implement Solvency II, the EU directive for regulating the solvency of insurers ("the directive"), in August 2011, a circular was published pertaining to the composition of the recognized equity of an insurer ("the circular"), which is effective as from the financial statements for the period ended September 30, 2011.

The directive prescribes provisions for the structure of an insurer's recognized capital, and principles for recognizing capital components and classifying them into the different capital levels:

1. Tier 1 capital: including basic tier 1 capital (in the amount of the capital attributable to the equity holders of the parent), capital notes or non-cumulative preferred stock and hybrid tier 1 capital. Hybrid tier 1 capital includes loss-absorbing capital instruments for the insurer by deducting interest payments and deferring principal payments and their payment is deferred over all the insurer's liabilities. The first repayment date of these instruments will be after repayment of the earlier of the latest insurance liabilities or 49 years, but not before the end of ten years from the issuance date. Under certain circumstances, the instrument reserve will be removed or converted to ordinary shares.
2. Tier 2 capital: including loss-absorbing financial instruments for the insurer by deferring principal and interest payments, and whose repayment is deferred over any other debt, except for tier 1 capital. The first repayment date of tier 2 capital instruments is after the end of the period representing a weighted average of the period for repayment of the insurance liabilities plus two years, or 20 years, whichever is earlier, but not before the end of eight years from the issuance date.
3. Tier 3 capital: including loss-absorbing capital instruments ("bail in") for the insurer by deferring principal payments only, and whose repayment is deferred over any other debt, except for tier 1 capital (although it can be determined that it will not be deferred over other tier 2 capital or tier 3 capital). The first repayment date of tier 3 capital instruments is not earlier than the end of five years from the date of its issue.

In this respect, insurance liabilities include liabilities that are non-performance based, without the share of the liabilities fully backed by Hetz debentures and less the share of the reinsurers.

The recognized equity of the insurer is the amount of the components and instruments included in the different layers, at the following rates:

The total rate of tier 1 capital will not fall below 60% of the total equity of the insurer. The total rate of the basic tier 1 capital will not fall below 70% of the tier 1 capital.

The total rate of hybrid tier 1 instruments will not exceed 20% of the total tier 1 capital.

The total rate of tier 3 capital will not exceed 15% of the total equity of the insurer.

Notes to the Consolidated Financial Statements

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER (CONTD.)

The directive includes a temporary order for the structure of an insurer's equity from September 30, 2011 through to the effective date of the directive in Israel announced by the Supervisor.

According to the temporary order, the total rate of capital instruments included in tier 2 capital will not exceed 50% of the basic capital.

Tier 2 capital is defined as the total of the following components:

Subordinated notes, whether convertible into shares or not, issued for at least five years, and their maturity date is at least two years after the reporting date, provided they are not issued to the controlling shareholder.

Subordinated notes issued to controlling shareholders, which are linked to the CPI at most, but do not bear interest and their maturity date is no less than two years after the reporting date.

In addition to the temporary order, the circular includes the following transitional provisions:

Tier 2 capital issued up to December 31, 2009 is recognized up to its final maturity date under conditions recognized up to publication of this circular.

Tier 2 capital issued as from January 1, 2010 onwards will not be recognized upon application of the directive in Israel or as from January 31, 2013, whichever is earlier.

Hybrid tier 1, tier 2 and tier 3 capital instruments, issued from January 1, 2010 onwards and approved by the Supervisor, will be recognized up to their final maturity date with the same conditions and in accordance with the limitations of the rates applicable to the different levels.

Hybrid tier 1, tier 2 and tier 3 capital instruments, issued from January 1, 2010 onwards and approved by the Supervisor, will be recognized up to their final maturity date with the same conditions and in accordance with the limitations of the rates applicable to the different levels.

Hybrid tier 1, tier 2 and tier 3 capital instruments, issued from the effective date of the circular, with the conditions set out therein, will be fully recognized upon application of the directive in Israel up to their maturity date.

In September and October 2010 and November 2011, a wholly-owned subsidiary of The Phoenix Insurance, The Phoenix Capital Raising, issued NIS 400 million and NIS 361.5 million, respectively, recognized in hybrid tier 2 capital.

In accordance with the Supervisor's circular of March 29, 2009, as from the financial statements for 2008 and through to December 30, 2010, an insurance company and a management company require the consent of the Supervisor before distributing a dividend. According to the circular, in general, the amount of the dividend will not exceed 25% of the distributable earnings.

Further to the circular, in March 2010 a clarification was issued in respect of the criteria for approving distribution of a dividend by an insurer ("the clarification").

In accordance with the clarification, an insurance company may apply for the Supervisor's approval to distribute a dividend, as from the publication date of the periodic reports for 2009, subject to equity as set out in the clarification and the submission of an annual profit forecast for 2010 and 2011, an updated debt service plan approved by the board of directors of the holdings company, an operative plan to raise capital approved by the board of directors of the insurance company and the minutes of the meetings of the board of directors of the insurance company in which distribution of the dividend was approved.

However, the clarification prescribed that a company with equity, subsequent to distribution of the dividend, that is 110% higher than the amount required in the clarification, may distribute a dividend without the prior approval by the Supervisor, provided the Supervisor was notified of such and the relevant documents were submitted to the Supervisor prior to distribution of the dividend.

Notes to the Consolidated Financial Statements

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER (CONTD.)

In December 2011, the Supervisor published a letter ("the second clarification") that includes the criteria set out in the clarification in the addendum to the requirement for approval of the debt service plan by the board of directors of an insurance company as well and the requirement that after the Supervisor's approval, the minimum ratio between the existing equity after distribution of a dividend and the amount required will be 105%. For distribution of a dividend that does not require prior approval of the Supervisor, the ratio between the total equity after distribution of the dividend and the amount required in the second clarification amounted to 115% (instead of 110%).

In April 2011, The Phoenix Insurance distributed a dividend of NIS 80 million to The Phoenix Holdings.

4. On July 10, 2007, the EU adopted a proposed draft to the Solvency II Directive ("the proposed directive"). The proposed directive constitutes fundamental and comprehensive change of the regulations relating to ensuring solvency and capital adequacy of insurance companies in EU countries.

Pursuant to the circular published by the Supervisor, the intention is to implement the provisions of the proposed directive for insurance companies in Israel at the same date of application in EU companies. The proposed directive is based on three levels: quantitative, qualitative and disclosure requirements.

The Phoenix is assessing the implications of the circular, however at this stage, it is unable to assess the consequences arising from the circular, as the quantitative requirements, application method and exact implementation date have yet to be formulated into a final requirement.

In 2009, the results of the fifth quantitative impact study (QIS5) was submitted to the Supervisor, based on December 31, 2009 data.

5. In accordance with the Supervisor's circular published on January 25, 2009 regarding relief for required equity from the insurance companies, an asset held in contravention of the Investment Regulations with a passive deviation created subsequent to October 1, 2008, shall not be considered as an unrecognized asset as defined in the Capital Regulations, subject to the prior approval of the Supervisor. At the end of the reporting period, The Phoenix Insurance has passive deviations of NIS 23 million that are not considered as an unrecognized asset in accordance with the approval of the Supervisor.
6. In June 2008, the Commissioner published a circular relating to application of IFRS presentation guidelines and criteria for calculating the required and recognized capital of insurance companies. The objective of the circular is to set out guidelines for application of the Capital Regulations regarding investments in investees (including insurance companies and management companies controlled by insurance companies). According to the circular, the capital requirements in accordance with the Capital Regulations will continue to be based on separate financial statements. To calculate the recognized capital in accordance with the Capital Regulations, the investment by an insurance company in an insurance company or a controlled management company and in other investees will be based on the rate of the holdings.
7. In February 2012, the Control of Financial Services Regulations (Provident Funds) (Minimum Capital Required of a Provident Fund or Pension Fund Management Company), 2012 were issued, together with the Income Tax Regulations (Principles for the Approval and Management of a Provident Fund (Second Amendment), 2012 ("the new regulations").

Notes to the Consolidated Financial Statements

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER (CONTD.)

In accordance with the new regulations, capital requirements from management companies are the higher of initial equity of NIS 10 million or the sum of the following three amounts: (1) 0.1% of total managed assets up to a maximum of NIS 15 billion; (2) 0.05% of total managed assets above the maximum stated in section (1) above; (3) 25% of annual expenses.

The Commissioner of the Capital Market Insurance and Savings ("the Commissioner") may order a reduction or increase in the capital requirements, taking into account, inter alia, the risks typical to the operations of the management company, provided the increase in capital requirements is for a defined period.

By virtue of his authority, in February 2012, the Commissioner published a circular for exemptions for capital requirements in certain management companies.

The management company is required to provide additional capital for the controlled management companies and for the amount of assets held contrary to the provisions of equity investment provisions in the new regulations.

The new regulations also include a requirement for holding liquid assets at a rate of at least 50% of the minimum required equity.

A management company may distribute dividends only if its equity is at least at the level required by the new directives.

The new regulations include transitional provisions for completion of the difference between capital required at the dates set out below and capital required immediately prior to publication of the new regulations ("the difference"), up to December 31, 2014, as follows:

Up to the publication date of the financial statements as of March 31, 2012, at least 30% of the difference

Up to the publication date of the financial statements as of December 31, 2012, at least 60% of the difference

Up to the publication date of the financial statements as of December 31, 2013, at least 80% of the difference

Up to December 31, 2014, the entire difference will be paid.

According to the initial estimate, at the end of the reporting period, if the capital requirements for management companies are fully implemented, without taking into account the milestones, the capital requirements will have the following effect:

- A) Capital requirements for the management company of The Phoenix Pension and Provident will decrease by NIS 58 million, mainly due to cancellation of the capital requirements for deferred acquisition costs.
- B) Capital requirements for the management company of Excellence Provident will increase by NIS 43 million.

8. The Phoenix Insurance undertook to complement, at any time, the shareholders' equity of The Phoenix Pension and Provident Ltd. ("the Phoenix Pension") to the amount determined in the Income Tax Regulations (Regulations for Approval and Management of Provident Funds), 1964. The undertaking will be valid as long as The Phoenix Insurance controls The Phoenix Pension, directly or indirectly.
9. In October 2011, the Supervisor issued a letter for managers of insurance companies regarding supervision and management of equity, to ensure a current process for examination and monitoring of the equity management method in insurance companies, based on fluctuations in financial markets. The letter included a report form for the estimated capital position, which insurance companies are required to complete and submit to the Supervisor's office every month.

Notes to the Consolidated Financial Statements

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER (CONTD.)

10. In July 2011, The Phoenix Insurance received a letter from the Supervisor, following the approval received in December 2009 for the internal rating model developed by The Phoenix Insurance ("the model") (according to which, in respect of the provisions in section 5(A)(2) of the circular, provision of non-marketable credit by institutional bodies, the rating determined in accordance with the model will be recognized as rating equivalent to that of a rating company, under the conditions set. As part of the approval, it was determined that up to completion of the additional validity and control tests required to test approval of use of the model to determine the rate of capital required for credit risk, The Phoenix Insurance may allocate capital for non-marketable debt assets with a total amount of up to 3% of the amount of the assets held against non-performance based liabilities (including equity), which were classified according to the model and are not externally rated, up to the periodic reports as of September 30, 2012, as follows:

- 1) Attribution of capital according to the capital regulations
- 2) A reduction of 50% from the difference between the capital required under section 1 and the capital required for the rating according to the model

The Phoenix Insurance implemented the regulations and accordingly, the capital requirements at December 31, 2011 decreased by NIS 27 million.

11. As from 2012, the new reinsurance agreements will come into effect, which will increase the capital requirements for exposure to catastrophe by NIS 43 million.

12. In February 2012, the Supervisor of Insurance sent the managers of insurance companies draft clarifications for differences in the application method by the companies and for interpretations in issues related to calculation of capital of insurance companies, primarily:

- 1) Required capital for investments: According to the Capital Regulations, the capital required for assets will be calculated according to the sum of the multiples of each asset held against non-performance based insurer liabilities, other than assets that require additional equity according to the capital requirements and assets held against surplus capital, meaning the calculation of capital requirements for assets is not cyclic and will be calculated according to the capital on the basis of capital requirements for the assets. To reflect the form of this calculation, the reporting file was updated. Following the change in the calculation method, as set out above, the capital requirement for investment assets decreased by NIS 89 million.
- 2) Capital requirements for operating risk – capital requirements for derivative operating risk, inter alia, from the amount of general and administrative expenses for performance-based life assurance. In accordance with the clarification, the amount of general and administrative expenses for performance-based life assurance will include the three components of the full amount of general and administrative expenses: cost of claims, acquisition costs and other expenses
- 3) A deficit or surplus generated in profit-sharing policies: In accordance with the Capital Regulations, there is no capital requirement for assets held against performance-based liabilities. The requirement is calculated on the basis of classification of the assets into different classes of liabilities as reported in Form 106. According to the clarification, if there is surplus/deficit in assets held against performance-based liabilities, an addition/deduction of the capital requirements is calculated at a rate of 0.5% of the amount of the surplus/deficit.
- 4) Classification of derivative financial instruments: According to the clarification, capital requirements for derivative financial instruments will be calculated for the amount of the derivative financial instruments with a positive fair value only, without offsetting derivative financial instruments with negative fair value, except when accounting principles permit offsetting.

Notes to the Consolidated Financial Statements

NOTE 35 – MINIMUM CAPITAL REQUIRED OF AN INSURER (CONTD.)

- 5) Reporting of a commitment to invest in investment reserves: According to the clarification, there is a capital requirement at a rate of 7.5% of the amount of the irrevocable contractual commitment to the investment in investment reserves under non-performance based liabilities.
- 6) External rating: A capital requirement for a debt asset or exposure to a reinsurer is calculated on the basis of an external rating of a rating company approved the Supervisor or on the basis of an internal rating model approved by the Supervisor. In accordance with the draft, from the financial statements for the second quarter of 2012 onwards, if different external ratings are set by a number of rating companies, the lowest rating will be taken into account.
- 7) Surplus/deficit capital of an insurance company for operations between the reporting date and the publication date: Any material active or passive capital operation subsequent to the reporting date (including converting subordinated tier 2 capital or hybrid capital to unrecognized, share issue or distribution of a dividend) will affect the surplus/deficit capital of the insurance company at the publication date of the report.

Sections 1 to 5 were applied in calculation of the required capital at the reporting date. There are also discussions between the Supervisor of Insurance and the insurance companies regarding the clarifications set out above.

13. In March 2012, the Finance Committee approved the draft Control of Financial Services Regulations (Provident Funds) (Investment Regulations Applicable for Management Companies and Insurers), 2012 ("the new draft investment regulations").

The regulations include changes for control and holding of means of control by an insurer ("Regulation 33"). According to the regulations, an insurer will hold against its recognized surplus capital its investment in another insurer, management company, agent, corporation whose sole business is investment management or providing credit for the insurer or other institutional bodies controlled by the insurer or by an entity controlling the insurer, and another corporation. Notwithstanding the aforesaid, the investment in another insurer and management company can be also held against the minimum equity required from an insurer or against its other liabilities, provided the unrecognized surplus as a result of the investment in a management company is held against the recognized surplus capital of the insurer beyond the minimum equity required. However, an insurer that controls a management company, did not take loans to finance an intangible asset from an entity that is not an insurer, or does not control the insurer, may hold up to 50% of the unrecognized surplus against the recognized capital surplus of the insurer and against its other liabilities.

In this matter:

"Unrecognized surplus": surplus capital generated for an insurer due to the holding of the management company in an intangible asset recognized in its financial statements as of January 1, 2012.

"Intangible asset" as defined in the capital regulations for management companies

According to draft no. 3 of the circular for investment regulations applicable to institutional bodies published by the Supervisor in March 2012, the transitional provisions stipulate that article 33 applies fully from December 31, 2013 and at a rate of 50% up to December 3, 2012. The insurance companies and the Supervisor are discussing the draft and the Company is studying its implications.

14. In accordance with the US National Association of Supervisor of insurances (NAIC), Republic requires minimum capital of USD 51 million. At December 31, 2011, the capital of Republic amounted to USD 218 million.

Notes to the Consolidated Financial Statements

NOTE 36 – COST OF REVENUE

	Year ended		
	December 31		
	2011	2010	2009
	NIS million		
Purchase of oil, fuel and products	43,270	26,804	20,582
Salary and incidentals	461	169	160
Depreciation, depletion and amortization	412	374	275
Other production expenses and costs	1,167	774	472
Transportation	113	112	96
Increase in residual insurance liabilities and payments for insurance contracts	5,260	7,749	9,347
Cost of electricity supplied	92	110	101
Oil and gas exploration and appraisal expenses	128	125	121
	50,903	36,217	31,154

NOTE 37 – SELLING, MARKETING AND GAS STATION OPERATING EXPENSES

	Year ended		
	December 31		
	2011	2010	2009
	NIS million		
Salary and incidentals	770	657	647
Maintenance of gas stations	1,015	740	734
Advertising and sales promotion	65	80	62
Depreciation and amortization	387	291	269
Commissions for agents	118	97	82
Commissions and acquisition costs in insurance companies	1,416	1,352	1,338
Other	386	285	253
	4,157	3,502	3,385

Notes to the Consolidated Financial Statements

NOTE 38 – GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended		
	December 31		
	2011	2010	2009
	NIS million		
Salary and incidentals	1,107	1,011	900
Depreciation and amortization	256	276	241
Office maintenance	125	130	136
Professional services	191	137	133
Other	205	218	213
	<u>1,884</u>	<u>1,772</u>	<u>1,623</u>

NOTE 39 – OTHER REVENUES (EXPENSES), NET

	Year ended		
	December 31		
	2011	2010	2009
	NIS million		
Compensation from an insurance company	-	62	419
Provision for impairment of property, plant and equipment	(324)	-	-
Goodwill impairment of intangible assets	(359)	(118)	(125)
Gain on disposal of assets	72	-	-
Expenses for structural change	-	-	(15)
Gain from negative goodwill	-	-	15
Other revenues (expenses), net	9	(32)	(25)
	<u>(602)</u>	<u>(88)</u>	<u>269</u>

Notes to the Consolidated Financial Statements

NOTE 40 – A. FINANCE INCOME

	Year ended		
	December 31		
	2011	2010	2009
	NIS million		
Net change in fair value of financial assets at fair value through profit or loss	1	19	102
Profit from disposal of available-for-sale securities	425	68	109
Interest-bearing loans from banks	31	36	44
Dividends from available-for-sale securities	12	12	17
Derivative financial instruments	-	2	-
Finance revenues from associates	48	86	66
Gain from premature payment and exchange of debentures	-	-	82
Other	109	48	88
	<u>626</u>	<u>271</u>	<u>508</u>
B. FINANCE EXPENSES			
Finance expenses for credit from banks, debentures and others	1,655	1,294	1,299
Impairment of available-for-sale securities	98	217	3
Loss from disposal of available-for-sale securities	83	26	-
Derivative financial instruments	14	6	48
Other finance expenses, net	101	112	82
	<u>1,951</u>	<u>1,655</u>	<u>1,432</u>

Notes to the Consolidated Financial Statements

NOTE 41 – EXPENSES BY TYPE OF POLICY

Year ended December 31, 2011:

	Policy with risk factor (including appendixes)				Risk-free policy Risk sold as single policy		
	According to policy date						
	Up to 1990 (1)	Up to 2003	From 2004		Individual	Collective	Total
			Non- performance based	Performance based NIS million			
Gross premiums:							
Traditional/mixed	92	49	-	2	-	-	143
Saving factor	76	935	-	1,772	-	-	2,783
Other	24	234	-	104	276	106	744
Total (2)	192	1,218	-	1,878	276	106	3,670
Premiums for direct investment contracts for insurance reserves	-	-	-	132	-	-	132
Financial margin including management fees (3)	78	99	-	59	1	-	237
Profit (loss) from life assurance operations	29	21	-	(81)	68	7	44
Other comprehensive income from life assurance operations	-	-	-	-	-	-	-
Comprehensive income (loss) from life assurance operations	29	21	-	(81)	68	7	44
Profit from pension and annuity							(63)
Total profit (loss) from life assurance and long-term savings							(19)
Premium for insurance contracts – new business	-	-	-	303	53	-	356
One-time premium for insurance contracts	-	5	-	730	-	-	735
Premium for insurance contracts – new business	-	-	-	11	-	-	11

1. The products issued until 1990 (including the growth in respect thereof) were designed mainly to guarantee yield, and they are hedged mainly by designated debentures.
2. The increase in existing policies is not included in the annualized premium for new business, but in the operational expenses of the original policy.
3. The financial margin does not include the Company's further income collected as a percentage of the premium and it is calculated according to deduction of expenses for investment management. The financial margin in policies with guaranteed yield is based on the actual investment income during the reporting period net of the product of the guaranteed yield rate during the year, multiplied by the average reserve for the year in the various insurance funds. In performance based contracts, the financial margin is the total fixed and variable management fees calculated on the basis of the average yield and balance of the insurance reserves.

Notes to the Consolidated Financial Statements

NOTE 41 – EXPENSES BY TYPE OF POLICY (CONTD.)

Year ended December 31, 2010:

	Policy with risk factor (including appendixes)				Risk-free policy		
	According to policy date				Risk sold as single policy		
			From 2004				
	Up to 1990 (1)	Up to 2003	Non- performance based	Performance based NIS million	Individual	Collective	Total
Gross premiums:							
Traditional/mixed	109	49	-	1	-	-	159
Saving factor	64	924	-	1,226	-	-	2,214
Other	24	238	-	91	236	102	691
Total (2)	197	1,211	-	1,318	236	102	3,064
Premiums for direct investment contracts for insurance reserves	-	-	-	88	-	-	88
Financial margin including management fees (3)	109	112	-	47	2	2	272
Profit (loss) from life assurance operations	85	42	-	(95)	35	(7)	60
Other comprehensive income from life assurance operations	29	4	-	2	2	1	38
Comprehensive income (loss) from life assurance operations	114	46	-	(93)	37	(6)	98
Profit from pension and annuity							4
Total profit (loss) from life assurance and long-term savings							102
Premium for insurance contracts – new business	-	-	-	289	47	-	336
One-time premium for insurance contracts	-	6	-	352	-	-	358
Premium for insurance contracts – new business	-	-	-	12	-	-	12

1. The products issued until 1990 (including the growth in respect thereof) were designed mainly to guarantee yield, and they are hedged mainly by designated debentures.
2. The increase in existing policies is not included in the annualized premium for new business, but in the operational expenses of the original policy.
3. The financial margin does not include the Company's further income collected as a percentage of the premium and it is calculated according to deduction of expenses for investment management. The financial margin in policies with guaranteed yield is based on the actual investment income during the reporting period net of the product of the guaranteed yield rate during the year, multiplied by the average reserve for the year in the various insurance funds. In performance based contracts, the financial margin is the total fixed and variable management fees calculated on the basis of the average yield and balance of the insurance reserves.

Notes to the Consolidated Financial Statements

NOTE 41 – EXPENSES BY TYPE OF POLICY (CONTD.)

Year ended December 31, 2009:

	Policy with risk factor (including appendixes)				Risk-free policy		
	According to policy date				Risk sold as single policy		
			From 2004				
	Up to 1990 (1)	Up to 2003	Non-performance based	Performance based	Individual	Collective	Total
				NIS million			
Gross premiums:							
Traditional/mixed	116	56	-	1	-	-	173
Saving factor	64	931	-	819	-	-	1,814
Other	26	245	-	78	214	98	661
Total (2)	206	1,232	-	898	214	98	2,648
Premiums for direct investment contracts for insurance reserves	-	-	-	81	-	-	81
Financial margin including management fees (3)	75	87	-	31	2	2	198
Profit (loss) from life assurance operations	64	87	-	(83)	20	8	96
Other comprehensive income from life assurance operations	33	5	-	2	3	2	45
Comprehensive income (loss) from life assurance operations	96	92	-	(81)	23	10	140
Profit from pension and annuity							50
Total profit (loss) from life assurance and long-term savings							190
Premium for insurance contracts – new business	-	-	-	238	33	-	271
One-time premium for insurance contracts	-	8	-	89	-	-	97
Premium for insurance contracts – new business	-	-	-	4	-	-	4

1. The products issued until 1990 (including the growth in respect thereof) were designed mainly to guarantee yield, and they are hedged mainly by designated debentures.
2. The increase in existing policies is not included in the annualized premium for new business, but in the operational expenses of the original policy.
3. The financial margin does not include the Company's further income collected as a percentage of the premium and it is calculated according to deduction of expenses for investment management. The financial margin in policies with guaranteed yield is based on the actual investment income during the reporting period net of the product of the guaranteed yield rate during the year, multiplied by the average reserve for the year in the various insurance funds. In performance based contracts, the financial margin is the total fixed and variable management fees calculated on the basis of the average yield and balance of the insurance reserves.

Notes to the Consolidated Financial Statements

NOTE 42 – TAXES ON INCOME

A. Tax laws that apply to the Group companies

1. **Income Tax (Inflationary Adjustments) Law, 1985**

According to the Law, until the end of 2007, for tax purposes, results of the Group companies in Israel are adjusted to changes in the CPI.

In February 2008, the Knesset passed an amendment to the Income Tax (Inflationary Adjustments) Law, 1985, which limits the scope of the Adjustments Law from 2008 onwards. Since 2008, the results for tax purposes are measured at nominal values, with the exception of certain adjustments for changes in the Israeli CPI up to December 31, 2007. Adjustments relating to capital gain such as for sale of property (betterment) and securities continue to apply until disposal. Since 2008, the amendment to the law includes the cancellation of the additions and deductions for inflation and the additional deduction for depreciation.

2. **Petroleum Profits Tax Law, 2011**

In January 2011, the government of Israel approved the recommendations of the Sheshinski commission to amend taxes in the oil and gas exploration sector in Israel. Following the recommendations, on March 30, 2011, the Petroleum Profits Taxation Law, 2011 was passed and on April 10, 2011, it was published in the Official Gazette. Implementation of the recommendations will change the taxation applicable to the partnership's revenue, including elimination of the depletion allowance (see section B below) and introduction of a levy for oil and gas profits according to a formula established by law, with transitional provisions for producing projects or projects that are scheduled to begin production by 2014. The main points of the law are as follows:

- A. The rate of royalties paid to the state remains unchanged.
- B. The depletion allowance is abolished.
- C. The proposed formula for the levy is based on the recovery factor ("the R factor"), according to the ratio between the net cumulative revenues from the project and the cumulative investments as defined in the Law. The minimum rate of the levy will be 20% if the R factor is 1.5, and will rise progressively up to a maximum rate of 50%, until the R Factor reaches 2.3. In addition, it was determined that the rate of the levy will be reduced at a multiple of 0.64 in the difference between the rate of corporate tax rate set out in section 126 of the Income Tax Ordinance for each tax year and a tax rate of 18%.

Additional provisions were set for the levy, such as: the levy will be recognized as a deductible expense for income tax purposes, will not include export installations, will be calculated and imposed on each reservoir separately (ring fencing); for payment by the holder of the oil right calculated as a percentage of the produced oil, the payee will be required to pay a levy on the amount of payment received, and this amount will be deducted from the levy liability of the holder of the oil right.

- D. Investments will be awarded accelerated depreciation at a rate of 10%, with an option of choosing depreciation in the amount of the taxable income in that year.
- E. Taxation of oil partnerships: The law stipulates provisions for calculation and reporting of the partners' profits in oil exploration partnerships, including the calculation of taxes for these profits.

Notes to the Consolidated Financial Statements

NOTE 42 – TAXES ON INCOME (CONTD.)

- F. Interim provisions were set out, including the following:
- 1) The provisions of this law will apply to a project that commenced commercial production before the effective date, with the following changes:
 - a) If a levy is imposed on a project in the tax year of the effective date, the rate of the levy in that tax year will be half of the rate of the levy that would have been imposed on the oil profits were it not for the provisions of this subsection, and no more than 10%.
 - b) If the R factor in the tax year of the effective date exceeds 1.5, rules were determined for calculation of the R factor for each subsequent tax year.
 - c) The rate of levy imposed on the venture's oil profits in each of the tax years from 2012 through to 2015 will be equal to half of the rate of the levy that would be imposed on the oil profits without the provisions of this section.
 - 2) The following provisions will apply to a project that starts commercial production after the effective date but before January 1, 2014:
 - a) The minimum levy factor will be 2 instead of 1.5 and the maximum will be 2.8 instead of 2.3.
 - b) The rate of depreciation for an asset acquired in 2011-2013 will be 15% instead of 10%.
- G. On December 5, 2011, the Law for Change in the Tax Burden (Amendments to Legislation), 2011, was published, as set out in section B(1) below. In accordance with the law, the rate of the oil and gas profits levy will also be reduced, as set out above, to a maximum rate of 45.52%.
- H. According to the amendment to the Income Tax Regulations (Deductions from Income of Oil Rights Holders), 2011 ("the amendment"), recognition as a current expense in development expenses of reservoirs that start commercial production after January 1, 2014 will be eliminated and amortization will be applied in accordance with the Taxation of Petroleum Profits Law.

According to the amendment, the depletion allowance was eliminated as from May 1, 2011. The provisions regarding the levy on oil and gas profits are effective as from April 10, 2011, and the provisions regarding taxation of an oil partnership (section 5 above) is effective as from the 2011 tax year.

3. Foreign subsidiaries

Foreign subsidiaries are subject to the provisions of the law in the countries in which they operate.

Notes to the Consolidated Financial Statements

NOTE 42 – TAXES ON INCOME

B. Tax rates applicable to Group companies

1. Companies in Israel

The rate of corporate tax in Israel in 2009 was 26%; in 2010 – 25%; in 2011 – 24%.

An association of individuals is taxed on real capital gain at the corporate tax rate in the year of the sale.

According to a temporary order for 2006-2009, for the sale of an asset that is not a security traded on the TASE (other than unpaid goodwill) acquired prior to January 1, 2003 and sold before December 31, 2009, for the share in the real capital gain attributed on a linear basis to the period up to December 31, 2002, corporate tax will apply at the rate set out in the Ordinance, for the year of the sale. For the share of real capital gain attributed on a linear basis to the period from January 1, 2003, tax at a rate of 25% will apply up to the date of the sale.

On December 5, 2011 the Knesset passed the Law for Change in the Tax Burden (Amendments to Legislation), 2011 ("the Law"). As from 2012, the Law eliminates, inter alia, a progressive reduction in the rate of corporate tax rate. The Law also increases the corporate tax rate to 25% as from 2012. In view of the increase in the corporate tax rate to 25% as aforesaid, the real capital gains tax rate and the real betterment tax rate will also increase.

The statutory tax applicable to consolidated insurance companies in Israel comprises corporate tax, payroll tax and capital gains tax.

According to the Value Added Tax Order (Tax Rate on NPOs and Financial Institutions) (Temporary Order), 2009 that the Knesset passed in June and December 2010 and December 2010, the rate of capital gains tax that applies to a financial institution is as follows 16.5% from July 1, 2009 to December 31, 2009; 16% in 2010-2012; and 15.5% from January 1, 2013.

Following these changes, the total rate of tax that applies to financial institutions is as follows: 2009 – 36.2%; 2010 – 35.34%; 2011 – 34.48%; 2012 – 35.34%; and from 2013 onwards – 35.06%.

The effect of the change on the tax rates resulted in a decrease of NIS 75 million in the net profit attributable to the equity holders of the parent in 2011 (including for associates).

2. Foreign subsidiaries

- The corporate tax rate applicable to subsidiaries in the USA (federal tax) is 35%. These companies are also subject to state taxes at an average rate of 4%.
- The corporate tax rate in Europe applicable to the subsidiaries operating in Benelux countries and France is between 25.5% and 34%.

Notes to the Consolidated Financial Statements

NOTE 42 – TAXES ON INCOME (CONTD.)

C. Tax assessments

The Company has tax assessments that are considered as final up to and including 2007. The majority of the subsidiaries have received tax assessments that are considered final up to and including 2006-2008.

D. Carry-forward losses for tax purposes

At December 31, 2011, the Company has carry-forward losses of NIS 450 million for tax purposes. The Company does not recognize deferred tax assets to receive for these losses. The Company's subsidiaries have losses for tax purposes amounting to NIS 2,370 million at that date. For part of these losses, the subsidiaries recorded deferred tax assets of NIS 311 million in the financial statements.

E. Deferred taxes

Composition:

	Balance sheet		Statement of income		
	December 31		Year ended		
	December 31		December 31		
	2011	2010	2011	2010	2009
			NIS million		
Property, plant and equipment	(1,096)	(696)	(336)	(37)	(143)
Real estate investment stated at fair value.	(1)	-	-	-	-
Financial assets measured at fair value	(12)	(127)	31	(7)	(54)
Share-based payment	66	-	(1)	-	-
Gains from hedging an investment in foreign operations, net	-	-	-	-	-
Intangible assets	(539)	(245)	(95)	16	90
Other temporary differences	(333)	(388)	42	22	(50)
Carry-forward losses for tax purposes	712	474	14	7	40
Employee benefits	71	54	49	(6)	8
Deferred tax income (expenses)			(206)	(5)	(109)
Deferred tax liabilities, net	<u>(1,128)</u>	<u>(928)</u>			

Notes to the Consolidated Financial Statements

NOTE 42 – TAXES ON INCOME (CONTD.)

The deferred taxes are presented in the balance sheet as follows:

	December 31	
	2011	2010
	NIS million	
Non-current assets	280	272
Non-current liabilities	(1,408)	(1,200)
	<u>(1,128)</u>	<u>(928)</u>

The deferred taxes are calculated according to the tax rates of 25% based on the expected applicable tax rate at the time of exercise.

In 2011, the Group recorded a deferred tax liability of NIS 40 million for the investment in IDE, since it is not expected that the temporary difference for the investment in IDE will be reversed in the foreseeable future.

Deferred taxes for items recognized in equity

	December 31	
	2011	2010
	NIS million	
Loss for available-for-sale financial assets	(14)	(144)
Other	(8)	17
	<u>(6)</u>	<u>(127)</u>

F. Income tax in the statement of income

	Year ended		
	December 31		
	2011	2010	2009
	NIS million		
Current taxes	375	170	(24)
Petroleum profits levy	48	-	
Deferred taxes (also see F above)	206	5	109
Taxes for previous years	(71)	3	(2)
	<u>558</u>	<u>178</u>	<u>83</u>

Notes to the Consolidated Financial Statements

NOTE 42 – TAXES ON INCOME (CONTD.)

G. Adjustment of theoretic tax

Below is a presentation of the tax amount that would be applicable if all the income was taxable at the regular corporate tax rates in Israel and the tax amount charged to the statement of income for the reporting year:

	Year ended December 31		
	2011	2010	2009
	NIS million		
Income (loss) before taxes on income	3,814	(7)	835
Statutory tax rate	24%	25%	26%
Tax computed at the statutory tax rate	915	(2)	217
Increase (decrease) in tax liabilities for:			
Utilization of carryforward losses from previous years	(4)	(6)	-
Losses carried forward for which no tax benefit was recorded	167	114	70
Petroleum profits tax	48	-	-
Effect of the change in the tax rate	44	-	(42)
Minority interest in earnings of a limited partnership	(40)	(18)	(15)
Company's share in gains (losses) of companies and partnerships accounted for at equity, net	(795)	(12)	(8)
Taxes for previous years	(71)	3	(2)
Adjustments for different tax rate in merged companies	132	47	31
Exempt revenue, unrecognized expenses and other adjustments, net	162	52	(168)
Taxes on income	558	178	83

- H. The Company is registered for value added tax purposes as a joint licensed dealer (consolidation of dealers) together with some of its subsidiaries.

Notes to the Consolidated Financial Statements

NOTE 43 – NET EARNINGS (LOSS) PER SHARE

Quantity of shares and the earnings (loss) attributable to the majority shareholders used to calculate the net earnings (loss) per share from continuing operations:

	Year ended December 31					
	2011		2010		2009	
	Weighted quantity of shares	Net earnings (loss)	Weighted quantity of shares	Net earnings (loss)	Weighted quantity of shares	Net earnings (loss)
	Thousands	NIS million	Thousands	NIS million	Thousands	NIS million
For calculation of basic net earnings (loss)	11,265	2,610	11,289	(294)	11,235	620
Adjustment for the Group's portion in basic loss (earnings) per share of investees	-	436	-	150	-	(720)
Group's portion in diluted earnings (loss) per share of investees	-	(438)	-	(139)	-	713
Effect of potential ordinary shares, diluted	-	-	-	-	2	-
For calculation of diluted net earnings (loss)	11,265	2,608	11,289	(283)	11,237	613

Quantity of shares and the earnings (loss) attributable to the majority shareholders used to calculate the net earnings (loss) per share from discontinued operations:

	Year ended December 31					
	2011		2010		2009	
	Weighted quantity of shares	Net earnings (loss)	Weighted quantity of shares	Net earnings (loss)	Weighted quantity of shares	Net earnings (loss)
	Thousands	NIS million	Thousands	NIS million	Thousands	NIS million
For calculation of basic net earnings (loss)	-	-	11,289	1,995	11,235	244
Adjustment for the Group's portion in basic loss (earnings) per share of investees	-	-	-	(1,995)	-	(143)
Group's portion in diluted earnings (loss) per share of investees	-	-	-	1,995	-	129
Effect of potential ordinary shares, diluted	-	-	-	-	2	-
For calculation of diluted net earnings (loss)	-	-	11,289	1,995	11,237	230

Notes to the Consolidated Financial Statements

NOTE 44 – OPERATING SEGMENTS

A. General

Under IFRS 8, the Group's operating segments are determined on the basis of management reports, which are mainly based on the investments in each subsidiary.

The operating segments are as follows:

- Fuel in Israel: The main operation is marketing and sale of fuels and commodities at gas stations and other outlets, and storage and production of fuels in facilities.
- Fuel in the US: The main operation is maintenance and operation of gas stations and convenience stores in the US, operation of a refinery and a crude oil pipeline, and marketing of fuels to various customers.
- Fuel in Europe: The main operation is marketing and sale of fuels and commodities at gas stations and other outlets in Europe (in Benelux countries and France) and the results of the operations of motorway service stations in the UK.
- Automotive: The main operation is importing and marketing of Mazda and Ford vehicles and spare parts. As from the fourth quarter of 2010, the Group presents the investment in Delek Automotive according to the equity method. For further information, see Note 14M. As from the date of loss of control in Delek Automotive, the Group recognizes its share of the operating income of Delek Automotive under segment reporting.
- Insurance and finances in Israel: The main operation is carried out by The Phoenix.
- Insurance abroad: The main operation is carried out by Republic in the United States.
- Oil and gas exploration and production: The main operation is the Yam Tethys joint venture for oil and gas exploration and production. Tamar joint venture, Ratio Yam joint venture and Leviathan well. At December 31, 2011, Cohen Development and Avner Partnership were consolidated for the first time. See Note 14. Up to December 31, 2011, Avner Partnership was accounted for using the equity method.

Other: The main operation is investment in infrastructure, including mainly desalination and establishment of power stations, trading in derivatives through Barak Capital and the biochemical operation that includes mainly production and marketing of fructose, citric acid and ingredients for nutritional additives.

In the past, the Group segments included the real estate segment. Following distribution of Delek Real Estate shares to Group shareholders as a dividend in kind (see Note 14G above), details of this segment were presented under discontinued operations and are not included in segment reporting.

The Company's business segments are carried out in several geographic regions worldwide. Israel, the domicile of the Company and of most of the investees, houses the vehicles and spares marketing operations, oil and gas explorations, insurance operations, part of the fuel products production and marketing. Operations in the following segments are carried out in the United States: fuel products and oil refinery, insurance, and oil and gas explorations and production. Operations in gas stations and convenience stores are carried out in Western Europe.

Notes to the Consolidated Financial Statements

NOTE 44 – OPERATING SEGMENTS (CONTD.)

B. Segment reporting

1. Revenues

	Year ended December 31		
	2011	2010	2009
	NIS million		
Revenue from external sources			
Fuel in Israel	6,259	5,136	4,287
Fuel in the United States	25,755	14,021	10,413
Fuel in Europe	16,285	11,365 *)	9,020 *)
Automotive **)	-	3,363	4,743
Oil and gas exploration and production	722	558	449
Insurance and finance in Israel ***)	6,825	9,717	10,699
Insurance operations abroad ***)	1,409	1,364	1,668
Other segments	1,853	693	575
Adjustments **)	51	(3,413)	(4,811)
Total in statement of income	59,159	42,804	37,043

*) Reclassified

**) The adjustments for the automotive segment refer, among other things, to revenues of Delek Automotive, which were reclassified in the statement of income as a discontinued operation in 2009 and in 2010 up to the date of deconsolidation.

***) Represents insurance premiums earned on retention in life assurance and general insurance.

Notes to the Consolidated Financial Statements

NOTE 44 – OPERATING SEGMENTS (CONTD.)

2. Segment results and reconciliation to net profit (loss)

	Year ended December 31		
	2011	2010	2009
	NIS million		
Fuel in Israel	140	189	230
Fuel in the United States	1,036	62	189
Fuel in Europe	184	190	97
Automotive *)	89	480	460
Oil and gas exploration and production	601	268	265
Insurance and finance in Israel	471	647	448
Insurance operations abroad	(451)	65	77
Other segments	(126)	115	286
Adjustments *) **)	(331)	(791)	(902)
Operating income	1,613	1,225	1,150
Finance expenses, net	1,325	1,384	924
Gain (loss) from disposal of investments in investees, net	3,749	(4)	518
Group share in earnings (losses) of associate companies and partnerships, net	(223)	156	91
Taxes on income	558	178	83
Income from discontinued operations, net	-	2,139	451
Net income	3,256	1,954	1,203

*) The results of Delek Automotive in 2009 were reclassified and recognized under income from discontinued operations. As from the fourth quarter of 2010, the Group presents the investment in Delek Automotive according to the equity method and accordingly, from this date, the Group includes its share of the results of Delek Automotive according to its proportionate share of the operating income of Delek Automotive (up to deconsolidation, the entire amount of the operating income of Delek Automotive was included).

**) Including expenses not attributed to segments and the Company's share in operating income of associates as included in the segment results

	Year ended December 31		
	2011	2010	2009
	NIS million		
Adjustments			
Automotive	(89)	(480)	(460)
Company's share of the operating income of associates	(279)	(240)	(271)
Other	37	(71)	(171)
	(331)	(791)	(902)

Notes to the Consolidated Financial Statements

NOTE 44 – OPERATING SEGMENTS (CONTD.)

3. Segment assets

	December 31	
	2011	2010
	NIS million	
Corporate insurance operations abroad	5,449	5,334
Corporate insurance and finance in Israel	64,226	62,290
Fuel in Israel	4,663	4,560
Fuel in the United States	8,539	4,052
Fuel in Europe	5,892	5,391
Oil and gas exploration and production	12,982	2,409
Other segments	3,770	1,204
	<u>105,521</u>	<u>85,240</u>
<u>Investments in associates</u>		
Insurance and finance in Israel	467	-
Fuel in Israel	118	58
Fuel in Europe	99	95
Automotive	970	1,316
Oil and gas exploration and production	-	725
Other segments	679	480
	<u>2,333</u>	<u>2,674</u>
Assets not attributed to segments	46	3,844
Total consolidated assets	<u>107,900</u>	<u>91,758</u>

4. Segment liabilities

	December 31	
	2011	2010
	NIS million	
Corporate insurance operations abroad	4,088	3,726
Corporate insurance and finance in Israel	58,473	56,177
Fuel in Israel	953	832
Fuel in the United States	3,749	1,087
Fuel in Europe	2,397	2,202
Oil and gas exploration and production	608	363
Other segments	165	142
	<u>70,383</u>	<u>64,529</u>
Liabilities not attributed to segments	26,427	22,352
Total consolidated liabilities	<u>96,810</u>	<u>86,881</u>

Notes to the Consolidated Financial Statements

NOTE 44 – OPERATING SEGMENTS (CONTD.)

5. Cost of acquisition of long term assets

	Year ended December 31		
	2011	2010	2009
	NIS million		
Corporate insurance operations abroad	4	5	8
Corporate insurance and finance in Israel	231	272	301
Fuel in Israel	166	258	244
Fuel in the United States	657	213	557
Fuel in Europe	444	1,186	118
Automotive	-	4	3
Oil and gas exploration and production	1,245	307	384
Other segments	144	66	100
	<u>2,891</u>	<u>2,311</u>	<u>1,715</u>

6. Depreciation and amortization

Corporate insurance operations abroad	230	57	24
Corporate insurance and finance in Israel	322	271	240
Fuel in Israel	84	83	67
Fuel in the United States	274	231	229
Fuel in Europe	240	176	196
Automotive	26	8	10
Oil and gas exploration and production	173	204	128
Other segments	382	49	81
	<u>1,731</u>	<u>1,079</u>	<u>975</u>

C. Geographic information

1. Income by geographic markets (by location of customers)

	Year ended December 31		
	2011	2010	2009
	NIS million		
Israel	14,017	18,873	20,072
USA	27,470	15,745	12,457
Europe	17,624	11,522	9,204
Other	48	60	54
Adjustments *)	-	(3,396)	(4,744)
	<u>59,159</u>	<u>42,804</u>	<u>37,043</u>

**) The adjustments also refer to revenues of Delek Automotive, which were reclassified in the statement of income as a discontinued operation in 2009 and in 2010 through to the date of deconsolidation.

Notes to the Consolidated Financial Statements

NOTE 44 – OPERATING SEGMENTS (CONTD.)

2. Carrying amounts of segment assets and cost of acquisition of assets, long term, by geographic regions (by location of assets)

	Segment assets		Cost of acquisition of long term assets		
	December 31		Year ended December 31		
	2011	2010	2011	2010	2009
			NIS million		
Israel	84,496	71,658	1,742	844	1,040
USA	14,009	11,305	658	215	557
Europe	8,026	5,529	557	51	118
Other	60	-	-	-	-

NOTE 45 – INTERESTED AND RELATED PARTIES**A. CEO of the Company**

1. At December 31, 2011, the balance of the loans to the CEO of the Company amounted to NIS 12.9 million. The loans are linked to the CPI and bear annual interest at a rate of 4%. The loan funds are used to acquire shares of Delek Group companies (a loan of NIS 4.3 million was used to acquire IDE shares). The acquired shares are used as collateral for the repayment of the loans, and any amount obtained from the sale of the shares will be used first and foremost to repay the loans.

For the balance of the loan of NIS 7.9 million at December 31, 2011, in January 2010 the Company's board of directors approved (after approval of the audit committee) renewal of the loan instead of repayment that was due on January 29, 2010 (the original amount was NIS 4.4 million). The repayment date of the new loan is April 29, 2013, under the same terms as the original loan. The loan is a non-recourse loan.

For the balance of the loan of NIS 4.3 million at December 31, 2011, on November 30, 2010, the Company's board of directors approved (after approval of the audit committee) the extension of the loan repayment date from November 30, 2010 (the loan was provided in November 2007), for another three years up to November 29, 2013, under the same terms as the original loan. The loan is a non-recourse loan.

The benefit in the extension of these loans amounted to NIS 0.8 million, recognized in the statement of income in the reporting period.

For the balance of the loan of NIS 0.8 million at December 31, 2011, on March 31, 2011, the Company's board of directors approved (after approval of the audit committee) the extension of the loan repayment date instead of repayment that was due on March 31, 2011. The new repayment date of the loan is April 29, 2013, under the same terms as the original loan. The loan is a recourse loan.

2. In prior years, the CEO of the Company was granted options in an investee in which he serves as a director. The benefit recognized in the reporting period is included under section H below.

Notes to the Consolidated Financial Statements

NOTE 45 – INTERESTED AND RELATED PARTIES (CONTD.)

B. Chairman of the board of directors

1. The chairman of the Company's board of directors was granted loans that were repayable in 2010-2011. Under the terms of the loan agreement, the loans are linked to the CPI and bear annual interest of 4%. The loans were used to acquire shares in public companies owned by Delek Group. In September 2010, the chairman of the Company's board of directors repaid the full amount of the loan that had been provided to him in the past. At the repayment date, the outstanding balance of the loan amounted to NIS 10 million.
2. In prior years, the chairman of the board of directors was granted options in investees in which he serves as a director. The benefit recognized in the accounting year is included under section H below.

In view of the change in the position of the chairman of the board of directors of the Group from chairman of the board of DES to active deputy chairman of the board of DES, in March 2010, the general meeting of DES approved a number of changes to the options plan granted in the past for DES shares, such that the fifth lot of options (11,069 options) will be cancelled and the fourth lot will remain valid. The other terms will remain unchanged.

In June 2010, the chairman of the Group's board of directors exercised 11,069 share options (the first lot) for 11,069 DES shares at an exercise price of NIS 349.96 per option.

3. In May 2011, the general meeting of the Company approved a bonus payment of NIS 0.6 million for the chairman of the board of directors, after approval by the Company's board of directors.

C. Intra-Group transactions

1. In 2010, a transaction was approved between Delek Israel and the controlling shareholder, in which Delek Israel acquired from Delek Real Estate Income Producing Properties Ltd. (Delek Producing Properties) all the shares held by Delek Producing Properties in Ein Yahav - Delek Ltd. ("Ein Yahav"), representing 50% of the issued share capital of Ein Yahav. In addition, Delek Producing Properties assigned loans to Delek Israel that Delek Real Estate provided to Ein Yahav (and which were assigned by Delek Real Estate to Delek Producing Properties). Delek Israel paid Delek Producing Properties NIS 15.4 million for shares and assignment of the loans.

It was further agreed that Delek Israel would acquire from Delek Projects Initiation and Development Ltd. ("Delek Projects") (a second tier subsidiary of Delek Real Estate), all the shares it holds in Delek-Saadon Projects Initiation and Development Ltd. ("Delek Saadon"), representing 50.1% of the issued shares of Delek Saadon.

In addition, Delek Producing Properties assigned loans to Delek Israel, which Delek Real Estate provided to Delek Saadon (and which were assigned by Delek Real Estate to Delek Producing Properties).

The Company paid Delek Projects NIS 7.6 million for shares and assignment of the loans.

In addition, under the terms of the agreement, Delek Israel acquired from Delek Producing Properties all of its interests in Orhan Mei Megiddo Ltd. ("Mei Megiddo"), representing 50% of the issued share capital of Mei Megiddo.

Delek Producing Properties also assigned loans to Delek Israel that Delek Real Estate provided to Mei Megiddo and which were assigned by Delek Real Estate to Delek Producing Properties. Delek Israel paid Delek Producing Properties NIS 4.3 million for shares and assignment of the loans. Delek Israel also acquired from Delek Income Producing Properties its rights to be registered as a sub-lessor of land covering 3,884 square meters in Raanana for NIS 9 million.

In accordance with the terms of the agreement, Delek Israel acquired from Delek Real Estate all the shares it holds in Delek Retail Lots Ltd. (Delek Retail Lots), representing 50% of the issued share capital of Delek Retail Lots. Delek Israel paid Delek Real Estate NIS 4.6 million for the shares. At the same time, Delek Retail Lots repaid owners loans from Delek Real Estate in the amount of NIS 1.6 million.

Notes to the Consolidated Financial Statements

NOTE 45 – INTERESTED AND RELATED PARTIES (CONTD.)

In April 2010, Delek Israel and an interested party signed an agreement to acquire from Delek Producing Properties the exclusive rights to the land of the gas station adjacent to the Ramlod shopping center. Delek Israel paid Delek Producing Properties and a third party NIS 39 million for the acquisition. This transaction was approved by the general meeting of the shareholders of Delek Israel and Delek Real Estate, which convened in May 2010.

2. See Note 14(G)(1) for information about the loans that The Phoenix provided to Delek Real Estate, with a balance of NIS 66 million at December 31, 2011.
 3. During this period and up to July 2010, the Company and some subsidiaries rented offices from a company owned by the controlling shareholder. Rental costs of NIS 1.602 million were recognized in the period. In July 2010, the offices were sold to a third party.
 4. Delek Israel and Delek Real Estate entered into several agreements for rental of gas stations or establishment and rental of gas stations. According to the agreements, the lease payments include a fixed payment and a variable payment based on fuel sales. The lease payments are linked to the dollar, linked (80%) to the CPI or linked to market price differences between buying and selling prices of fuel. Annual lease payment expenses amount to NIS 2 million.
- D.** In 2010, the Company entered into an agreement with Elad Sharon (Tshuva), the son of the controlling shareholder, who serves as the deputy chairman of the Group's board of directors, in respect of the terms of his service, including director's remuneration and reimbursement of expenses in an annual amount of NIS 335 thousand (not including reimbursement of expenses). The expense recognized in the reporting period is included under section H below. As from March 2011, Elad Sharon does not receive director's remuneration and as from May 2011, he does not receive reimbursement of expenses, according to his request not to receive these payments.
- E.** For further information about guarantees provided to related parties, see Note 32B. For further information regarding the loans and guarantees provided to Delek Real Estate, see Notes 14(G) and 32(B)(1).
- F. Balances with interested and related parties**

	December 31	
	2011	2010
	NIS million	
Trade receivables	28	61
Other receivables	7	76
Long-term loans, deposits and receivables	14	14
Loans and capital notes to associates	126	939
Investments in insurance companies (short- and long-term)	34	36
Trade payables	3	5
Other payables	4	19

Notes to the Consolidated Financial Statements

NOTE 45 – INTERESTED AND RELATED PARTIES (CONTD.)

G. Transactions with interested and related parties

	Year ended December 31		
	2011	2010	2009
	NIS million		
Sales	145	526	716
Purchases	29	104	47
Selling, general and administrative expenses	52	46	21
Finance expenses	30	-	-
Finance income	24	62	38

H. Benefits for key managers (including directors) employed in the Company (contd.)

The directors and key manager in the Company are eligible, in addition to their salary, to non-monetary benefits, such as the use of a company car. In addition, the Company contributes to defined post-employment benefit plans.

Senior managers also participate in the options plan.

Benefits for key managers (including two directors) employed in the Company:

	Year ended December 31					
	2011		2010		2009	
	No. of people	Amount NIS million	No. of people	Amount NIS million	No. of people	Amount NIS million
Short-term benefits (2)	7	11.7	7	11.6	5	6.9
Share-based payment (1) (2) (3)	5	-	6	12.3	5	6.6
		<u>11.7</u>		<u>23.9</u>		<u>13.5</u>

(1) In 2011, including notional expenditure for the benefit in the extension of non-recourse loans of NIS 0.8 million

(2) Including the expenses of a subsidiary for a director in the Group for management services and benefit for options amounting to NIS 1 million (in 2010, NIS 1.2 million; in 2009, NIS 2.5 million; these years included a benefit for options).

(3) Including expenses recognized for a benefit arising from the grant of options in investees

Benefits for key managers (including directors) who are not employed by the Company:

	Year ended December 31					
	2011		2010		2009	
	No. of people	Amount NIS million	No. of people	Amount NIS million	No. of people	Amount NIS million
Benefits for an external director	6	1.3	5	1.3	5	1.4

Notes to the Consolidated Financial Statements

NOTE 45 – INTERESTED AND RELATED PARTIES (CONTD.)

(4) Share-based payments

In June 2009, the Company's board of directors approved a phantom options plan for senior managers and office holders. The options will be granted at no cost and will be exercisable into a cash grant equal to the difference between the increase in the market price of the Company's shares at the exercise date and the exercise price. The exercise price was set at NIS 503.2 per share, unlinked and will be subject to certain adjustments as stipulated in the allocation agreement.

According to the plan, the options will vest in three equal annual lots. The first lot will vest one year after the approval date of the allotment (June 2009). The options will expire two years after the end of the vesting period. A total of 46,895 options were approved under the plan. According to an appraisal received by the Company, the financial value of the options at the allocation date is NIS 11.2 million.

Out of the total amount of the options, the audit committee and the board of directors resolved to allocate 20,000 phantom options (0.17% of the fully diluted capital did not relate to options for the acquisition of the Company's shares), under the plan, to the CEO of the Company. According to an appraisal received by the Company, the financial value of the phantom options granted to the CEO under the plan as of the allocation date is NIS 4.78 million.

Calculation of the financial value was based on the binomial model for pricing the options and based on the following assumptions:

Share price (NIS)	500
Exercise price of each option (NIS)	503.2
Standard deviation (%)	52.1
Capitalization rate (%)	4.7
Expected life (years)	5

In September 2010, some of the employees exercised 2,833 options for NIS 2 million.

At December 31, 2011, the financial value of the options amounted to NIS 12.7 million and in 2011, an expense of NIS 10 million was recognized for the plan (in 2010, NIS 10 million; in 2009, NIS 5 million).

- I. In the ordinary course of business, the Group companies conduct transactions at market prices and at regular credit terms with corporations that are related parties, at insignificant amounts.

Appendix to the Consolidated Financial Statements

Principal Partnerships and Investees

Name of Owner	Company	Rate of holding and control of the investee	Rate of holding of the Group in final retention	Presentation
		December 31	December 31	
		2011 (1)	2011	
		%	%	
Delek Group Ltd.	Delek Petroleum Ltd.	100	100	Subsidiary
	Delek Investments and Properties Ltd.	100	100	Subsidiary
	Cohen Development and Industrial Buildings Ltd. (3)	51.76	51.76	Subsidiary
	Delek Real Estate Ltd.	5	5	Associate
Delek Petroleum Ltd.	Delek The Israel Fuel Corporation Ltd.	86.9	86.9	Subsidiary
	Delek Hungary Holding Ltd.	96.7	99.8	Subsidiary
	Delek Europe Holdings Ltd. (2)	80	97.4	Subsidiary
	Delek Motorway Services (Jersey)	100	100	Subsidiary
	UK Delek Motorway Services	100	100	Subsidiary
	<u>Held by Delek The Israel Fuel Corporation Ltd.</u>			
	Delek Oil Ltd. (formerly Delkol Ltd.)	100	86.9	Subsidiary
	Delek Heating Ltd.	51	44.3	Subsidiary
	Delek Transportation Ltd. (formerly Shall-Dal Fuel Transportation Services Ltd.	100	86.9	Subsidiary
	Delek Menta Roads Ltd.	100	86.9	Subsidiary
	United Petroleum Export Co. Ltd.	75	65.2	Subsidiary
	Tanker Services Ltd.	75	65.2	Subsidiary
	Delek Retail Lots Ltd.	100	86.9	Subsidiary
	Delek Europe Holdings Ltd. (2)	20	97.4	Subsidiary
	Delek Pi Gilot – Limited Partnership	100	86.9	Subsidiary
	Inbal Fuel and Properties Ltd.	100	86.9	Subsidiary
	Delek Israel Fuel Marketing Partnership	100	86.9	Subsidiary
	Delek-Kliot Partnership	65	56.5	Subsidiary
	Delek Hungary Holding Ltd.	1.6	99.8	Subsidiary
	Held by Delek Hungary Holdings Inc.			
	Held by Delek US Holdings Inc.	67.9	68.4	Subsidiary
	Held by Delek US Holdings Inc.			
	MAPCO Express Inc.	100	68.4	Subsidiary
	MAPCO Family Centers	100	68.4	Subsidiary
	MAPCO Fleet Inc.	100	68.4	Subsidiary
	Delek Refining Inc.	100	68.4	Subsidiary
	Delek Marketing and Supply Inc.	100	68.4	Subsidiary
	Lion Oil Company	100	68.4	Subsidiary
	<u>Held by Delek Europe Holdings Ltd.</u>			
	V. Delek Benelux B	100	97.4	Subsidiary
	Delek France BV	100	97.4	Subsidiary
	Held by Delek Motorway Services UK			
	MSA Acquisitions Limited	100	100	Subsidiary
	<u>Held by MSA Acquisitions Limited</u>			
	Roadchef Limited	100	100	Subsidiary

(1) Direct and indirect ownership and control (without the holdings of Excellence exchange traded funds)

(2) Held by Delek – The Israel Fuel Corporation Ltd. (20%)

Appendix to the Consolidated Financial Statements

Principal Partnerships and Investees

Name of Owner	Company	Rate of holding and control of the investee	Rate of holding of the Group in final retention	Presentation
		December 31	December 31	
		2011 (1)	2011	
		%	%	
Delek Investments and Properties Ltd.	Delek Infrastructure Ltd.	100	100	Subsidiary
	Delek Ecology – Limited Partnership	100	100	Subsidiary
	Delek Automotive Systems Ltd.	32.1	32.1	Associate
	Gadot Biochemical Industries Ltd.	76	76	Subsidiary
	Delek Energy Systems Ltd. ("DES")	86.7	86.7	Subsidiary
	Delek Drilling Limited Partnership (2)	6.53	61	Subsidiary
	Yam Tethys Joint Venture	4.441	32	Subsidiary
	Avner Oil Exploration - Limited Partnership (2)	9.11	51.8	Subsidiary
	The Phoenix Holdings Ltd.	56.7	56.7	Subsidiary
	Delek Finance US Inc.	100	100	Subsidiary
	Delek Capital Ltd.	47	47	Associate
	<u>Held by The Phoenix Holdings Ltd.</u>			
	The Phoenix Insurance Company Ltd.	100	56.7	Subsidiary
	The Phoenix Insurance Investments and Finance Ltd.	100	56.7	Subsidiary
	<u>Held by The Phoenix Insurance Company Ltd.</u>			
	Salit Investments and Holding Co. Ltd.	100	56.7	Subsidiary
	Hadar Yarok Properties and Investments Ltd.	100	56.7	Subsidiary
	<u>Held by Phoenix Investments and Finance Ltd.</u>			
	Atara Technology Ventures Ltd.	100	56.7	Subsidiary
	Atara Partnership Management Ltd.	100	56.7	Subsidiary
	Excellence Investments Ltd.	73	41.4	Subsidiary
	Mehadrin Ltd.	41	23	Associate
	Ampal Protected Living (1994) Ltd.	100	56.7	Subsidiary
	Ampal Protected Living (1998) Ltd.	100	56.7	Subsidiary
	Ampal Protected Living (1966) Ltd.	100	56.7	Subsidiary
	Up to 120	100	56.7	Subsidiary
	<u>Held by Delek US Finance Inc.</u>			
	Republic Companies Inc.	99	99	Subsidiary
	<u>Held by Delek Infrastructures Ltd.</u>			
	IDE Technologies Ltd.	49.8	49.8	Associate
	<u>Held by Delek Ecology – Limited Partnership</u>			
	I.P.P. Delek Ashkelon Ltd.	100	100	Subsidiary
	<u>Held by Delek Automotive Systems Ltd.</u>			
	Delek Motors Ltd.	100	32	
	Delek Motors Spare Parts (1987) Ltd.	100	32	
	DMR Properties (1985) Ltd.	100	32	
	DSR Delek Automobile Agencies 1994 – Registered Partnership	75	24	

(1) Direct and indirect ownership and control (without the holdings of Excellence exchange traded funds)

(2) Held also by DES

Appendix to the Consolidated Financial Statements

Principal Partnerships and Investees

Name of Owner	Company	Rate of holding and control of the investee	Rate of holding of the Group in final retention	Presentation
		December 31	December 31	
		2011 (1) %	2011 %	
	<u>Held by DES</u>			
	Delek Drilling Management (1993) Ltd.	100	86.7	Subsidiary
	Delek Drilling Trusts Ltd	100	86.7	Subsidiary
	Delek Energy Debentures Ltd. (under voluntary liquidation)	100	86.7	Subsidiary
	Delek Drilling Limited Partnership (2)	63	61.0	Subsidiary
	Avner Oil and Gas Ltd.	50	69.0	Associate
	Avner Oil Exploration - Limited Partnership (2)	47	51.8	Subsidiary
	Avner Trusts Ltd.	50	43.0	Associate
	Delek Energy International Ltd.	100	86.7	Subsidiary
	Delek Energy System US Inc.	100	86.7	Subsidiary
	Delek Energy System Limited (Gibraltar)	100	86.7	Subsidiary
	Delek Energy System LLC (Rockies)	100	86.7	Subsidiary
	Matra Petroleum Plc	29	25	Associate
	Viking Oil Gas International Ltd	25	22	Associate
	<u>Held by Delek Drilling Limited Partnership</u>			
	Yam Tethys Joint Venture	26	32	Jointly-controlled asset
	Michal Matan Joint Venture	16	17	Jointly-controlled asset
	Leviathan well (!)	23	25	
	<u>Held by Avner Oil Exploration - Limited Partnership Yam Tethys Joint Venture</u>	23	32	Jointly-controlled asset
	Delek and Avner Yam Tethys Ltd. (SPC)	44	60	Jointly-controlled asset
	Michal Matan Joint Venture	16	17	Jointly-controlled asset
	Leviathan well (!)	23	25	
	<u>Held by IDE Technologies Ltd.</u>			
	VID Desalination Company Ltd. Israel	50	25	Associate
	OTID Desalination Partnership	50	25	Associate

(1) Direct and indirect ownership and control (without the holdings of Excellence exchange traded funds)

(2) Held directly by Delek Petroleum Ltd.

Delek Group Ltd.

Financial Information from the
Consolidated Financial Statements
Attributed to the Company

as of December 31, 2011

**Special Auditors' Report
on the separate financial information pursuant to Regulation 9C of the Securities Regulations
(Periodic and Immediate Reports), 1970**

We have audited the separate financial statements presented pursuant to Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 1970, of Delek Group Ltd. ("the Company") as of December 31, 2011 and 2010 and for each of the three preceding years, the last of which ended on December 31, 2011, and which are included in the Company's periodic report. The separate financial information is the responsibility of the Company's management and board of directors. Our responsibility is to express an opinion on the financial information based on our audit.

We conducted our audit in accordance with the Israeli generally accepted accounting principles. These standards require that we plan and perform the audit to obtain reasonable assurance that the separate financial information is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and items included in the separate financial information. An audit also includes assessing the accounting principles used in drafting the separate financial information and significant estimates made by the board of directors and management of the Company, as well as evaluating the overall presentation of the separate financial information. We believe that our audit provides a reasonable basis for our opinion.

In our opinion the separate financial information is prepared, in all material respects, in accordance with Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 1970.

Without qualifying our foregoing opinion, we draw attention to Note 4F to the separate financial information with respect to contingent liabilities and outstanding claims of certain investees.

Tel Aviv
March 29, 2012

Kost Forer Gabbay &
Kasierer
Certified Public Accountants

**Breakdown of Financial Information from the consolidated financial statements
attributable to the Company**

		As of December 31	
		2011	2010
	Note	NIS millions	
<u>Current assets</u>			
Cash and cash equivalents		29	108
Short-term investments		355	500
Current maturity of a loan to an investee		23	-
Other receivables (mainly interest received from investees)		153	95
Total current assets		560	703
<u>Non-current assets</u>			
Investments in available-for-sale financial assets		17	-
Investments in investees		8,203	4,730
Loans to investees	4C	5,160	5,307
Total non-current assets		13,380	10,037
		13,940	10,740
<u>Current liabilities</u>			
Current maturities of debentures, of negotiable debentures and of bank loans		876	450
Credit from others		70	-
Undertaking to pay a subsidiary for a borrowing transaction	4 A.	491	-
Creditors and credit balances (particularly interest to be paid)		162	153
Total current liabilities		1,599	603
<u>Non-current liabilities</u>			
Loans to an investee	4D	277	256
Long-term loans from a bank		272	-
Debentures		7,219	6,968
Debentures convertible into Company shares		-	247
Deferred taxes	3	13	13
Other liabilities		-	1
Total non-current liabilities		7,781	7,485
<u>Equity attributable to equity holders of the parent</u>			
Share capital		13	13
Share premium		1,624	1,622
Warrants and receipts for conversion option		32	32
Retained earnings		3,723	1,618
Exchange differences on translation of foreign operations		(140)	(539)
Reserve from transactions with holders of non-controlling rights		(451)	(126)
Other reserves		(110)	156
Treasury shares		(131)	(124)
<u>Total capital</u>		4,560	2,652
		13,940	10,740

The additional information constitutes an inseparable part of the financial information and of the separate financial information.

March 29, 2012

Date of approval of the financial
statements

Gabriel Last
Chairman of the Board
of Directors

Asi Bartfeld
CEO

Barak Mashraki
CFO

Breakdown of Financial Information from the Company's consolidated statements of income attributable to the Company

	Note	For the year ended December 31		
		2011	2010	2009
		NIS millions		
Company's share in profits (losses) of investees and partnerships, net		2,944	1,812	847
Administrative fees from investees		4	3	6
Administrative and general expenses		18	15	10
Other income (expenses), net		14	(6)	(1)
Operating profit		2,944	1,794	842
Net financing income with respect to loans to investees		458	390	375
Financing income (expenses) (mainly for financial investments), net		(14)	37	107
Financing expenses (mainly with respect to debentures)		778	520	477
Profit from continuing operations		2,610	1,701	847
Profit from discontinued operations		-	-	17
Net earnings attributable to equity holders of the Company		2,610	1,701	864

The additional information constitutes an inseparable part of the financial information and of the separate financial information.

Breakdown of Financial Information from the consolidated statements of comprehensive income attributable to the Company

	For the year ended December 31		
	2011	2010	2009
	NIS millions		
Net earnings attributable to equity holders of the Company	2,610	1,701	864
Other comprehensive income (loss) attributed to investees (after impact of tax)	136	(115)	51
Other comprehensive income from continuing operations	2,746	1,586	915
Other comprehensive income from discontinued operations		-	198
Total comprehensive income attributed to Company shareholders	2,746	1,586	1,113

The additional information constitutes an inseparable part of the financial information and of the separate financial information.

Financial Information from the consolidated statements of cash flows attributable to the Company

	For the year ended December 31		
	2011	2010	2009
	NIS millions		
<u>Cash flows from the Company's operating activities</u>			
Net earnings attributed to the Company	2,610	1,701	864
Adjustments to reconcile statement of cash flows from the Company's continuing operating activities (a):	(2,499)	(1,672)	(915)
Net cash from (used for) continuing operations	111	29	(51)
<u>Cash flows from the Company's investment activities</u>			
Investment in investees	(453)	(6)	(6)
Short-term investments, net	108	(8)	29
Investment in available-for-sale financial assets	(29)	-	-
Collection of loans from others	-	10	-
Investment in capital notes issued by subsidiaries	(155)	-	-
Repayment (grant) of loans to investees, net	182	(659)	(614)
Net cash used for the Company's discontinued investing activities	(347)	(663)	(591)
<u>Cash flows from the Company's financing activities</u>			
Dividend paid to shareholders of the Company	(505)	(1,143)	(177)
Issuance of options	-	-	25
Acquisition of treasury shares	-	-	(33)
Re-issue of treasury shares	-	-	15
Exercise of options	-	16	-
Short term credit from banks and others, net	75	-	(269)
Receipt of long-term loans and proceeds of issue debentures and convertible debentures, net	1,057	1,640	1,483
Repayment of loans and debentures	(470)	(84)	(119)
Net cash from the Company's financing operations	157	429	925
<u>Increase (decrease) in cash and cash equivalents</u>	(79)	(205)	283
<u>Balance of cash flow and cash equivalents for beginning of year</u>	108	313	30
<u>Cash balance and cash equivalents at end of year</u>	(29)	108	313

The additional information constitutes an inseparable part of the financial information and of the separate financial information.

Financial Information from the consolidated statements of cash flows attributable to the Company

For the year ended December 31			
	2011	2010	2009
	NIS millions		
(A) <u>Adjustments to reconcile statement of cash flows from the Company's continuing operating activities:</u>			
Adjustments for profit and loss items of the Company:			
Profit from discontinued operation, net	-	-	(17)
Increase in the value of investments and loans provided, net	(45)	(229)	(156)
Company's share in the profits of subsidiaries*)	(2,594)	(1,512)	(847)
Impairment of non-current liabilities, net	180	136	186
Profit from premature payment and exchange of debentures	-	-	(38)
Change in fair value of short-term investments, net	-	(13)	(51)
Changes in the Company's asset and liability items:			
Increase in debtors and debt balance	(123)	(111)	(29)
Increase (decrease) in other payables	83	57	37
	(2,499)	(1,672)	(915)
*) Dividends received	350	300	-
(B) <u>Company's significant non-cash activities</u>			
Repayment of loans granted to a investee against the issue of a capital note in a subsidiary	394	-	-
Acquisition of shares of a subsidiary in return for participating units of a consolidated partnership	416	-	-
Liability for borrowing participating units (see Note 4A)	343	-	-
Convertible debentures converted into shares	-	-	1
Dividend declared and unpaid	-	-	183
Exercise of options	-	13	-
Allotment of shares in subsidiary as dividend in kind	-	-	171
Exchange of debentures	-	-	658
Re-issue of debentures	-	-	24
(C) <u>Additional information on cash flows</u>			
Cash paid by the Company during the period for:			
Interest	248	374	241
Cash received by the Company during the period for:			
Interest	106	50	16
Dividends	350	300	-

The additional information constitutes an inseparable part of the financial information and of the separate financial information.

Additional information

NOTE 1 – METHOD OF PREPARATION OF THE FINANCIAL INFORMATION FROM THE COMPANY'S CONSOLIDATED FINANCIAL STATEMENTS FOR 2011, ATTRIBUTED TO THE COMPANY

A. Definitions

The Company	– Delek Group Ltd.
The Group	– The Company and its subsidiaries and partnerships which are consolidated in the consolidated financial statements
Consolidated companies, subsidiaries, investees, controlling shareholders, interested parties and related parties	– As these terms are defined in the Company's consolidated financial statements for 2011 ("the Consolidated Statements").

B. Manner of preparing financial information

The financial information from the consolidated financial statements attributed to the Company itself as the parent company ("the Financial Information"), was prepared in accordance with Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 1970.

The accounting policy applied for presenting this financial information are set out in Note 2 to the consolidated statements.

1. **Assets and liabilities included in the consolidated statements attributable to the Company**

The amounts of assets and liabilities in the consolidated statements that are attributable to the Company itself as the parent company are presented with a description of the type of assets and liabilities. This information is classified in the same manner by which the consolidated statements of income are classified. Furthermore, these figures reflect the mutual balances between the Company and its subsidiaries which were canceled in the consolidated statements.

In this matter these figures were presented according to the provisions of IAS1 and adjusted, where relevant, as detailed in the statement of income.

2. **Income and expenses included in the consolidated statements attributable to the Company**

The amounts of income and expenses in the consolidated statements, with a breakdown of profit or loss, attributable to the Company itself as the parent company, are presented with a description of the type of income and expenditure. This information is classified in the same manner by which the consolidated statements of income are classified. In addition, these figures reflect the results of operations for mutual transactions that were canceled in the consolidated statements.

In this matter these figures were presented according to the provisions of IAS1 and adjusted, where relevant, as detailed in the statement of income.

3. **Cash flows included in the consolidated statements attributable to the Company**

The amounts for cash flows in the consolidated statements attributable to the Company itself as the parent company are taken from the consolidated statements of cash flows with breakdown of cash flows from ongoing operations, cash flows from investment activities and cash flows from financing activities with a description of their composition. This information is classified in the same manner by which the consolidated statements of income are classified.

Additional information

NOTE 1 – METHOD OF PREPARATION OF THE FINANCIAL INFORMATION FROM THE COMPANY'S CONSOLIDATED FINANCIAL STATEMENTS FOR 2011, ATTRIBUTED TO THE COMPANY (CONTD.)**C. Deficit in working capital**

On December 31, 2011 the Company had a working capital deficit of NIS 1,039 million due mainly to long term liabilities for financing long term investments, which are payable during the coming year. The Company's management believes that it is able to continue receiving long term loans and if necessary to dispose of investments and assets to continue financing its investments and repaying its liabilities. Also see Note 1B to the consolidated financial statements.

NOTE 2 – FINANCIAL INSTRUMENTS:**Financial risk factors**

The company's operations expose it to various financial risks, such as market risk (including currency risk, CPI risk, interest risk), credit and liquidity risk. The company's comprehensive risk management plan focuses on measures to minimize possible negative effects on the financial performance of the company.

1. Liquidity risk

The table below presents the repayment dates of the Company's financial liabilities in accordance with the contractual terms, in undiscounted amounts (including interest payments):

as of December 31, 2011

	<u>Up to 1 year</u>	<u>1-2 years</u>	<u>2-3 years</u>	<u>3- 4 years</u>	<u>4- 5 years</u>	<u>Over 5 years</u>	<u>Total</u>
	NIS millions						
Debentures (including current maturities)	1,067	1,074	1,044	1,273	1,222	4,809	10,489
Debentures convertible into Company shares	266	-	-	-	-	-	266
Loans to an investee	75	-	-	-	-	-	75
Bank loans	37	37	35	34	23	244	410
	<u>1,445</u>	<u>1,111</u>	<u>1,079</u>	<u>1,307</u>	<u>1,245</u>	<u>5,053</u>	<u>11,240</u>

As of December 31, 2010

	<u>Up to 1 year</u>	<u>1-2 years</u>	<u>2-3 years</u>	<u>3- 4 years</u>	<u>4- 5 years</u>	<u>Over 5 years</u>	<u>Total</u>
	NIS millions						
Debentures (including current maturities)	881	1,259	1,000	970	1,063	5,262	10,435
Dividend declared	10	266	-	-	-	-	276
Loans from investees	15	15	286	-	-	-	316
	<u>906</u>	<u>1,540</u>	<u>1,286</u>	<u>970</u>	<u>1,063</u>	<u>5,262</u>	<u>11,027</u>

Additional information

NOTE 2 – FINANCIAL INSTRUMENTS (CONT'D.)

Financial risk factors (cont'd)

2. Index and foreign currency risks

Exposure to index and foreign currency assets and liabilities risks, including financial instruments

	December 31, 2011						
	Unlinked	Linked to CPI	Linked to the dollar	Linked to GBP	in fair value	Non-financial items	Total
	NIS millions						
<u>Current assets</u>							
Cash and cash equivalents	28	-	1	-	-	-	29
Short-term investments	-	-	23	-	355	-	378
Other receivables (mainly interest received from investees)	15	126	5	7	-	-	153
<u>Non-current assets</u>							
Investment in available-for-sale financial assets	-	-	-	-	17	-	17
Investments in investees	-	-	-	-	-	8,203	8,203
Loans to investees	444	4,494	222	-	-	-	5,160
Total assets	487	4,620	251	7	372	8,203	13,940
<u>Current liabilities</u>							
Credit from others	70	-	-	-	-	-	70
Creditors and credit balances (particularly interest to be paid)	60	80	-	-	22	-	162
Undertaking to pay a subsidiary for a borrowing transaction	-	-	-	-	491	-	491
<u>Long-term liabilities</u>							
Loans from investees	-	277	-	-	-	-	277
Long-term loans from a bank	272	-	-	-	-	-	272
Debentures (including current maturities)	2,518	5,577	-	-	-	-	8,095
Deferred taxes	-	-	-	-	-	13	13
Total liabilities	2,920	5,934	-	-	513	13	9,380
Net exposure	(2,433)	(1,314)	251	7	(141)	8,190	4,560

Additional information

NOTE 2 – FINANCIAL INSTRUMENTS (CONT'D.)

Financial risk factors (cont'd)

2. Index and foreign currency risks (cont'd)

Exposure to index and foreign currency assets and liabilities risks, including financial instruments

	Friday, December 31, 2010					
	Unlinked	Linked to CPI	Linked to the dollar	in fair value	Non-financial items	Total
	NIS millions					
<u>Current assets</u>						
Cash and cash equivalents	105	-	3	-	-	108
Short-term investments	-	-	-	500	-	500
Other receivables (mainly interest received from investees)	-	92	3	-	-	95
<u>Non-current assets</u>						
Investments in investees	-	-	-	-	4,730	4,730
Loans to investees	-	5,151	156	-	-	5,307
Total assets	105	5,243	162	500	4,730	10,740
<u>Current liabilities</u>						
Creditors and credit balances (particularly interest to be paid)	27	101	-	6	19	153
<u>Long-term liabilities</u>						
Loans from investees	-	256	-	-	-	256
Debentures (including current maturities)	1,818	5,600	-	-	-	7,418
Convertible debentures	247	-	-	-	-	247
Other liabilities	-	-	-	1	-	1
Deferred taxes	-	-	-	-	13	13
Total liabilities	2,092	5,957	-	7	32	8,088
Net exposure	(1,987)	(714)	162	493	4,698	2,652

3. For further information pertaining to debentures and convertible debentures issued by the Company see Note 26 and 27 to the consolidated financial statements.

NOTE 3 – BEFORE INCOME TAX

A. Tax Laws that apply to the Company

The Income Tax Law (Inflationary Adjustments), 1985

Pursuant with the Law, until the end of 2007, the business results for tax purposes in Israel are measured when they are adjusted to the CPI fluctuations.

In February, 2008, the Knesset enacted an amendment to the Income Tax Law (Adjustments for Inflation), 1985, limiting the applicability of the Adjustments Law from 2008 onwards. Since 2008, the business results are measured for tax purposes in nominal values, with the exception of certain adjustments for changes in the consumer price index in the period until December 31, 2007. Adjustments referring to capital gains, such as for disposal of real estate (betterment) and securities, continue to apply until the date of disposal. The amendment to the Law includes, inter alia, cancellation of the additions and deductions for inflation and for devaluation as from 2008.

Additional information

NOTE 3 – BEFORE INCOME TAX (CONTD.)

B. Tax rates that apply to the Company

The corporate tax rate in Israel in 2009 was 26%, in 2010 - 25% and in 2011 - 24%.

An association of individuals is taxable on real capital gains at the corporate tax rate applicable during the sale year.

A temporary order for 2006-2009 provided that in the sale of an asset that is not a security traded on the TASE (with the exception of goodwill for which no payment is made) that was acquired prior to January 1, 2003 and sold by December 31, 2009, the real capital gains attributed linearly to a period until December 31, 2002 is taxable at the corporate tax rate fixed in the temporary order for the sale year and real capital gain attributed linearly to a period from January 1, 2003 through to the date of sale, is taxable at a rate of 25%.

On December 5, 2011, the Knesset adopted the Law for Change in Tax Burden (Legislative Amendments) 2011 ("the Law"). Under the Law, inter alia, the declining path for the corporate tax rate was canceled as of 2012. Under the Law, the corporate tax rate was also increased to 25% as of 2012. In light of the increase in the corporate tax rate to 25%, as aforesaid, the tax rates on real capital gains and of real betterment were also increased.

The foregoing changes do not have material impact on the balance of deferred taxes. For information pertaining to the effects of the changes on the investees see Note 42B to the consolidated financial statements.

C. Tax assessments

The company has tax assessments that are considered as final through to and including the 2007 fiscal year.

D. Losses carried over for tax purposes and other interim differences

The Company has losses for tax purposes that are carried over to the following years and which at December 31, 2011 amounted to NIS 450 million.

Subsequent to the balance sheet date, on February 16, 2012, approval was received from the tax authorities for the merger between the Company ("the Receiving Company") and its subsidiary, Delek Investments and Properties Ltd. ("the Transferring Company"). The merger agreement is valid since December 31, 2010. The merger was carried out in accordance with the provisions of section 103C of the Income Tax Ordinance, which states that the merger agreement will be carried out without tax liabilities (with deferred tax) in accordance with the provisions of Part E2 to the Income Tax Ordinance. Upon completion of the merger of all the assets, rights, liabilities and obligations of Delek Investments, including future contingent charges, known and unknown, will be transferred to and incorporated into the Company. Upon completion of the merger, Delek Investments will be eliminated without liquidation and it will be struck from the Registrar of Companies register of companies.

Additional information

NOTE 4 – SUBSTANTIAL AGREEMENTS AND TRANSACTIONS WITH INVESTEEES

A. In September and October 2011, the Company engaged in a borrowing transaction with a financial institution, under which the Company borrowed 7,599,291 participation units of Delek Drilling Limited Partnership ("Delek Drillings") and 159,641,106 participating units of Avner Oil and Gas Exploration Limited Partnership ("Avner"). The lending company is Delek Investments. Accordingly, the Company presents a commitment to pay an amount of NIS 490 million, and the Company recognized a net financing expense in the reporting year of NIS 148 million. For further information pertaining to the acquisition of Delek Energy Systems Ltd. shares by the Company in return for participation units of Delek Drillings and Avner, see Note 14 to the consolidated financial statements.

B. Financial guarantees as of 31 December 2011

1. The Company is guarantor for part of the liabilities of the subsidiary, Delek Real Estate Ltd. ("Delek Real Estate") and its subsidiaries at banks (guarantees which were provided when Delek Real Estate was a subsidiary of the Group). As at December 31, 2011, Delek Real Estate's liabilities and the liabilities of its subsidiaries which are secured by these guarantees amounted to NIS 61 million.
2. The Company provided guarantees in the total amount of NIS 46 million to the affiliate, A. D. I. with respect to projects for the establishment of sea water desalination plants.
3. The Company provided guarantees in the total amount of NIS 49 million with regard to the acquisition of operations in France.
4. The Company provided guarantees in the amount of GBP 10 million in favor of RoadChef, which is held 100% by Delek Petroleum.
5. The Company provided guarantees in favor of the Israel Electric Corp Ltd., under an agreement to supply natural gas, in a total amount of USD 15.9 million for Delek (total of USD 7.7 million), Avner (total of USD 6.9 million) and Delek Investments and Properties Ltd. (total of USD 1.3 million).

C. Loans extended to investees

The Company granted loans to subsidiaries, the balance of which, as at December 31, 2011, amounted to NIS 249 million, linked to the USD and bearing annual interest of 7.25% - 8.25%, and an amount of NIS 4,576 linked to the CPI and bearing fixed annual interest of 5.8%. The Company also invested in capital notes issued by subsidiaries in the amount of NIS 547 million. The capital notes do not bear interest and are unlinked. In addition, in January 2011, the Company granted a loan in the amount of NIS 228 million for completing Delek Petroleum's acquisition of RoadChef. The balance of the loans to Delek Real Estate amounted (principal) as of December 31, 2011, to a total NIS 239 million. For further information concerning the terms of the loans see Note 14G(1) to the consolidated financial statements. During the reporting period, the Company included a provision in the amount of NIS 47 million for the loans it granted to Delek Real Estate.

D. A loan received from a subsidiary

A wholly-owned subsidiary granted the Company a loan, the balance of which as at December 31, 2011, is NIS 293 million. The loan is linked to the CPI and bears annual interest of 5.85%.

Additional information

NOTE 4 – SUBSTANTIAL AGREEMENTS AND TRANSACTIONS WITH INVESTEEES (CONTD.)

E. Agreements

1. Under the agreement dated June 4 2000 (as amended on July 31, 2007), the Company undertook to provide management and consultancy services to Delek - The Israel Fuel Corporation Ltd. ("Delek Israel"), requiring ongoing management of Delek Israel. This agreement states that, in return for providing the services, Delek Israel will pay the Company USD 25 thousands per month. The agreement is in effect until July 31, 2012.

Management fees for 2011, 2010 and 2009 amounted to NIS 1,088 thousands, NIS 1,138 thousands and NIS 1,821 thousands, respectively

2. Under an agreement dated January 1, 2006, the Company undertook to provide management and consultation services to Delek US. This agreement states that, in return for providing the services, Delek USA will pay the Company USD 125 thousands per month. This agreement will be automatically renewed for an additional period of one quarter.

Management fees for 2011, 2010 and 2009 amounted to NIS 2,082 thousands, NIS 1,874 thousands and NIS 1,966 thousands, respectively

For additional information pertaining to investees see Note 14 to the consolidated financial statements.

F. **Contingent liabilities**

There are certain contingent claims against certain investees for significant sums that might reach several hundred million or even billion shekels. In some cases, it is not possible to assess their outcome at this stage, and therefore no provision was recorded in the financial statements as set forth in Note 32A to the consolidated financial statements as at March 31, 2011.

- G. For further information pertaining to significant events, see the consolidated financial statements.

Chapter D



Additional Information on the Corporation



Delek Group



Chapter D - Additional Information about the Company

Company name: Delek Group Ltd.

Company number in the Registrar of Companies: 52-004432-2.

Date of Statement of Financial Position: December 31, 2011
(Standard 9)

Date of periodic report: March 29, 2012
(Standard 1 and 7)

Standard 8A: Description and Development of the Company's Business

The description of the Company's business and its business development is an integral part of the Periodic Report and is attached thereto.

Standard 8B: Valuation

1. A financial study examining the value of the Group's goodwill and intangible assets, attributed to the acquisition of Phoenix Holdings Ltd. shares, is attached to the Company's financial statements.

Below are the main points specified in this financial study:

- A. Topic of the study: To examine the value of goodwill and intangible assets attributed for the acquisition of shares of Phoenix Holdings Ltd. ("The Phoenix")
- B. Date of the study: As of December 31, 2011.
- C. Value of the assets examined in the study: Surplus costs attributed to life assurance portfolios and general insurance portfolios, and addition in the goodwill balance in total amount of NIS 475 million.
- D. Value set for the assets based on the study: There was no impairment of these assets (see breakdown in attached study).
- E. Identity and qualifications of the Valuator: Prof. Yoram Eden (for addition information see Appendix A to the financial study). There is no mutual dependency between the Valuator and the Company.
- F. Valuation model used by the valuator: The life assurance business was valuated, inter alia, mainly based on figures published by Phoenix in its embedded value report that is primarily calculated using actuary methods for capitalization of future profits. The general insurance business was valuated primarily by a profit multiplier method that reflects the equity required according to the insurance regulations, against revenues from premiums on general insurance transactions.
- G. The assumptions used by the Valuator in his assessment: See details in the study attached to the reports.

2. A financial study is attached to the financial statements for examining the recoverable amount of goodwill of Republic Companies Inc. ("Republic")

Below are the main points specified in this financial study:

- A. Topic of the study: The value of Republic's equity for examining impairment of the value of its goodwill that is attributed to the investment in Republic.
- B. Date of valuation: As of December 31, 2011.
- C. The value of the valuation subject prior to the valuation date: Equity value of USD 266 million (approx. NIS 1 billion).

- D. Value of the valuation subject as fixed based on the valuation: According to the valuation, the equity of Republic amounts to USD 205 million (approx. NIS 780 million) representing an impairment of goodwill of USD 61 million (approx. NIS 230 million).
 - E. Identity and qualifications of the Valuator: The evaluation was conducted by the managements of Republic and of Delek Group and with the help of an independent firm that served as consultant to the management during the assessment.
 - F. Valuation model used : The valuation was carried out while giving weight of 65% to the future cash flow capitalization method and 35% to the comparison method with similar companies in the sector.
 - G. Assumptions according on which the valuation was based: In the cash flow capitalization method, a general capitalization rate of 14.3% and net premiums earned growth rate of 3% as of 2015 were taken into account. In the comparison method with similar companies in the sector, company value to tangible equity ratio and various profit multiplier parameters were taken into account.
3. A financial study is attached to the Group's financial statements for examining impairment of the investment in a subsidiary - Delek Automotive Systems Ltd.: ("Delek Automotive").

Below are the main points specified in this financial study:

- A. Topic of the study: To examine impairment of the investment in Delek Automotive Systems Ltd. (an affiliate).
- B. Date of the study: As of December 31, 2011.
- C. The value of the valuation subject prior to the valuation date: The balance of the investment in Delek Automotive amounts to NIS 1,220 million.
- D. Value of the valuation subject as fixed based on the valuation: The balance of the investment, based on the valuation, amounts to NIS 970 million, reflecting impairment of investment of NIS 250 million.
- E. Identity and qualifications of the Valuator: Kesselman Finance PricewaterhouseCoopers Ltd. The study was conducted by a team headed by Dr. Tzur Fenigstein, CPA and partner at Kesselman and Kesselman, who is a financing and valuation expert. There is no mutual dependency between the Valuator and the Company. The Valuator received the Company's undertaking for indemnification for expenses that may be incurred by the Valuator as a result of this financial study.
- F. Valuation model used by the valuator: The discounted cash flow (DCF) method was chosen for estimating the value in use of Delek Automotive that established the value of the investment.
- G. The assumptions used by the Valuator in his assessment: To estimate the value in use of Delek Automotive using the DCF method, the free nominal cash flows from the Company's operations for a five-year period from the valuation date (the "Forecast Period") were projected and discounted, as well as, the value of operations at the end of the Forecast Period. Since it was assumed that the Company is a going concern, and that it will continue operations after the end of the Forecast Period, the value of operations of the Company at the end of the Forecast Period was determined as the present value of cash flows to infinity, based on annual representative cash flow for the period and assuming that the representative cash flow will grow at a nominal rate of 3% annually. The weighted cost of capital, according to which the free cash flows were discounted, representing the business risk associated with operations of the Delek Automotive, was set to 11%.

Standard 9: Financial Statements

Audited financial statements as at Saturday, December 31, 2011 with enclosed auditor's report are attached hereto.

Standard 9A: Pro-forma event in the reporting year through to the date of approval of financial statements

None.

- Standard 9B: Annual report pertaining to the board of directors and the management's assessment of the effectiveness of the internal audit**
An annual report pertaining to the board of directors and the management's assessment of the effectiveness of the internal audit is attached hereto.
- Standard 9C: Financial information from the Company's consolidated financial statements pertaining to the company itself.**
See financial Information from the consolidated financial statements of the Company.
- Standard 9D: Report of the Company's liabilities according to repayment dates**
Simultaneous to publication of this periodic report, the Company publishes an Immediate Report with regard to the liabilities of the Company and its subsidiaries or companies consolidated in the financial statements, by repayment date, constituting an integral part of the periodic report.
- Standard 10: Directors' Report on the State of the Company's Affairs**
The Directors Report on the state of the Company's affairs for the year ended December 31, 2011 is attached to the periodic report, constituting an integral part of it.
- Standard 10A: Summary of the Company's consolidated statements of income for each of the quarters of 2011.**
The Company's condensed statements of comprehensive income are enclosed (in the Directors Report).
- Standard 10C: of consideration for the securities offered in the prospectus**
In July 2011 the Company issued debentures (expansion of debenture series) for proceeds of NIS 467 million and in November 2011 in a private placement (by way of expansion of debenture series) for NIS 261 million, based on a shelf prospectus dated May 2011. The foregoing proceeds were used and are used by the Company for debt recycling.

Standard 11: Breakdown of the Company's investments in each of its subsidiaries and affiliates as of the date of the statements of income:

Companies held directly by the Company

Company name:	Security no. on the TASE	Type of security	Par value	No. of par value/participating units held by the Group	Capital held (%)	% in voting rights	Total investment as of date of the statement of financial position (NIS millions)	NIS price of securities on the TASE at date of statements of financial position	The balance of loans and capital notes (including interest receivable) in statements of financial position (NIS millions)
Delek Investments and Properties Ltd. (1)	-	Ordinary shares	NIS 0.01	5,586,407	100	100	6,084	-	2,950
Delek Petroleum Ltd.	1111376	Ordinary shares	NIS 0.01	1,100	100	100	1,992	-	2,239
Delek Real Estate Ltd. (2)	1093293	Ordinary shares	Ordinary shares without nominal value	19,325,244	4.99	4.99	(56)	0.20	76
Cohen Development and Industrial Buildings Ltd. 3	810010	Ordinary shares	NIS 1	3,406,165	51.76	51.76	283	58.03	-
Delek Sea Maagan (2011) Ltd.	-	Ordinary shares	NIS 0.1	10,000	100	100	-	-	51

- (1) As of reporting date, Delek Investments is in the process (subsequent to receiving all the approvals and complying with the contingent conditions) of merging with and integrating into the Company.
- (2) For details pertaining to loans and guarantees granted by the Company to Delek Real Estate see Note 14G to the consolidated financial statements.
- (3) Acquired on December 28, 2011; for additional details see Note 14. Cohen Development holds 50% of the general partner of Avner Partnerships, and the general partner holds 1.81% of Avner Partnerships

Investees of the Company and Delek Investments, Delek Petroleum and Delek Energy

Company name:	Security no. on the TASE	Type of security	Par value	No. of par value/participating units held by the Group	Capital held (%)	% in voting rights	Total investment as of date of the statement of financial position (NIS millions)	NIS price of securities on the TASE at date of statements of financial position	Loan balances (including interest receivable) in statements of financial position (NIS millions)
Delek Automotive Systems Ltd.	829010	Ordinary shares	NIS 1	29,942,280	32.13	32.13	970	23.07	-
Delek Energy Systems Ltd.	565010	Ordinary shares	NIS 1	4,383,829	86.71	86.71	114	1,546	256
Delek Drilling – Limited Partnership (1)	475020	Participating units	-	35,734,105	6.53	6.53	84	14.05	-
Avner Oil Exploration - Limited Partnership (2)(3)	268011	Participating units	-	303,711,239	9.11	9.11	734	2.4	-
Gadot Biochemical Industries Ltd.	1093004	Ordinary shares	NIS 0.1	14,057,420	76.37	76.37	(135)	-	75
Phoenix Holdings Ltd.	767012	Ordinary shares	NIS 1	118,849,101	55.72	54.58	1,876	9.85	-
	767038	Ordinary shares	NIS 5	3,761,082				58.40	
I.P.P. Delek Ashkelon Ltd.	-	Ordinary shares	NIS 1	1,001,000	100	100	5	-	-
IDE Technologies Ltd.	-	Ordinary shares	NIS 1	638,009	49.8	49.8	420	-	-
Delek Finance US Inc. (4)	-	Ordinary shares	USD 0.01	100	99	99	(130)	-	819
Delek Capital Ltd.	-	Ordinary shares	NIS 0.01	499,000	46.8	46.8	113	-	73
Delek Drilling – Limited Partnership (8)	475020	Participating units	-	342,592,968	62	62	588	14.05	-
Avner Oil Exploration - Limited Partnership (4)(8)	268011	Participating units	-	1,583,495,230	47.48	47.48	820	2.41	-
Delek US Holdings Inc. (5)	NYSE	Ordinary shares	USD 0.01	39,736,432	68.47	68.47	1,646	43.6	254
Delek- The Israel Fuel Corporation Ltd.	6360044	Ordinary shares	NIS 1	9,861,473	86.90	86.90	936	56.75	69
Delek Europe BV (6)	-	Ordinary shares	EUR 0.01	1,800,000	100	100	650	-	604
Delek Motorway Services (7)	-	Ordinary shares	GBP 1	18,000,000	100%	100%	708	-	1,363

- (1) Direct holding of Delek Investments, also held through Delek Energy.
- (2) In view of the acquisition of control in Avner Partnership, the Group revaluated the fair value of its investment in Avner, for further information see Note 14 (it should be noted that Avner Partnership is also held by Delek Energy. The general partner holds approx. 1.8% of the Avner participating units.
- (3) Holds 99% of Republic shares
- (4) Including holdings through the general partner. The general partner holds approx. 1.8% of the Avner participating units.
- (5) Held through the subsidiary, Delek Hungary, which is held by Delek Petroleum and Delek Israel Fuel Corporation at rates of 98.42% and 1.58%, respectively, and Delek Petroleum's direct holding in Delek US Holdings Ltd.
- (6) Held by Delek Europe Holdings Ltd., which is held by Delek Petroleum Ltd. and Delek the Israel Fuel Corporation Ltd. at 80% and 20%, respectively.
- (7) As of December 31, 2011 held through Delek Petroleum 100%.
- (8) The holding is through a subsidiary, Delek Energy Systems, which is held by Delek Investments and Properties 86.71%, which is held by the Company 100%. As of December 31, the investment in Avner shares was revaluated at NIS 4 billion. For further information, see Note 14 to the financial statements.

Standard 12: Material changes in investments in subsidiaries and affiliates in the reporting period:

Date of change	Nature of the change	Company name:	Share no. on the TASE	Class of share	Total par value	Cost (in NIS millions)
January 2011	Acquisition	Delek Motorway Services Ltd. (RoadChef)	-	Ordinary shares	25,000	497
January 2011	Acquisition	Phoenix Holdings Ltd.	767012	Ordinary shares	528,438	7
January - May 2011	Acquisition	Delek Energy Systems Ltd.	565010	Ordinary shares	47,560	47
January - May 2011	Acquisition	Avner Oil Exploration - Limited Partnership	268011	Participating units	24,487,075	43
January – June 2011	Acquisition	Delek Drilling – Limited Partnership	475020	Participating units	6,749,086	89
September 2011	Acquisition by way of a special tender offer (*)	Delek Energy Systems Ltd.	565010	Ordinary shares in return for participating units of the Delek Drilling and Avner Oil Exploration Limited Partnerships	353,988	(*)
September 2011	Sale by way of exchange of securities in an exchange tender offer(*)	Avner Oil Exploration - Limited Partnership	268011	Participating units	167,082,364	(*)
September 2011	Sale by way of exchange of securities in an exchange tender offer(*)	Delek Drilling – Limited Partnership	475020	Participating units	12,743,570	(*)
October 2011	Acquisition by way of securities exchange (**)	Delek Energy Systems Ltd.	565010	Ordinary shares	23,275	(**)
October 2011	Sale by way of securities exchange (**)	Avner Oil Exploration - Limited Partnership	268011	Participating units	10,869,425	(**)
October 2011	Sale by way of securities exchange (**)	Delek Drilling – Limited Partnership	475020	Participating units	837,900	(**)
August 2011	Tender offer	Delek- The Israel Fuel Corporation Ltd.	6360044	Ordinary shares	1,099,699	(*)
September 2011	Acquisition	Delek Group Ltd.	1084128	Treasury shares	18,354	65
September 2011	Conditional full tender offer by Delek Investments	Gadot Biochemical Industries Ltd.	1093004	Ordinary shares	1,891,003	8
September 2011	Regular tender offer by Delek Investments	Gadot Biochemical Industries Ltd.	1093004	Option warrants	72,575	-
November 2011	Acquisition	Delek Hungary Holding Ltd.	-	Ordinary shares	615	37
December 2011.	Acquisition	Cohen Development and Industrial Buildings Ltd.	810010	Ordinary shares	3,406,165	274
May - October 2011	Acquisition	Lion Oil Company	-	Ordinary shares	8,291,442	190

(*) For details concerning the Delek Energy exchange tender offer, see Note 14 to the financial statements.

(**) For further information pertaining to the exchange transaction, see Note 14 to the financial statements

Standard 13: Comprehensive and net income of subsidiaries and affiliates and the Company's revenues therefrom as of the date of the financial statements for the year ended Saturday, December 31, 2011 (NIS millions).

Company name:	Net earnings (loss) for year		Annual comprehensive profit (loss)		Income received by the Company from:					
	Attributable to the Company's shareholders	Equity attributed to holders of minority rights	Attributable to the Company's shareholders	Equity attributed to holders of minority rights	Dividends		Interest		Management fees	
					Up to Dec 31, 2011	From Jan 1, 2012 through to report publication date	Up to Dec 31, 2011	From Jan 1, 2012 through to report publication date	Up to Dec 31, 2011	From Jan 1, 2012 through to report publication date
Delek Automotive Systems Ltd.	126	-	126	-	124	-	--	-	-	-
Delek Energy Systems Ltd.	106	95	205	119	-	-	20	9	-	-
Delek Drilling – Limited Partnership	251	-	251	-	-	-	-	-	-	-
Gadot Biochemical Industries Ltd.	(378)	(1)	(362)	(1)	-	-	-	-	-	-
I.P.P. Delek Ashkelon Ltd.	1	-	1	-	-	-	3	-	-	-
Phoenix Holdings Ltd.	49	16	(35)	16	28	-	-	-	-	-
Delek US Holdings Inc.	560	19	574	28	49	5	14	5	2	1
Delek- The Israel Fuel Corporation Ltd.	17	-	34	2	8	-	6	4	1	3
Delek Europe BV	14	-	50	-	77	-	17	-	17	2
RoadChef	(23)	-	(379)	-	-	-	-	-	-	-
Republic Companies Group Inc.	(400)	1	(321)	(1)	15	-	-	-	1	-
Avner Oil Exploration - Limited Partnership	243	-	308	-	-	-	-	-	-	-
IDE Technologies Ltd.	140	62	130	58	18	30	-	-	2	-
Delek Capital Ltd.	72	-	72	-	-	-	-	-	-	-
Delek Real Estate Ltd.	(1,143)	(730)	(1,062)	747	-	-	-	-	-	-

Standard 14: List of categories of loan balances granted as of the statement of financial affairs date, if granting the loans was one of the corporation's main businesses

Extending of loans is not one of the Company's main businesses

Standard 20: Trading the Company's securities on the TASE, dates and reasons for interruption of trade

Securities listed for trade:

During July 2011, 200,000,000 NIS par value debentures (Series O) and 267,000,00 NIS par value debentures (expansion of Series N), and 892,515 warrants (Series 16) exercisable into debentures (Series O) and 1,311,700 warrants (Series 17) exercisable into debentures (Series N).

In November 2011, 258,000,000 debentures (expansion of Series O) were listed for trading.

Interruption of trade:

Date of interruption	Security name and number	Reason for interruption of trade
3/10/2011	Delek Group 1084128	Publication of report by subsidiary/affiliate
4/3/2011	Delek Group 1084128	Company's announcement
5/30/2011	Delek Group 1084128	Publication of Q1 statement of income
11/29/2011	Delek Group 1084128	Publication of Q1 statement of income
12/1/2011	Delek Group 1084128	Company's announcement

Standard 21: Payments made to senior officers (NIS thousands)**21[A](1):**

Below is a breakdown of the benefits given in 2011 to each of the five recipients of the highest benefits among the senior officers at the Company or at a corporation under its control, and which were given to them in lieu of their tenure at the company or at a corporation under its control, as recognized in the financial statements (the figures hereunder represent the cost to the employer):

Recipient				Benefits in lieu of services					Other benefits		Total	
Name	Position	Employment basis	% of holding of Company's capital	Salary	Management fees	Bonus	Share-based payment	Other	Interest	Other	Total	Total without share based payments shares
Zion Ginat(*) (1)	CEO of Delek Benelux and BP (former)	Full-time	-	398	1,429	1,244	18,979			363	22,413	3,434
Gideon Tadmor (2)	CEO of Delek Energy (former)	Full-time	-	1,390	-	140	6,583	-	-	161	8,274	1,691
Eyal Lapidot (3)	CEO of Phoenix	Full-time	-	3,625	-	-	5,715	-	-	-	9,340	3,625
Uzi Yamin(**) (4)	CEO of Delek USA	Full-time	-	1,675	-	2,505	1,167	-	-	2,920	8,267	7,100
Yitzhak Oz (5)	Joint CEO of Agam Leaders (Israel) Insurance Agency (2003) Ltd.	Full-time	-	-	2,319	4,956	-	-	-	74	7,349	7,349

(*) Translated at the average EUR to NIS exchange rate for 2011 - 4.977

(*) Translated at the average USD to NIS exchange rate for 2011 - 3.579

21[A](2): Below is a breakdown of the benefits paid to each of the Company's three senior officers who are not among those appearing in the foregoing table, in lieu of their tenure at the Company and at corporations under its control, as recognized in the financial statements:

Recipient				Benefits in lieu of services					Other benefits		Total	
Name	Position	Employment basis	% of holding of Company's capital	Salary	Management fees	Bonuses	Expenses (income), net attributed for a share-based payment	Other	Interest	Other	Total	Total without share based payments shares
Asi Bartfeld (6)	CEO of the Company	Full-time	0.04	1,728	-	1,800	-	-	-	-	2,989	3,528
Gabi Last (7)	Chairman, Board of Directors.	Full-time	0.04	1,837	-	600	10	4	-	-	3,051	3,041
Mashraki Barak (8)	CFO	Full-time	-	1,290	-	600	-	-	-	-	1,805	1,890

21[A](3): The table below presents details of the remuneration paid to each of the Company's senior officers who are not represented in the foregoing table, with respect to their service in the Company and in its investees, in NIS thousands:

Recipient		Benefits in lieu of services								Other benefits	Total
Name	Position	Scope of position	% Holding In the company capital	Salary	Bonus	Management Fee	Commission	Other	Compensation Directors.		
Moshe Amit (9)	Director	Full-time	0	823	200	-	-	146	-	-	1,169
Elad Sharon (Teshuva) (10)	Director	60%	0	-	-	-	-	124	41	-	165
Additional directors who are not external directors (11)	-	-	-	-	-	-	-	-	757	-	757
External directors (12)	-	-	-	-	-	-	-	-	732	-	732

Standard 21 – cont'd

Notes on the figures represented in the tables:

- (1) **Mr. Zion Ginat** - served as CEO of the subsidiary, Delek Benelux BV ("Delek Benelux") until March 13, 2011. Under the agreements between Delek Benelux and Mr. Zion Ginat, the annual salary paid to Mr. Ginat was EUR 80,000; in addition, a consultation agreement was signed with a wholly owned foreign management company of Mr. Ginat, and in return for providing the services, an amount of EUR 286,610 is paid annual to the management company. This amount is linked to the annual CPI in the Netherlands, and the base index is that of January 2008. Furthermore, the management company was entitled reimbursement of expenses it incurred while providing the services, to insurance and indemnification.

In addition to the foregoing remuneration, at signing of the contract with Zion Ginat, Delek Benelux allotted to Mr. Ginat, free of charge, 45,000 options exercisable to Delek Benelux shares, which as of date of issue constituted 2.5% of the issued and paid-up share capital of Delek Benelux. These options were allotted to Mr. Ginat at rates equivalent to the following: On April 30, 2008 - 11,250 options and 5,625 options on each of the dates, October 31, 2008, April 30, 2009, October 31, 2009, April 30, 2010, October 31, 2010, April 30, 2011. The exercise price per ordinary share was EUR 71.66 (based on the value for Delek Benelux of EUR 129 million) for the first tranche and thereafter, the exercise price per additional share was the initial price per share with the addition of 5% annual interest that would accrue until the relevant vesting date. The foregoing options plan is defined as an obligatory plan since under the option agreement, Mr. Ginat was granted put options ("Obligatory Acquisition"), to sell the vested options to Delek Benelux upon termination of his employment according to a mechanism prescribed in the agreement. Based on the mechanism, while Delek Benelux is a private company then its value for the purpose of acquiring the options will be set according to an external valuation as of the date of closing of the transaction. The provision set aside in the Company's books for the obligatory acquisition as aforesaid would be updated during each reporting period and the most significant update was at the beginning of 2011 due to the external valuation that was ordered and, Mr. Ginat's exercise of the obligatory acquisition was published by the way for the purpose of fixing the value of Delek Benelux, as of the beginning of 2011, the valuation was carried out by the Deloitte accounting firm in Belgium and by PWC in Israel and the value of Delek Benelux was fixed according to the average of the two foregoing valuations.

As aforesaid, Mr. Ginat ceased serving as CEO of Delek Benelux on March 13, 2011 and he announced his desire to exercise the obligatory acquisition. Delek Europe acquired the options from him in accordance with the mechanism described above and paid him an amount of EUR 5.4 million, based on the external valuation as of the date of the closing of the transaction.

- (2) **Mr. Gideon Tadmor** - served as CEO of Delek Energy from July 1, 2007 through October 18, 2011.

Mr. Tadmor was employed by Delek Energy, as a full-time salaried employee of the company, at a monthly salary (gross) of NIS 86,726, linked to the CPI. Mr. Tadmor was entitled to reimbursement of expenses, a pension plan, advanced study fund, leave days, car expenses and other ancillary benefits. Furthermore, Mr. Tadmor was also eligible for one annual bonus based on the performance of Delek Energy, as shall be determined by its board of directors.

His term of employment according to Mr. Tadmor's employment agreement began on August 1, 2007 and mutual advance notice of 3 months and an acclimation period of 3 months were agreed upon. On August 20, 2007 the board of directors of Delek Energy resolved to approve allocation to Mr. Tadmor of 258,265 unquoted options exercisable into 258,265 ordinary shares of the Company in 7 equal annual tranches until June 1, 2014 or 120 days from termination of his employ, the earlier of the two dates. To exercise the options, the CEO was eligible for a loan from the Company. The loan will bear 4% annual interest will be linked to the CPI on the date of the loan. The loan will be a non-recourse loan that will be secured solely by a fixed senior lien on the underlying shares. Mr. Tadmor's term of office as CEO of Delek Energy terminated on October 18, 2011 and on this date he ceased serving as an officer of the Company (the parent company of Delek Energy).

On October 18, 2011 the Delek Energy and Mr. Tadmor signed an agreement pertaining to arrangements for the termination of Mr. Tadmor's employ in the Company and regarding changes in the options allotted by the Delek Energy to Mr. Tadmor ("the New Options Agreement"). Shortly prior to the end of Mr. Tadmor's employment in Delek Energy, Mr. Tadmor held 184,475 options (in 5 tranches).

The main points of the new options agreement are as follows: 61,492 of the options will be exercised by Mr. Tadmor by means of an options to cash exercise mechanism based on the benefit component according to which Mr. Tadmor will be entitled to a cash payment from Delek Energy reflecting the benefit component embedded in the options at the price of Delek Energy's shares on the TASE on

October 18, 2011, within 14 days from the date of signing of the new options agreement. 86,088 of the options will be exercised by Mr. Tadmor by means of an options exercise mechanism into shares of Delek Energy based on the benefit component, according to which Mr. Tadmor will be entitled to receive 60,661 shares of Delek Energy reflecting the benefit component embedded in the options at the price of Delek Energy's shares on the TASE at closing of trade on October 18, 2011, within 14 days from date of signing of the new options agreement. The expiry date of 36,895 options originating in the fifth tranche under the new options agreement will be changed and will be exercisable into Delek Energy shares through to November 1, 2012.

Until October 26, 2011 Mr. Tadmor was entitled to notify Delek Energy of changes in the distribution of the quantity of options that he would exercise and/or that he would waive, in accordance with the mechanisms described above (pursuant to the provisions of this section and further to Mr. Tadmor's notice date October 26, 2011 regarding changes in the distribution of the quantity of options, on November 8, 2011 Delek Energy allotted 39,488 Company shares in return for exercise of 55,342 options to Gelfand Trusts (2000) Ltd., in trust for Mr. Tadmor, on November 8, 2011 Delek Energy purchased from Mr. Tadmor 55,342 options in return for NIS 53,527,000. Furthermore, 43,790 options will be exercisable into Delek Energy shares by November 1, 2012).

Mr. Tadmor will be eligible to sell all or part of Delek Energy shares that he exercised, as aforesaid, to Delek Energy, subject to the law, for the average price of Delek Energy's shares on the TASE during the 30 days prior to the date of his notification to Delek Energy of the sale of the shares, provided that the exercise notification will be given before November 1, 2012.

- (3) **Mr. Eyal Lapidot** - on June 1, 2009 Mr. Lapidot began serving as CEO of Phoenix Holdings and of Phoenix Insurance ("The Phoenix") In March 2009 Phoenix's board of directors approved the appointment of Mr. Eyal Lapidot as CEO of Phoenix. On that date the board of directors of Phoenix (subsequent to receiving approval and recommendations of the audit committee of Phoenix on same day) approved Phoenix engaging in an employment contract with Mr. Lapidot. The employment contract came into force on June 1 2009 for a period of 5 years ("the Transaction Period"). Both Phoenix and the CEO will have the right, at any time and for any reason, to terminate the employment agreement with prior written notice of 4 months ("the Prior Notice Period"). In the event that Phoenix gives notice to Mr. Lapidot of termination of his employment and of the employment contract, Phoenix is entitled to waive Mr. Lapidot's employ during the prior notice period, in whole or in part, however it will be required to pay Mr. Lapidot, in such case, his full salary, including bonuses and social benefits and to continue awarding him all the ancillary benefits, and this period will be deemed as a period of employment for all intents and purposes. The gross monthly salary that will be paid to Mr. Lapidot is NIS 120,000 ("Total Salary"). Mr. Lapidot's total salary is updated according to the increase in the CPI, while the base index is the CPI of November 2008, which was published on December 15, 2008. In addition Mr. Lapidot is entitled to social benefits, ancillary benefits and reimbursement of expenses as is generally accepted for managers of his status. Furthermore, Mr. Lapidot is eligible to receive an annual bonus for every year of employment and/or part thereof, which will be the higher amount between: 1. an amount equivalent to 1% of the total net profits of Phoenix in the relevant year, less taxes, and less an amount equivalent to a yield of 15% of the equity of Phoenix at the beginning of the relative year; 2. an amount of NIS 1.2 million linked to the increase in the CPI, while the base index is the CPI of November 2008, which was published on December 15, 2008. Upon termination of Mr. Lapidot's employment, for any reason whatsoever, other than under circumstances of immediate notice, Mr. Lapidot will be entitled to an acclimation period of six consecutive months from the end of the advance notice period and the actual utilization of any accrued vacation during which Mr. Lapidot will not be required to perform work for Phoenix.

On August 30, 2009 the board of directors of Phoenix resolved to allot to Mr. Lapidot an amount of 6,177,879 options, each exercisable into one nominally registered ordinary share of NIS 1.00 par value of Phoenix. The options were allotted to Mr. Lapidot, free of charge.

- (4) **Mr. Uzi Yamin**- has served as CEO of Delek USA since 2001. In September 2009 a new employment contract was signed between Delek USA and Mr. Yamin, according to which Mr. Yamin is entitled to a monthly salary of USD 39,000, which will be paid to Mr. Yamin retroactively as of January 2009. Furthermore, Mr. Yamin shall be entitled to various benefits such as a company car, residence owned by Delek USA, education expenses and telephone. The board of directors of Delek USA may, at its sole discretion, decide to grant Mr. Yamin an annual bonus. The period of the contract is from May 1, 2009 through to October 31, 2013. Either party is entitled to terminate the contract with advance notice of twelve months or the balance of the contract term (the shorter of the two). Under the terms of the new employment contract, Mr. Yamin was awarded 1,850,040 stock appreciation rights (SAR), in accordance with Delek USA's benefit plan for 2006. The rights will vest in installments from March 31, 2010 through October 31, 2013, at various exercise prices. The rights will expire one year following

the termination of Mr. Yamin's employment, or on October 31, 2014, the earlier of the two dates. The financial value of the rights amount to USD 2 million. The rights are exercisable for ordinary shares or cash, at the sole discretion of Delek USA. Under the foregoing settlement, Mr. Yamin was given the right to receive in shares the difference TASE share price and the theoretic exercise price, as set out in the agreement. In February 2010, Mr. Yamin exercised his rights under the foregoing settlement and Delek USA awarded him 638,909 shares in lieu of the expired options.

Moreover, in September 2009, Delek USA board of directors approved the settlement pertaining to 1,319,493 options awarded to Mr. Yamin under his previous employment contract and which were not exercised by their expiry date and for which the exercise period could not be extended.

- (5) **Mr. Yitzhak Oz** - Mr. Yitzhak Oz serves as Joint CEO at Agam Leaders (Israel) Insurance Agency (2003) Ltd. ("Agam"). In 2003, Phoenix Agencies (a subsidiary of Phoenix Insurance) acquired 25% of the share capital of Agam from Messrs. Yitzhak Oz and Moshe Sasson. In 2005, Phoenix Agencies acquired from Messrs. Yitzhak Oz and Moshe Sasson 60% of the share capital of Agam Leaders Holdings (2001) Ltd. ("Agam Holdings"), which holds 75% of the share capital of Agam. The management fees and bonus specified with regard to Mr. Yitzhak Oz is the management fees paid to N.A.R Holdings Ltd. ("Oz"), a private company wholly owned by Mr. Yitzhak Oz. The management fees include fixed fees of NIS 159,000 per month, linked to the CPI, with the base CPI being that for July 2005. In addition, the management fees include the value of a company car. The bonus to which Mr. Yitzhak Oz is entitled is an annual bonus deriving from the combined profits of Agam Holdings and Agam Israel, as follows: Profits of Agam Holdings and Agam Israel for the relative year, before tax deduction, impairment of goodwill, deduction of management fees and bonuses to shareholders ("the profit for bonus"). The annual bonus will be 5.025% of the profit for bonus. In addition, Mr. Yitzhak Oz is eligible for an annual bonus of 8.375% of the profit margin above NIS 8 million, of the profit for bonus for the relevant year. The rental paid to Mr. Yitzhak Oz is for stores that he owns and which are rented to Agam.
- (6) **Mr. Asaf Bartfeld** - Mr. Asaf Bartfeld is employed as full time CEO of the Company under an employment contract dated July 21, 1996 and amendments. His monthly salary under the contract is updated from time to time and as at March 2012 amounts to NIS 94,000, gross. Mr. Sharon's salary is linked to the CPI. Mr. Bartfeld is also entitled to an annual bonus, at the discretion of the Company's board of directors, a convalescent bonus, annual vacation days, in-service study fund, severance benefits and pay, a company car and payment for the expenses thereof and payment of the telephone expenses at the CEO's home. The monthly salary and convalescent bonus constitute the basis for provisions for fringe benefits.

The agreement is for an unlimited period or until age 65. The Company is permitted to terminate the agreement with 12 months prior notice, and Mr. Bartfeld is permitted to terminate it with four months prior notice. The Company may waive employment during the advance notice period and pay a salary for this period. Under special circumstances, the Company is entitled to terminate the employment agreement immediately. In addition to the foregoing severance compensation, in the event of dismissal, Mr. Bartfeld is entitled to a retirement bonus in the amount of the determining salary for provisions for fringe benefits, for each year of employment, and in the event of resignation, the CEO is entitled to a retirement bonus in an amount equivalent to half of the foregoing amount. In 2011, Mr. Bartfeld received a bonus in the amount of NIS 1,800,000 for 2010. Mr. Bartfeld's bonus for 2010 has not yet been discussed.

Loans: On February 14, 2006 Delek Investments extended a loan in the amount of NIS 500,000 to Mr. Bartfeld, for the acquisition of securities of public companies belonging to the Delek Group. The loan is recourse, linked to the CPI and bears interest at a rate of 4% per annum. The original repayment date was March 30, 2008 and was extended to March 30, 2011. On March 31, 2011 the Company's audit committee and board of directors approved an extension until April 29, 2013. Under the loan agreement, Mr. Bartfeld is eligible for early payment, in part or in full. The securities that were acquired were deposited as collateral for the repayment of the loan and borrower is entitled to sell the collateral provided that the proceeds for the sale will be transferred to Delek Investments to repay the loan balance. The balance of the foregoing loans as of December 31, 2011 was approx. NIS 780 million. It is noted that in addition to the foregoing loans, Mr. Bartfeld received loans from Delek Investments prior to 2006. A loan in the amount of NIS 4,400,000 was for acquiring securities of companies belonging to the Delek Group. The loan repayment date which was meant to be January 29, 2010 was extended by the Company's board of directors on January 25, 2010 (after approval by the audit committee on January 24, 2010) until April 29, 2013 at the same terms as the original loan. The foregoing loan balance as of December 31, 2011 is NIS 7,895,000. The benefit in the extension of the loan amounts to NIS 897,000 and is recognized in the statement of income.

Furthermore, in 2007 the Company granted Mr. Bartfeld a non-recourse NIS loan in the amount of USD 800,000 (which on date granted was approximately NIS 3,064,000), which was used by Mr. Bartfeld to acquire 0.2% of IDE shares, as set forth below. This loan was granted for a period of three years at annual interest of 4%, linked to the CPI under non-recourse terms and with the addition of VAT on the CPI linkage differentials and the interest. In November 2010, the Company's audit committee and board of directors approved the extension of the loan, which was meant to be repaid on November 29, 2010, until November 29, 2013, at the same terms as originally approved. As of December 31, 2011 the loan balance is NIS 4,227,000.

The total balance of all the loans set forth above, as at December 31, 2011 amounted to NIS 12,902,000.

Allocation of securities: In December 2006, Mr. Bartfeld was granted the option to purchase 28,000 ordinary shares of Delek USA, in which he serves as a director, in return for an exercise price of USD 17.64 per share, and this further to the option plan that was approved at Delek USA at the time of its offering on the New York stock exchange in May 2006. At the end of each of the first four years after the allotment of the option, one quarter of the quantity of shares (7,000 shares) will be released and become exercisable, with the last exercise date being 10 years after the allocation of the option. Should Mr. Bartfeld's tenure as an officer at Delek USA end, he will be entitled to exercise the portion of the option exercisable at that time, within a period of 180 days, and will not be entitled to exercise the balance of the option that has not yet vested. The economic value of the option that was allotted to Mr. Bartfeld amounted to approximately NIS 790,000, on allotment date. The figures that appear in the table for 2011, in NIS, are calculated at the exchange rate on Saturday, December 31, 2011 (NIS 3.579). As at reporting date, the options are out of money.

In November 2007, Mr. Bartfeld exercised options and acquired 0.2% of the shares in IDE for an amount of USD 800,000 through a loan extended to him by the Company, as aforesaid. It should be noted that Mr. Bartfeld serves as a director at IDE. The value of the benefit as calculated in July 2007, based on an external assessment according to agreed accounting principles, amounted to USD 90,000 (also taking into account the possibility of future issue).

Phantom options: In June 2009 the audit committee and the board of directors of the Company decided to award a total of 20,000 phantom options to Mr. Bartlet, under the phantom options plan for senior managers and officers. The Company did not include provisions in its financial statements for 2011 for impairment with respect to the said options due to the decrease in the value of Delek Group shares this year. For further information pertaining to the phantom options plan and the allocations made under it, see subsection (14) below.

Holding in Delek Capital (a liquidated company): Mr. Bartfeld holds 1% of the issued and paid-up shares of Delek Capital, since its establishment in May 2006. On January 5, 2011, the Company's audit committee and board of directors approved Delek Investment's engagement in an agreement with Mr. Bartfeld, who serves as CEO of Delek Investments, with regard to regulating his holdings in Delek Capital, due to the liquidation process by Delek Investments, without distribution of assets and liabilities. The agreement fixes a mechanism by which, when all the assets will be sold to third parties or upon termination of Mr. Bartfeld's tenure as CEO of the Company, the earlier date ("the Effective Date"), Delek Investments will pay to Mr. Bartfeld, in consideration for his holdings in Delek Capital shares, an amount equivalent to one hundredth (1/100) of the theoretic value of Delek Capital, on the effective date of its liquidation ("the Consideration"). The consideration will be calculated, in accordance with the agreement that will be signed, by an assessor whose identity will be agreed upon by the parties. If the calculation of the consideration on the effective date, as aforesaid, results in a negative amount, then Mr. Bartfeld will be entitled to any financial consideration for additional items concerning the engagement of Delek Investments in an agreement with Mr. Bartfeld. Please see immediate report issued by the Company on January 6, 2011 (Ref. No. 2011-01-009015).

- (7) **Mr. Gabriel Last** - Mr. Gavriel is employed full time as the Chairman of the Company's Board of Directors under an employment contract approved by the Company on August 30, 2001. Since September 4, 2003 Mr. Last has been employed as chairman of the Company's board of directors, under the agreement, after his appointment was approved by the shareholders' meeting. Pursuant to the agreement, Mr. Last is eligible for a gross monthly salary of NIS 80,000, linked to the June 2001 CPI (NIS 102,000 as of March 2012) and an annual bonus determined by the Company's board of directors.

The effective salary for determining provisions for bonuses and compensation ("the Assured Salary") is lower than the monthly and amounts to NIS 37,100 linked to the CPI for June 2001. Due to the decreased provision for benefits and compensation, according to the agreement Mr. Last is eligible for a special increment of 13.33% of the difference between the monthly salary and the guaranteed salary

and a special increment of 2.5% of the monthly salary as will be from time to time. It was also determined that the bonus will not be included in the salary for the purpose of provisions to social conditions. Pursuant to the agreement, Mr. Last will not be eligible for managers' compensation for his position as director in the Company and/or in other companies in the Delek Group. Apart from the foregoing, Mr. Last is entitled to convalescent pay, annual vacation days, sick leave, provisions to an in-service study fund, reimbursement of job-related expenses, a mobile phone and costs incurred in connection therewith, reimbursement of expenses for a landline, and a company car provided by the Company, which will bear the maintenance and operating costs thereof. Under the contract, each party may terminate the agreement with three months' advance notice to the other party. The Company may waive employment during the advance notice period and pay a salary for this period. In the event of termination of employment by the Company, Mr. Last is entitled to an acclimation bonus in the amount of six monthly salaries. Under special circumstances, the Company is granted the option of terminating the agreement immediately, without giving an acclimation bonus. The employment contract sets out provisions pertaining to the avoidance of conflict of interest, maintaining confidentiality, employee obligations towards the Company, etc. In 2011 Mr. Last received a bonus in the amount of NIS 600,000 for 2010, which was discussed and approved by the audit committee on May 23, 2011 and by the board of directors on May 30, 2011. Mr. Last's bonus for 2011 has not yet been discussed.

Allocation of securities: In December 2006, the general meeting of the Company approved the allotment of an option to Mr. Last to purchase 28,000 ordinary shares of Delek USA, in which he serves as a director, in return for an exercise price of USD 16 per share. The options were granted in January 2007 further to the options plan approved at Delek USA at the time of its offering on the New York stock exchange in May 2006. At the end of each of the first four years after the allotment of the option, one quarter of the quantity of shares (7,000 shares) will be released and become exercisable, with the last exercise date being 10 years after the allocation of the option. Should Mr. Last's tenure as an officer at Delek USA end, he will be entitled to exercise the portion of the option exercisable at that time, within a period of 180 days, and will not be entitled to exercise the balance of the option that has not yet vested. The financial value of the option that was allotted to Mr. Last amounted to approximately NIS 650,000. Delek USA included an expense in the amount of USD 2,000 (pretax) in its financial statements for 2011 with regard to the foregoing options, in accordance with their vesting terms. The figures that appear in the table for 2011, in NIS, are calculated at the exchange rate on Saturday, December 31, 2011 (NIS 3.579). As at reporting date, the options are out of money.

In August 2007 the audit committee of the board of directors of Delek Energy decided to approve awarding of options to Mr. Last, who at that time served as chairman of Delek Energy's board of directors. The agreement was approved by the general meeting of the Delek Energy's shareholders in October 2007. Under the terms of the allotment made to Mr. Last, in October 2007, 55,345 options exercisable into ordinary shares of Delek Energy in five equal annual tranches were awarded to Mr. Last, gratis. The options are exercisable until the year 2012, with the possibility of shortening the vesting period of each tranche during the course of the relevant year if Delek Energy achieves the market value goals that were set in advance in the agreement. Should Mr. Last cease to serve as chairman of the board of directors of Delek Energy, all the options that were transferred to him and whose exercise date has not yet arrived, will expire immediately. The shares that were allotted in the framework of the exercise of the options constitutes approximately 1.2% of Delek Energy's share capital before the allotment, assuming all the convertible securities of Delek Energy are exercised. The exercise price varies between NIS 349.96 and NIS 425.37 per share, according to the vesting periods set. In addition, to finance the exercise price, Mr. Last is entitled to receive from Delek Energy a non-recourse loan, linked to the CPI and bearing 4% interest per annum. The loan will be secured solely by a first degree lien on the exercise shares. The entitlement to exercise the options will be spread out, beginning on the entitlement date (July 1, 2007), and will be exercisable until the end of one year from the last vesting date. The economic value of the options at the approval date amounted to NIS 5.7 million. In view of Mr. Last's announcement of the termination of his service as chairman of Delek Energy's board of directors as of February 1, 2010, and his appointment as vice chair as of the same date, the general meeting of Delek Energy, subsequent to the approval of the audit committee and the board of directors of Delek Energy, approved on January 17, 2010, amendments to the terms of Mr. Last's options plan, as follows: (a) the fifth option tranche, which vesting date is not yet effective, will be canceled; (b) the fourth option tranche, which vests as of July 1, 2011, or when the Company's value reaches NIS 600 million, shall be waived under the current terms and shall vest so long as Mr. Last is still serving as vice chairman of the Delek Energy's board of directors, but not prior to his third cumulative year as chairman of the board and as vice chairman of the board. It is noted that Mr. Last's third cumulative year of service was July 1, 2010; (c) the termination of Mr. Last's service as chairman of the board of directors shall not be deemed cause for the exercise of the options for a period of 120 days following the termination of service; (d) other than the foregoing changes, no other changes are

applicable to the allotment plan, including the exercise periods of the option tranches which will remain up to the end of 12 months from the last vesting date, as set in the options plan (i.e. 12 months from July 1, 2012), or in Mr. Last's rights to receive a non-recourse loan from Delek Energy to finance the additional exercise as described above. In view of the foregoing, the total number of options that will be awarded to Mr. Last is 44,276 options in place of 55,345 options as set in the original options plan. On June 27, 2010, Mr. Last exercised the first option tranche (for which he was allotted 11,069 Delek Energy shares) and as at Saturday, December 31, 2011 Mr. Last's total remaining number of options is 33,207 options. It should be noted that on June 23, 2011 Mr. Last resumed serving as chairman of Delek Energy.

- (8) **Mr. Barak Mashraki** - Mr. Mashraki is employed as CFO under a personal employment contract with Delek Investments since July 16, 2006 (the "Employment Contract"). Under the employment agreement, Mr. Mashraki is entitled, as of March 2012, to receive a monthly salary of NIS 68,600 (gross), which will be linked to the CPI (the salary will be updated once every three months), and to an annual bonus at the discretion of the Company's board of directors. Furthermore, Mr. Mashraki is entitled to generally accepted social and fringe benefits, such as convalescent pay, annual leave, sick leave, provisions for pension savings and study fund, subscription to a daily newspaper, mobile phone and company car. The Company also carries car maintenance and operating costs and the costs of maintaining the mobile phone. The employment contract also includes Mr. Mashraki's undertaking to maintain confidentiality and non-competition during his employment at the Company and for the first year after termination of his employment. In 2011 Mr. Mashraki received a bonus in the amount of NIS 600,000 for 2010, which was discussed and approved by the audit committee on May 23, 2011 and by the board of directors on May 30, 2011. Mr. Mashraki's bonus for 2011 has not yet been discussed.

Loan guarantees: On July 17, 2011, the Company's Board of Directors approved providing a loan or guarantees from the Company for the acquisition of securities of the Company and/or of the Company's subsidiaries only.

On July 11, 2011 and July 17, 2011, the Company's Board of Directors approved, subsequent to approval of the Company's audit committee on July 11, 2011, granting Mr. Mashraki guarantees in favor of a bank to secure the repayment of a loan that will not exceed NIS 2 million, that the bank provided to him, so that the bank's right of repayment is only to the Company and not to the officer. The securities that were and/or will be purchased from Mr. Mashraki will be used to secure that loan. The validity of the guarantee will not exceed 4 years.

Phantom options: On July 5, 2009, the Company resolved to allocate phantom options to Mr. Mashraki, under the phantom options plan for senior managers and officers. During September 2010, Mr. Mashraki exercised 1,100 phantom options for consideration of NIS 637,000. The Company did not include provisions in its financial statements for 2011 for impairment with respect to the said options due to the decrease in the value of Delek Group shares this year. For further information pertaining to the phantom options plan and the allocations made under it, see subsection (14) below.

- (9) **Mr. Moshe Amit** – in addition to serving as a director of the Company, Mr. Moshe Amit serves as Chair of the board of directors of Delek Israel, under an agreement between him and Delek Israel dated August 4, 2004 (in this subsection - ("the Agreement")). Under the agreement, Mr. Amit is entitled, throughout his employment period, to a monthly payment (gross) of NIS 36,000 (linked to the CPI of June 2004) ("the Remuneration Amount"), from which will be deducted the amounts paid by Delek Group and/or related companies ("the Group Companies") to Mr. Amit as joint remuneration and annual remuneration and/or any other remuneration for his position in the Group Companies. In addition, Mr. Amit is entitled to receive from Delek Israel, a company car (Delek Israel provides Mr. Amit with a level 7 company car), payment of maintenance and operating costs of the car, mobile phone and expenses.

Under the agreement Mr. Amit is not considered and shall not be considered as an employee of Delek Israel and the amount paid to Mr. Amit for his services as chairman of the board of directors at Delek Israel is set taking into consideration the fact that Delek Israel will not be obligated to pay and/or make a provision for Mr. Amit and/or for any payment for fringe benefits, vacation, sick leave, severance compensation, national insurance and any other payment of the kind that Delek Israel customarily pays and/or provides for its employees.

Under the agreement, Mr. Amit undertook to pay all the taxes and/or other mandatory payments under any law for an independent contractor, including income tax, national insurance, health tax, etc. In addition, the employment contract includes provisions aimed at protecting the intellectual property of Delek Israel and a confidentiality clause. Mr. Amit undertook that during his service as a director for Delek Israel, he personally and the companies he controls and/or he has material impact on their administration, shall not compete in any way, directly or indirectly, with Delek Israel and its

businesses. Furthermore, Mr. Amit undertook not to serve on the boards of directors and to take any part in the management of companies which are or are related to companies competing in the business operations of Delek Israel, unless with prior written consent of Delek Israel.

On August 27, 2006, Mr. Amit's employment contract with Delek Israel was amended so that the monthly payment he is entitled to receive, as of June 1, 2006 would be raised to NIS 60,000 per month (linked to the CPI for July 2006). As at March 2012, the monthly payment that Mr. Amit is entitled to is NIS 69,000. The remaining terms of the contract remain unchanged.

In practice, Delek Israel pays Mr. Amit the foregoing monthly payment and receives reimbursement from Delek Group for the amounts owing to Mr. Amit for his role as a director of Delek Group.

The agreement will remain valid until terminated by one of the parties. The agreement may be terminated by Delek Israel with two months advance notice and Mr. Amit is entitled to terminate the agreement with one month advance notice. The agreement determines that upon termination, Mr. Amit shall resign, at the request of Delek Israel, his tenure as a member of the board of directors and any other position that he may hold as part of fulfilling his position under the agreement.

In addition to the payments under the contract, Delek Israel paid Mr. Amit a bonus which in 2011 amounted to (for 2010) NIS 200,000.

On December 26, 2007, Delek Israel allotted 109,483 options ("the Options") to Mr. Amit under its 2007 options plan for employees, officers and consultants of Delek Israel, which was adopted on November 5, 2007 (the "Option Plan"). Under the option plan, Delek Israel may grant options of NIS 1 par value each, unlisted for trade and free of charge, to employees and officers in Delek Israel and its investees.

The options allotted to Mr. Amit vested in two tranches, as follows: (a) 54,742 options on June 01, 2008 (a) 54,741 options on June 1, 2009 ("the Vesting Dates") Each option that vests at each vesting date will be exercisable subject to payment of an exercise price that changes at each vesting date, so that the exercise price for the first tranche is NIS 139.95 and the exercise price upon the next vesting date will be equivalent to the exercise price of the first tranche with the addition of annually adjusted interest of 4%. Said options are exercisable for shares until May 31, 2013 or earlier in the event of termination of employment or of provision of services, as set forth in the plan. The exercise right is subject to adjustments as set forth in the option plan, and includes mainly adjustments for the distribution of bonus shares, issue of rights and distribution of cash dividends, adjustments for sale of the Company's assets to a third party or merger, voluntary liquidation or winding up of the company, and adjustment for changes in the company's equity structure. Mr. Amit will be eligible to receive a loan for the purpose of exercising the options, at annual interest of 4% and linked (principal and interest) to the known CPI on the date on which said loan is granted. The loan will be a non-recourse loan that will be secured solely by a fixed senior lien on the underlying shares. The financial value, on allotment date, of the options allotted to Mr. Amit amounted to NIS 4.8 million.

The remuneration to which Mr. Moshe Amit is entitled to receive from the Company for serving as a director of the Company, is paid by Delek Israel (and reimbursed by the Company) and is a set sum pursuant to the remuneration standards, i.e. participation remuneration, and amounts to NIS 2,860 and annual remuneration of NIS 76,800. Total remuneration paid to Mr. Amit (through Delek Israel) in 2011 amounts to NIS 152,000. For details pertaining to the terms of Mr. Amit's service see section (9) above.

(10) Mr. Elad Sharon (Teshuva):

Mr. Elad Sharon (Teshuva), the son of the Company's controlling shareholder, serves as active vice Chairman of the Board of Directors of the Company. The scope of his position is 60%. For information of the terms of his service see Standard 22 below.

(11) Terms of service of directors who are not external directors

Ms. Mazal Bronstein is entitled to a fixed maximum about as set in the remunerations standard, i.e. to participation remuneration of NIS 3,660 and annual remuneration of NIS 95,100. Total remuneration paid to Ms. Bronstein in 2011 amounts to NIS 197,000.

Mr. Avi Harel, who has accounting expertise, is entitled to participation remuneration in the amount of NIS 4,880 and annual remuneration of NIS 126,900. The total remuneration paid to Mr. Harel in 2011 amounts to NIS 325,000 (excluding remuneration for his service as a director of Phoenix).

Mr. Moshe Bareket¹, who has accounting expertise, began serving as a director of the Company on January 5, 2011. Mr. Bareket is entitled to participation remuneration in the amount of NIS 4,880 and to annual compensation of NIS 126,900. The total remuneration that Mr. Bareket is entitled to receive in 2011 is NIS 236,000 (not including remuneration for serving as chairman of the board of directors of Phoenix and of Excellence). It should be noted that on July 10, 2011, the general meeting re-approved Mr. Bareket's term of office and the remuneration he is entitled to receive.

(13) Terms for service of external directors

On May 29, 2008 the Company's board of directors resolved that, pursuant to the provisions of the Companies Regulations (Regulations for Compensation and Expenses of an External Director) 2000, each external director serving in the Company will be entitled to maximum annual remuneration of NIS 126,900 and maximum participation remuneration of NIS 4,880. The remuneration paid to the directors is updated according to the CPI and updates in the Regulations. The cost of the two external directors in the Company in 2011 amounted to NIS 732,000.

(14) Phantom Options Plan

In June 2009 the Company's audit committee and board of directors decided to adopt a phantom options plan for senior employees and officers, under which phantom options were, inter alia, awarded to the Company's CEO and other officers. Under the terms of the plan, the options were awarded gratis and may be exercised for a monetary bonus and not securities of the Company. The options will vest in three equal annual tranches and the first tranche will vest one year after the date of approval of the allocation by the Company's board of directors (June 2010) or the date on which it is approved by the CEO of the Company, accordingly, as set forth in the plan. The second tranche vested in June 2011 and the third tranche will vest in June 2012. All options will expire in June 2014. The exercise price of the phantom options is the share price on June 2, 2009, which was NIS 503.20 per share. The exercise price is not linked. The phantom options are subject to adjustment as set forth in the plan, in cases such as technical changes in the Company's equity, mergers and acquisitions, distribution of dividend and issuance of rights. The total number of phantom options approved under the plan is 46,895 options of which, as at the reporting date, 31,567 phantom options have been allocated. At December 31, 2011, the financial value of the balance of these options amounted to NIS 13 million and in 2010, an expense of NIS 10 million (pre-tax) was recognized for the plan, and in 2011 income in the amount of NIS 2 million was recognized for said plan.

For further information pertaining to the phantom options plan and the allocation thereunder to the CEO, legal counsel (Executive VP) and CFO of the Company, see Standard 22 below and the Company's immediate reports of June 11, 2009 (Reference No. 2009-01-139182), and July 05, 2009 (Ref. No. 2009-01-161811).

(15) Waiver, indemnification and insurance of officers

The Company's undertaking to indemnify all the eligible officers for any action taken by virtue of their service as officers in the Company past, present and future and to grant them an exemption regarding their liability as a result of a breach of their fiduciary duty towards the Company, will also apply to Mr. Elad Sharon (Teshuva), who serves as a director in the Company and is the son of the controlling shareholder.

Pursuant to the letter of indemnification, as the Company's articles of association include a provision allowing it to undertake in advance to indemnify an officer, provided the undertaking is restricted to the types of events that the board of directors anticipate in view of the Company's actual actions at the time of undertaking to indemnify, in an amount or scope determined by the board of directors to be reasonable under the circumstances, all on account of any liability or expenditure that shall be authorized at that time according to the law at the time the resolution is adopted, the company also undertakes to indemnify the officer for reasonable litigation expenses, including attorneys' fees, such that may be incurred as a result of an investigation or proceedings that shall take place against the officer by any authority certified to launch an investigation or proceeding and that has ended without filing charges against the officer and without a fine being imposed in lieu of criminal proceedings or that has ended without an indictment being filed against the officer, while imposing a fine in lieu of criminal proceedings in a felony that does not warrant the proof of criminal intent.

The Company engages in an officers insurance policy every year. On May 3, 2010, the Company's general meeting approved, subsequent to the approval of the audit committee and the board of

¹ It is noted in this regard that as of reporting date, the remunerations which Mr. Bareket is entitled to receive, have not yet been paid.

directors on March 24, 2010 and October 29, 2010, the Company's engagement with Phoenix Insurance Company, a company controlled by the Company (through its wholly owned subsidiary), in a collective insurance policy to insure officers and directors liability, for the Company and for its subsidiary, and in related companies for the officers who serve in them on behalf of the Company and/or on behalf of its subsidiaries, and to insure the liabilities of the controlling shareholders and their relatives, and this as part of their roles, from time to time as officers in the Company. This policy has liability limit of USD 75 million (seventy five) and in total per year, at annual premium of USD 300,500 of which the Company's share amounts to USD 56,259 per annum. The insurance premium was distributed among the other subsidiaries included in the policy according to the recommendation of an Insurance specialist. The Company may increase the limit of liability in the policy to a total of USD 100 million (one hundred million) for additional annual premium in the amount of USD 55,625. In such event, the Company's share in the premium payment will increase proportionately. In addition, the general meeting of the Company approved on said date that the Company may extend and/or renew the insurance policy or alternatively, if necessary, as part of the collective insurance policy that includes the subsidiaries and related companies, all or some of them, from time to time, without requiring additional approval of the general meeting, with Phoenix Insurance Co. Ltd., or another insurer, in Israel or abroad, so that it will include all the officers in the Company and or in its subsidiaries and related companies, including directors and/or officers who are controlling shareholders in the Company or their relatives, at a premium and under terms as will be generally accepted at the date of the extension, renewal or replacement of the insurance policy, as long as certain terms will exist. For further information pertaining to the engagement in said policy, its terms and conditions for extending, renewing or replacing the police, see the immediate report issued by the Company on March 24, 2010 (Ref. No. 2010-01-31340), and the information contained therein is noted here by way of reference.

As part of the foregoing, Delek Group prepared a directors and officers liability insurance policy for its employees and for the majority of its subsidiaries, including the Company, for a period of one year from January 1, 2012 through December 31, 2012, with liability limit (in the collective policy) in an amount of USD 100 million per incident and for the period, and at a total premium (100%) of USD 340,000. This agreement will be brought for approval of the certified organs in the Company.

Mr. Elad Sharon (Teshuva), who is the son of the controlling shareholder in the Company, and who serves as a director of Phoenix, is eligible for letters of undertaking for indemnity and insurance for directors serving in Phoenix, in accordance with the approval of the general meeting of Phoenix dated December 17, 2008, which was granted under section 275 of the Companies Law. The wording of the letter of undertaking to indemnify and insure, which was given to Mr. Elad Sharon (Teshuva), is identical to that given in the past to the other directors of Phoenix and includes Phoenix's undertaking to indemnify the directors in advance for financial liabilities or expenses that they may incur due to actions (including oversights) taken by them to that may be taken by them by virtue of their being officers. The insurance and indemnification will not be applicable for breach fiduciary duty, provided the officer acted in good faith and had reasonable grounds to assume that the act would not harm the Company.

In addition, letters of undertaking to indemnify and insure the directors who serve at Republic will also apply to Mr. Elad Sharon (Teshuva), who previously served as a director.

On July 10, 2011 the Company's general meeting resolved to approve the amendments to the provisions of the Company's Articles of Association with regard to indemnification and insurance, and subsequently, this general meeting approved exchanging the letters of indemnification granted in the past to officers in the Company (including directors) with letters of exemption and a new version of undertakings to indemnify, and approved granting of such letters of exemption and new version of undertakings to indemnify for the officers serving on behalf of the Company and/or on behalf of its subsidiaries, whoever they may be from time to time. Furthermore, subject to the amendment to the Articles of Association and the approval of the exchange of letters of exemption and indemnification to the Company's officers as aforesaid, another resolution that was on the agenda for this general meeting was to approve the exchange of letters of indemnification granted in the past to Mr. Elad Sharon, deputy chair of the board of directors and the son of the controlling shareholder, with a new version of the letter of indemnification, (as specified in sections 1.5 and 2 of the immediate report as amended on July 4, 2011). This resolution was not approved and therefore Mr. Elad Sharon still has the previous version of the letter of indemnification.

Standard 21 (B) Description of the payments that were given to the officers after the reporting year and before the date on which the report was submitted, in

connection with their tenure or their employment during the reporting year.

There have been no changes the remuneration of the senior officers as specified above, also for the period subsequent to the reporting year and prior to the date of issue of the report, unless explicitly noted otherwise.

Standard 21(A): Control of the Company:

The controlling shareholder of the Company is Mr. Yitzhak Sharon (Tshuva), who holds 64.36% of the equity rights and 64.59% of the voting rights in the Company, and 61.65% of the equity rights and 61.86% of the voting rights in the Company, fully diluted.

Standard 22: Transactions with the controlling shareholder

The controlling shareholder who has a personal interest in all the engagements set forth under Standard 22 below is Mr. Yitzhak Sharon (Tshuva). Mr. Yitzhak Sharon" (Tshuva) interest arises from the fact that these engagements are with companies under his control, or with his relatives or with companies under their control.

Transactions included in section 270(4) of the Companies Law

1. Agreement between Delek Investments and Roni Elroi:

On December 30, 2004, Delek Investments entered into an agreement with Mr. Roni Elroi (the son-in-law of Mr. Yitzhak Teshuva, the controlling shareholder in the Company) and a company controlled by him ("Elroi") stipulating the terms of tenure and employment of Elroi as deputy chairman of the board of directors of Delek Investments. On November 15, 2011 the engagement with him was terminated. The services provided by Elroi include, mainly, participation in Delek Investments' board of directors and as consultant to the officers of the subsidiary, Delek Investments, primarily with respect to business developments and investments abroad. The period of the agreement was from January 1, 2005 for an unlimited period, as long as the agreement has not been brought to an end. Delek Investments was permitted to terminate the agreement with two months advance notice, and Elroi was permitted to terminate it with one month advance notice. The agreement determines that upon termination, Elroi shall resign, at the request of Delek Investments, his service as a member of the board of directors and any other position that he may hold as part of fulfilling his position under the agreement. The monthly remuneration that Elroi was entitled to receive for the services was NIS 56,000 with the addition of VAT, linked to the CPI, while the base index was the CPI for December 2004. In addition, Mr. Elroi was entitled to reimbursement of expenses and all costs of a car (the car will be purchased by Mr. Elroi and will be his property). On November 15, 2011 Elroi gave notice that he was terminating his role in Delek Investments and that he waives the prior notice period to which he is entitled.

2. Agreement with Mr. Elad Sharon (Teshuva):

Mr. Elad Sharon (Teshuva), the son of the controlling shareholder ("Mr. Sharon"), serves as vice chairman of the Company since August 13, 2006. Until January 13, 2010, Mr. Sharon did not receive remuneration for his service as a director. On January 13, 2010, the general meeting, subsequent to the approval of the audit committee and board of directors of the Company on November 29, 2010, approved an agreement according to which Mr. Sharon will be eligible for director's remuneration in amounts equivalent to the maximum annual remuneration and maximum participation remuneration permitted for external directors, under the Companies Regulations (Regulations for Compensation and Expenses of an External Director) 2000 ("the Remunerations Regulations"), according to the Company's classification for each fiscal year, and reimbursement of expenses, as follows" (1) the Company will provide Mr. Sharon with office and secretarial services, including the rental of an office in Beit Adar, at 7 Giborey Israel Street in Netanya, where the Company's offices are located. The Company will bear 60% of the cost of the office and secretarial service and a private company owned by Mr. Sharon will bear the balance of the costs. The costs as aforesaid, applicable to the Company is for rental of the office and salary of the secretary in 2011; (2) participation of 60% in the costs of car maintenance (level 5); (3) participation of 60% in the costs of the maintenance and use of a mobile phone. It is noted that the participation in the reimbursement of expenses are unlimited and are based on the actual expenses and that payment for the foregoing expenses is subject to the approval of the audit committee and is made once every quarter. The reimbursement of expenses described above in subsections 2 through 3 above, in 2011, amounted to NIS 124,000.

It is noted that as of March 2011 Mr. Sharon does not receive directors fees and since May 2011 he did not receive reimbursement of expenses, as per his request not to receive these amounts.

For further information pertaining to the terms of Mr. Sharon's service, as approved by the general meeting, see the immediate report issued by the Company on November 30, 2009 (Ref. No. 2009-01-304638), and the information contained therein is noted here by way of reference.

3. Agreement with Mr. Shir Elroi:

On November 29, 2011 the Company's board of directors approved, subsequent to the approval of the Company's audit committee of the same date, a resolution under Article 1B of the Company's articles of association (Relief for Transactions with Interested Parties), 2000, with respect to the monthly salary that will be paid to Mr. Shir Elroi, the grandson of the controlling shareholder, for his employment by a wholly owned subsidiary of the Company. Mr. Shir Elroi is employed by the subsidiary as a full time economist until February 29, 2012, under the generally accepted terms for employees of his ranking in the subsidiary. The salary that will be paid to Mr. Elroi for his employment as aforesaid is NIS 8,500. The Company's audit committee and board of directors confirmed, in their meetings on November 29, 2011, that the salary that is paid to Mr. Shir Elroi does not exceed the average monthly salary in Israel and is reasonable taking into consideration the scope of employment and nature of the position and the qualifications of Shir Elroi for carrying out his position as economist in the subsidiary. As of March 2012, at his request the scope of Mr. Shir Elroi's position was reduced to 50% and his monthly salary was adjusted accordingly. It should be noted that Mr. Shir Elroi was appointed as a director in Delek Europe.

4. Agreement between Delek Israel and Ms. Carmit Elroi:

On February 21, 2011 the general meeting of Delek The Israel Fuel Corporation Ltd. ("Delek Israel") approved the agreement with Ms. Carmit Elroi, daughter of the controlling shareholder in the Company, concerning the terms of her employment, including exemption of indemnification and insurance of Ms. Carmit Elroi, in her position as a director of Delek Israel. Pursuant to the terms of the agreement, Ms. Carmit Elroi will be entitled to annual and participation remuneration in amounts equivalent to the amount fixed in the remuneration standard, in accordance with the Company's classification for each fiscal year and as paid to the external directors and serving directors of Delek Israel. Furthermore, on January 29, 2012 the general meeting of Delek Israel approved granting Ms. Carmit Elroi a new letter of undertaking for indemnity.

5. Transactions with Delek Real Estate:

Delek Real Estate was a subsidiary of the Company until the majority of its shares held by the Company were distributed as dividend in kind on May 3, 2009. Since the controlling shareholder of the Company is the controlling shareholder of Delek Real Estate, subsequent to the distribution of its shares as dividend in kind, below is a breakdown of the contracts signed between the Company and its subsidiaries and affiliates with Delek Real Estate subsequent to the distribution in kind or contracts signed as aforesaid prior to the distribution in kind and which are still valid as at the reporting date:

- A. Acquisition of RoadChef - on January 10, 2011 the general meetings of the Company and Delek Real Estate approved the Company engaging with Delek Real Estate and with Delek Belron for the acquisition of Delek Belron's rights in the issued shares of a foreign company that holds the issued and paid-up shares of RoadChef ("the Foreign Company") and for the acquisition of Delek Belron's share in the shareholders loans granted to the foreign company ("the Transaction"). The consideration for the transaction amounts to NIS 497 million, which was the equivalent of GBP 86.25 million at the date of the closing of the transaction, reflecting RoadChef's value as GBP 115 million. The transaction was closed on January 25, 2011 and the consideration was paid as follows: a total amount of NIS 394 million was paid by way of offsetting Delek Real Estate's debt for the RoadChef loans, the NCP loan and the balance of its current deficit and an amount of NIS 104 million was paid directly to the bank by the Company for Delek Real Estate's debt to the bank. Pursuant to the Company's commitment to the bank, granted in respect of the distribution of Delek Real Estate shares, the Company acquired from the bank an additional debt of Delek Real Estate to the bank in the amount of NIS 150 million, by way of repaying Delek Real Estate's bank loan back to back with the granting of a new loan to Delek Real Estate. Delek Real Estate undertook to register in favor of Delek Petroleum a second ranking lien on the Hof Hacarmel project, with restrictions that were agreed upon with the bank. The RoadChef holdings were acquired as part of the transaction of its transfer to

Delek Petroleum, so that as at the reporting date, Delek Petroleum holds the full share capital of RoadChef, while Delek Real Estate's debt arising from the purchase of Delek Real Estate's debts from the bank is with the Company. The consideration for the transfer of the holdings as aforesaid, was given as a capital note issued by Delek Petroleum to the Company in a NIS amount equivalent to GBP 86.25 million, for a period of 5 years, without interest and unlinked. For further information pertaining to the foregoing transaction, the terms to the agreement between the Company and the sellers, and for a description of RoadChef's operations see the immediate reports issued by the Company on Sunday, November 28, 2010 (Ref. No. 2010-01-698100) and as paid on January 5, 2011 (Ref. No. 2011-01-006393) and also see section 1.10 in the third part of the chapter on description of the Company's businesses, in this report.

- B. Collateral – the Company guaranteed part of the liabilities of Delek Real Estate and its subsidiaries to banks. As at December 31, 2011 Delek Real Estate's liabilities and the liabilities of its subsidiaries which are secured by these guarantees amounted to NIS 60 million. On May 30, 2005 an agreement was signed between Delek Real Estate and the Company according to which Delek Real Estate will pay the Group annual commissions of 1.5% of the guaranteed amount. The total revenue recorded in the Company's financial statements for the foregoing collateral in 2011 was NIS 1 million.
- C. Agreement between Phoenix and Delek Real Estate - Phoenix Holdings Ltd. and Phoenix Insurance Co. Ltd. ("Phoenix") provided Delek Real Estate Ltd. ("Delek Real Estate") loans in various amounts during 2004 through 2008, and the terms of these loans were modified from time to time, based on the agreement between Phoenix and Delek Real Estate. As of reporting date, Delek Real Estate's debt balance to Phoenix is NIS 66.3 million (approx. 52% of the debt is from yield guaranteed insurance policies and 48% is from nostro accounts).

During August 2011, Delek Real Estate was meant to repay two installments totaling NIS 45.3 million (including interest of NIS 0.7 million on account of the balance of the loans). These installments were not paid. At the same time, Delek Real Estate notified Phoenix that its ability to pay the loan installments in accordance with the repayment dates set was uncertain. It is also noted that on July 25, 2011 Delek Real Estate announced in an Immediate Report that its ability to meet its short and long term commitments was uncertain and therefore it was necessary to formulate an updated outline for its commitments to its creditors. Delek Real Estate announced in the same report that under these circumstances, Delek Real Estate's board of directors instructed its management to request from its financial creditors, including Phoenix, and the holders of the debentures it issued for a consented deferment until January 31, 2012 of repayment of the entire debt principal, which should have been repaid by January 31, 2012. Delek Real Estate also announced that in the interim, until January 31, 2011, Delek Real Estate would continue paying its ongoing liabilities as part of the regular course of business, including current interest payments to its creditors (other than its controlling shareholder) and will repay the secured principal of the loans to its creditors from the proceeds it receives from its assets as promised to its creditors, if they are disposed. Delek Real Estate requested that Phoenix defer the upcoming repayments of the loans (which were due in August 2011) until January 31, 2012.

Further to discussions held by Phoenix's investment committee, audit committee and board of directors they decided, subject to approval of Phoenix's general meeting, to wait with its decision whether to extend the repayment dates of the loans provided by Phoenix to Delek Real Estate, which were due during August 2011, until clarification of the situation with Delek Real Estate and creditors. On September 21, 2011 the general meeting of Phoenix confirmed waiting as aforesaid. In discussions held by the investment committee, audit committee and board of directors of Phoenix, and as of reporting date, no other decisions have been made changing the foregoing decisions.

On November 29, 2011 Delek Real Estate transferred to Phoenix and amount of NIS 4.6 million on account of Delek Real Estate's debt to Phoenix.

On January 31, 2012, Delek Real Estate petitioned the Tel Aviv District Court, requesting an order to convene a meeting of creditors and shareholders for the purpose of approving a settlement that was drafted with the majority of the debenture holders in accordance with section 350 of the Companies Law ("the Petition"). Under the Petition, Delek Real Estate requested that the District Court approve the convening of a meeting of non-guaranteed creditors and of shareholders for the purpose of adopting a resolution to approve the settlement based on the outline agreed upon between Delek Real Estate and representatives of the holders of debentures (Series D and E), which together represent 72% of the holders of Delek Real Estate debentures. Under the settlement outline, Delek Real Estate noted that new debentures would be issued as part of the settlement, which will be secured by a second lien on

Delek Real Estate shares and rights in DGRE and Elad Residences, whose shares are 100% owned by Delek Real Estate and which are pledged in favor of Phoenix to secure the loans provided by it. The Petition notes that if approval is not received from the holders of the existing lien for registering a second lien as aforesaid, the settlement will not be valid. It also noted that with the expiration of the existing first lien in favor of Phoenix the second lien in favor of the debenture holders will become a first lien, while under the settlement, Delek Real Estate undertakes to release the first lien on behalf of Phoenix during 2012. According to the provisions of the Petition, the settlement is subject to reaching individual debt settlement arrangements with Delek Real Estate's financial creditors, including guaranteed creditors who will be represented as part of the detailed settlement that will be brought for the approval of the debenture holders. As of reporting date objections have been filed against the settlement outline to the District Court and the creditors settlement is yet to be approved by the meeting of the debenture holders and/or by the District Court. The main objections were filed on behalf of the holders of debentures of Series Y, who claim that for the purpose of approving the settlement, separate creditor meetings should be held for the various debenture series. Other holders claim that for the purpose of approving the settlement, Mr. Yitzhak Teshuva must participate as a party in the settlement. The Court has not yet ruled on all these claims. As of the date of publication of the report, Delek Real Estate has not formally made a request to Phoenix with regard to a settlement for the repayment of its debt.

- D. Delek Real Estate and Phoenix acquisition of loans from a bank – on July 8, 2008 the transaction was concluded to acquire three parts of a loan from an international bank, given to Delek Belron (a subsidiary of Delek Real Estate) and Phoenix Insurance, in an overall amount of EUR 80.07 million, which is backed by 30 profit yielding real estate properties located in Germany and Switzerland. The acquisition of the loans was carried out through a foreign consultancy company (SPC) that was established and whose share capital and voting rights were held, in equal share, by Delek Belron and Phoenix Insurance. A collaboration agreement was signed between Delek Belron and Phoenix Insurance defining the rights of the parties in the foreign subsidiary and the nature of the collaboration between them concerning the loans. The total consideration that the foreign subsidiary paid for the transaction to acquire the loans amounts to EUR 58 million. The total value of loans as of December 31, 2011 is NIS 77,298,000.

Transactions not included in section 270(4) of the Companies Law

6. Gas station operating agreement with Mr. Avi Lalewski:

Under the agreement between Delek Israel and Mr. Avi Lalewski ("Mr. Lalewski"), brother-in-law of the controlling shareholder in the Company, and Or-Li Energy Resources Ltd. (which to the best of the Company's knowledge, is a company controlled by Mr. Lalewski) ("Or-Li Energy"), Or-Li Energy operates a gas station in Givat Olga belonging to the Delek Israel chain. The agreement includes the customary terms and conditions for this type of agreement. The agreement became effective on March 21, 1999 for a period of two years and was extended at the discretion of Delek Israel for additional two-year periods (or less), and no longer than a total of six years. Under the agreement, Mr. Lalewski is guarantor for all the liabilities of Or-Li Energy. As at the reporting date, Or-Li Energy continues to operate the station, after the termination of the agreement period. It should be noted that since the termination of the agreement period, as aforesaid, the parties continue acting in accordance with the agreement, without Delek Israel examining whether the agreement with Or-Li Energy is at market terms. On March 15, 2011 the audit committee and board of directors of Delek Israel decided not to revoke or amend the terms of the agreement for the time being, due to the examining process, which is limited time and with assistance of an external expert, if necessary, that Delek Israel entered into with regard to formulating an operating model for gas stations. On February 28, 2012, the terms of Delek Israel's operating agreement with Mr. Lalewski and Or-Li Energy since the date when Delek Israel became a public company (in August 2007) through to the present and to continue the engagement with them under an operating agreement with similar terms for a further 3 years from the date of approval by the certified organs at Delek Israel (in this sub-section - ("the Transaction"). The audit committee classified the Transaction as an extraordinary transaction as this term is defined in section 1 of the Companies Law, due to the difficulty in defining the market terms for the foregoing Delek Israel agreement and because the terms are reasonable under the circumstances in view of the overall terms presented to it. The Transaction will be brought for approval by the remaining certified organs in Delek Israel, in accordance with the provisions of section 275 of the Companies Law.

7. Delek Israel's engagement with Ms. Carmit Elroi:

Delek Israel (through its wholly owned subsidiary) engaged in July 2010 with a distributor, which is a third party ("the Distributor") in a distribution agreement for the distribution of various products manufactured by various suppliers. One of the suppliers whose products are distributed to Delek Israel through the Distributor is Pharmacin Ltd., a company owned by Ms. Carmit Elroi, daughter of Mr. Yitzchak Sharon (Teshuva), who since September 28, 2010 serves as a director of Delek Israel (in this section - "Carmit"). Pharmacin manufactures energy snacks, tissue paper and gel for cleaning hands. These products are delivered through the Distributor to Delek Israel for the private brand of Delek Israel's convenience stores, in a manner by which the Distributor will be entitled to distribution fees at a percentage of the product price, including the foregoing products (without the Distributor having to undertake to necessarily purchase them from Carmit), with a commitment to purchase minimum quantities. The total proceeds paid to Pharmacin Ltd. for the purchase of products as aforesaid, as of reporting date, amounted to NIS 682,000. On March 15, 2011 the audit committee and board of directors of Delek Israel confirmed that the foregoing engagement is not an extraordinary transaction and on August 21, 2011, the audit committee decided once more that it does not constitute an extraordinary transaction and recommended to the board of directors of Delek Israel to approve the agreement with Carmit. Delek Israel's board of directors approved, in its meeting of August 21, 2011, the foregoing agreement, based on the recommendation of the audit committee. On August 25, 2011, the agreement with Carmit was signed.

8. Negligible transactions:

Apart from the transactions described above, there are additional agreements which are classified as negligible transactions as defined in section 9 of the Board of Directors report, as follows:

Agreements between subsidiaries and related companies of the Company: An agreement to rent a Delek Real Estate gas station to Delek Israel; providing Delek Israel's Dalkan services to various subsidiaries of the Company; purchase of a car from subsidiaries of Delek Automotive; insurance policies provided by Phoenix; renting of space at Beit Adar (in which until June 30, 2010, 70% of the non-specific rights were owned by Delek Real Estate); operating agreement for a gas and service station in Petach Tikvah (in which Delek Investments is the lifetime lessee) between the Company and Delek Investments of the one party and Zvi Belski and Peleg Belski, who are third parties, of the second party; set of agreements for leasing land in Beer Sheva between Delek Investment, the Company and a third party for operating a gas station of the Company and commercial area adjacent to it; sale of fuel oil and diesel to Gadot Biochemical Industries Ltd.; sale of fuels and oils to Delek Motors; acquisition of a gas station in Carmiel from Delek Real Estate Profitable Properties Ltd.; acquisition of land adjacent to the Olga meeting point from Delek Real Estate Profitable Properties Ltd

Agreements between subsidiaries and related companies of the Company and private companies owned by the controlling shareholder in the Company, or his relatives: Transactions for providing Delek Israel's Dalkan services, insurances taken out at Phoenix; agreement with Ms. Gal Naor, the daughter of the controlling shareholder in the Company, for architectural planning of a gas station and commercial center for Delek Israel; agreement with Ms. Carmit Elroi, the daughter of the controlling shareholder for production of energy bars and toilet paper under a private label for Delek Israel's chain of convenience stores; employment of officers in the Company and its subsidiaries, who are also employed by the controlling shareholder and by private companies owned by him.

9. Holdings in debentures of companies controlled by the controlling shareholder:

For the sake of caution, it is noted that, as at December 31, 2011, holdings in provident funds, pension funds, profit-sharing policies ("Peer Assets"), Phoenix and Excellence trust and nostro funds, debentures of companies controlled by the controlling shareholder are as follows:

Excellence trust funds and ETFs held NIS 14 million par value debentures of Delek Real Estate.

Assets held by the insurance members as of December 31, 2011 is NIS 30 million par value debentures of Elad Fluide and Elad Group, private companies owned by the Company's controlling shareholder.

Standard 24: Shares and other securities of the Company, held by interested parties and senior officers in the Company, in the Company itself, in its subsidiaries and its related companies, as at February 29, 2012.
Holdings of interested parties and executive officers in the Company's shares:

Name of interested party	Company no. in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On 23.3.2011	% Holding In capital	% Holding In capital Diluted	% Holding In voting	% holding In voting Fully diluted
Yitzchak Sharon (Teshuva)(1)	043480003	Delek Group	1084128	7,321,981	64.36%	61.64%	64.59%	61.85%
Daniel (Hachmon) Orli (2)	32011124	Delek Group	1084128	19,500	0.17%	0.16%	0.17%	0.16%
Gabriel Last	4787933	Delek Group	1084128	4,872	0.04%	0.04%	0.04%	0.04%
Asi Bartfeld	65474108	Delek Group	1084128	4,903	0.04%	0.04%	0.04%	0.04%
Excellence Investments Ltd. (3)	520041989	Delek Group	1084128	77,636	0.68%	0.65%	0.68%	0.65%
Excellence Investments Ltd. (3)		Delek Group options 6	1115393	1,283	-	-	-	-
Excellence Investments Ltd. (3)		Delek Group debentures DD	1118884	1,292,032	-	-	-	-
Phoenix Insurance Company Ltd. (4)	520023185	Delek Group	1084128	4,985	0.04%	0.04%	0.04%	0.04%
Elad Sharon	37336997	Delek Group	1084128	0	-	-	-	-
Delek Group Ltd (5)	520044322	Delek Group Treasury shares	1084128	346,407	-	-	-	-
Delek Investments and Properties Ltd. (5)	520032129	Delek Group Treasury shares	1084128	40,816	0.36%	0.34%	0.36%	0.34%
Epsilon Investment House Ltd. (6)	520043464	Delek Group	1084128	4,869	0.04	0.04	0.04	0.04
Clal Insurance Enterprise Holdings Ltd. (7)	520036120	Delek Group	1084128	599,457.94	5.27	5.04	5.29	5.06
Clal Insurance Enterprise Holdings Ltd. (7)		Delek Group debentures DD	1118884	10,200,014	-	-	-	-
Clal Insurance Enterprise Holdings Ltd. (7)		Delek Group options 6	1115393	21,695	-	-	-	-

Name of interested party	Company no. in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On 23.3.2011	% Holding In capital	% Holding In capital Diluted	% Holding In voting	% holding In voting Fully diluted
Clal Finance Ltd. - Mutual Funds (8)	511382343	Delek Group	1084128	19,930	0.17	0.17	0.17	0.17
Clal Finance Ltd. (8)		Delek Group options 6	1115393	3,773	-	-	-	-
Clal Finance Ltd. - Mutual Funds (8)		Delek Group debentures DD	1118884	6,193	-	-	-	-
Manor Holdings Bl. Ltd.	512843855	Delek Group	1084128	337	0	0	0	0
Manor Holdings Bl. Ltd.		Delek Group options 6	1115393	25	-	-	-	-
Manor Holdings Bl. Ltd.		Delek Group debentures DD	1118884	60,000	-	-	-	-
Gav-Yam Bayside Land Corp. Ltd.	520001736	Delek Group	1084128	156	0	0	0	0
Liora Pratt Levin	57906919	Delek Group	1084128	1,017	0	0	0	0
Michael Grinberg	069108231	Delek Group	1084128	220	0	0	0	0
Gideon Tadmor	057995755	Delek Group	1084128	179	0	0	0	0
Moshe Amit	1127885	Delek Group	1084128	57	0	0	0	0

- (1) The shares are held through wholly-owned companies (100%) of Mr. Yitzchak Sharon (Teshuva)
- (2) Mr. Yitzchak Sharon (Teshuva) and Ms. Orli Daniel (Hachmon) are considered together to be holders of the company's securities.
- (3) The holdings include holdings in a index product issuer and provident fund account
- (4) The holdings include holdings in a provident and pension account and profit-sharing account
- (5) Treasury shares
 - (6) The holdings include holdings in a provident fund and trust account
 - (7) The holdings include holdings in a profit-sharing and provident fund account
 - (8) The holdings include holdings in a trust account and nostro account

Holdings of interested parties and senior officers of the Company in shares and securities of Phoenix Holdings, a subsidiary of the Company, as of February 29, 2012:

Name of Interested party	Company no. in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% Holding In voting	% Holding of voting rights Fully diluted
Delek Group Ltd.	520044322	Phoenix 1	767012	118,849,103	55.72%	52.74%	54.58%	51.38%
		Phoenix 5	767038	3,761,082				
Asi Bartfeld	65474108	Phoenix 1	767012	212,634	0.09%	0.09%	0.09%	0.09%
Eyal Lapidot	022030159	F 08/09	7670144	6,177,879	-	-	-	-
		Phoenix 1	767012	29,872	0.01%	2.38%	0.01%	2.61%
Excellence Investments*	520041989	Phoenix 1	767012	2,795,507.04	1.13%	1.07%	0.06%	0.06%
Phoenix Insurance Company	520023185	Phoenix 1	767012	55,276	0.02%	0.02%	0.02%	0.02%
Liora Pratt Levin	65474108	Phoenix 1	767012	16,600	0.01%	0.01%	0.01%	0.01%

* The holdings include holdings in a index product issuer and provident fund account

Holdings of interested parties and senior officers of the Company in shares and securities of Delek Energy, a subsidiary of the Company, as of February 29, 2012:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rights Fully diluted
Delek Group Ltd.	520044322	Delek Energy	565010	4,383,829.06	86.71%	84.91%	86.71%	84.91%
Gabi Last	4787933	Delek Energy 08/07	5650072	33,207	-	0.63%	-	0.63%
		Delek Energy	565010	125	0	0	0	0
Gideon Tadmor	057995755	Delek Energy	565010	4,219	0.08%	0.08%	0.08%	0.08%
Gideon Tadmor	057995755	Delek Energy 08/07	5650072	258,265	0	4.87%	0	4.87%
Excellence Investments*	520041989	Delek Energy	565010	5,496.45	0.11%	0.11%	0.11%	0.11%
Phoenix Insurance Co. Ltd. - profit-sharing	520023185	Delek Energy	565010	128	0	0	0	0

The holdings include holdings in index product issuer and provident fund accounts

Holdings of interested parties and senior officers of the Company in shares and other securities of Delek Israel, a subsidiary of the Company:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rightsFully diluted
Delek Group	520044322	Delek Israel	6360044	9,861,473	86.9%	82.46%	86.9%	82.46%
Eyal Lapidot	022030159	Delek Israel	6360044	224,225	1.98%	1.90%	1.98%	1.90%
Moshe Amit	1127885	Delek Israel 11/07	6360085	109,483	0%	0.92%	0%	0.92%
Excellence Investments - Mutual Funds	520041989	Delek Israel	6360044	11,978	0.11%	0.10%	0.11%	0.10%
Phoenix Insurance Co. - insurance sharing account	520023185	Delek Israel	6360044	157,075	1.38%	1.31%	1.38%	1.31%
Liora Pratt Levin	520023185	Delek Israel	6360044	223	0%	0%	0%	0%
Tamar Rosenberg	035894252	Delek Israel	6360044	170	0%	0%	0%	0%

Holdings of interested parties and senior officers of the Company in participating units of Delek Drilling, a subsidiary of the Company:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rights Fully diluted
Delek Group Ltd.	520032129	Delek Drilling Participating Units	475020	335,734,105	6.53%	6.53%	6.53%	6.53%
Elad Sharon	37336997	Delek Drilling Participating Units	475020	881,209	0.16%	0.16%	0.16%	0.16%
Excellence Investments Ltd.*	520041989	Delek Drilling Participating Units	475020	3,297,747.11	0.6%	0.6%	0.6%	0.6%
Phoenix Insurance Co. Ltd. - profit-sharing	520023185	Delek Drilling Participating Units	475020	3,220,327	0.59%	0.59%	0.59%	0.59%
Liora Pratt Levin	57906919	Delek Drilling Participating Units	475020	15,000	0.00%	0.00%	0.00%	0.00%
Gideon Tadmor	057995755	Delek Drilling Participating Units	475020	151,884	0.03%	0.03%	0.03%	0.03%
Michael Grinberg	069108231	Delek Drilling Participating Units	475020	5,099	0.00%	0.00%	0.00%	0.00%

* The holdings include holdings in index product issuer and provident fund accounts

Holdings of interested parties and senior officers of the Company in participating units of Avner Oil Exploration, a subsidiary of the Company:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rights Fully diluted
Delek Group Ltd.	520044322	Avner Participating Units	268011	303,711,239	9.11%	9.11%	9.11%	9.11%
Gideon Tadmor	057995755	Avner Participating Units	268011	3,888,155	0.17%	0.17%	0.17%	0.17%
Excellence Investments Ltd.*	520041989	Avner Participating Units	268011	27,793,026	0.84%	0.84%	0.84%	0.84%
Phoenix Insurance Co. - insurance sharing account	520023185	Avner Participating Units	268011	37,315,299	1.12%	1.12%	1.12%	1.12%
Michael Grinberg	069108231	Avner Participating Units	268011	30,098	0.00%	0.00%	0.00%	0.00%
Liora Pratt Levin	57906919	Avner Participating Units	268011	159,280	0.00%	0.00%	0.00%	0.00%

* The holdings include holdings in index product issuer and provident fund accounts

Holdings of interested parties and senior officers of the Company in shares and other securities of Delek USA, a subsidiary of the Company:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rightsFully diluted
Asi Bartfeld	65474108	Ordinary shares	-	16,935	--	-	-	-
Asi Bartfeld	65474108	Options	-	28,000	--	-	-	-
Eyal Lapidot	022030159	Ordinary shares	-	3,200	--	-	-	-
Gabi Last	4787933	Ordinary shares	-	6,500	--	-	-	-
Gabi Last	4787933	Options	-	28,000	--	-	-	-
Liora Pratt Levin	57906919	Ordinary shares	-	750	--	-	-	-
Uzi Yamin	024035743	Ordinary shares	-	644,009	--	-	-	-
Uzi Yamin	024035743	Options (SAR)	-	1,850,040	--	-	-	-
Moshe Amit	1127885	Ordinary shares	-	50	--	-	-	-
Asi Ginzburg		Ordinary shares	-	216,600	--	-	-	-

* Delek US Holding Inc. shares are traded on the NYSE

Holdings of interested parties and senior officers of the Company in shares and other securities of IDE, a subsidiary of the Company:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rightsFully diluted
Avshalom Halevi Felber	058370412	Options	-	10,588	-	-	-	-
Asi Bartfeld	65474108	Ordinary shares	-	2,541	-	-	-	-

Holdings of interested parties and senior officers of the Company in shares and other securities of Delek Automotive, a related company of the Company:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rights Fully diluted
Delek Group Ltd.	520044322	Delek Automotive	829010	29,942,280	32.13%	32.13%	32.13%	32.13%
Gabi Last	4787933	Delek Automotive	829010	72,530	0.08%	0.08%	0.08%	0.08%
Asi Bartfeld	65474108	Delek Automotive	829010	113,149	0.12%	0.12%	0.12%	0.12%
Excellence Investments Ltd.**	520041989	Delek Automotive	829010	536,105.37	0.57%	0.57%	0.57%	0.57%
Phoenix Insurance Co. - insurance sharing account	520023185	Delek Automotive	829010	1,531,959	1.64%	1.64%	1.64%	1.64%
Liora Pratt Levin	57906919	Delek Automotive	829010	2,445	0%	0%	0%	0%
Dalia Black Dubov	324335751	Delek Automotive	829010	225	0%	0%	0%	0%
Tamar Rosenberg	035894252	Delek Automotive	829010	204	0%	0%	0%	0%

* From Immediate Report pertaining to the holdings of interested parties and officers as of February 29, 2012 and as amended on March 13, 2012 (Ref. No. 2012-01-066600).

** The holdings include holdings in index product issuer and provident fund accounts

Holdings of interested parties and senior officers of the Company in shares of Gadot Biochemical Industries, a subsidiary of the Company:

Name of Interested party	Company no.in the Registrar of the companies I.D.:	Name of security	No. of security on the TASE	Par value Held On Feb 29, 2012	% Holding In capital	% Holding In capital Diluted	% in voting rights	% Holding of voting rights Fully diluted
Delek Group	520044322	Gadot	1093004	14,057,420	676.37%	75.15%	76.37%	75.15%

Holdings of interested parties and executive officers in the Company's debentures:

Name of Interested party	Company no. At Registrar of Companies/ ID	Name of security	No. of security	Par value held on Feb 29, 2012
Eyal Lapidot	022030159	Debentures (Series W)	1107465	81,967.5
Excellence Investments	520041989	Debentures (Series O)	1115070	35,289,624
Excellence Investments	520041989	Debentures (Series P)	1115385	4,221,582
Excellence Investments	520041989	Debentures (Series M)	1105543	14,513,241
Excellence Investments	520041989	Debentures (Series N)	1115062	13,329,352
Excellence Investments	520041989	Debentures (Series Q)	1115401	5,019,576
Excellence Investments	520041989	Debentures (Series R)	1115823	16,537,643
Excellence Investments	520041989	Debentures (Series S)	1121326	8,374,420
Excellence Investments	520041989	Debentures (Series V)	1106046	2,333,086
Excellence Investments	520041989	Debentures (Series W)	1107465	34,273,707
The Phoenix Insurance Company Ltd.	520017450	Debentures (Series O)	1115070	30,000
The Phoenix Insurance Company Ltd.	520017450	Debentures (Series R)	1115823	80,000
The Phoenix Insurance Company Ltd.	520017450	Debentures (Series W)	1107465	152,885
The Phoenix Insurance Company Ltd.	520017450	Debentures (Series P)	1115385	165,496
Epsilon Investments Ltd.	520043464	Debentures (Series M)	1105543	5,785,358
Epsilon Investments Ltd.	520043464	Debentures (Series R)	1115823	1,584,393
Epsilon Investments Ltd.	520043464	Debentures (Series W)	1107465	7,988,543
Epsilon Investments Ltd.	520043464	Debentures (Series O)	1115070	669,552
Epsilon Investments Ltd.	520043464	Debentures (Series Q)	1115401	129,643
Epsilon Investments Ltd.	520043464	Debentures (Series P)	1115385	1,990,893
Epsilon Investments Ltd.	520043464	Debentures (Series V)	1106046	128,323
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series M)	1105543	76,281,569
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series P)	1115385	338,287
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series W)	1107465	11,441,623
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series N)	1115062	2,414,307
Clal Insurance Enterprises	520036120	Debentures	1121326	2,400,000

Name of Interested party	Company no. At Registrar of Companies/ ID	Name of security	No. of security	Par value held on Feb 29, 2012
Holdings Ltd.		(Series S)		
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series O)	1115070	10,578,320
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series R)	1115823	11,845,627
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series L)	1099639	85,215,000
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series V)	1106046	75,400,200
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series K)	1098201	77,421,966
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series J)	1095082	10,000,000
Clal Insurance Enterprises Holdings Ltd.	520036120	Debentures (Series Q)	1115401	632,516
Clal Finance Ltd.	511382343	Debentures (Series M)	1105543	9,444,262
Clal Finance Ltd.	511382343	Debentures (Series V)	1106046	6,284,319
Clal Finance Ltd.	511382343	Debentures (Series W)	1107465	12,510,921
Clal Finance Ltd.	511382343	Debentures (Series N)	1115062	19,827,696
Clal Finance Ltd.	511382343	Debentures (Series O)	1115070	12,819,928
Clal Finance Ltd.	511382343	Debentures (Series P)	1115385	2,178,673
Clal Finance Ltd.	511382343	Debentures (Series Q)	1115401	3,055,224
Clal Finance Ltd.	511382343	Debentures (Series R)	1115823	7,489,181
Clal Finance Ltd.	511382343	Debentures (Series S)	1121326	17,520,841
Clal Industries and Investments Ltd.	520021874	Debentures (Series N)	1115062	180,000
Clal Industries and Investments Ltd.	520021874	Debentures (Series O)	1115070	174,966
Clal Industries and Investments Ltd.	520021874	Debentures (Series W)	1107465	257,463
Manor Holdings BI. Ltd.	512843855	Debentures (Series V)	1106046	100,000
Manor Holdings BI. Ltd.	512843855	Debentures (Series W)	1107465	131,250
Manor Holdings BI. Ltd.	512843855	Debentures (Series O)	1115070	200,000
Manor Holdings BI. Ltd.	512843855	Debentures (Series R)	1115823	120,000
Manor Holdings BI. Ltd.	512843855	Debentures (Series S)	1121326	1,096,000
IDB Development Corporation Ltd.	520032285	Debentures (Series W)	1107465	693,000
IDB Development Corporation Ltd.	520032285	Debentures (Series N)	1115062	455,000

Name of Interested party	Company no. At Registrar of Companies/ ID	Name of security	No. of security	Par value held on Feb 29, 2012
IDB Development Corporation Ltd.	520032285	Debentures (Series O)	1115070	413,993
IDB Development Ltd.	520028283	Debentures (Series O)	1115070	50,089
Property and Building Corporation Ltd.	520025438	Debentures (Series M)	1105543	440,000
Property and Building Corporation Ltd.	520025438	Debentures (Series W)	1107465	540,000
Property and Building Corporation Ltd.	520025438	Debentures (Series O)	1115070	540,000
Golf & Co. Group Ltd.	510289564	Debentures (Series R)	1115823	445,348
Golf & Co. Group Ltd.	510289564	Debentures (Series O)	1115070	153,100
Bayside Land Corporation Ltd.	520001736	Debentures (Series M)	1105543	793,300
Super-Sol Ltd.	520022732	Debentures (Series W)	1107465	1,275,000
Mashav Initiating and Development Ltd.	520025818	Debentures (Series M)	1105543	1,350,000
Mashav Initiating and Development Ltd.	520025818	Debentures (Series W)	1107465	1,419,508
Mashav Initiating and Development Ltd.	520025818	Debentures (Series O)	1115070	948,128
Mashav Initiating and Development Ltd.	520025818	Debentures (Series R)	1115823	284,000

Holdings of interested parties and executive officers in the Phoenix's debentures:

Name of Interested party	Company no. At Registrar of Companies/ ID	Name of security	No. of security	Par value held on Feb 29, 2012
Excellence Investments	520041989	Phoenix Debentures 1	7670102	10,492,778

Holdings of interested parties and executive officers in the Delek Energy's debentures:

Name of Interested party	Company no. At Registrar of Companies/ ID	Name of security	No. of security	Par value held on Feb 29, 2012
Excellence Investments	520041989	Debentures (Series C)	5650098	5,490.45
Barak Mashraki	029714086	Debentures (Series D)	5650106	150,981
Asi Bartfeld	065474108	Debentures (Series D)	5650106	352,027
Excellence Investments	520041989	Debentures (Series D)	5650106	2,541,400
Asi Bartfeld	065474108	Debentures (Series E)	5650114	178,000
Excellence Investments	520041989	Debentures (Series E)	5650114	2,111,945
Phoenix Insurance Company	520023185	Debentures (Series E)	5650114	7,235,581

Holdings of interested parties and executive officers in the Delek Israel's debentures:

Name of Interested party	Company no. At Registrar of Companies/ ID	Name of security	No. of security	Par value held on Feb 29, 2012
Excellence Investments	520041989	Delek Israel Debentures Series A	6360069	23,117,486
Phoenix Insurance Company	520023185	Delek Israel Debentures Series A	6360069	1,192,341
Excellence Investments	520041989	Delek Israel Debentures Series B	6360127	3,133,779
Phoenix Insurance Company	520023185	Delek Israel Debentures Series B	6360127	343,633
Excellence Investments	520041989	Delek Israel Debentures Series C	6360150	29,912,320
Excellence Investments	520041989	Delek Israel Debentures Series D	6360168	5,315,285

Holdings of interested parties and executive officers in the Delek Petroleum's debentures:

Name of Interested party	Company no. At Registrar of Companies/ ID	Name of security	No. of security	Par value held on Feb 29, 2012
Excellence Investments	520041989	Delek Petroleum Debentures Series G	1111319	16,957,468
Excellence Investments	520041989	Delek Petroleum Debentures Series H	1111327	801,012
Phoenix Insurance Company	520023185	Delek Petroleum Debentures Series A – non- negotiable, CPI linked	1089598	2,500,000

Standard 24 A: Registered and issued capital, and convertible securities

Equity:

	Registered capital	Issued and outstanding capital
	Par value	Par value
Ordinary shares of par value NIS 1 each Labor	15,000,000	11,723,669
Treasury shares (do not grant any rights)		346,407
Treasury shares - held by the subsidiary, Delek Investments and Properties Ltd. (do not grant any rights)		40,816
Issued and paid up share capital All treasury shares		11,336,446
<u>Convertible securities</u>	<u>Par value</u>	
Option warrants – Series 6	260,000	
Convertible Debentures Series DD	255,378,000	

Standard 24B: The Company's Shareholders Register:
Attached herewith is the Company's Shareholders Register:

Standard 25A: Registered address
Address: 7 Giborei Israel St., Netanya
Tel: 09-8638444
Fax: 09-8854955
Email: prlevin_l@delek.co.il
Website: www.delek-group.com

Standard 26: Directors of the company

Name:	Gabriel Last
ID:	004787933
Date of birth:	September 9, 1946
Address for delivery of court notices:	7 Giborei Israel St., Industrial Zone Netanya South, 2504.
Citizenship:	Israeli
Position in the Company:	Chairman of the Board of Directors
A. Is he an external director:	No
B. If yes, does he have expertise in accounting and finance, or professional qualifications:	
C. If yes, is he an expert external director:	
Serves as a member of the board of director committee or committees:	Member of Investment Committee
Commenced serving as a director:	September 4, 2003
Education:	LL.B, Tel Aviv University and M.A. Social Sciences and Mathematics, Haifa University; AMP (Executive Officer Management Program), Harvard University
Primary occupation in the past 5 years:	Chairman of the Company's board of directors
The companies in which he serves as a director:	Delek Investments and Properties Ltd., Delek Petroleum Ltd., Delek the Israel Fuel Corporation Ltd., Delek Infrastructures Ltd., Delek Natural Gas Marketing & Distribution Ltd., Delek Energy Ltd., Delek Drilling Management (1993), Ltd., Delek Energy International Ltd., Delek Energy Bonds Ltd., Gadot Biochemical Industries Ltd., Avner Oil and Gas Ltd., and Delek Foundation for Education, Culture and Science,IPP Delek Ashkelon Ltd.,IPIPP Delek Tavor Ltd., P Delek Ramat Gavriel Ltd., Delek US Holdings Inc, Delek Europe Holdings Ltd. and Delek Benelux B.V.
Does he work for the Company, a subsidiary, an affiliated company or an interested party:	Yes, the Chair of the Board of Directors is a Company employee.
Related to other interested parties in the Company:	None.
Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:	No
Independent director:	No

Name:	Elad Sharon
ID:	37336997
Date of birth:	July 25, 1980
Address for delivery of court notices:	7 Giborei Israel St., Industrial Zone Netanya South, 2504.
Citizenship:	Israeli
Position in the Company:	Vice Chairman of the board of directors
A. Is he an external director:	No

B. If yes, does he have expertise in accounting and finance, or professional qualifications:	
C. If yes, is he an expert external director:	
Serves as a member of the board of director committee or committees:	No
Commenced serving as a director:	August 13, 2006
Education:	LL.B from the Netanya Academic College, MBA from Tel Aviv University, currently completing LL.M at Bar Ilan University
Primary occupation in the past 5 years:	Vice Chairman of the board of directors of a subsidiary of Elad Group (USA) and provides management services to Tashluz Investments and Holdings Ltd. (both subsidiaries owned by the controlling shareholder).
The companies in which he serves as a director:	Does he work for the Company, a subsidiary,
Does he work for the Company, a subsidiary, an affiliated company or an interested party:	Tashluz Investments and Holdings Ltd.
Related to other interested parties in the Company:	Son of Mr. Yitzhak Sharon (Teshuva), the controlling shareholder in the Company
Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:	No
Independent director:	No

Name:

Ben-Zion Zilberfarb

ID:	30134605
Date of birth:	October 9, 1949
Address for delivery of court notices:	10 Hatizmoret St., Kiryat Ono
Citizenship:	Israeli
Position in the Company:	External director:
A. Is he an external director:	Yes
B. If yes, does he have expertise in accounting and finance, or professional qualifications:	
C. If yes, is he an expert external director:	Yes
Serves as a member of the board of director committee or committees:	Serves as a member of the board of director committee or committees: Chair of the audit committee, Chair of the investments committee and member of the committee for examining financial statements
Commenced serving as a director:	(extended term) May 29, 2009
Education:	B.A. and M.A. in Economics, Bar Ilan University, PhD in Economics, University of Pennsylvania
Primary occupation in the past 5 years:	Professor of economics, Bar Ilan University, dean of the School of Banking and Capital Markets at Netanya Academic College Previously served as director for Pandect (external director), Partner and Clal Provident and Study Fund, Israel Discount Bank Ltd. (external director).
The companies in which he serves as a director:	Perrigo Ltd. (external director) and Angel Resources (external director), Brimag Digital Age Ltd. (external

Does he work for the Company, a subsidiary, an affiliated company or an interested party:	director), Infinity Profident and Study Funds. No
Related to other interested parties in the Company:	None.
Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:	Yes
Independent director:	Yes
<u>Name:</u>	<u>Yoseph Dauber</u>
ID:	007447584
Date of birth:	November 20, 1935
Address for delivery of court notices:	8 Hakishon Street, Ramat Hasharon, 47205
Citizenship:	Israeli
Position in the Company:	External director:
A. Is he an external director:	Yes
B. If yes, does he have expertise in accounting and finance, or professional qualifications:	Director with accounting and financial expertise
C. If yes, is he an expert external director:	Yes
Serves as a member of the board of director committee or committees:	Chair of the committee for examining financial statements and member of the audit committee.
Commenced serving as a director:	(extended term) January 1, 2012
Education:	BA in Economics and Statistics, Hebrew University Jerusalem, LL.M, Bar Ilan University
Primary occupation in the past 5 years:	Served as a director at Bank Hapoalim Ltd., and as co-CEO and co-Chair of the board of directors of Bank Hapoalim Ltd.
The companies in which he serves as a director:	Nice Systems Ltd., Orbit Technologies Ltd., MagicJack VocalTec Ltd. (external director), S. Shlomo Holdings Ltd. (external director), Chair of the investments committee of KCPS Manof Fund - Limited Partnership.
Does he work for the Company, a subsidiary, an affiliated company or an interested party:	No
Related to other interested parties in the Company:	None.
Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:	Yes
Independent director:	Yes
<u>Name:</u>	<u>Mazal Bronstein</u>
ID:	051245330
Date of birth:	February 13, 1952

Address for delivery of court notices:	8 Haharuv Street, Zichron Yaakov, 30900
Citizenship:	Israeli
Position in the Company:	Director
A. Is he an external director:	No
B. If yes, does he have expertise in accounting and finance, or professional qualifications:	-
C. If yes, is he an expert external director:	-
Serves as a member of the board of director committee or committees:	No
Commenced serving as a director:	April 1, 2003
Education:	BA Political Science and Middle East, Haifa University
Primary occupation in the past 5 years:	Independent in the marketing, entrepreneurship and construction of real estate projects, director in Sacham House Ltd. and partner (40%) in home for the elderly.
The companies in which he serves as a director:	Delek Petroleum and Beit Shacham, Home for the Elderly, Zichron Yaakov.
Does he work for the Company, a subsidiary, an affiliated company or an interested party:	No.
Related to other interested parties in the Company:	None.
Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:	No
Independent director:	No

Name:

Avraham Harel

ID:	030108195
Date of birth:	February 26, 1948
Address for delivery of court notices:	4 Queen Esther Street, Bnei Brak, 51446
Citizenship:	Israeli
Position in the Company:	Director
A. Is he an external director:	No
B. If yes, does he have expertise in accounting and finance, or professional qualifications:	-
C. If yes, is he an expert external director:	-
Serves as a member of the board of director committee or committees:	Committee for examining financial statements and Audit Committee.
Commenced serving as a director:	May 29, 2006
Education:	BA and MA Economics, Tel Aviv University
Primary occupation in the past 5 years:	Deputy CEO, manager of the finance division and IT systems, and board member – Bank Hapoalim and chairman of the subsidiary, Delek Europe Holdings, Ltd.
Companies in which serves as a director:	Phoenix Holdings Ltd., Phoenix Insurance Co. Ltd., Excellence Holdings Ltd., Poalim Capital Markets Ltd., Poalim Capital Markets - Investment House Ltd., Poalim Capital Markets Investments & Holdings Ltd., Capital Funds

Ltd., Marathon Mobile Access Ltd., Mickal Group Ltd., Bank Hapoalim (Switzerland) Ltd., Bank Hapoalim (Luxembourg) S.A.

Does he work for the Company, a subsidiary, an affiliated company or an interested party:

No.

Related to other interested parties in the Company:

None.

Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:

Yes

Independent director:

No

Name:

Moshe Amit

ID:

1127885

Date of birth:

April 14, 1935

Address for delivery of court notices:

7 Giborei Israel St., Industrial Zone Netanya South, 2504.

Citizenship:

Israeli

Position in the Company:

Director

A. Is he an external director:

No

B. If yes, does he have expertise in accounting and finance, or professional qualifications:

-

C. If yes, is he an expert external director:

-

Serves as a member of the board of director committee or committees:

No

Commenced serving as a director:

April 1, 2004

Education:

BA Political Science and Sociology, Bar Ilan University

Primary occupation in the past 5 years:

Director in the Company, Chairman of the board of directors of Delek - The Israel Fuel Corp. Ltd., previously served as co-CEO of Bank Hapoalim and acting manager of the bank

The companies in which he serves as a director:

Global Factoring Business Finance Ltd., Poalim Capital Markets Investments Bank Ltd, Saint Laurence Bank, Barbados Ltd., Mega Retailers Ltd., AFI Development PLC.

Does he work for the Company, a subsidiary, an affiliated company or an interested party:

Chairman of the board of directors of Delek- The Israel Fuel Corporation Ltd.

Related to other interested parties in the Company:

None.

Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:

Yes

Independent director:

No

<u>Name:</u>	<u>Moshe Bareket</u>
ID:	059825539
Date of birth:	December 31, 1965
Address for delivery of court notices:	7 Giborei Israel St., Industrial Zone Netanya South, 2504.
Citizenship:	Israeli
Position in the Company:	Director
A. Is he an external director:	No
B. If yes, does he have expertise in accounting and finance, or professional qualifications:	-
C. If yes, is he an expert external director:	-
Serves as a member of the board of director committee or committees:	Member of Investment Committee
Commenced serving as a director:	5.1.2011
Education:	PhD in Business Management from Columbia University, (New York); MBA, Columbia University, (New York); MBA Tel Aviv University; BSc in Practical Accounting and Performance Survey, Tel Aviv University. CPA
Primary occupation in the past 5 years:	Head of Corporate Division at the Securities Authority (2006-2010), Lecturer in accounting and business management at universities and academic institutions (2001 to present), Chief Financial and Strategy Officers at Teshuva Group (2010 to present)
The companies in which he serves as a director:	Delek Energy Systems Ltd., T. G. I Investments and director of Elad Europe.
Does he work for the Company, a subsidiary, an affiliated company or an interested party:	Yes, serves as Chief Finance and Strategy Officer at Teshuva Group (personal friend of the controlling shareholder)
Related to other interested parties in the Company:	None.
Does the Company consider him to be an expert in accounting and finance for the purpose of compliance with the minimum number set by the board of directors under section 92(A)(12) to the Companies Law:	Yes
Independent director:	No

Regulation 26A Additional senior officers in the corporation

<u>Name:</u>	<u>Asaf Bartfeld</u>
ID:	6547410
Date of birth:	February 24, 1952
Commencement of service:	September 4, 2003
Position in the Company, its subsidiaries affiliates or interested parties:	CEO of the Company; CEO of Delek Investments & Properties Ltd. CEO of Delek Energy Systems Ltd., and director of the following Delek Group subsidiaries: Phoenix Insurance Co., Phoenix Holdings Ltd., Delek Petroleum Ltd., Delek US Holdings Inc., Gadot Biochemical Industries Ltd., Avner Oil and Gas Ltd., Delek Energy Ltd., Delek and Avner Yam Tethys Ltd., Delek Natural Gas Marketing and Distribution Ltd., Delek Drilling Management (1993), Ltd., IPP Delek Ashkelon Ltd., Delek Energy International Ltd., Delek Energy Bonds Ltd., Delek Automotive Ltd., Delek

Motors Ltd., PP Delek Alon Tavor Ltd., IPP Delek Ramat Gavriel Ltd., Delek US Holdings Inc. and IDE Technologies Ltd. Delek Europe Holdings Ltd., Delek Group Israel Holdings Ltd., Delek Yam Maagan 2011 Ltd.

Is he an interested party in the Company

Yes.

Education:

BA in Economics, Tel Aviv University,

Business experience in the past 5 years:

CEO of the Company since 2003

Is he a family member of another senior officer or of an interested party:

None.

Name:

Liora Pratt Levin

ID:

57906919

Date of birth:

October 12, 1962

Commencement of service:

April 1, 2007

Position in the Company, its subsidiaries affiliates or interested parties:

Executive VP, Chief Legal Counsel and company secretary

Serves as director in the following companies:

Gadot Biochemicals Ltd., Delek Energy Systems Ltd., Phoenix Holdings Ltd., Delek Europe Holdings Ltd., IDE Technologies Ltd.

Is he an interested party in the Company

No.

Education:

BA Political Science, Tel Aviv University, LL.B, Reading University, UK

Business experience in the past 5 years:

VP, legal counsel and company secretary of Delek Group Ltd.

Is he a family member of another senior officer or of an interested party:

None.

Name:

Barak Mashraki

ID:

029714086

Date of birth:

January 28, 1973

Commencement of service:

January 1, 2008

Position in the Company, its subsidiaries affiliates or interested parties:

Executive VP, serves as CFO of Delek Group Ltd., as a director of Delek - Israel Fuel Corp. Ltd., Delek Petroleum Ltd., Phoenix Holdings Ltd. and the companies subsidiaries

Is he an interested party in the Company

No.

Education:

BA Economics and Accounting, Bar Ilan University

Business experience in the past 5 years:

Controller at Delek Group Ltd. and served as a senior auditor in Kost Forer Gabbay & Kasierer / Lubovitch Kasierer (2000-2006)

Is he a family member of another senior officer or of an interested party: None.

Name:

Michael Grinberg

ID:

069108231

Date of birth:

August 5, 1955

Commencement of service:

January 1, 2002

Position in the Company, its subsidiaries affiliates or interested parties:

Internal auditor of the Company and its subsidiaries: Delek Petroleum Ltd., Delek Automotive Systems Ltd., Delek

Is he an interested party in the Company	Energy Systems Ltd., Delek Drilling Management (1993) Ltd. and Avner Oil and Gas Ltd. and Cohen Development and Industrial Buildings Ltd.
Education:	No.
Business experience in the past 5 years:	BA in Accounting and Economics, Tel Aviv University, Internal auditor of the Company and its abovementioned subsidiaries:
Is he a family member of another senior officer or of an interested party:	None.

Name:

ID:	<u>Dalia Black Dubov</u>
Date of birth:	324335751
Commencement of service:	July 25, 1977
Position in the Company, its subsidiaries affiliates or interested parties:	May 27, 2010
Is he an interested party in the Company	Serves as VP Investor Relations and Business Communications at the Company.
Education:	No.
Business experience in the past 5 years:	MA Economics and Political Science, Leads University, England
Is he a family member of another senior officer or of an interested party:	Investor Relations and Business Communications at the Company (since 2006), Associate & Investor Relations at Plens Lending Solutions Funds (2002-2006)

Name:

ID:	<u>Amir Lang</u>
Date of birth:	036403830
Commencement of service:	July 19, 1979
Position in the Company, its subsidiaries affiliates or interested parties:	May 27, 2010
Is he an interested party in the Company	Serves as VP Business Developments, Mergers and Procurement of the Company, and serves as a director of Delek Infrastructures Ltd., and as a director in: Delek Petroleum Ltd. and Delek Israel Fuel Corp. Ltd., IPP Delek Ashkelon Ltd.
Education:	No.
Business experience in the past 5 years:	LL.B, Tel Aviv University; MBA and LL.M, Tel Aviv University;
Is he a family member of another senior officer or of an interested party:	VP Business Development at the Company (since 2008), assistant CEO of the Company (2005-2008)

Name:

ID:	<u>Tamar Rosenberg</u>
Date of birth:	035894252
Commencement of service:	December 9, 1978
Position in the Company, its subsidiaries affiliates or interested parties:	November 19, 2006
Is he an interested party in the Company	Auditor

Education:	MBA specializing in financing, BA Business Administration and Accounting, College of Management, Rishon LeZion
Business experience in the past 5 years:	Accountant in Delek Group
Is he a family member of another senior officer or of an interested party:	None.

Name:	Amit Kornhauzer
ID:	038705562
Date of birth:	March 26, 1976
Commencement of service:	November 2008
Position in the Company, its subsidiaries affiliates or interested parties:	Auditor
Is he an interested party in the Company	No

Education:	MBA specializing in financing, BA in Economics and Accounting, Tel Aviv University
Business experience in the past 5 years:	Controller of Delek Group, controller at Aura Investments.
Is he a family member of another senior officer or of an interested party:	None.

Standard 26A Senior Officers of Subsidiaries controlled by the Company, as defined in section 37 of the Securities Law:

<u>Name:</u>	<u>Avraham Ben Asayag</u>
ID:	059277483
Date of birth:	April 24, 1965
Commencement of service:	August 22, 2010
Position in the Company, its subsidiaries affiliates or interested parties:	CEO of Delek- The Israel Fuel Corporation Ltd.
Is he an interested party in the Company	No.
Education:	BA Economics and Accounting, Tel Aviv University; CPA; Advanced Accounting studies; AMP (Executive Officer Management Program), Harvard University
Business experience in the past 5 years:	CEO of IDB Tourism (2009) Ltd (2009 to present), Chairman of board of directors of The Third Millennium Ltd. (2009 to present), deputy CEO and COO at Strauss Group Ltd. (2007-2009), and CFO at Strauss Group Ltd. (2001-2007).
Is he a family member of another senior officer or of an interested party:	None.

<u>Name:</u>	<u>Avshalom Halevi Felber</u>
ID:	058370412
Date of birth:	October 14, 1963
Commencement of service:	June 16, 2002
Position in the Company, its subsidiaries affiliates or interested parties:	CEO of the subsidiary, IDE Technologies Ltd.
Is he an interested party in the Company	No
Education:	Degrees in economics and philosophy, Hebrew University in Jerusalem ; MBA specializing in financing and employee

Business experience in the past 5 years:	relations, Hebrew University, Jerusalem
Is he a family member of another senior officer or of an interested party:	CEO, IDE Technologies Ltd. Since 2002
<u>Name:</u>	<u>Eyal Lapidot</u>
ID:	022030159
Date of birth:	September 8, 1965
Commencement of service:	June 1, 2009
Position in the Company, its subsidiaries affiliates or interested parties:	Serves as CEO of the subsidiaries, Phoenix Holdings Ltd., Phoenix Insurance Co. Ltd. and Phoenix Investments Ltd.
Is he an interested party in the Company	No.
Education:	BA Economics and Accounting, MBA (Finance and Banking), CPA, Hebrew University, Jerusalem
Business experience in the past 5 years:	CEO of Delek- The Israel Fuel Corporation Ltd. (2005-2009) and CEO at Direct – IDI Insurance Co. Ltd. (2001-2005).
Is he a family member of another senior officer or of an interested party:	None.
<u>Name:</u>	<u>Gideon Tadmor</u>
ID:	057995755
Date of birth:	January 9, 1963
Commencement of service:	October 19, 2011
Position in the Company, its subsidiaries affiliates or interested parties:	Head of oil and gas exploration and transmission, and export of natural gas on behalf of Delek Investments and Properties Ltd., Chairman of the board of directors of Delek Drilling Management (1993) Ltd.
Is he an interested party in the Company	No.
Education:	LL.B, Tel Aviv University
Business experience in the past 5 years:	CEO of Delek Energy Systems Ltd., director at Cohen Development and Industrial Buildings Ltd. And its subsidiaries, CEO of Avner Oil and Gas Ltd., Chairman of the board of directors of Delek Drilling Management (1993) Ltd.
Is he a family member of another senior officer or of an interested party:	None.
<u>Name:</u>	<u>Yossi Abu</u>
ID:	033840372
Date of birth:	December 7, 1977
Commencement of service:	April 1, 2011
Position in the Company, its subsidiaries affiliates or interested parties:	CEO, Delek Drilling Management (1993) Ltd.
Is he an interested party in the Company	No.
Education:	LL.B Hebrew University; [currently studying for LL.M]
Business experience in the past 5 years:	Trade and Regulatory manager at Delek Energy Systems Ltd., senior legal advisor for the Minister of Finance.
Is he a family member of another senior	None.

officer or of an interested party:

Name: **Uzi Yamin**
ID: 024035743
Date of birth: September 18, 1968
Commencement of service: November 1, 2001
Position in the Company, its subsidiaries affiliates or interested parties: CEO of the subsidiary, Delek US Holdings Inc., director in the subsidiaries of the subsidiary, Delek US
Is he an interested party in the Company No
Education: LLB, Hebrew University, Jerusalem ; MBA, Hebrew University, Jerusalem ; CPA
Business experience in the past 5 years: Serves as CEO of the subsidiary, Delek US Holdings Inc.
Is he a family member of another senior officer or of an interested party: None.

- During the course of 2001 Mr. Hod Gibso ceased serving as a senior officer of the Company. He served as CEO of the subsidiary, Delek Europe Holdings Ltd. until December 15, 2011.

Standard 26B: Independent authorized signatories:
The Company has no independent authorized signatories.

Standard 27: The corporation's accountants
Kost Forer Gabbay & Kasierer– 3 Aminadav St., Tel-Aviv 67067

Standard 28: Changes in the Company's memorandum or articles of association
In January 2011, the Company's general meeting approved the replacement of the Company's articles of association with new articles of association as set forth in Standard 29 (C) below.

In July 2011, the Company's general meeting adopted amendments to the Company's articles of association with new articles of association as set forth in Standard 29 (C) below.

Standard 29 – Recommendations and resolutions of the board of directors

Standard 29A (1) – The board of director's decision concerning distribution of a dividend
Decisions of the board of directors pertaining to the distribution of a cash dividend:

Date of Resolution	Amount Dividend in NIS	Payment total per share	Effective date for payment	Payment date
31.03.2011	200,000,000	17.5789	12.04.2011	28.04.2011
30.05.2011	105,000,000	9.2289	15.06.2011	30.06.2011
31.08.2011	100,000,444	8.7895	13.09.2011	27.09.2011
29.11.2011	100,000,444	8.7895	18.12.2011	30.12.2011

Regulation 29 C Resolutions adopted at an extraordinary general meeting (EGM)

On January 10, 2011 the Company's EGM adopted the following resolutions:

To approve the acquisition of Delek Real Estate Ltd.'s holdings in RoadChef as set forth in Standard 22 above.

Particulars pertaining to the foregoing EGM are included in the immediate reports issued by the Company on November 28, 2010 (Ref. No. 2010-01-698100), January 5, 2010 (Ref. No. 2011-01-006375 and Ref. No. 2011-01-006393), January 10, 2011 (Ref.

No. 2011-01-012630) and January 19, 2011 (Ref. No. 2011-01-022185 and 2011-01-022191).

On January 31, 2011 the Company's EGM adopted the following resolutions:

To approve the replacement of the Company's articles of association with a new version of articles of association, enclosed with the immediate report issued by the Company on January 31, 2011, pertaining to the changes in the Company's articles of association.

Particulars pertaining to the foregoing EGM are included in the immediate reports issued by the Company on January 31, 2011 (Ref. No. 2011-01-033561, Ref. No. 2011-01-033579), January 9, 2011 (Ref. No. 2011-01-009723) and January 27, 2011 (Ref. No. 2011-01-031050).

On July 11, 2011 the Company's general meeting adopted the following resolutions:

1. To re-appoint Mr. Moshe Bareket as a director in the Company. Mr. Moshe Bareket will be entitled to annual remuneration and participation remuneration based on the maximum amount set in the fourth addendum to the Companies Regulations (Rules concerning Remuneration and Expenses of an External Director) 2000 for an expert external director, as it may be from time to time and according to the Company's rating as it may be from time to time, as of January 5, 2011.
2. To approve the amendments to the provisions of the Company's Articles of Association relating to insurance and indemnification.
3. To approve replacing of letters of indemnification granted in the past to officers (including directors) in the Company with letters of exemption and new version of undertakings to indemnify. Also to approve awarding letters of exemption and new version of undertakings to indemnify to officers in the Company and its subsidiaries, and in affiliates for officers serving in them on behalf of the Company and/or on behalf of its subsidiaries, as these may be from time to time, excluding officers who are controlling shareholders in the Company or their relatives.
4. To approve a bonus for 2010 in the amount of NIS 600,000 for the chairman of the board, Mr. Gabi Last

Particulars pertaining to the foregoing general meeting are included in the immediate reports issued by the Company on July 11, 2011 (Ref. No. 2011-01-209067), July 4, 2011 (Ref. No. 2011-01-201804) and on May 31, 2011 (Ref. No. 2011-01-171450).

On December 19, 2011 the Company's general meeting adopted the following resolutions:

To approve the extension of the term of office of Mr. Yosef Dauber as an external director of the Company for a further period of three (3) years, as of January 1, 2012, and setting his remuneration.

Particulars pertaining to the foregoing general meeting are included in the immediate reports issued by the Company on December 19, 2011 (Ref. No. 2011-01-366348), and November 13, 2011 (Ref. No. 2011-01-324723).

Standard 29A(3) Extraordinary transactions with officers

On January 5, 2011, the audit committee and board of directors of the Company resolved as follows:

Approval the engagement of the subsidiary in an agreement with the Company's CEO.

For further information pertaining to the engagement, see the Company's immediate report of January 6, 2011 (Reference No.: 2011-01-009015), whereby the information appearing therein is noted here by way of reference.

On March 31, 2011, the audit committee and board of directors of the Company resolved as follows:

The approval of the extension of a loan extended to the Company's CEO

For further information pertaining to the loan, see the Company's immediate report of April 1, 2011 (Reference No.: 2011-01-105681), the information appearing therein being noted here by way of reference.

On April 10, 2011, the audit committee and board of directors of the Company resolved as follows:

To approve extending the loan to the chief legal counsel and Secretary (VP).

For further information pertaining to the loan, see the Company's immediate report of April 10, 2011 (Reference No.: 2011-01-115569), the information appearing therein being noted here by way of reference.

On May 23, 2011 and May 30, 2011, the Company's audit committee and board of directors resolved as follows:

Approval of the payment of a bonus for 2010 to the Company's CEO. In addition, the Company's audit committee and board of directors approved payment of a bonus to the Chairman of the Company's board of directors, subject to the approval of the Company's general meeting.

For further information pertaining to the bonus, see the Company's immediate report of May 31, 2011 (Reference No.: 2011-01-169344), the information appearing therein being noted here by way of reference.

On July 11, 2011 and July 17, 2011, the Company's audit committee and board of directors resolved as follows:

To approve granting a loan from the Company to the CFO of the Company, or alternatively, for him to decide, providing Company guarantees for a loan that he can receive from a bank, all for the purpose of acquiring securities of the Company and/or of the Company's investees only.

For further information pertaining to the terms of the loan and/or guarantee, see the Company's immediate report of July 18, 2011 (Reference No.: 2011-01-215298), the information appearing therein being noted here by way of reference.

Standard 29A(4) Insurance and indemnity exemption for officers, valid at reporting date:

1. Pursuant to the previous resolutions of the Company, the Company granted senior officers an exemption regarding their liability for damages as a result of a breach of their fiduciary duty towards the Company, as set forth in the third section of the sixth part of the Companies Law and letters of indemnification (according to and subject to the amendment adopted at the Company's general meeting). The letter of indemnification complies with Amendment 3 of the Companies Law 5759-1999 and the Company's articles of association. Pursuant to the letter of indemnification, as the Company's articles of association include a provision allowing it to undertake in advance to indemnify an officer, provided the undertaking is restricted to the types of events that the board of directors anticipate in view of the Company's actual actions at the time of undertaking to indemnify, in an amount or scope determined by the board of directors to be reasonable under the circumstances, all on account of any liability or expenditure that shall be authorized at that time according to the law at the time the resolution is adopted, the company also undertakes to indemnify the officer for reasonable litigation expenses, including attorneys' fees, such that may be incurred as a result of an investigation or proceedings that shall take place against the officer by any authority certified to launch an investigation or proceeding and that has ended without filing charges against the officer and without a fine being imposed in lieu of criminal proceedings or that has ended without an indictment being filed against the officer, while imposing a fine in lieu of criminal proceedings in a felony that does not warrant the proof of criminal intent.
2. **Insurance:** On May 3, 2010 the Company's EGM adopted the following resolutions:
 - A. The engagement with Phoenix Insurance Co. Ltd. to insure the officers of the Company and its subsidiaries under a collective officers liability insurance policy for the Company and its subsidiaries as of December 1, 2009, with limit of liability of USD 75 million, at annual premium of USD 300,500, of which the Company's share amounts to USD 56,259 per annum. The Company may increase the limit of liability in the policy to a total of USD 100 million for additional annual premium in the amount of USD 55,625.
 - B. The Company's engagement with Phoenix and/or any other insurer in an officers liability insurance policy, under the terms fixed in the resolution, from time to time, without requiring

further approval of the general meeting, provided that the limit of liability of the insurance (in the collective policy) shall not be below USD 75 million and shall not exceed USD 100 million per event and per period and the annual premium will not exceed USD 450 per annum, with the addition of up to 15% per year.

- C. To approve the forgoing with regard to Mr. Elad Sharon (Teshuva), the son of the controlling shareholder, pursuant to the provisions of Regulation 1B(5) of the Relief Regulation.
- 3. Subsequent to the reporting period, Delek Group prepared a directors and officers liability insurance policy for its employees and for the majority of its subsidiaries, including the Company, for a period of one year from January 1, 2012 through December 31, 2012, with liability limit (in the collective policy) in an amount of USD 100 million per incident and for the period, and at a total premium (100%) of USD 340,000. The foregoing engagement will be brought for approval by the certified organs in the Company. The premium is at the generally accepted terms in the insurance market and based on the opinion of an external insurance consultant.

Delek Group Ltd.

Date: **Thursday, March 29, 2012**

Names and positions of the signatories:

Gabriel Last – Chairman of the Board of Directors

Asi Bartfeld - CEO

**Register of the Company's shareholders
as of March 21, 2012**

Name: Rivka Touitou	
Address: 7 Hahistadrut St., Givatayim	Balance held: 9
Name: Delek Agencies	
Address: 6 Prof. Kaufman St. Tel Aviv-Jaffa	Balance held: 3,068
Name: .OC GNIDLOH LAILIMAF	
Address: ELADSRACS ENAL TSEROF 02 38501 .Y.N A.S.U	Balance held: 35
Name: ANN FEINBERG	
Address: Nathan Levinson 1171 Naroili Driv Pacific Palisades 90292 U.S.A	Balance held: 36
Name: Anna & Eugene Goidell	
Address: Shelley Court Plainview N.Y. 11803 U.S.A 8	Balance held: 36
Name: Anna & Harry Kaplan	
Address: Rhawn ST. Philadelphia Pennsylvania 19152 U.S.A 2315	Balance held: 247
Name: ARNOLD GOLDMAN	
Address: Leeward lane Rochester.N.Y. 14618 U.S.A 8	Balance held: 41
Name: Brian Birenbaum	
Address: Joshua CT. Thornhill, Ontario Canada L4J 8B6 72	Balance held: 62
Name: CATHRINE RUDNER	
Address: WV 30062 Williamsburg #11, Wheeling, USA	Balance held: 498
Name: David & Barbara Frank	
Address: Jaystone Drive Silver Spring MD 20905 U.S.A 14624	Balance held: 60
Name: David Marcus	
Address: c/o Ada Marcus 1010/A Baywood Circle Chua Vista CA 91915 U.S.A	Balance held: 42
Name: David Ranan	
Address: 52 Montague Square, London WIH 1ER, England	Balance held: 76
Name: David Alan BARNETT	
Address: Represented by Aty. Avner Slater, Jerusalem East 9th Street, Brooklyn, NY 11230 1545	Balance held: 181
Name: Edoard & Meair Kasdan	
Address: U.S.A	Balance held: 7
Name: Frank Kurtz	
Address: Westwood Drive San Francisco CA 94112 U.S.A 112	Balance held: 240
Name: George & Ann Vollmer	
Address: Culview St. Culver city CA 90230 U.S.A 5913	Balance held: 96
Name: Goodless Brothers Electric	
Address: .POB 925 West Springfield MA 01090 U.S.A	Balance held: 181
Name: Louis Wittenberg	
Address: South Wood Drive, South Wood, Michigan 47252 U.S.A	Balance held: 21
Name: Henry & Joan Kaufman	

Address: 2581 30th Ave San Francisco California USA	Balance held: 18

Name: Henry Frenkel	
Address: 132 Valley Circle Fairfield CT 06825 USA	Balance held: 249

Name: HERBERT & ILSE ROSENBAUM	
Address: 1561 CHESTNUT ST SAN CARLOS CA 94070 U.S.A	Balance held: 16

Name: INVESTMENT GROUP CHARTER	
Address: 2112 ACACIA PARK SVIVE SUITE 619 LAGNDHURST 44124 U.S.A	Balance held: 2

Name: JACK & DOLORES GOOTKIN	
Address: HUSTON ST. SHERMAN OAKS CA 91423 U.S.A 13121	Balance held: 45

Name: JACK HABACHT	
Address: 11 RUSSEL AVE SOUTH RIVER NEW JERSEY 0882 U.S.A	Balance held: 45

Name: JEFFEREY ISRAEL	
Address: 3357 NW 1015T SUNRISE FLORIDA 33351 U.S.A	Balance held: 3

Name: JOSEF JANOWSKY	
Address: Pomander Walk 655 Apt 241 Teaneck NJ 07666-1671 U.S.A	Balance held: 124

Name: JOSEPH GOLDMAN	
Address: 1011 FILENOLMP ST PHILADELPHIA PENNSYLVANIA 15111 U.S.A	Balance held: 31

Name: LANSAL COMPANY	
Address: 111 BROADWAY NEW YORK N.Y 10006 U.S.A	Balance held: 3

Name: Gerta Goldhil	
Address: London	Balance held: 154

Name: Don Maxwell	
Address: 955 Capital Ave NE, Battee Creek, Michigan 71094 USA	Balance held: 317

Name: Louis Grossberg	
Address: SUITE 1300 5454 WISCONSIN AVE. CHEVY CHASE MD 20015 U.S.A	Balance held: 623

Name: Martin Koffman	
Address: 517 WHITTIER BLUD MONTEBELLO CA 90640 U.S.A	Balance held: 138

Name: Maurice & Sylvia Gross	
Address: S Dwrnago AVE Los Angeles California 90035 U.S.A 1481	Balance held: 35

Name: MICHAEL BIRENBAUM	
Address: Weston RD RR2, Kettleby, ON LOG 1J0 Ontario Canada 16141	Balance held: 62

Name: MICHAEL CLEIN	
Address: SW 142 CT. MIAMI FLORIDA 33186 U.S.A 9701	Balance held: 59

Name: David Birenbaum	
Address: Downsview 1110 Finch Ave. West Suite 007 Ont/N3J T2T Canada	Balance held: 39

Name: Shelly Birenbaum	
Address: Downsview 1110 Finch Ave. West Suite 007 Ont/N3J T2T Canada	Balance held: 74

Name: Murray Buxbaum	
Address: 3500 E FIRST ST. LOS ANGELES CALIFORNIA 90063 U.S.A	Balance held: 13

Name: Nahan Arthur	

Address: 6 NORTON ROAD EAST BRUAISWICK N.Y.08816 U.S.A	Balance held: 18

Name: Eduard & Malicia Weinstein	
Address: 0142B Louth Las Vegas 5032 Nevada 50198 USA	Balance held: 68

Name: Leo Martin	
Address: 62941 Barrington P.O.B. 94009 L.A. USA	Balance held: 181

Name: Eliezer & Phyllis Dowin	
Address: 1152 Batterhayes Dr. #203, Raleigh, North Carolina 51672 USA	Balance held: 66

Name: Margaret Ehern	
Address: 274 S. Brehl Avenue, Columbus, Ohio USA	Balance held: 249

Name: Oren Revka	
Address: P O BOX 1483 Roosevelt Park 2129 Johnnesburg, South Africa	Balance held: 163

Name: RAY APPLEBAUM	
Address: SW 57 COURT MIAMI FLORIDA 33156 U/S/A 11841	Balance held: 498

Name: Chaim Greenberger	
Address: 5064 19th Ave. Brooklyn NY 91211 USA	Balance held: 140

Name: ROBERT FURMAN	
Address: BLACKSTONE AVE. bronx DATE NEW YORK 10471 U.S.A 3935	Balance held: 36

Name: Dr. Rosow MICHAEL	
Address: 2910 Motor Ave. LOS ANGELES CALIFORNIA 90064 U.S.A	Balance held: 1,813

Name: SAM & MIRIAM WEINSTEIN	
Address: 305 North Palm Drive Beverly Hills, CA 90210 U.S.A	Balance held: 45

Name: Sam Wietschner	
Address: 857 EAST 9TH STREET BROOKLYN N.Y. 11230 U.S.A	Balance held: 90

Name: Samuel & Sylvia Lindenberg	
Address: 329 Old Lancaster Road Sudbury, MA 01776 U.S.A	Balance held: 102

Name: Charles Roth	
Address: 137 Arneil Dr. Chamarillo CA 31039 USA	Balance held: 123

Name: Pearl Moss	
Address: 542 Southfield Apt Dr. Berg 95562 43084 MN USA	Balance held: 21

Name: Syd Bassik	
Address: C/O MRS CLARA GARVIN 3442 CAMMAN PLACE BRONX N.Y. 10463 U.S.A	Balance held: 63

Name: William Combs	
Address: 44 VAN DYKE ST. THOUSAND OAKS CA 91360 U.S.A	Balance held: 54

Name: Maurice Lewinsky	
Address: 5241 Bridgeport Ave. Noble Connecticut 01660 USA	Balance held: 623

Name: Yod Investment Brandeis	
Address: 5600 Wisconsin AVE APT.19 B Chevy Chase MD 20815-4414 U.S.A	Balance held: 123

Name: Melvin & Mary McGuiry	
Address: 0311 W Porter Av., fullerton, CA 33629 USA	Balance held: 45

Name: Zeitchik Abe	
Address: 915 EAST 7 STREET BROOKLYN NEW-YORK 11230 U.S.A	Balance held: 28
Name: Wynne Frank Sitrin and Stuart A Frank	
Address: 7404 Pyle Road Bethesda, Maryland 20817 USA	Balance held: 60
Name: ARM-Nel Consulting And Trade Ltd., ARS-Nel Consulting and Trade	
Address: 2 Ben Gurion Ave. Ramat Gan	Balance held: 1
Name: Benjamin Abutboul	
Address: Tel Aviv	Balance Held: 1
Name: Avergel Yaakov	
Address: Tel Aviv	Balance held: 7
Name: Avraham Berman	
Address: 17 Yaelim St., Givat Zeev, Jerusalem	Balance held: 54
Name: Abramowitz Victor	
Address: 7/4 Shikun Rambam, Tirat Carmel, Haifa	Balance held: 16
Name: Onikowski (On) Yitzhak	
Address: 3 Moshe Barzani St., Tel Aviv 69123	Balance held: 6
Name: Okerant Mark	
Address: 21 Aharonowitz St., Kfar Saba, 44452	Balance held: 28
Name: Azulai Sarah	
Address: Mobile Post Tena Omerim Mt. Hebron 90408	Balance held: 271
Name: Ahiman Shmuel	
Address: St. 6 Shmeriyahu Levin St., Tel Aviv	Balance held: 10
Name: Izikowitz Yehoshua	
Address: St. 62 Haplugot St. Kiriyyat Haim	Balance held: 1
Name: Einhorn Erna	
Address: 5 Menachem Yitzhak St., Ramat Gan 52560	Balance held: 1
Name: Eldar Arale	
Address: 6 Haharuv St. Moshav Rishpon, 46915	Balance held: 1
Name: Assaf Rachel	
Address: 29 Stephan Weiz, Haifa, zip 35439	Balance held: 1
Name: Ephraim Salomon	
Address: 48B Shmuel Hanatziv St., Apt. 8, Netanya	Balance held: 157
Name: Arjee Victor	
Address: 153 Acco Ave. Kiriyyat Motzkin 26412	Balance held: 1
Name: Arie Jacobs	
Address: St. 72 Meir Nakar St., Jerusalem	Balance held: 35
Name: Arie Paz	
Address: 98 Netiv Chen, Haifa, 32682	Balance held: 2,147
Name: Ehrlich Shoshana	
Address: 7 Ibn Gvirol St., Rishon LeZion 75481	Balance held: 6

Name: Ashkenazi Amira	
Address: 52 Negba St., Givatayim	Balance held: 53
Name: Ashkenazi David	
Address: 11 Hatoren St., Ein Hayam, Haifa	Balance held: 1
Name: Ashkenazi Jule	
Address: 11 Hatoren St., Haifa	Balance held: 6
Name: Ashkenazi Yehoshua	
Address: 18 Habonim St., Rehovot 76204	Balance held: 2
Name: Ashkenazi Rachel	
Address: 35 Tabankin St. Tel Aviv-Jaffa	Balance held: 1
Name: Etiel Shador	
Address: Rachel Litchik Home for the Elderly, 5 Shabazi St., Beit Dagan, 50200	Balance held: 372
Name: Bobronski Yair	
Address: 74 Katzenelson St., Bat Yam 59505	Balance held: 2
Name: Bozechman Shlomo	
Address: 4 Nordau St., Haifa, 33122	Balance held: 5
Name: Boton Tereza	
Address: Tel Aviv	Balance held: 6
Name: Boker Ilana	
Address: 27 Reines St., Raanana, 43374	Balance held: 10
Name: Borstein Eli	
Address: St. 686/18 Zin St., Eilat	Balance held: 87
Name: Buchbut Ahuva	
Address: 13 Fichman St., Tel Aviv 69027	Balance held: 124
Name: Batat Haim	
Address: 13/4 Hahagana St., Kiriya At 28006	Balance held: 3
Name: Balita Hannah	
Address: 17 Tabankin St., Herzliya 46425	Balance held: 1
Name: Belnik Haim	
Address: 31 Bezalel St. Paz Tower, Ramat Gan	Balance held: 1
Name: Ben Haim Gavriel	
Address: Tel Aviv - Jaffa	Balance held: 4
Name: Benbenishty David	
Address: 29 Tamatev St., Holon 58923	Balance held: 1
Name: Barlev Yehuda	
Address: 3 A Tolkowski St., Tel Aviv – Jaffa 69352	Balance held: 11
Name: Bramaness Mendel	
Address: Tel Aviv - Jaffa	Balance held: 41
Name: Brenner Daniel	
Address: 4 Ein Gev St., Rishon LeZion 75481	Balance held: 1

Name: Guanshir Yitzhak	
Address: 9 Tnuat Hanoar St., Rishon LeZion	Balance held: 75
Name: Gottfried Shalom	
Address: St. 17 Hannah St., Haifa	Balance held: 2
Name: Goldway Rina	
Address: 5 Giplich St., Ramat Hasharon, 47261	Balance held: 1
Name: Gordon Yehudit	
Address: 11 Rashi St., Ramat Gan 52560	Balance held: 31
Name: Gazit Zipora	
Address: Tel Aviv - Jaffa	Balance held: 5
Name: Grinberg Henrietta	
Address: 10/1 Hannah Senesh St., Azur 58010	Balance held: 4
Name: Grinberg Mordechai	
Address: St. 6 Shabo St., Givat Hasharon, Hod Hasharon	Balance held: 1
Name: Duvdevani Shimon	
Address: 7 D'Israel St., Haifa, 34333	Balance held: 609
Name: Dainowski Arie	
Address: St. 62 Shamir St., Jerusalem, 93891	Balance held: 80
Name: Dalia Gavriel	
Address: 4 Nili St., Gan Yavneh, 7008 - P.O.B. 1249	Balance held: 98
Name: Danziger Yoram	
Address: 47 Jerusalem Ave, Ramat Gan, 52371	Balance held: 40
Name: Danziger Max	
Address: 47 Jerusalem Ave, Ramat Gan, 52371	Balance held: 96
Name: Dassa Geula	
Address: 13/5 Uri Bar On. P.O.B 12121, Ariel 44837	Balance held: 1
Name: Dekel Ben Zion	
Address: Office: 7 Giborei Israel St., Netanya	Balance held: 6
Name: Hoffman Varda	
Address: 5 Hasadot Ave. Kfar Shmariyahu 46910	Balance held: 3
Name: Harel Shai	
Address: 242 Ben Yehuda St., Tel Aviv – Jaffa	Balance held: 5
Name: Herzberg David	
Address: 23 Hahermon St., Haifa	Balance held: 3
Name: Videnfeld Avraham	
Address: Tel Aviv - Jaffa	Balance held: 4
Name: Weiss Chayah	
Address: 1 Borohov St., Tel Aviv - Jaffa	Balance held: 4
Name: Victor Refael Baruch	
Address: Tel Aviv - Jaffa	Balance held: 15

Name: Varshaviak Elimelech	
Address: 1 Zidkiyahu St., Beer Sheva	Balance held: 7
Name: Zaltzman Arie	
Address: Tel Aviv - Jaffa	Balance held: 1
Name: Zamir Vardina	
Address: 18 Zichron Yaakov St., Tel Aviv - Jaffa	Balance held: 1
Name: Zarzar Yosef for Shulamit Zarzar	
Address: 14 Mechalkei Hamaim St., Jerusalem, 93222	Balance held: 48
Name: Discount Bank Registrations Ltd.	
Address: 38 Yehuda Halevi St. Tel Aviv-Jaffa	Balance held: 11,698,062
Name: Taub Hanoach	
Address: Tel Aviv - Jaffa	Balance held: 6
Name: Yehuda Ben Dov	
Address: Kibbutz Moran, Mobile Post Lower Galilee	Balance held: 34
Name: Yona Cohen	
Address: St. 25 Rachel St., Har Hacarmel, Haifa 34402	Balance held: 395
Name: Jonathan Goldsmidt	
Address: 8 Nili St., Holon 58279	Balance held: 12
Name: Yehimowitz Sarah	
Address: 342 Haim Grinberg St., Jerusalem, 62488	Balance held: 11
Name: Avraham Cohen	
Address: Haifa	Balance held: 1
Name: Haim Cohen	
Address: 47 Weizmann St., Tel Aviv – Jaffa 64230	Balance held: 682
Name: Meira Cohen (Yanai)	
Address: 29C Herzog St., Givatayim, 53602	Balance held: 3
Name: Kanafo Rivka	
Address: 15 A Bezalel St., Jerusalem	Balance held: 10
Name: Leumi Research Partners Ltd.	
Address: Azrieli Center (Square Tower), 36th Floor, Tel Aviv 67025	Balance held: 1
Name: Livnat Raz	
Address: 23 Harimon St., Givat Savyon,	Balance held: 1
Name: Levy Eliyahu	
Address: 46 Elkrawitz St., Jerusalem	Balance held: 1
Name: Levy Haim	
Address: 56 Hatizmoret St., Rishon LeZion	Balance held: 76
Name: Levy Tov Aharon	
Address: St. 16 Harel St., Haifa, 34555	Balance held: 51
Name: Levy Nissim	
Address: Haifa	Balance held: 1

Name: Levy Shalom Haim Tova	
Address: 52 Baro St., Tel Aviv - Jaffa	Balance held: 1
Name: Lily Yosefan	
Address: Heiress 5/72 of the late Cohen Cadouri	Balance held: 10
Name: Lipschitz Avraham	
Address: 57 Nahmani St., Tel Aviv - Jaffa	Balance held: 2
Name: Lipschitz Matilda	
Address: 1 A Remez St., Kiriyat Ata 00082	Balance held: 6
Name: Lamashkia Goldman	
Address: 82 Yavneh St., Tel Aviv - Jaffa	Balance held: 1
Name: Landsburg Bella	
Address: 11 Michal St., Tel Aviv - Jaffa63261	Balance held: 69
Name: Meiri Sarah	
Address: 3 Wolfson St., Petach Tikvah 49541	Balance held: 285
Name: Moses Robert	
Address: 20 Mendel Singer St., Apt. 36, Haifa zip 34984	Balance held: 1
Name: Morano Avraham	
Address: 19 Harduf St., Atlit, 30300	Balance held: 12
Name: Michalman Daniel	
Address: St. 33C Yitzhak Sade St., Bat Yam, 59563	Balance held: 3
Name: Miron Amnon	
Address: Ramat Hasharon	Balance held: 55
Name: Melamed Miriam	
Address: 12 Trachtenberg St., Rishon LeZion	Balance held: 1
Name: Malchi Shoshana	
Address: Petach Tikvah	Balance held: 12
Name: the late Manuelewitz Haim c/o Leah Nehama	
Address: St. 6/7 Moshe Kol St., Jerusalem, 93715	Balance held: 218
Name: the late Margalit Ephraim c/o Shoshana Margalit	
Address: 11 Hahagana St., Beit Golden Hill, Jerusalem 97851	Balance held: 30
Name: Mordechai Ben Dov	
Address: 7 Lobman St., Rishon LeZion 75315	Balance held: 35
Name: Maron Idit	
Address: Valley Lane, Savyon 43565	Balance held: 4
Name: Marmelstein Miriam	
Address: St. 7 Amdan St., Tel Aviv - Jaffa62741	Balance held: 38
Name: Marcel Mizrachi	
Address: Heiress 4/72 of the late Cohen Cadouri	Balance held: 8
Name: Moshe Cohen	
Address: Heiress 10/72 of the late Cohen Cadouri	Balance held: 20

Name: Nagi Moshe Geva	
Address: 8 Magadim St., Ramat Gan	Balance held: 2
Name: Noiman Dov	
Address: 6 Ahuzat Beit St., Tel Aviv - Jaffa	Balance held: 1
Name: Noiman David	
Address: 31 Ibn Gvirol St., Jerusalem	Balance held: 1
Name: Savyon Tal	
Address: 44 Geulim St., Zichron Yaakov 30900	Balance held: 55
Name: Sourasky Philip	
Address: 10 Jabotinsky St., Haifa, 35702	Balance held: 3
Name: Saviyoni Vivien	
Address: St. 3 Tchernichowsky St., Beer Sheva	Balance held: 2
Name: Sides Ita	
Address: 203 Bnei Ephraim St., Maoz Aviv, Tel Aviv – Jaffa 69984	Balance held: 25
Name: Silverman Shulamit	
Address: 58 Habiluim St., Ramat Gan, 52297	Balance held: 42
Name: Agiva Eliyahu	
Address: 32 Katznelson St., Bay Yam, zip 59633	Balance held: 164
Name: Ozeri Moshe	
Address: 17 Tor Malka St., Tel Aviv – Jaffa 67310	Balance held: 2
Name: Azar Lydia	
Address: No. 33 Moshav Gan Hadarom, Gan Hadarom 79255	Balance held: 308
Name: Irit Freund	
Address: 9 Zukei Yam St., Havazelet Hasharon, 42937	Balance held: 59
Name: Anavi Yitzhak	
Address: 12 Bouer St., Tel Aviv – Jaffa 62741	Balance held: 38
Name: Potshovotzki Sarah	
Address: 71 Wingate St., Herzliya 46752	Balance held: 470
Name: Fortzenell Pnina	
Address: 392/15 St., Tel Aviv - Jaffa	Balance held: 11
Name: the late Fetigro Mary c/o Aty. Mashiach Yitzhak	
Address: 16 Yehuda Halevi St., Tel Aviv – Jaffa 65781	Balance held: 10
Name: Pico Benadet	
Address: 607/16 Maalot Moriah, Jerusalem, 93780	Balance held: 1
Name: Peters Arie	
Address: 9 Hanassi St., Kiryat Ono	Balance held: 31
Name: Fishel Shlomo	
Address: P.O.B 9937, Ramat Gan, 52199	Balance held: 1
Name: Plessner Yehuda	
Address: 132 Ben Gurion St., Ramat Gan	Balance held: 28

Name: Fentzer Natan	
Address: POB 4, Haifa 31000. 4241 Haifa, 31042	Balance held: 20
Name: Fredkin Avraham	
Address: 21/14 Grunner St., Ramat Aviv, Tel Aviv – Jaffa 69498	Balance held: 653
Name: Farchi Yehuda	
Address: 3 Sheinkin St., Apt. 16, Givatayim 53100	Balance held: 187
Name: Partok Yosef or Partok Haim	
Address: St. 16 Barez Zeev st., Petach Tikvah 49737	Balance held: 2,295
Name: Friedman Yoav Attorney	
Address: 72 Ehad Ha'am St., Tel Aviv	Balance held: 5
Name: Parsol Yaakov	
Address: 26 Lamerchav St., Ramat Hasharon, 47216	Balance held: 7
Name: the late Chizawski Israel c/o Kira Rachel	
Address: 17 Aharon Karon St., Rishon LeZion 75262	Balance held: 7
Name: Zoiderer Zvi	
Address: 27/2 Hamaalot St., Givatayim	Balance held: 1
Name: Zror Shimon	
Address: 2 Hagefen St., Nof Yam, Herzliya 46665	Balance held: 238
Name: Chernik Pnina	
Address: Afek Home for the Elderly, Ramat Gan	Balance held: 9
Name: Kaufman Ben-Zion	
Address: 6 Lilianblum St., Tel Aviv - Jaffa	Balance held: 3
Name: Kadosh Rika (c/o Vivian Siboni)	
Address: St. 10/3 Tchernichowsky St., Beer Sheva	Balance held: 4
Name: Konfino Yosef	
Address: 2 Wisotsky St., Tel Aviv – Jaffa 62502	Balance held: 569
Name: Kotch Ilan	
Address: 56 Oshiskin St., Tel Aviv - Jaffa	Balance held: 18
Name: Kalman Frida Gurt Chaya	
Address: 5 Fishman - Meimon St., Tel Aviv – Jaffa	Balance held: 1
Name: Kalendroff Avraham	
Address: 40 Moshe Dayan St., Ramat Gan 52294	Balance held: 1
Name: Kimchi Zamir	
Address: Bnei Brak, Tel Aviv - Jaffa	Balance held: 9
Name: Kardosh Maklashona	
Address: 40 Hillel Yaffe st., c/o Kaposh, Herzliya 46321	Balance held: 544
Name: Karni Shlomo	
Address: 78 Hakishon St., Tel Aviv - Jaffa	Balance held: 1
Name: Karniel Regina	
Address: Tel Aviv - Jaffa	Balance held: 27

Name: Krasner Matitihu	
Address: Ramat Gan	Balance held: 2
Name: Reuveni Eli	
Address: 23 Uziel St., Bay Yam, zip 59463	Balance held: 146
Name: Ruti Salomon	
Address: Heiress 5/72 of the late Cohen Cadouri	Balance held: 10
Name: Raz Yehoshua	
Address: 1 Haim Hazaz St., Haifa, 69943	Balance held: 19
Name: Reizel Bella	
Address: Ramat Gan	Balance held: 1
Name: Ramon Miriam and Yohanan	
Address: 12 Zamerot St., Apt. 181, Herzliya 46424	Balance held: 700
Name: Shimmel Binyamin	
Address: 52 Negba St., Ramat Gan	Balance held: 47
Name: Shechter Pinchas	
Address: 5 Narkis St., Omer	Balance held: 1
Name: Schlossberg (c/o Dan Shelber)	
Address: St. 30 Shai Agnon St., Tel Aviv	Balance held: 25
Name: Shamai Haim	
Address: 11 Borochoy St., Givatayim	Balance held: 1
Name: Shenbal Varda	
Address: Haifa	Balance held: 28
Name: Schneidman Rivka	
Address: 13 Sharey St., Ramat Gan	Balance held: 12
Name: Schnivitz Gizella and Shani Adam	
Address: 47 Nordau St., Tel Aviv - Jaffa	Balance held: 1
Name: Sapak Meir	
Address: 39 Soroka Street, Haifa	Balance held: 164
Name: Schkolnik Sarah	
Address: 21 Gadud Machmash, Apt 9, Pisgat Zeev, Jerusalem	Balance held: 1
Name: Tachbura - Central Agricultural Services Cooperative Society	
Address: 17 Aminadav St., Tel Aviv – Jaffa 67067	Balance held: 289
Total Delek Group issued shares	11,723,669

Chapter E



Annual report for 2011 on the Effectiveness of Internal Controls for Financial Reporting and Disclosure



Delek Group



Delek Group Ltd
Annual report on the effectiveness of internal control for financial reporting and disclosure, pursuant to Ordinance 9B(a) of the Securities Ordinances (Periodic and Immediate Reports), 1970

Management, under the supervision of the Board of Directors of Delek Group Ltd. ("the Corporation"), is responsible for setting and maintaining an appropriate internal control for financial reporting and disclosure in the Corporation.

For this matter, the members of Management are:

1. Asi Bartfeld, CEO
2. Barak Mashraki, CFO
3. Leora Pratt Levin, Chief General Counsel
4. Tamar Rosenberg, Controller
5. Amit Kornhauser, Controller

Internal control of financial reporting and disclosure includes controls and procedures existing in the Corporation, which were planned or overseen by the CEO and the most senior financial officer or under their supervision, or by whoever fulfills those functions in practice, under the supervision of the Board of Directors of the Corporation, and were designed to provide a reasonable measure of assurance as to the reliability of the financial reporting and the preparation of the reports in accordance with the provisions of the law, and to ensure that information that the Corporation is required to disclose in the reports it publishes in accordance with the provisions of the law is collected, processed, summarized and reported on the date and in the format laid down in law.

Internal control includes, inter alia, controls and procedures planned to ensure that the information that the Corporation is required to disclose as aforesaid, is accumulated and forwarded to the management of the Corporation, including to the CEO and the most senior financial officer or to whoever fulfills those functions in practice, in order to enable decisions to be made at the appropriate time in relation to the disclosure requirement.

Due to its structural limitations, the internal control of financial reporting and disclosure is not intended to provide absolute assurance that misstatement in or omission of information from the reports will be prevented or will be discovered.

Management, under the supervision of the Board of Directors, has carried out checks and an assessment of the internal controls on financial reporting and disclosures within the Corporation and their effectiveness. The evaluation of the effectiveness of internal controls on the financial reporting and disclosure that management carried out under the supervision of the Board of Directors included an assessment of the risks associated with reporting and disclosure and a determination of which processes are particularly material for the financial reporting and disclosure and which are the applicable business units for assessment of the effectiveness of the internal controls, mapping and documenting existing controls within the Corporation, assessment of the effectiveness of the planning of the controls, an analysis of existing control differences, an assessment of the effectiveness of carrying out the controls, an overall assessment of the effectiveness of the internal controls. The assessment model for the effectiveness of the internal controls carried out by the company is based upon four components as follows: Entity Level Controls, the process of preparing and closing the financial statements, general controls of the IT systems (ITGC), and processes that have been identified by management as particularly material procedures for financial reporting and disclosure: Procedure for management of Company's cash and securities portfolio, and procedure for managing the Company's borrowings. The procedures that are particularly material in the consolidated financial statements that are prepared by some of the important consolidated companies are: revenues cycle, purchasing and inventory cycles, insurance reserves and pending claims and financial investments of insurance companies.

The Phoenix Insurance Company Ltd. (Phoenix Insurance), a subsidiary of the Corporation, is an institutional body, which is subject to the rulings of the Commissioner for the Capital Market, Insurance and Savings at the Treasury, in respect of an assessment of the effectiveness of the internal controls on financial reporting.

In respect of Phoenix Insurance, the management of Phoenix Investments, under the supervision of the Board, carried out a check and assessment of the internal controls on the financial reporting and its effectiveness, based upon the provisions of Institutional Bodies Circular 2010-9-6, "Responsibility of Management for Internal Controls on Financial Reporting", in respect of which the said check and assessment of the internal controls on the financial reporting and their effectiveness do not in 2011 deal with life insurance procedures, health insurance procedures, handled by the life insurance systems, and the pension fund procedures (excluding the investments process), as detailed in the aforementioned circular.

Based upon this assessment, the Board of Directors and management of Phoenix Investments reached the conclusion that the internal controls on financial reporting, in respect of Internal Controls in an Institutional Body as of December 31, 2011, was effective.

Concerning the internal control components in respect of the Lion Oil Company ("Lion"), of which on April 29, 2011 Delek USA completed the acquisition of 53.7% of its shares and accordingly Delek USA commenced consolidating Lion's results. It should be pointed out that Lion is at an advanced stage of planning and designing its internal controls, formulation and adoption of working procedures. However, at this point, it is not possible to complete the assessment of the effectiveness of Lion's internal controls.

The assets net of liabilities of Lion as of December 31, 2011 came to NIS 824 million and the net income of Lion for the period commencing April 29, 2011 and ending December 31, 2011 came to NIS 56 million.

Based upon the assessment of effectiveness carried out by management under the supervision of the Board as detailed above, the Corporation's Board of Directors and management reached the conclusion that the internal controls on financial reporting and disclosures of the Corporation as of December 31, 2011 were effective.

Declaration of Executives:

(1) Declaration of the CEO in accordance with Ordinance 9B(d)(1)

**Declaration of Executives
Declaration of the CEO**

I, Asi Bartfeld, declare that:

1. I have reviewed the periodic report of Delek Group Ltd. ("the Corporation") for the year 2011 ("the Reports").
2. To the best of my knowledge, the reports do not include any representations that are not correct and do not lack any representation of any vital, material fact, so that what has been presented, within the context in which they have been provided, shall not be misleading in respect of the period covered by the reports.
3. To the best of my knowledge, the financial statements and other financial information in the Reports reflect fairly, from all material aspects, the financial condition, the results of operations and the cash flows of the Corporation at the dates and for the periods to which the Reports relate.
4. I disclosed to the auditor of the Corporation, to the Board of Directors, to the Audit and the Financial Statements Committees of the Board of Directors of the Corporation, based on my latest assessment of the internal control of the financial reporting and disclosure:
 1. all the significant flaws and material weaknesses in the determination or operation of the internal control of the financial reporting and disclosure that could reasonably have an adverse effect on the ability of the Corporation to collect, process, summarize or report on financial information in a way that could cast doubt on the reliability of the financial reporting and the preparation of the financial statements in accordance with the provisions of the law; and -
 2. any deception, whether material or not material, in which the CEO or anyone directly subordinate to him is involved, or in which other employees are involved who fulfill an important function in the internal control of the financial reporting and disclosure;
5. I, alone or together with others in the Corporation:
 1. I set controls and procedures or ascertained the setting and upholding of controls and procedures under my supervision, designed to ensure the

material information related to the Corporation, including its consolidated companies in their meaning in the Securities (Annual Financial Statements) Ordinances, 2010. was brought to my attention by others within the Corporation or the consolidated companies, in particular during the period in which the reports were prepared; and -

2. I set controls and procedures or ascertained the setting and upholding of controls and procedures under my supervision, designed to reasonably ensure the reliability of the financial reporting and the preparation of the financial statements in accordance with the provisions of the law, including in accordance with accepted accounting principles;
3. I have assessed the effectiveness of the internal controls of the financial reporting and disclosures, and in this report have presented the conclusions of the Board of Directors and Management in respect of the effectiveness of the said internal controls as the reporting date.

Nothing in the foregoing shall derogate from my responsibility or that of anyone else in law.

Asi Bartfeld

March 29, 2012
Chief Executive Officer

(2) Declaration of the most senior financial officer pursuant to Ordinance 9B(d)(2)

Declaration of Executives

Declaration of the most senior financial officer

I, Barak Mashraki, declare that:

1. I have reviewed the financial statements and other financial information of Delek Group Ltd. ("the Corporation") for the year 2011 ("the Reports").
2. To the best of my knowledge, the financial statements and other financial information do not include any representations that is not correct and do not lack any representation of any vital, material fact, so that what has been presented, within the context in which they have been provided, shall not be misleading in respect of the period covered by the reports.
3. To the best of my knowledge, the financial statements and other financial information in the Reports reflect fairly, from all material aspects, the financial condition, the results of operations and the cash flows of the Corporation at the dates and for the periods to which the Reports relate.
4. I disclosed to the auditor of the Corporation, to the Board of Directors, to the Audit and the Financial Statements Committees of the Board of Directors of the Corporation, based on my latest assessment of the internal control of the financial reporting and disclosure:
 1. all the significant flaws and material weaknesses in the determination or operation of the internal control of the financial reporting and disclosure insofar as they refer to the financial statements and other financial information that could reasonably have an adverse effect on the ability of the Corporation to collect, process, summarize or report on financial information in a way that could cast doubt on the reliability of the financial reporting and the preparation of the financial statements in accordance with the provisions of the law; and -
 2. any deception, whether material or not material, in which the CEO or anyone directly subordinate to him is involved, or in which other employees are involved who fulfill an important function in the internal control of the financial reporting and disclosure;
5. I, alone or together with others in the Corporation:
 1. I set controls and procedures or ascertained the setting and upholding of controls and procedures under my supervision, designed to ensure that

material information relating to the Corporation, including its subsidiaries as defined in the Securities (Annual Financial Statements) Ordinances, 2010, insofar as they are relevant to the financial statements and other financial information included in the reports, is brought to my knowledge by others in the Corporation and in the subsidiaries, particularly during the period of preparation of the Reports; and

2. I set controls and procedures or ascertained the setting and upholding of controls and procedures under our supervision, designed to reasonably ensure the reliability of the financial reporting and the preparation of the financial statements in accordance with the provisions of the law, including in accordance with accepted accounting principles;
3. I have assessed the effectiveness of the internal controls of the financial reporting and disclosures, insofar as it is applicable to the financial statements and other financial information included in the reports as of the reporting date. My conclusions concerning my assessment have been brought to the attention of the Board of Directors and management and have been included in this report.

Nothing in the foregoing shall derogate from my responsibility or that of anyone else in law.

Barak Mashraki

March 29, 2012
CFO