The Israel Corporation Limited

Financial Statements
As at September 30, 2003
(Unaudited)

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Contents

Directors' Report to the Shareholders of Israel Corporation Ltd.

For the Nine Months Ended September 30, 2003

DESCRIPTION OF THE CORPORATION AND ITS BUSINESS ENVIRONMENT

The Israel Corporation Ltd. (hereinafter – the Corporation) is an investment company engaged in the initiation, promotion and development of businesses in Israel and abroad, and is actively engaged in management of its Group companies.

The Corporation is held 60% by the Ofer Group, and 20% by Bank Leumi Le-Israel B.M. In February 2003, the holdings structure was changed by the various parties in the Ofer Brothers Group (see section Events Occurring During the Period of the Report and Thereafter).

The Corporation's strategy is designed to adapt its business structure to the business reality in Israel and globally, while expanding the Group's geographic dispersion and international market penetration with respect to manufacturing and marketing.

In the recent period and especially following the events of September 11, 2001, and the worldwide economic slowdown, the Group has been making efforts to reduce expenses and bring about cost savings in the framework of extensive efficiency plans that were implemented by the Group companies prior to the slowdown, and the results of these efforts are reflected in their operating results. In addition, the Group has been taking steps to improve the cash flows of the companies.

The Group's activities are centered, mainly, in the chemicals, shipping, energy, advanced technology and communications sectors, through an array of investee companies. The Corporation's headquarters provides management services, through a wholly-owned subsidiary, and is also actively involved in the strategic planning and business development of the investee companies.

CHANGES IN THE INVESTMENT PORTFOLIO

A. Tower Semiconductor Ltd. (hereinafter – Tower)

(1) In February 2003, Tower, Israel Corporation Technologies (I.C. Tech) Ltd. (hereinafter – "I.C. Tech"), the primary Wafer partners, and an additional partner in Tower (hereinafter – "the Investors") consented to amend their agreements with Tower, in connection with the payment on account of the fifth milestone, in the amount of $41.0 million. In accordance with this amendment, the condition of reaching the milestone was removed, as were the other directives which Tower did not meet.
Pursuant to the amendment, upon receipt of the required approvals, the Investors will invest $24.6 million in Tower's capital ($4.4 million of which by I.C. Tech). The balance of the payment, in the amount of $16.4 million, is to be invested in Tower's capital, subject to an additional fundraising by Tower, in the amount of $26 million, no later than December 31, 2003 ($2.9 million of which by I.C. Tech).
In exchange for the initial investment, in the amount of $24.6 million (hereinafter – "the First Installment"), the Investors will receive ordinary shares of Tower based on a price of $3 per share (which constitutes the average price of Tower's shares in the 30 trading days prior to the decision of Tower's Board of Directors to amend the investment agreement). Regarding the balance of the payment, in the amount of $16.4 million (hereinafter – "the Second Installment "), the Investors will receive ordinary shares of Tower according to a price per share which is based on the share price at which Tower raises the additional amount of $26 million.

In addition, the primary Wafer partners were granted an option to convert, during January 2006, an amount of up to $13.2 million out of the amounts recorded as unutilized long-term customers' advances, to ordinary shares of Tower at a price which is based on the average trading price of Tower's shares in the 15 trading days prior to December 31, 2005. The amendment was subject to certain approvals, mainly of the banks – which was received subsequent to the balance sheet date (as stated in Section (4)).

(2) During the period of the report, further to the consent of the banks to provide Tower with interim financing in the amount of $67 million, the Investors transferred the amount of $15.9 million on account of the First Installment ($2.9 million of which by I.C. Tech).
As a result of the investment, I.C. Tech's share in Tower declined from 28.5% to 27.3%. The capital loss realized by the Group, in the amount NIS 7 million, was recognized by the Corporation in its financial statements for 2002.

(3) Subsequent to the balance sheet date, Tower, I.C. Tech, and the Investors agreed to amend their agreements with Tower and to invest the balance of the payment in respect of the fifth milestone, in the amount $25.1 million, with no contingency on raising of the additional funds by Tower, as stated in Section (1).
In consideration of the balance of the amount for the First Installment, totalling $8.7 million, Tower is to issue shares to I.C. Tech and the Investors based on a share price of $3 per share, and in consideration for the Second Installment, totalling $16.4 million, Tower is to issue shares based on a share price which is based on the price in the next issuance which Tower shall execute or the average trading prices of Tower's shares, if an issuance is not executed in the period determined.
The amendment is subject to additional approvals including, among others, of the General Meeting of Tower's shareholders.

The primary Wafer partners agreed to postpone use of the amounts recorded as long-term customer's advances, to which they are entitled in respect of their purchases in the years 2004–2006 and, in exchange, they were granted an option to convert any amount which may be used out of the advances in every quarter in these years to shares of Tower based on the average trading price of Tower's shares on the stock exchange on those dates. Alternatively, amounts not converted to shares as stated above, will be paid by Tower on December 31, 2007. Such amounts will bear interest of Libor + 2.5% which is to be paid on a current basis.

(4) Subsequent to the balance sheet date, Tower reached an agreement with the banks regarding amendment of its credit facility agreements for the financing of FAB2. In the framework of the amendment, the Israel Corporation gave the banks a letter of commitment as part of the arrangements required by them for the granting of safety net by the main shareholders of Tower as a condition for the continued provision of financing by the banks to Tower.

1. In the letter of commitment it was provided that the security to be provided by the Israel Corporation relates to Tower's obligation to raise additional funds, in the amount of $152 million, by December 31, 2005 (in accordance with the dates and conditions as stated in the credit agreement (hereinafter – "the Additional Capital").

2. Pursuant to the letter of commitment, the banks are permitted, under certain conditions, to require Tower to issue a prospectus to its shareholders through an issuance of rights to acquire debentures convertible in shares of Tower as well as the issuance of options for the acquisition of Tower shares, all of this on the conditions provided in the letter of commitment. The amount of the issuance shall not exceed the amount which Tower did not succeed in raising in accordance with its obligation to the banks up to that time.

   Should Tower not be successful in issuing a prospectus on the required dates, the Corporation shall invest in Tower by means of a private offering of convertible debentures on the same terms as they would have been included in a public issuance.

3. The total amount of the Corporation's liability to invest in Tower pursuant to the letter of commitment, shall not exceed $50 million. The letter of commitment provides, that the investments of certain main shareholders in Tower, if made, shall be considered as fulfillment of the Corporation's liability under the letter of commitment (as detailed in the letter of commitment).
The Corporation's liability under the letter of commitment is given against the liability of the banks to provide, concurrent with execution of an investment by the Corporation, additional financing to Tower, in the amount of $43 million (in addition to credit of $500 million as provided in the credit agreement). The letter of commitment states that the banks will provide the financing as stated, in proportion to the amounts which the Corporation and certain shareholders provide, such that against every $50 provided by the Corporation and those shareholders, the banks will provide additional credit to Tower of $43.
In any event, the Corporation is not required to invest more than 50/93 of the amount which is to be raised at that time (including its share in respect of exercise of its rights as a shareholder).

4. The letter of commitment states, subject to the conditions therein, that certain amounts which the Corporation chooses to invest in Tower, whether through a public issuance or a private offering, even if the bank does not exercise its right to realize the security, shall be taken into account regarding the total amount of its liability under the letter of commitment, and this investment shall be considered as part of the Additional Capital.

5. The letter of commitment shall expire on the earlier of the following dates: (a) completion of the raising of $152 million by Tower as additional capital, as defined in Tower's credit agreement; (b) June 30, 2006; or (c) the date on which the Corporation (and the main shareholders in Tower) invests $50 million pursuant to the terms of the safety net.

6. Tower's credit agreement with the banks includes, among other things, a condition according to which the sale of Tower shares in excess of amounts determined in the agreement will convey to the banks the right to call the credit granted to Tower for immediate repayment. The said condition includes the gradual reduction over the years of the amount of shares the sale of which is limited. In any event, this limitation will not include Tower securities acquired by the Corporation or Group companies after the signing of the letter of commitment.

7. Tower agreed to indemnify the Corporation in the amount of up to $100 million, for expenses and damages stemming from claims caused to the Corporation as a result of its commitment to the banks to provide the safety net.

(5) Tower requested that the Investments Center approve the updated plan for construction of FAB2, in light of the fact that the period for the investments in FAB2 will be extended for more than 5 years from the date of receipt of the original approval from the Investments Center.
Tower's Management estimates that a satisfactory arrangement will be reached with the Investments Center.

(6) On November 14, 2003, Tower submitted a prospectus to the U.S. Securities and Exchange Commission for purposes of a public offering of ordinary shares. Tower is offering to the public 12 million ordinary shares and it granted the underwriters in the issuance an option for a period of 30 days to acquire an additional 1.8 million ordinary shares, at the price determined in the issuance, for purposes of covering excess orders, if any.
After the issuance, if it is executed, the Group's share in Tower will decline from 27.3% to 21.3%.

B. In the first quarter of the period of the report, Kol 1 Investments in Communications (H.L.) Ltd. (hereinafter – "Kol 1") sold its entire holdings (40%) in RSL Com Finland OY, in exchange for €14 million (of which €3.2 million is a repayment of shareholders' loans). Kol 1 realized a net, after-tax gain of roughly NIS 46.2 million.

C. In the third quarter of the period of the report, the I.C. Tech invested $1.5 million in Oren Semiconductors Inc. (hereinafter – "Oren"). In addition, the Corporation converted a shareholders' loan, in the amount of $2.5 million, into shares of Oren. As a result of the investment and conversion of the loan, the Group's share in Oren's shareholders' equity increased from 17.7% to 23.5% and an excess of cost over book value was created, in the amount of $2.7 million, which was allocated to intangible assets. Up to the time of the increase in the rate of holdings, the investment in Oren was presented based on the cost method of accounting, whereas commencing with the third quarter of the period of the report, the investment is presented based on the equity method of accounting.

D. During the period of the report, the Corporation transferred the amount of $6.5 million to PSINet Europe B.V. (hereinafter – "PSINet"), as a shareholders' loan.

E. Subsequent to the balance sheet date, Sorbie Holding Ltd. (hereinafter - "Sorbie") and PSINet, affiliated companies of the Corporation (hereinafter - "the Companies"), entered into an agreement with other shareholders in the Companies (hereinafter - "the Partner"), pursuant to which Sorbie acquired its shares from the partners. In addition, the partners transferred to the Corporation and the other shareholders in PSINet, their shares in PSINet. In exchange, the partners received two subsidiaries of the Companies. As a result of the transaction, the rate of the Corporation's share in Sorbie and PSINet increased to 61.4%.

F. Regarding exercise of the option for sale of Oil Refineries Ltd., see "Effect of External and Other Factors".

FINANCIAL POSITION

The total assets, as at September 30, 2003, amounted to NIS 15,507 million, compared with NIS 16,868 million, as at September 30, 2002.

The balance of long-term investments, loans and receivables as at September 30, 2003 amounted to NIS 1,548 million, compared with NIS 1,765 million as at September 30, 2002.

The Corporation's shareholders' equity as at September 30, 2003 amounted to NIS 2,077 million, compared with NIS 1,999 million as at December 31, 2002.

The Corporation's working capital as at September 30, 2003 amounted to NIS 495 million, compared with negative working capital of NIS 43 million as at December 31, 2002.

The cash flows generated by operating activities in the current period amounted to NIS 1,636 million compared with NIS 1,347 million in the corresponding period of last year.

SOURCES OF FINANCING OF THE CORPORATION AND THE HEADQUARTERS COMPANIES

As at September 30, 2003, the total financial liabilities of the Corporation and its wholly-owned and controlled headquarters companies (hereinafter – "the Headquarters Companies"), amounted to NIS 2,264 million.

As at September 30, 2003, the Corporation and the Headquarters Companies had investments in liquid assets of NIS 707 million, invested, primarily, in CPI-linked and shekel Treasury Bills and medium-term dollar debentures.

In the current period, the Corporation and the Headquarters Companies repaid current maturities of long-term loans in the amount of NIS 321 million (including NIS 56 million which were scheduled to be repaid up to December 2004).

In the current period covered by the report, one of the Headquarters Companies renewed a long-term loan in the amount of $32.5 million, which is repayable in one lump-sum in 2008.

In the current period covered by the report, one of the Headquarters Companies sold NIS 3 million par value debentures which are convertible into shares of the Corporation for a consideration of NIS 3 million.

RESULTS OF OPERATIONS

The Corporation ended the period of the report with earnings of NIS 251 million, compared with a loss of NIS 85 million in the corresponding period last year.

Set forth below are the factors which impacted the results of operations in the period of the report:

A. Israel Chemicals Ltd. (hereinafter – "ICL") finished the period of the report with earnings of NIS 396.6 million compared with earnings of NIS 342.6 million in the corresponding period last year.

B. ZIM Israel Navigation Co. Ltd. (hereinafter – "ZIM") finished the period of the report with earnings of NIS 128.1 million compared with a loss of NIS 63.7 million in the corresponding period last year.

C. Oil Refineries Ltd. (hereinafter – "ORL") finished the period of the report with earnings of NIS 163.1 million, compared with a loss of NIS 149.8 million in the corresponding period last year.

D. Tower Semiconductor Ltd. (hereinafter – "Tower") finished the period of the report with a loss of NIS 303.2 million, compared with a loss of NIS 167.9 million in the corresponding period last year. The third quarter of the period of the report includes, for the first time, depreciation and amortization expenses with respect to fixed and other assets relating to FAB2 in the amount of NIS 76.7 million.

E. The results for the period of the report include non-recurring expenses, net, in the amount of NIS 10 million. Without the non-recurring expenses, the earnings for the period amounts to NIS 261 million, compared with a loss of NIS 12 million, without non-recurring expenses, in the corresponding period of last year.

F. The financing expenses of the principal Group companies decreased in the period of the report, as a result of the decrease in the dollar interest rate as well as due to the earnings in the marketable securities investments portfolio. For some of the companies, the reduction in the financing expenses derives from a real revaluation of the dollar exchange rate. The financing expenses in the consolidated financial statements amounted to NIS 118 million in the period of the report compared with NIS 303 million in the corresponding period last year.

The Corporation ended the third quarter of the period of the report with earnings of NIS 94 million, compared with a loss of NIS 19 million in the corresponding quarter last year.

The Corporation's financial results for the third quarter were affected by the following factors:

A. ICL concluded the quarter with earnings of NIS 128.8 million, compared with earnings of NIS 127.7 million in the corresponding quarter last year.

B. ZIM concluded the quarter with earnings of NIS 102.7 million, compared with earnings of NIS 1.0 million in the corresponding quarter last year.

C. ORL concluded the quarter with a loss of NIS 47.9 million, compared with a loss of NIS 81.2 million in the corresponding quarter last year.

D. In the third quarter of the period of the report, the Corporation included its share in Tower's losses, in the amount of NIS 46 million while, on the other hand, it reduced the provision for decline in value for its investment in Tower (which was recorded in 2002), by the same amount.

E. The financing expenses in the quarter amounted to NIS 53 million, compared with NIS 90 million in the corresponding quarter last year.

As an investment company, the results of the Corporation's operations are affected by the results of the operations of its investee companies and by non-recurring gains/losses.

Following is a brief summary of the financial results of the Corporation and the principal investees:

ISRAEL CHEMICALS LTD.

ICL finished the period of the report with earnings of NIS 396.6 million, compared with earnings of NIS 342.6 million in the corresponding period last year.

ICL finished the third quarter of the period of the report with earnings of NIS 128.8 million, compared with earnings of NIS 127.7 million in the corresponding quarter last year.

In the period of the report, the ICL continued to contend with the slowdown in the global economy and with the increase in the prices of energy, main raw materials (particularly sulfur) and marine shipping prices, along with a revaluation in the exchange rate of the NIS to the dollar. On the other hand, ICL enjoyed a certain increase in demand in the fertilizers segment, as well as a strengthening of the euro, the British pound and the Japanese yen in comparison with the dollar. ICL also benefited from the decline in the dollar interest rates.

ICL is taking steps to adapt its marketing and production policy to the global market conditions, and is focusing on improvement of the cash flows, diversification of the sources of financing and implementation of efficiency and cost savings activities.

Sales of the ICL Group totaled NIS 7.6 billion in the period of the report, compared with NIS 6.7 billion in the corresponding period last year, an increase of 13.9%. The increase in sales in the ICL Group reflects, mainly, an increase in turnover in the fertilizers segment, primarily due to an increase in the prices of fertilizers and potash, as well as an increase in the quantities of potash and fertilizers sold, which can be traced, in part, to consolidation of Cleveland Potash Ltd. (hereinafter – "CPL"), the results of which were included in the corresponding period of last year starting from May. The upward revaluation of the euro against the dollar also contributed to the increase in revenues from sales in Europe.

ICL's selling and marketing expenses and general and administrative expenses increased during the period of the report over the corresponding period last year, this being due to an increase in volume, including as a result of consolidation of the results of CPL, an increase in marine shipping prices and the effect of the upward revaluation of the shekel and the euro against the dollar. Part of the increase was offset by the efficiency measures employed by the ICL Group.

The financing expenses for the period of the report amounted to NIS 127.6 million, compared with NIS 177.8 million in the corresponding period last year. The decrease in financing expenses stems, mainly, from a decrease in the average dollar interest rates for the period, and from a decrease of NIS 267 million in the average loan balances.

Other expenses, net, during the period of the report amounted to NIS 47.5 million, compared with NIS 64.6 million in the corresponding period last year. These expenses stem, mainly, from write-down of the production facilities, write-down of non-current inventory and a provision recorded in respect of early retirement of employees.

In the third quarter of the period of the report, ICL's sales increased by 10.5% over the corresponding quarter last year. The increase in sales reflects, mainly, an increase in turnover, particularly as a result of an increase in prices in the fertilizers segment as well as an increase in the quantities of potash and fertilizers sold. Part of the increase in sales, was offset by a decline in volume and a drop in the prices of certain other products. The upward revaluation of the euro against the dollar also contributed to the increase in revenues from sales in Europe.

The selling and marketing expenses and general and administrative expenses also increased over the third quarter of last year, this being due to an increase in quantities sold of some of the products, an increase in marine shipping prices and the effect of the upward revaluation of the shekel and the euro against the dollar.

Subsequent to the balance sheet date, a long-term agreement was signed between ICL Industrial Products and a competing company, Great Lakes Chemical Corporation (hereinafter – "GLCC") for the supply of bromine and bromine compounds.

ICL Industrial Products and GLCC are among the world's three largest producers of bromine.

ZIM ISRAEL NAVIGATION CO. LTD.

ZIM finished the period of the report with earnings of NIS 128.1 million compared with a loss of NIS 63.7 million in the corresponding period last year. ZIM finished the third quarter of the period of the report with earnings of NIS 102.7 million compared with earnings of NIS 15.1 million in the second quarter of the period of the report and earnings of NIS 1.0 in the corresponding quarter last year.

ZIM's sales in the period of the report amounted to NIS 6.7 billion compared with NIS 5.3 billion in the corresponding period last year. The increase in sales derives from an increase of 3.4% in the average shipping fees compared with the corresponding period last year, and an increase of 23.5% in the quantity of containers shipped.

In the third quarter of the period of the report, ZIM's sales amounted to NIS 2.4 billion compared with NIS 1.9 billion in the corresponding quarter last year.

The variable expenses in the period of the report increased by 20.5% over the corresponding period last year while, as stated, there was an increase of 23.5% in the quantity of containers shipped.

The leasing expenses in the period of the report increased by 28.4% over the corresponding period last year.During the period of the report, Zim continued to implement efficiency measures, and there has been an improvement in results notwithstanding the increase in ship leasing costs and the high level of fuel prices.

ZIM's financing expenses in the period of the report amounted to NIS 101.5 million, a decline of 22.8% compared with the corresponding period last year. The decline stems, mainly, from the decline in the Libor interest rate, and a decrease in exchange rate differences expenses in respect of long-term loans, which derives from hedging transactions executed during the period of the report.

The marine container shipping activities is characterized by seasonality, both annual and quarterly.

During the period of the report, Zim entered into agreements for the leasing of two container ships for a period of 10 years, with an option to extend the period and to acquire one other ship from this series. The ships are to be placed into service during 2004 and 2005.

TOWER SEMICONDUCTOR LTD.

Tower finished the period of the report with a loss of NIS 303.2 million, compared with a loss of NIS 167.9 million in the corresponding period last year.

Tower finished the third quarter with a loss of NIS 164.7 million, compared with a loss of NIS 64.5 million in the corresponding quarter last year.

In the third quarter of the period of the report, Tower placed FAB2 into service. The results for the third quarter include depreciation and amortization of fixed and other assets, in the amount of NIS 76.7 million, which are not included in the corresponding quarter last year.

In the period of the report, there was an increase in the marketing, administrative and general expenses and research and development expenses as well as an increase in the cost of sales, which were partly offset by an increase in total sales.

During the period of the report, Tower's sales totaled NIS 184.5 million, compared with NIS 160.9 million in the corresponding period last year.

In the third quarter of the period of the report, there was an increase in administrative and general expenses and financing expenses, compared with the third quarter of last year.

During the period of the report, Tower received several initial orders from its Wafer partners and others for the production of chips in FAB2 having geometric shapes of 0.18 μ, and during the third quarter, sales thereof were recorded. The process of installing additional production machines in FAB2 is proceeding as planned.

Regarding amendment of the agreements with respect to the fifth milestone, see the section "Changes in the Investment Portfolio".

Regarding a lawsuit against Tower, the Israel Corporation and directors of Tower, see the Section "Events Occurring During the Period of the Period and Thereafter.

OIL REFINERIES LTD.

ORL finished the period of the report with earnings of NIS 163.1 million, compared with a loss of NIS 149.8 million in the corresponding period last year.

ORL finished the third quarter with a loss of NIS 47.9 million, compared with a loss of NIS 81.2 million in the corresponding quarter last year.

For the first time since the outbreak of the security events, which began in September 2000, and the worsening of the recession in the local market, there was an increase in fuel consumption of 2.2% over the corresponding period last year, which stemmed, mainly, from an increase consumption of crude oil and diesel heating fuel.

The refining sector finished the period of the report with earnings of NIS 89 million, compared with a loss of NIS 189 million in the corresponding period last year.

The continued lack of production of oil by Iraq, the sharp increase in natural gas prices in the United States (due to a shortage) and as a result the switch-over to consumption of crude oil products, and the low inventory levels of gasoline in the United States, gave rise to an increase in prices from the low point of $23.5 per barrel of crude oil of the Brent type in the second quarter, to roughly $30 per barrel during August.

The crude oil prices, which fluctuated during the third quarter in the upper limit of OPEC's price range ($22–$28 per barrel), jumped at the end of September to $31 per barrel, due to the decision of OPEC's ministers to cutback production by 900 thousand barrels per day, to 24.5 million barrels per day.

The average price of one barrel of crude oil during the period of the report was $29, compared with $24 in the corresponding period last year, and $28 in the third quarter of the period of the report compared with $27 in the corresponding quarter last year.

Margin on refining activities ($ per ton):

	January–March	**April–June**	**July–September**	**January–September**
2003	23.0	17.5	16.5	19.0
2002	4.0	13.2	10.6	8.9

During the period of the report, the financing income amounted to NIS 66 million, compared with financing expenses of NIS 122 million in the corresponding period last year. In the third quarter of the period of the report, the financing expenses amounted to NIS 108 million, compared with financing expenses of NIS 73 million in the corresponding quarter last year. The large fluctuations in the financing category derives, mainly, from a devaluation or real upward revaluation of the shekel versus the dollar. In the period of the report, there was a real upward revaluation of 4.8%, compared with a real devaluation of 3.1% in the corresponding period last year. In the third quarter of the period of the report, there was a real devaluation of 4.0% compared with a real devaluation of 1.5% in the corresponding quarter last year.

In the period of the report, ORL's share in the earnings of its investee companies amounted to NIS 74 million, compared with NIS 50 million in the corresponding period last year.

In the first quarter, ORL raised NIS 1.4 billion by means of a private issuance of debentures.

EXPOSURE TO MARKET RISKS AND RISK MANAGEMENT

During the period of the report, the Supervisor of Banks in Bank of Israel published an amendment to the limitations on the debt of a borrower and of a group of borrowers (Directive No. 313). The amendment, which includes, among other things: a change in the definition of a group of borrowers so as to now also include borrowers which have significant connections between them, provides as well that a person controls an entity also if he holds the highest percentage of any type of means of control, and also cancels the section which permits splitting the debt of a group of borrowers which consists of a jointly controlled investee company or a partnership of several controlling interests.

The Corporation’s Management is unable to assess at this point, the impact of the Directive on the Group’s financial liabilities to banks.

Aside from this, there was no material change with respect to the exposure to market risks and the management thereof as they were reported in the Directors’ Report as at December 31, 2002.

EFFECT OF EXTERNAL AND OTHER FACTORS

A. The ORL concession

ORL operates in accordance with a concession it received to construct, operate and maintain facilities and auxiliary plants for purposes of refining mineral oils. The concession received the force of law pursuant to the Anglo-Iranian Oil Treaties Ordinance from 1938. The concession is valid up to October 2003.

On December 12, 2002, an arrangement was signed between ORL, the Government and the Israel Corporation in connection with all that involved with the period after expiration of the concession. Based on the arrangement, upon expiration of the concession period (October 18, 2003), all of ORL's rights deriving from the concession will terminate, and an arrangement will enter into effect according to which, subject to the conditions of the arrangement, the highlights of which are detailed below, ORL shall be permitted to continue to hold the assets it held on the eve of expiration of the concession (hereinafter – "the Assets"). The arrangement was made for 25 years, commencing October 18, 2003 (hereinafter – "the First Period"). ORL – or if it is split up into two separate refineries, each of the separate refineries – was granted an option to continue the aforesaid period for an additional 25 years, provided it notifies the Government no later than two years before the end of the First Period.

The arrangement provides that each side reserves the right to petition the court for clarification of the disagreement regarding the question whether or not all of ORL's assets return, by virtue of the historical concession, to the ownership of the Government without consideration, however in any case, any decision made regarding this matter will be implemented only at the end of the arrangement period (25 years or 50 years, as the case may be). If a final court decision is rendered, each side will be permitted to implement its provisions regarding recording of the rights in the Assets, provided such registration will not adversely affect the validity of the remainder of the arrangement's provisions and ORL's right to pledge the Assets in the ordinary course of its business, subject to the provisions of the arrangement. The arrangement conveyed to the State the right to record a caveat on the arrangement's content, on all the real estate assets, and to remove the caveat as stated at any time. Subject to theses provisions, no change shall be made to the recording of the Assets. During the arrangement period, ORL is permitted to execute transactions in the Assets in the regular course of business, and the decision in a disagreement with respect to the Assets shall apply to the proceeds from transactions as stated as well as to assets which ORL shall acquire in the future. A transaction in the Assets, except for a lien in the regular course of business, which does not exceed the period of the arrangement, requires approval of the Accountant General, who shall act in this matter in accordance with the Government's Decision No. 2796, dated November 25, 2002. The Government and ORL recorded caveats on the real estate which is the subject of the arrangement.

During the arrangement period, ORL shall pay to the Government annual permit fees in a fixed amount of $3 million plus additional annual amounts which are dependent on ORL's earnings, as follows: 8% of the annual earnings before taxes and permit fees, in the range of $0–$40 million; plus, 10% of the annual earnings before taxes and permit fees, in the range of $40–$70 million; plus, 12% of the annual earnings before taxes and permit fees, in the range of $70–$90 million. In any case, the amounts paid to the Government as permit fees shall not exceed (including the fixed payment) the amount of $11.6 million. All the amounts shall be translated into shekels in accordance with an exchange rate of $1 = NIS 4.80, linked to the CPI (base index of May 2002). The "annual earnings before taxes" will be defined and measured based on annual, audited consolidated financial statements, and will include ORL's share in earnings or losses of subsidiary and affiliated companies having separate activities as well as capital gains and losses, however will not include gains and losses from activities through companies operating overseas or sale of the holdings in companies operating overseas.

Subsequent to the balance sheet date, ORL paid the first installment in accordance with the arrangement. The Accountant General in the Ministry of Finance notified ORL that the amount it paid was deposited in a separate account, so long as the conditions precedent stipulated in the arrangement were, in his opinion, not fulfilled. ORL responded to the Accountant General that the agreement was signed by the Government after all the required approvals had been received, and after its signature approvals of the Board of Directors of ORL and the Board of Directors of the Israeli Corporation were also received, and that upon the receipt thereof the agreement entered into effect. Therefore, the amount paid to the Government by ORL was properly paid pursuant to a valid agreement.

In the arrangement, the Government committed that if and to the extent possible, it will assist ORL in the transition without interferences from the concession period to the arrangement period (recognition of the existing construction, orderly licensing and construction processes, establishment of an industrial council).

Pursuant to the agreement, upon expiration of ORL's rights under the concession, ORL will be subject – commencing from the end of the end of the original concession period (October 18, 2003) and thereafter, to the construction and planning laws and additional local laws, in connection with the Haifa oil refinery. During 2002, the Manager of the Ministry of the Interior appointed an investigation committee for the boundaries of the Municipality of Haifa, Nesher and Kiryat Ata, Zvulun and the area of the oil refineries.

During the period of the report, the Committee published its recommendations, pursuant to which the aforesaid area will be annexed to the Municipality of Haifa; the area will be administered by means of a joint governing body of the four local authorities bordering on the area, representatives of the factories operating therein, representatives of the public and representatives of Government ministries. The Committee also recommends that the governing body should handle all matters involved with running the area as an industrial area, similar to the definitions of a local industrial council in the Local Council Ordinance. The Committee further recommended that determination of the initial Municipal Tax levy shall be with the approval of the Minister of the Interior and it shall be imposed gradually (a discount shall be given which will be reduced from year to year over a 3–5 year period). ORL requested to present its position to the Minister of the Interior, which supports the establishment of a local industrial council in the area, prior to the reaching of a decision. If lands belonging to ORL are included within the boundaries of any local authority, ORL would be expected to be subject to Municipal Tax payments for the Haifa refinery as well.

ORL declared in the agreement that it is aware that the Government intends to initiate legislation which will govern the fuel industry, including regulation, which could affect the arrangement, even though there is no intention to affect the aspects of the arrangement which involve the Assets and the permit fees.

In addition, ORL declared that it is aware that the Government and the Israel Corporation agree to act regarding the matter of the split-up of ORL as detailed in the appendix to the agreement, which was signed between them and which constituted an integral part of the arrangement between the Government and the Israel Corporation.

During the period of the report, a petition was filed with the Supreme Court sitting as the High Court of Justice by the Israeli Society for Proper Government (hereinafter – "the Petitioner"), for the issuance of conditional and interim orders, which will direct the Prime Minister, the Minister of Finance, the Minister of National Infrastructures, the Government Companies Authority, ORL, the Israel Corporation and others, to provide reasons why they should not be prevented from acting in accordance with the arrangement and/or why they do not act to cancel the arrangement. The petitioner's main reasons are that the arrangement negatively impacts the principle of equality and equitable allocation, and it circumvents the tender laws by granting private parties a concession to use Government assets in a process having – based on the petitioner's contention – various deficiencies. The Court refused to grant the petitioner's request for interim orders which will prevent realization of the arrangement up to the time of the decision on the petition.

The Israel Corporation submitted its response to the petition, in the framework of which it expressed its position that there is no basis for the petition. ORL, in its response, objected to the petition and its reasoning and supported implementation of the arrangement.

The Petitioner once again submitted a request for interim orders which would prevent the Government from: taking steps to obtain an exemption from a tender for the arrangement, acquire or sell rights and/or shares of the Israel Corporation in ORL and to prepare a new agreement or revisions to the arrangement. Up to the date of publication of the financial statements, no orders were not issued.

On September 15, 2003, the Government decided to set up an inter-office team which will examine all of the issues affecting the ORL at this time, directing attention to the letters of the Attorney General, dated July 7, 2003 and August 13, 2003. At first, the team will examine the agreement and the alternatives thereto, including, postponement of the date of the option held by the Israel Corporation, the agreement's conditions, including the license fees determined therein, and the valuations performed by the Government and the Israel Corporation as a result of the agreement, and shall formulate its position. Taking into account its conclusions, the team is permitted to conduct negotiations with the Israel Corporation. For detail of the Government's decision, see below.

B. The splitting of ORL's facilities into separate ownerships

In August 1999, the Government decided to adopt policies in connection with the structure of the fuel industry which include, among other things, creation of competition between the Haifa refinery and the Ashdod refinery, while separating the ownership thereof. The decision also relates to operational matters of ORL in the marketing and petrochemical fields, as well as control over fuel product prices.

In November 1999, the Board of Directors of ORL was requested by the Government Companies Authority to relate to the proposed resolution to the Ministerial Committee on Privatization, concerning the split-up of ORL and the transfer of the Ashdod refinery to the ownership of the Israel Corporation. The Board of Directors of ORL has requested clarifications on an array of issues in order to be able to formulate its position (see also Note 3 to the financial statements).

During 2000–2001, a committee appointed by the Minister of Finance and the Minister of National Infrastructures, reexamined the issue of the split-up of ORL and, in 2001, it submitted its conclusions. The committee recommended not to wait until the end of the concession and to immediately arrange the matters related to the end of the concession. In respect of the structure of the fuel industry and the split-up of ORL, the committee does not see any reason for changing the policy of the Government regarding the future structure of the fuel industry, as reflected in the Government's decision dated August 22, 1999. Nevertheless, if it becomes necessary, the Government's decision will be amended so as to make it possible for ORL, in the opinion of the Government, to enter into the marketing sector and the petrochemicals area, and to remove the control over prices. The committee recommended conducting discussions with ORL and the Israel Corporation for the purpose of arranging the relationship with them in a manner which will facilitate implementing the Government decision regarding the split-up of ORL, while arranging, among other things, the issue of the end of the concession and finding a solution for the matter of treatment of the Assets at the end of the concession.

In Appendix C to the arrangement, dated December 2, 2002, regarding the matter of ORL's concession, an appendix which was signed by the Government and the Israel Corporation, the Israel Corporation committed to cooperate to the extent required by the Government, for purposes of split-up of ORL into two separate refineries (Haifa and Ashdod). A mechanism was also determined for performance of valuations as well as a mechanism regarding for sale of the Israel Corporation's shares in ORL or, in the case of a split-up of ORL, acquisition by the Israel Corporation of one of the two refineries. In this case, the Israel Corporation will pay to the Government or receive therefrom, the difference between the relative value of the Israel Corporation's share in ORL (26%) and the value of the split-up refinery which it shall choose, based on the valuations performed pursuant to the arrangement.

In the period of the report, the two aggregate valuations were submitted. One from an appraiser on behalf of the Israel Corporation, pursuant to which the total value of ORL is NIS 2,234 million, and the other from an appraiser on behalf of the Government, pursuant to which the total value of ORL is NIS 2,143 million.

On August 5, 2003, the Israel Corporation notified the Government that in light of the fact that the negotiations with the Government regarding participation of the Israel Corporation in the split-up have not been completed, and due to the dates provided in the appendix to the arrangement, it has decided not to exercise the option it was granted in Appendix C to the arrangement, to participate in the split-up of ORL into two separate refineries and, therefore, the provisions of Section 4 of that Appendix shall apply, according to which the Israel Corporation shall sell to the Government or to a party which the Government shall instruct, all ORL shares owned by the Israel Corporation, within 30 days, at a price which constitutes an average between the two aggregate valuations of ORL, this being subject to certain monetary adjustments.

Nonetheless, the Israel Corporation is prepared to continue the negotiations with the Government regarding its participation in the split-up.

The Government is permitted to instruct that the execution date of the sale transaction shall be postponed for an additional period which shall not exceed two years from June 6, 2003.

The Israel Corporation clarified, that at this point, it can not be known whether the transaction will ultimately be consummated, taking into account, among other things, the following items:

1. The results of the judicial decision with respect to the petition filed by the Israeli Society for Proper Government (as described above in the ORL concession section).

2. The need for approvals which according to the Government's position (with which the Israel Corporation disagrees) are required by law, including a tender exemption.

3. The results of the negotiations (if held) with the Government regarding the matter of the Israel Corporation's participation in the split-up of ORL into two separate refineries, one in the Haifa Bay and the other in Ashdod.

On September 15, 2003, the Government made the following decision: "Further to Government Decisions No. 126, dated August 22, 1999, and No. 2796, dated November 25, 2002, the decision of the Committee of Ministers for Privatization Matters MH/2, dated October 20, 2001, and the agreement signed between the Government and the Israel Corporation, dated December 2, 2002, which has not yet received all the required approvals (hereinafter – "the Agreement"), to advance the split-up of the oil refineries and the privatization thereof, in the following manner:

1. To set up an inter-office team which will include representatives of the Ministry of Finance, Ministry of National Infrastructures, Ministry of Justice and the Supervisor of Restrictive Business Practices. The work of this team will be managed by the Ministry of Finance.

2. The team will examine all of the issues affecting the oil refineries at this time, directing attention to the letters of the Attorney General, dated July 7, 2003 and August 13, 2003. At first, the team will examine the agreement and the alternatives thereto, including, postponement of the date of the option held by the Israel Corporation, the agreement's conditions, including the license fees determined therein, and the valuations performed by the Government and the Israel Corporation as a result of the agreement, and shall formulate its position. Thereafter, and in accordance with its positions, as stated, it shall examine, among other things, the most appropriate and efficient way for executing the split-up of ORL and the privatization thereof and arranging the holdings of each of the split-up refineries in investee companies, directly and indirectly by ORL. The team is authorized to make a decision regarding the matter of postponement of the date of the option, as stated, and there is no need to include this matter in the framework of the team's recommendations, as stated in Section 5.

3. Taking into account its conclusions in Section 2, the team is permitted to conduct negotiations with the Israel Corporation with respect to, among other things, split-up of ORL and the ownership structure in ORL and its investee companies, directly or indirectly, after the split-up.

4. In addition, the team will make recommendations with respect to the target structure, including supervision of prices, the reciprocal relationships which will remain between the two oil refineries, including, principles regarding the transfer of feedstock between them and between them and the petrochemicals industry and additional areas of activity for the separate refineries or for the controlling interests therein, including the dates from commencing the activities as stated.

5. The team is to submit its recommendations within 30 days for approval by the Committee of Ministers for Privatization Matters or approval by the Committee of Ministers for Society and Economic Matters, as will be determined by the Minister of Finance, and it is permitted to submit partial recommendations regarding urgent matters within 20 days. The team's recommendations regarding Section 4, may be submitted within 60 days.

6. Up to 30 days after submission of the team's conclusions, and taking such conclusions into account, the Manager of the Companies Authority shall submit, in coordination with the Supervisor of Budgets, the Attorney General, Ministry of National Infrastructures, Ministry of Justice and the Restrictive Business Practices Authority, a proposed decision to the Committee of Ministers for Privatization Matters regarding privatization of ORL by means of its split-up and sale of the Government's holdings after the split-up. The proposed decision is to relate to, among other things, to the extent necessary, the following matters:

   A. Split-up of ORL into two sister companies: ORL Haifa Ltd. (hereinafter – "ORL–Haifa") and ORL Ashdod Ltd. (hereinafter – "ORL–Ashdod"), such that all the assets, rights, liabilities and employees involved with the refining activities in Haifa shall remain in ORL–Haifa, and all the assets, rights, liabilities and employees involved with the refining activities in Ashdod shall be transferred to ORL–Ashdod.

   B. Determination of the ways for privatization and the course for sale of the Government's holdings in ORL–Haifa and ORL–Ashdod after the split-up.

Up to the publication date of the financial statements, the inter-ministerial team had not yet submitted its recommendations.

In the assessment of ORL, all that stated above regarding the arrangement, if implementation thereof is decided on and such implementation is, in fact, effected, will have a material impact on ORL, however, at this stage, ORL is not able to estimate and quantify such impact on its financial position.

The management of the Israel Corporation adopts the assessment of ORL.

C. Pursuant to the treaty known as the Montreal Protocol, to which Israel is a party, production and consumption of methyl bromine for soil fumigation in developed countries are being gradually reduced to zero by the year 2005. Sales during the period of the report, to which the prohibition will apply in 2005, were $28.0 million and the operating profit in respect thereof came to $6.6 million. Sales of methyl bromine for soil fumigation to developing countries, is expected to continue until 2015.

   Methyl bromine has other uses aside from soil fumigation, such as: pre-shipment treatment, quarantine, raw material or intermediate material for production of another material or product (feedstock), recycling or reuse. These uses are not controlled by the Montreal Protocol. Sales of the agricultural division of the industrial products during the period of the report for uses and to customers who, to the extent currently known, will not be covered by the production and marketing prohibition in 2005, amounted to $31.0 million. The operating profit with respect to these sales was $8.8 million.

   ICL's strategy is to continue operating in the area of soil fumigation, even after the prohibition of methyl bromine for the above uses takes effect. Therefore, over the recent years efforts are being made to develop, license and market new applications and substitutes for methyl bromine in this important market.

D. Contrack-Line Ltd. (hereinafter – Contrack) has filed a suit in the Tel-Aviv District Court against Dead Sea Works Ltd. (hereinafter – DSW) and against others, for infringement of a patent regarding a dredge which was designed for crushing salt mushrooms and with respect to the violation of other alleged rights of the plaintiff regarding the dredge.

The District Court ruled that DSW violated the patent. In respect of this ruling an appeal was submitted to the Supreme Court. Mediation proceedings between the parties were not successful and the case is pending hearing of the appeal.

Concurrent with the appeal and on the basis of the aforementioned ruling, Contrack filed a financial claim with the District Court against DSW in the amount of $50 million in respect of the damages/loss it incurred. Contrack requested an exemption from the court fee and the Court permitted Contrack to pay a token fee in the amount of NIS 10 thousand in respect of a claimed amount of up to $20 million. Both sides have submitted appeals on this decision. Rendering of a decision on these appeals has been deferred until after the decision on the appeals which are in the Supreme Court.

DSW has recorded a provision in its books which, in its estimation, based on the opinion of its legal counsel and taking into account the above-mentioned development in the proceedings, is sufficient to cover any exposure arising from such proceedings.

E. On May 29, 2001, a class action suit was filed against Fertilizers and Chemicals Ltd. (hereinafter – Fertilizers) and other defendants, under the Abatement of Environmental Nuisances Law (Civil Actions), 1992. In the claim, the plaintiffs contend that the defendants are polluting the Kishon stream. The plaintiffs request that the Court issue an order to cease the discharge of wastes into the Kishon and to restore the stream to its condition prior to discharge of the wastes.

On September 13, 2001 and on May 22, 2002, December 31, 2002, and March 20, 2003, monetary claims in the total amount of $30 million were filed against Fertilizers and many other defendants regarding the dumping of wastes into the Kishon stream, which allegedly caused the plaintiffs to contract cancer.

These claims are in addition to other claims filed against Fertilizers with respect to bodily injuries and economic damages allegedly caused to the plaintiffs as a result of pollution of the Kishon stream, for which the plaintiffs claim that Fertilizers is also responsible. On August 24, 2003, a request was filed with the court to join 62 additional plaintiffs to one of the additional claims mentioned above.

In the opinion of the management of Fertilizers, based on the opinion of its legal counsel handling the claims, it is not yet possible to evaluate the risk inherent in the claims and, therefore, no provision has been included in the financial statements in respect thereof.

F. A water appeal is pending in the Court for Water Matters, which was filed by a Man, Nature and Law against the Water Commissioner and against two companies of ICL (see the Report of the Board of Directors for 2002). During the period of the report, a hearing was held on the appeal and opinions were submitted by the parties on the question of who is responsible for the pollution. As noted in the annual report, one of the ICL companies gave notice of its readiness to acquire the water from the drilling in question. There is no change in ICL's assessment in connection with the said proceedings.

EVENTS OCCURRING DURING THE PERIOD OF THE REPORT AND THEREAFTER

A. Millennium Investments Elad Ltd. (hereinafter – "Millennium") reported to the Company that the various parties in the Ofer Brothers Group signed an agreement regarding change in the structure of the holdings in the Israel Corporation. Millennium holds 50.6% of the share capital of the Israel Corporation.

In February 2003, the sale transaction was completed and, as a result, Mashat (Investments) Ltd. (hereinafter – "Mashat") holds 80% of the share capital of Millennium and Ofer (Ship Holdings) Ltd. holds 20% of the share capital of Millennium, as it did previously.

Mashat is controlled by a foreign trust whose beneficiaries are Idan Ofer and his family. Ofer (Ship Holdings) Ltd. is held in equal shares by L.I.N. (Holdings) Ltd. (controlled by Eyal Ofer), Doron Ofer and Udi Angel.

B. During the period of the report, the shares of the Israel Corporation were consolidated, in such a manner that every ordinary share (Series 1) became an ordinary share of the Corporation, this being as a result of the amendment of the Income Tax Ordinance No. 132, 2002, which amended the Israel Corporation Ltd. Law, 1969) (hereinafter – "the Israel Corporation Law"). Pursuant to the amendment, some of the tax benefits provided in the framework of the Israel Corporation Law were cancelled and, therefore, there is no longer a need for the distinction which was made in the issuance in 2001 between the different classes of shares. Since the requirement to distinguish between the different classes of shares derived from the requirements of the Income Tax Commission, the Corporation requested and received approval in writing from the Income Tax Commission that, among other things, there is nothing preventing consolidation of the Corporation's different classes of shares traded on the stock exchange for income tax purposes. In addition, the Income Tax Commission notified the Corporation, that an issuance of shares by the Corporation commencing with the 2003 tax year will not adversely affect the exemptions and benefits to which the Corporation was entitled in the framework of the Israel Corporation Law.

C. In January 2003, Yehuda Ezra, CPA, ceased to serve as the Corporation's internal auditor. As of this date, Miki Blumenthal, CPA, is serving as the Corporation's internal auditor.

D. In January 2003, the Corporation's Board of Directors decided to change the terms of the stock options plan of its employees. Pursuant to the change, at the time of exercise of the options, the offeree will be issued shares (or will receive shares held by the Corporation or by a company it controls) in the value of the benefit only, and the offeree will pay only the par value of the shares actually issued to him (or will not pay any amount – in a case of a transfer of shares held by the Corporation or by a company it controls, in place of an issuance of shares), and not the exercise price of all the shares with respect to which he gave a notice of exercise.

In addition, the Corporation's Board of Directors decided to change the exercise period under the options' plan, such that the exercise period will be 36 months in place of 24 months, as provided in the existing conditions of the options' plan.

E. During the period of the report, a notification was given regarding change of the CEOs in Tower, commencing from June 2003. As of this date, Mr. Carmel Vernia will serve as Chairman of the Board of Directors and acting CEO of Tower.

F. During the period of the report, Mr. Ovadia Eli completed his service as Chairman of ORL.

G. On March 27, 2003, the Corporation's Board of Directors decided to distribute an interim cash dividend, in the aggregate amount of approximately NIS 99 million. The dividend was distributed on April 24, 2003.

H. On August 26, 2003, the Corporation's Board of Directors decided to distribute cash dividend, in the aggregate amount of approximately NIS 36 million. The dividend was distributed on October 2, 2003.

I. During the period of the report, Mr. Yechiel Borohoff completed his service as a director of the Corporation (substitute for Mr. Idan Ofer).

J. During the period of the report, the Corporation submitted the required documents in connection with the Corporation's participation in the process of sale of the State's shares in ZIM the Israel Navigation Company Ltd.

K. In July 2003, certain shareholders of Tower filed a claim in a U.S. court against Tower, certain of its directors, certain Wafer partners and main investors, including the Israel Corporation. The plaintiffs, which have requested, among other things, that their claim be certified as a class action, have raised contentions under the U.S. Securities Law from 1934, in connection with inaccurate reports and omission of information by the defendants in material sent to the shareholders of Tower in April 2002 relating to approval of the amendment of Tower's investment agreements with its Wafer partners and main investors in capital.

Tower and the Corporation believe that the claim has no basis and they intend to vigorously oppose it.

L. The proposed Law for Economic Policy for the 2004 Fiscal Year (Legislative Amendments), 2003 (the Economic Plan), which passed a first-call on November 5, 2003, and which is presently before the Knesset, includes legislative changes in various areas which may, if passed as presently drafted, have an adverse effect, directly or indirectly, on the Group's results. Since it is not possible to know what the final version of such legislation will be and whether it will ultimately be passed, it is not possible at the present time to estimate the extent of the impact on the Group's results.

M. In September 2003, the Corporation's General Meeting approved the appointment of Ms. Anat Keynan as an external director of the Corporation in place of Ms. Irit Isakson, and Mr. Yair Sarusi as an external director of the Corporation in place of Prof. Avishai Braverman.

In addition, Mr. Doron Ofer and Mr. Zvi Zamir ceased to serve as directors.

N. During the period of the report, an Extraordinary General Meeting of the Corporation approved acquisition of liability insurance for directors and officers.

O. Regarding the Corporation's agreement with the banks to provide safety net for Tower, see the Section "Changes in the Investment Portfolio.

ADDITIONAL INFORMATION INCLUDED IN THE AUDITORS' REVIEW REPORT TO THE SHAREHOLDERS

The following is a quotation from the review report of the Auditors:

“We would call attention to that stated below:

A. As stated in Note 3 to the financial statements, regarding the petition submitted to the Supreme Court sitting as the High Court of Justice relating to the arrangement between Oil Refineries Ltd. (hereinafter - "ORL") and the Government of Israel and the Corporation, in connection with the period after the end of the concession period (October 18, 2003), regarding the possibility of splitting the refining facilities in Haifa and Ashdod into two separately owned refineries, and regarding ORL's assessments with respect to the material impact which cannot be estimated at this stage, of the aforementioned matters on the its financial position.

B. Note 4A.-E. to the financial statements relating to the uncertainty regarding the contingent liabilities of Israel Chemicals Ltd. (hereinafter – “ICL”) and of its subsidiaries. ICL has included provisions in its interim financial statements, relating to certain of these contingent liabilities, which in its opinion adequately cover the amounts of the liabilities, which may arise therefrom. No provisions have been included in ICL’s financial statements with respect to contingent liabilities, regarding which the amounts or the outcome of which cannot presently be estimated.

The Board of Directors expresses its appreciation to the Corporation's officers and employees and to the officers and employees of the Group companies for their contribution to achievement of the Group’s targets, including execution of its business strategy, efficiency measures and reaching the goals set by the companies.

Idan Ofer	**Yossi Rosen**
Chairman of the Board of Directors	**President and CEO**

November 20, 2003

The Board of Directors
<u>The Israel Corporation Limited</u>

Dear Sirs,

Review of the unaudited interim consolidated financial statements as at September 30, 2003

At your request, we have reviewed the interim consolidated balance sheet of The Israel Corporation Ltd. as at September 30, 2003 and the related consolidated statements of earnings, the statements of changes shareholders' equity and the consolidated statements of cash flows for the nine-month and three-month periods then ended.

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

We received review reports of other auditors, regarding the interim financial statements of certain subsidiaries, whose assets constitute 74.4% of the total consolidated assets as at September 30, 2003 and whose revenues constitute 90.7% and 91.0% of the total consolidated revenues for the nine-month and three-month periods then ended, respectively. Furthermore, the data included in the interim consolidated financial statements relating to the net asset value of the investments in affiliates stated on the equity basis and to the Group's equity in their operating results, is based on financial statements most of which were reviewed by other auditors.

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

In the course of our review, including the reading of the review reports of other auditors as stated above, nothing came to our attention which would indicate the necessity of making material modifications to the financial statements referred to above, in order for them to be in conformity with generally accepted accounting principles and in accordance with Section D of the Securities Regulations (Periodic and Immediate Reports), 1970.

We would call attention to that stated in:

1. As stated in Note 3 to the financial statements, regarding the petition submitted to the Supreme Court sitting as the High Court of Justice relating to the arrangement between Oil Refineries Ltd. (hereinafter - "ORL") and the Government of Israel and the Corporation, in connection with the period after the end of the concession period (October 18, 2003), regarding the possibility of splitting the refining facilities in Haifa and Ashdod into two separately owned refineries, and regarding ORL's assessments with respect to the material impact which cannot be estimated at this stage, of the aforementioned matters on the its financial position.

2. Note 4A.-E. to the financial statements relating to the uncertainty regarding the contingent liabilities of Israel Chemicals Ltd. (hereinafter – "ICL") and of its subsidiaries. ICL has included provisions in its interim financial statements, relating to certain of these contingent liabilities, which in its opinion adequately cover the amounts of the liabilities, which may arise therefrom. No provisions have been included in ICL's financial statements with respect to contingent liabilities, regarding which the amounts or the outcome of which cannot presently be estimated.

Sincerely,

Somekh Chaikin
Certified Public Accountants (Isr.)

November 20, 2003

Consolidated Balance Sheets as at

In terms of shekels of September 2003

	September 30 2003 (Unaudited) NIS millions	September 30 2002 (Unaudited) NIS millions	December 31 2002 (Audited) NIS millions
Current assets			
Cash and cash equivalents	**223**	221	148
Marketable securities	**628**	799	672
Short-term loans and deposits	**347**	74	58
Trade receivables	**1,074**	1,902	1,635
Other receivables	**843**	859	857
Inventories	**2,284**	*2,125	*2,292
	5,399	5,980	5,662
Long-term investments, loans and receivables			
Investments in investee companies	**1,147**	1,267	1,100
Investments in other companies	**249**	290	281
Deposits, loans and long-term receivables	**75**	87	82
Inventories	**77**	*121	*110
	1,548	1,765	1,573
Fixed assets	**7,707**	8,154	8,125
Other assets and deferred expenses	**853**	969	936
	15,507	16,868	16,296

* Reclassified.

Idan Ofer	**Yossi Rosen**	**Avisar Paz**
Chairman of the Board of Directors	President and CEO	Chief Financial Officer

November 20, 2003

	September 30 2003	September 30 2002	December 31 2002
	(Unaudited)	**(Unaudited)**	**(Audited)**
	NIS millions	**NIS millions**	**NIS millions**
Current liabilities			
Short-term credit from banks and others	**2,646**	2,481	3,121
Debentures convertible into shares of a subsidiary	**-**	-	360
Trade payables	**1,009**	948	1,047
Other payables	**1,213**	1,228	1,177
Proposed dividend	**36**	-	-
	4,904	4,657	5,705
Long-term liabilities			
Long-term liabilities to banks and others	**4,248**	5,763	4,809
Convertible debentures	**504**	563	180
Deferred taxes, net	**1,165**	1,033	1,039
Liability for employee severance benefits, net	**746**	710	710
	6,663	8,069	6,738
Minority interest	**1,863**	1,912	1,854
Shareholders' equity	**2,077**	2,230	1,999
	15,507	16,868	16,296

The accompanying notes are an integral part of the financial statements.

Consolidated Statements of Earnings

In terms of shekels of September 2003

	For the nine months ended September 30 2003 (Unaudited) NIS millions	For the nine months ended September 30 2002 (Unaudited) NIS millions	For the three months ended September 30 2003 (Unaudited) NIS millions	For the three months ended September 30 2002 (Unaudited) NIS millions	Year ended December 31 2002 (Audited) NIS millions
Sales, services and work executed	7,701	7,279	2,834	2,636	9,403
Cost of sales, services and work executed	5,232	4,975	1,956	1,807	6,458
Gross profit	2,469	2,304	878	829	2,945
Research and development expenses, net	98	102	33	34	133
Selling, transport and marketing expenses	1,265	1,104	471	376	1,488
General and administrative expenses	347	315	130	122	417
Operating income	759	783	244	297	907
Financing expenses, net	(118)	(303)	(53)	(90)	(359)
Other expenses, net	(18)	(90)	(3)	(31)	(322)
Earnings before taxes	623	390	188	176	226
Income tax	(241)	(173)	(71)	(81)	(190)
Earnings after taxes	382	217	117	95	36
Group's equity in earnings (losses) of affiliates, net	52	(139)	36	(52)	(148)
Minority interest in earnings of subsidiaries, net	(183)	(163)	(59)	(62)	(188)
Net earnings (loss) for the period	251	(85)	94	(19)	(300)
	NIS	**NIS**	**NIS**	**NIS**	**NIS**
Basic and diluted earnings (loss) per share					
Earnings (losses) per NIS 1 par value of the share capital	36.34	(12.34)	13.56	(2.78)	(43.58)

The accompanying notes are an integral part of the financial statements.

Statements of Changes in Shareholders' Equity

In terms of shekels of September 2003

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Proposed dividend subsequent to the balance sheet date	Retained earnings	Total
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the nine-month period ended September 30, 2003 (Unaudited)						
Balance as at the beginning of the period	1,476	(13)	(70)	99	507	1,999
Net earnings for the period	-	-	-	-	251	251
Dividend paid		-	-	(99)	1	(98)
Proposed dividend	-	-	-	-	(36)	(36)
Adjustments from translation of financial statements	-	-	(39)	-	-	(39)
Issuance of capital	(1)	1	-	-	-	-
Balance as at the end of the period	1,475	(12)	(109)	-	723	2,077
For the nine month period ended September 30, 2002 (Unaudited)						
Balance as at the beginning of the period	1,480	(21)	(93)	-	906	2,272
Net loss for the period	-	-	-	-	(85)	(85)
Adjustments from translation of financial statements	-	-	41	-	-	41
Realization of reserves due to realization of investment	-	-	(1)	-	-	(1)
Issuance of capital	(2)	5	-	-	-	3
Balance as at the end of the period	1,478	(16)	(53)	-	821	2,230

The accompanying notes are an integral part of the financial statements.

Statements of Changes in Shareholders' Equity (cont'd)

In terms of shekels of September 2003

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Proposed dividend subsequent to the balance sheet date	Retained earnings	Total
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the three-month period ended September 30, 2003 (Unaudited)						
Balance as at the beginning of the period	1,475	(12)	(159)	36	629	1,969
Net earnings for the period	-	-	-	-	94	94
Proposed dividend	-	-	-	(36)	-	(36)
Adjustments from translation of financial statements	-	-	50	-	-	50
Balance as at the end of the period	1,475	(12)	(109)	-	723	2,077
For the three-month period ended September 30, 2002 (Unaudited)						
Balance as at the beginning of the period	1,478	(16)	(57)	-	840	2,245
Net loss for the period	-	-	-	-	(19)	(19)
Adjustments from translation of financial statements	-	-	4	-	-	4
Balance as at the end of the period	1,478	(16)	(53)	-	821	2,230

The accompanying notes are an integral part of the financial statements.

Statements of Changes in Shareholders' Equity (cont'd)

In terms of shekels of September 2003

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Proposed dividend subsequent to the balance sheet date	Retained earnings	Total
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the year ended December 31, 2002 (Audited)						
Balance as at the beginning of the year	1,480	(21)	(93)	-	906	2,272
Net loss for the year	-	-	-	-	(300)	(300)
Proposed dividend subsequent to the balance sheet date	-	-	-	99	(99)	-
Adjustments from translation of financial statements	-	-	28	-	-	28
Realization and reduction of reserves due to decline in value of investment	-	-	(5)	-	-	(5)
Issuance of capital	(4)	8	-	-	-	4
Balance as at the end of the year	1,476	(13)	(70)	99	507	1,999

The accompanying notes are an integral part of the financial statements.

Consolidated Statements of Cash Flows

In terms of shekels of September 2003

	For the nine months ended		For the three months ended		Year ended
	September 30 2003	September 30 2002	September 30 2003	September 30 2002	December 31 2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flows generated by operating activities:					
Net earnings (loss) for the period	251	(85)	94	(19)	(300)
Adjustments to reconcile net earnings (loss) to net cash flows generated by operating activities (A)	1,385	1,432	328	595	1,940
Net cash inflow generated by operating activities	1,636	1,347	422	576	1,640
Cash flows generated by investing activities:					
Investments in investee and other companies	(28)	(61)	(16)	(6)	(149)
Acquisition of fixed assets and other assets	(439)	(590)	(130)	(218)	(843)
Long-term loans granted	(36)	(20)	(29)	(2)	(23)
Sale (acquisition) of marketable securities, net	89	(224)	(16)	(81)	(96)
Investment grant in respect of fixed assets	35	23	22	16	56
Proceeds from sale of fixed and other assets	7	51	4	5	59
Collection of long-term loans	16	24	7	5	31
Short-term loans and deposits in banks, net	(274)	(51)	(258)	8	(33)
Proceeds from sale of investments in investee and other companies	36	12	24	-	25
Excess cost paid on acquisition of subsidiary and returned	-	-	-	31	-
Acquisition of newly consolidated subsidiaries (B)	-	(107)	-	-	(107)
Proceeds from sale of investment in formerly consolidated subsidiaries (C)	-	-	-	-	(3)
Net cash outflow generated by investing activities	(594)	(943)	(392)	(242)	(1,083)

The accompanying notes are an integral part of the financial statements.

Consolidated Statements of Cash Flows (cont'd)

In terms of shekels of September 2003

	For the nine months ended		For the three months ended		Year ended
	September 30 2003	September 30 2002	September 30 2003	September 30 2002	December 31 2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flows generated by financing activities:					
Issuance of convertible debentures and receipt of long-term loans	505	1,240	313	369	1,532
Repayment of debentures and long-term liabilities	(1,464)	(1,016)	(371)	(493)	(1,730)
Short-term loans, net	229	(500)	153	(182)	(252)
Proceeds from exercise of options of employees in the Corporation and in a subsidiary	3	16	-	4	26
Acquisition of shares of subsidiary by its subsidiary	(10)	-	-	-	-
Dividend paid	(98)	-	-	-	-
Dividend paid to minority shareholders of subsidiaries	(130)	(59)	(78)	(4)	(121)
Net cash inflow (outflow) generated by financing activities	(965)	(319)	17	(306)	(545)
Translation differences of cash balances in autonomous investees	(2)	4	5	6	4
Increase in cash and cash equivalents	75	89	52	34	16
Balance of cash and cash equivalents at the beginning of the period	148	132	171	187	132
Balance of cash and cash equivalents at the end of the period	223	221	223	221	148

The accompanying notes are an integral part of the financial statements.

Consolidated Statements of Cash Flows (cont'd)

In terms of shekels of September 2003

	For the nine months ended		For the three months ended		Year ended
	September 30 2003	September 30 2002	September 30 2003	September 30 2002	December 31 2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
A. Adjustments to reconcile net earnings (loss) to net cash flows generated by operating activities					
Income and expenses not involving cash flows:					
Group's equity in results of affiliates, net, less dividend	(45)	187	(40)	96	200
Minority interest in earnings of subsidiaries, net	183	163	59	62	188
Depreciation and amortization	592	616	205	227	1,008
Deferred taxes, net	178	136	78	53	133
Capital losses (gains), net	(53)	(12)	(9)	(18)	19
Inflationary erosion of long and short-term loans granted and increase in value of marketable securities, net	(34)	51	8	8	51
Inflationary erosion of short and long-term loans and liabilities received, net	(24)	(11)	(27)	(2)	(33)
Increase (decrease) in liability for employee severance benefits, net	39	15	(5)	(13)	13
	836	1,145	269	413	1,579
Changes in asset and liability items:					
Decrease (increase) in trade and other receivables	513	9	(15)	29	285
Decrease (increase) in inventories	(37)	233	32	42	46
Increase in trade and other payables	73	45	42	111	30
	549	287	59	182	361
	1,385	1,432	328	595	1,940

Consolidated Statements of Cash Flows (cont'd)

In terms of shekels of September 2003

	For the nine months ended		For the three months ended		Year ended
	September 30 2003	September 30 2002	September 30 2003	September 30 2002	December 31 2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
B. Acquisition of newly consolidated subsidiaries					
Working capital (excluding cash and cash equivalents)	-	(9)	-	-	(9)
Fixed assets, other assets and long-term receivables	-	(43)	-	-	(43)
Deferred taxes	-	(55)	-	-	(55)
	-	(107)	-	-	(107)

	For the nine months ended		For the three months ended		Year ended
	September 30 2003	September 30 2002	September 30 2003	September 30 2002	December 31 2002
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
C. Proceeds from sale of investment in formerly consolidated subsidiaries					
Working capital (excluding cash and cash equivalents)	-	-	-	-	(4)
Long-term investments, fixed assets, other assets and receivables	-	-	-	-	3
Long-term liabilities	-	-	-	-	(2)
	-	-	-	-	(3)
D. Non-cash transactions					
Acquisition of fixed assets on supplier credit	**25**	**-**	**25**	-	89

The accompanying notes are an integral part of the financial statements.

Note 1 - Reporting Principles and Accounting Policies

A. General

1. These interim financial statements have been prepared in accordance with generally accepted accounting principles applicable to the preparation of interim period financial statements.

2. The accounting policies applied in the preparation of these financial statements are consistent with those applied in the financial statements of December 31, 2002.

3. These financial statements have been prepared in an abridged form as at September 30, 2003 and for the nine-month and three-month periods then ended. They should be read in conjunction with the annual financial statements as at December 31, 2002 and for the year then ended and their related notes.

4. Commencing January 1, 2003, the Corporation applies Accounting Standard No. 14 regarding "Interim Financial Reporting", and Accounting Standard No. 15 regarding "Impairment of Assets". The first-time application of these standards did not have a material impact on the results of operations.

B. Financial statements in inflation adjusted values

The financial statements have been prepared on the basis of historical cost adjusted for the changes in the general purchasing power of the Israeli currency.

The comparative figures are also stated in terms of shekels of September 2003.

Details of the rates of change in the Consumer Price Index (hereinafter – "the CPI") and the representative rate of exchange of the U.S. dollar (hereinafter – "the dollar"):

	CPI	Representative exchange rate of the U.S. $
	%	%
During the nine-month period ended September 30, 2003	(1.49)	(6.25)
During the nine-month period ended September 30, 2002	6.99	10.30
During the three-month period ended September 30, 2003	(0.98)	2.99
During the three-month period ended September 30, 2002	0.65	2.14
During the year ended December 31, 2002	6.50	7.26

Note 1 - Reporting Principles and Accounting Policies (cont'd)

C. Disclosure of the impact of new accounting standards in the period prior to their application

– Accounting Standard No. 12, "Discontinuance of Adjusting Financial Statements for Inflation". According to this Standard, the adjustment of financial statements for the effect of the changes in the general purchasing power of the Israeli currency will be discontinued as of January 1, 2003.

In December 2002, the Israel Accounting Standards Board published Accounting Standard No. 17, according to which implementation of Standard No. 12 is deferred until January 1, 2004. Therefore, the adjustment of the financial statements will be discontinued as of January 1, 2004, and until December 31, 2003, the Company will continue to prepare adjusted financial statements according to Opinion No. 36 of the Institute of Certified Public Accountants in Israel. The inflation-adjusted amounts included in the financial statements as at December 31, 2003, will be the basis for the nominal financial reporting starting January 1, 2004. The effect of Standard No. 12 depends on the rate of inflation and on the sources financing of the Corporation and the investee companies.

– Accounting Standard No. 13 – "The Effect of Changes in Foreign Exchange Rates". The Standard deals with the translation of transactions in foreign currency and the translation of financial statements of foreign operations for the purpose of including them in the financial statements of the reporting entity, commencing January 1, 2003.

According to Accounting Standard No. 17, application of this Standard was postponed to January 1, 2004.

In the Company's estimation, the impact of this Standard is not expected to have a significant impact on its results of operations, financial position and cash flows.

Note 2 - Investments and Supplementary Information

A. Tower Semiconductor Ltd. (hereinafter – Tower)

(1) In February 2003, Tower, Israel Corporation Technologies (I.C. Tech) Ltd. (hereinafter – "I.C. Tech"), the primary Wafer partners, and an additional partner in Tower (hereinafter – "the Investors") consented to amend their agreements with Tower, in connection with the payment on account of the fifth milestone, in the amount of $41.0 million.
Pursuant to the amendment, upon receipt of the required approvals, the Investors will invest $24.6 million in Tower's capital ($4.4 million of which by I.C. Tech). The balance of the payment, in the amount of $16.4 million, is to be invested in Tower's capital, subject to an additional fundraising by Tower, in the amount of $26 million, no later than December 31, 2003.

Note 2 - Investments and Supplementary Information (cont'd)

A. Tower Semiconductor Ltd. (hereinafter – Tower) (cont'd)

In exchange for the initial investment, in the amount of $24.6 million (hereinafter – "the First Installment"), the Investors will receive ordinary shares of Tower based on a price of $3 per share (which constitutes the average price of Tower's shares in the 30 trading days prior to the decision of Tower's Board of Directors to amend the investment agreement). Regarding the balance of the payment, in the amount of $16.4 million (hereinafter – "the Second Installment "), the Investors will receive ordinary shares of Tower according to a price per share which is based on the share price at which Tower raises the additional amount of $26 million.

In addition, the primary Wafer partners were granted an option to convert, during January 2006, an amount of up to $13.2 million out of the amounts recorded as unutilized long-term customers' advances, to ordinary shares of Tower at a price which is based on the average trading price of Tower's shares in the 15 trading days prior to December 31, 2005. The amendment was subject to certain approvals, mainly of the banks – which was received subsequent to the balance sheet date (as stated in Section (4)).

(2) During the period of the report, further to the consent of the banks to provide Tower with interim financing in the amount of $67 million, the Investors transferred the amount of $15.9 million on account of the First Installment ($2.9 million of which by I.C. Tech).

As a result of the investment, I.C. Tech's share in Tower declined from 28.5% to 27.3%. The capital loss realized by the Group, in the amount NIS 7 million, was recognized by the Corporation in its financial statements for 2002.

(3) Subsequent to the balance sheet date, Tower, I.C. Tech, and the Investors agreed to amend their agreements with Tower and to invest the balance of the payment in respect of the fifth milestone, in the amount $25.1 million, with no contingency on raising of the additional funds by Tower, as stated in Section (1).

In consideration of the balance of the amount for the First Installment, totalling $8.7 million, Tower is to issue shares to I.C. Tech and the Investors based on a share price of $3 per share, and in consideration for the Second Installment, totalling $16.4 million, Tower is to issue shares based on a share price which is based on the price in the next issuance which Tower shall execute or the average trading prices of Tower's shares, if an issuance is not executed in the period determined.

Note 2 - Investments and Supplementary Information (cont'd)

A. Tower Semiconductor Ltd. (hereinafter – Tower) (cont'd)

The primary Wafer partners agreed to postpone use of the amounts recorded as long-term customers' advances, to which they are entitled in respect of their purchases in the years 2004–2006 and, in exchange, they were granted an option to convert any amount which may be used out of the advances in every quarter in these years to shares of Tower based on the average trading price of Tower's shares on the stock exchange on those dates. Alternatively, amounts not converted to shares as stated above, will be paid by Tower on December 31, 2007. Such amounts will bear interest of Libor + 2.5% which is to be paid on a current basis.

The amendment is subject to additional approvals including, among others, of the General Meeting of Tower's shareholders and the Investments Center.

(4) Subsequent to the balance sheet date, Tower reached an agreement with the banks regarding amendment of its credit facility agreements for the financing of FAB2. In the framework of the amendment, the Israel Corporation gave the banks a letter of commitment as part of the arrangements required by them for the granting of safety net by the main shareholders of Tower as a condition for the continued provision of financing by the banks to Tower.

1. In the letter of commitment it was provided that the security to be provided by the Israel Corporation relates to Tower's obligation to raise additional funds, in the amount of $152 million, by December 31, 2005 (in accordance with the dates and conditions as stated in the credit agreement (hereinafter – "the Additional Capital").

2. Pursuant to the letter of commitment, the banks are permitted, under certain conditions, to require Tower to issue a prospectus to its shareholders through an issuance of rights to acquire debentures convertible in shares of Tower as well as the issuance of options for the acquisition of Tower shares, all of this on the conditions provided in the letter of commitment. The amount of the issuance shall not exceed the amount which Tower did not succeed in raising in accordance with its obligation to the banks up to that time.

   Should Tower not be successful in issuing a prospectus on the required dates, the Corporation shall invest in Tower by means of a private offering of convertible debentures on the same terms as they would have been included in a public issuance.

3. The total amount of the Corporation's liability to invest in Tower pursuant to the letter of commitment, shall not exceed $50 million. The letter of commitment provides, that the investments of certain main shareholders in Tower, if made, shall be considered as fulfillment of the Corporation's liability under the letter of commitment (as detailed in the letter of commitment).

Note 2 - Investments and Supplementary Information (cont'd)

A. Tower Semiconductor Ltd. (hereinafter – Tower) (cont'd)

The Corporation's liability under the letter of commitment is given against the liability of the banks to provide, concurrent with execution of an investment by the Corporation, additional financing to Tower, in the amount of $43 million (in addition to credit of $500 million as provided in the credit agreement). The letter of commitment states that the banks will provide the financing as stated, in proportion to the amounts which the Corporation and certain shareholders provide, such that against every $50 provided by the Corporation and those shareholders, the banks will provide additional credit to Tower of $43.
In any event, the Corporation is not required to invest more than 50/93 of the amount which is to be raised at that time (including its share in respect of exercise of its rights as a shareholder).

4. The letter of commitment states, subject to the conditions therein, that certain amounts which the Corporation chooses to invest in Tower, whether through a public issuance or a private offering, even if the bank does not exercise its right to realize the security, shall be taken into account regarding the total amount of its liability under the letter of commitment, and this investment shall be considered as part of the Additional Capital.

5. The letter of commitment shall expire on the earlier of the following dates: (a) completion of the raising of $152 million by Tower as additional capital, as defined in Tower's credit agreement; (b) June 30, 2006; or (c) the date on which the Corporation (and the main shareholders in Tower) invests $50 million pursuant to the terms of the safety net.

6. Tower's credit agreement with the banks includes, among other things, a condition according to which the sale of Tower shares in excess of amounts determined in the agreement will convey to the banks the right to call the credit granted to Tower for immediate repayment. The said condition includes the gradual reduction over the years of the amount of shares the sale of which is limited. In any event, this limitation will not include Tower securities acquired by the Corporation or Group companies after the signing of the letter of commitment.

7. Tower agreed to indemnify the Corporation in the amount of up to $100 million, for expenses and damages stemming from claims caused to the Corporation as a result of its commitment to the banks to provide the safety net.

(5) Tower requested that the Investments Center approve the updated plan for construction of FAB2, in light of the fact that the period for the investments in FAB2 will be extended for more than 5 years from the date of receipt of the original approval from the Investments Center.

Tower's Management estimates that a satisfactory arrangement will be reached with the Investments Center.

Note 2 - Investments and Supplementary Information (cont'd)

A. Tower Semiconductor Ltd. (hereinafter – Tower) (cont'd)

(6) In the third quarter of the period of the report, the Corporation included its share in Tower's losses, in the amount of NIS 46 million while, on the other hand, it reduced the provision for decline in value for its investment in Tower (which was recorded in 2002), by the same amount. The Corporation's share in Tower's losses included for the period of the report amounts to NIS 40 million, net.

B. In the first quarter of the period of the report, Kol 1 Investments in Communications (H.L.) Ltd. (hereinafter – "Kol 1") sold its entire holdings (40%) in RSL Com Finland OY, in exchange for €14 million (of which €3.2 million is a repayment of shareholders' loans). Kol 1 realized a net, after-tax gain of roughly NIS 46.2 million.

C. As part of undertakings of ICL and certain of its subsidiaries (hereinafter – "the Companies") from December 2002, in agreements for the sale customer receivables in the framework of a securitization transaction, to a foreign company which was established for this purpose and which is not owned or controlled by ICL, the balance of the customer receivables sold for cash, as at the balance sheet date, amounted to NIS 1,053 million (December 31, 2002 – NIS 413 million).

The anticipated maximum amount of the financial means which will be placed at the disposal of the acquiring company, for purposes of acquiring the customer receivables of the Companies is approximately NIS 1,110 million, on a current basis, in such a manner that the proceeds to be received from the customers whose debts were sold, will be used for acquisition of new customer receivables.

D. During the period of the report, the shares of the Israel Corporation were consolidated, in such a manner that every ordinary share (Series 1) became an ordinary share of the Corporation, this being as a result of the amendment of the Income Tax Ordinance No. 132, 2002, which amended the Israel Corporation Ltd. Law, 1969) (hereinafter – "the Israel Corporation Law"). Pursuant to the amendment, some of the tax benefits provided in the framework of the Israel Corporation Law were cancelled and, therefore, there is no longer a need for the distinction which was made in the issuance in 2001 between the different classes of shares. Since the requirement to distinguish between the different classes of shares derived from the requirements of the Income Tax Commission, the Corporation requested and received written approval from the Income Tax Commission that, among other things, there is nothing preventing consolidation of the Corporation's different classes of shares traded on the stock exchange for income tax purposes. In addition, the Income Tax Commission notified the Corporation, that an issuance of shares by the Corporation commencing with the 2003 tax year will not adversely affect the exemptions and benefits to which the Corporation was entitled in the framework of the Israel Corporation Law.

Note 2 - Investments and Supplementary Information (cont'd)

E. On March 27, 2003, the Corporation's Board of Directors decided to distribute an interim cash dividend, in the aggregate amount of approximately NIS 99 million. The dividend was distributed on April 24, 2003.

On August 26, 2003, the Corporation's Board of Directors decided to distribute cash dividend, in the aggregate amount of approximately NIS 36 million. The dividend was distributed on October 2, 2003.

F. In the third quarter of the period of the report, the I.C. Tech invested $1.5 million in Oren Semiconductors Inc. (hereinafter – "Oren"). In addition, the Corporation converted a shareholders' loan, in the amount of $2.5 million, into shares of Oren. As a result of the investment and conversion of the loan, the Group's share in Oren's shareholders' equity increased from 17.7% to 23.5% and an excess of cost over book value was created, in the amount of $2.7 million, which was allocated to intangible assets. Up to the time of the increase in the rate of holdings, the investment in Oren was presented based on the cost method of accounting, whereas commencing with the third quarter of the period of the report, the investment is presented based on the equity method of accounting.

G. During the period of the report, the Corporation transferred the amount of $6.5 million to PSINet Europe B.V. (hereinafter – "PSINet"), as a shareholders' loan.

H. Subsequent to the balance sheet date, Sorbie Holding Ltd. (hereinafter - "Sorbie") and PSINet, affiliated companies of the Corporation (hereinafter - "the Companies"), entered into an agreement with other shareholders in the Companies (hereinafter - "the partners"), pursuant to which Sorbie acquired its shares from the partners. In addition, the partners transferred to the Corporation and the other shareholders in PSINet, their shares in PSINet. In exchange, the partners received two subsidiaries of the Companies. As a result of the transaction, the rate of the Corporation's share in Sorbie and PSINet increased to 61.4%.

I. Regarding exercise of the option for sale of Oil Refineries Ltd., see Note 3.

Note 3 - Concessions

<u>Oil Refineries Ltd.</u>

ORL operates in accordance with a concession it received to construct, operate and maintain facilities and auxiliary plants for purposes of refining mineral oils. The concession received the force of law pursuant to the Anglo-Iranian Oil Treaties Ordinance from 1938. The concession is valid up to October 2003.

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

On December 12, 2002, an arrangement was signed between ORL, the Government and the Israel Corporation in connection with all that involved with the period after expiration of the concession. Based on the arrangement, upon expiration of the concession period (October 18, 2003), all of ORL's rights deriving from the concession will terminate, and an arrangement will enter into effect according to which, subject to the conditions of the arrangement, the highlights of which are detailed below, ORL shall be permitted to continue to hold the assets it held on the eve of expiration of the concession (hereinafter – "the Assets"). The arrangement was made for 25 years, commencing October 18, 2003 (hereinafter – "the First Period"). ORL – or if it is split up into two separate refineries, each of the separate refineries – was granted an option to continue the aforesaid period for an additional 25 years, provided it notifies the Government no later than two years before the end of the First Period.

The arrangement provides that each side reserves the right to petition the court for clarification of the disagreement regarding the question whether or not all of ORL's assets return, by virtue of the historical concession, to the ownership of the Government without consideration, however in any case, any decision made regarding this matter will be implemented only at the end of the arrangement period (25 years or 50 years, as the case may be). If a final court decision is rendered, each side will be permitted to implement its provisions regarding recording of the rights in the Assets, provided such registration will not adversely affect the validity of the remainder of the arrangement's provisions and ORL's right to pledge the Assets in the ordinary course of its business, subject to the provisions of the arrangement. The arrangement conveyed to the State the right to record a caveat on the arrangement's content, on all the real estate assets, and to remove the caveat as stated at any time. Subject to theses provisions, no change shall be made to the recording of the Assets. During the arrangement period, ORL is permitted to execute transactions in the Assets in the regular course of business, and the decision in a disagreement with respect to the Assets shall apply to the proceeds from transactions as stated as well as to assets which ORL shall acquire in the future. A transaction in the Assets, except for a lien in the regular course of business, which does not exceed the period of the arrangement, requires approval of the Accountant General, who shall act in this matter in accordance with the Government's Decision No. 2796, dated November 25, 2002. The Government and ORL recorded caveats on the real estate which is the subject of the arrangement.

During the arrangement period, ORL shall pay to the Government annual permit fees in a fixed amount of $3 million plus additional annual amounts which are dependent on ORL's earnings, as follows: 8% of the annual earnings before taxes and permit fees, in the range of $0–$40 million; plus, 10% of the annual earnings before taxes and permit fees, in the range of $40–$70 million; plus, 12% of the annual earnings before taxes and permit fees, in the range of $70–$90 million. In any case, the amounts paid to the Government as permit fees shall not exceed (including the fixed payment) the amount of $11.6 million. All the amounts shall be translated into shekels in accordance with an exchange rate of $1 = NIS 4.80, linked to the CPI (base index of May 2002).

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

The "annual earnings before taxes" will be defined and measured based on annual, audited consolidated financial statements, and will include ORL's share in earnings or losses of subsidiary and affiliated companies having separate activities as well as capital gains and losses, however will not include gains and losses from activities through companies operating overseas or sale of the holdings in companies operating overseas.

Subsequent to the balance sheet date, ORL paid the first installment in accordance with the arrangement. The Accountant General in the Ministry of Finance notified ORL that the amount it paid was deposited in a separate account, so long as the conditions precedent stipulated in the arrangement of principles were not fulfilled. ORL responded to the Accountant General that the agreement was signed by the Government after all the required approvals had been received, and after its signature approvals of the Board of Directors of ORL and the Board of Directors of the Israeli Corporation were also received, and that upon the receipt thereof the agreement entered into effect. Therefore, the amount paid to the Government by ORL was properly paid pursuant to a valid agreement.

In the arrangement, the Government committed that if and to the extent possible, it will assist ORL in the transition without interferences from the concession period to the arrangement period (recognition of the existing construction, orderly licensing and construction processes, establishment of an industrial council).

Pursuant to the agreement, upon expiration of ORL's rights under the concession, ORL will be subject – commencing from the end of the end of the original concession period (October 18, 2003) and thereafter, to the construction and planning laws and additional local laws, in connection with the Haifa oil refinery. During 2002, the Manager of the Ministry of the Interior appointed an investigation committee for the boundaries of the Municipality of Haifa, Nesher and Kiryat Ata, Zvulun and the area of the oil refineries. During the period of the report, the Committee published its recommendations, pursuant to which the aforesaid area will be annexed to the Municipality of Haifa; the area will be administered by means of a joint governing body of the four local authorities bordering on the area, representatives of the factories operating therein, representatives of the public and representatives of Government ministries. The Committee also recommends that the governing body should handle all matters involved with running the area as an industrial area, similar to the definitions of a local industrial council in the Local Council Ordinance. The Committee further recommended that determination of the initial Municipal Tax levy shall be with the approval of the Minister of the Interior and it shall be imposed gradually (a discount shall be given which will be reduced from year to year over a 3–5 year period). ORL requested to present its position to the Minister of the Interior, which supports the establishment of a local industrial council in the area, prior to the reaching of a decision. If lands belonging to ORL are included within the boundaries of any local authority, ORL would be expected to be subject to Municipal Tax payments for the Haifa refinery as well.

ORL declared in the agreement that it is aware that the Government intends to initiate legislation which will govern the fuel industry, including regulation, which could affect the arrangement, even though there is no intention to affect the aspects of the arrangement which involve the Assets and the permit fees.

Note 3 - Concessions (cont'd)

<u>Oil Refineries Ltd. (cont'd)</u>

In addition, ORL declared that it is aware that the Government and the Israel Corporation agree to act regarding the matter of the split-up of ORL as detailed in the appendix to the agreement, which was signed between them and which constituted an integral part of the arrangement between the Government and the Israel Corporation.

During the period of the report, a petition was filed with the Supreme Court sitting as the High Court of Justice by the Israeli Society for Proper Government (hereinafter – "the Petitioner"), for the issuance of conditional and interim orders, which will direct the Prime Minister, the Minister of Finance, the Minister of National Infrastructures, the Government Companies Authority, ORL, the Israel Corporation and others, to provide reasons why they should not be prevented from acting in accordance with the arrangement and/or why they do not act to cancel the arrangement. The petitioner's main reasons are that the arrangement negatively impacts the principle of equality and equitable allocation, and it circumvents the tender laws by granting private parties a concession to use Government assets in a process having – based on the petitioner's contention – various deficiencies. The Court refused to grant the petitioner's request for interim orders which will prevent realization of the arrangement up to the time of the decision on the petition.

The Israel Corporation submitted its response to the petition, in the framework of which it expressed its position that there is no basis for the petition. ORL, in its response, objected to the petition and its reasoning and supported implementation of the arrangement.

The Petitioner once again submitted a request for interim orders which would prevent the Government from: taking steps to obtain an exemption from a tender for the arrangement, acquire or sell rights and/or shares of the Israel Corporation in ORL and to prepare a new agreement or revisions to the arrangement. Up to the date of publication of the financial statements, no orders were not issued.

On September 15, 2003, the Government decided to set up an inter-office team which will examine all of the issues affecting the Corporation at this time, directing attention to the letters of the Attorney General, dated July 7, 2003 and August 13, 2003. At first, the team will examine the agreement and the alternatives thereto, including, postponement of the date of the option held by the Israel Corporation, the agreement’s conditions, including the license fees determined therein, and the valuations performed by the Government and the Israel Corporation as a result of the agreement, and shall formulate its position. Taking into account its conclusions, the team is permitted to conduct negotiations with the Israel Corporation.

For detail of the Government's decision, see below.

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

In May 1996, the Government appointed a team of experts to examine the structure of the oil refining industry in Israel. In November 1996, the team submitted its recommendations. The basic thrust of the report, is to split ORL into two separately owned companies, one is to operate the Haifa refinery and the other the Ashdod refinery. Upon completion of the split-up, these companies will be allowed to enter the wholesale oil-marketing field and, later on, into the retail oil marketing field as well. In this situation of open competition, the control of oil prices at the refinery gate will be gradually removed. The team also does not see any reason for restricting the entry of the oil refining companies into the petrochemical field. The Board of Directors of ORL rejected the recommendations of the said team of experts.

In a meeting held on August 13, 1997, the Government resolved to empower the Minister of National Infrastructures and the Minister of Finance to appoint a panel which is to formulate a reform of the oil refining industry, while examining the possibility of application of the following principles:

Separation of ORL’s activities between the refining plant in Haifa and the refining plant in Ashdod, with the aim of creating two companies where, in at least one of which, there will be no Government ownership; removal of the control over prices of oil products at ORL’s refinery gate upon completion of separation of the activities and in accordance with the competitive developments in the refining industry; maintenance of the set-up of ORL’s activities with respect to the non-marketing of distillates; prevention of cross ownership which will cause development of non-competitive corporate structures in the fuel market and the refining industry; arrangement of the matter of ORL’s concession received from the British Mandate Authorities; combining the operations of the petrochemical plants with those of ORL and guidance of the team set up for the purpose of preparation of a proposed law for the fuel market, and inclusion in the proposed law the structure of the refining industry and rules for operation therein, in accordance with the decision.

In addition, the Government resolved to proceed with the building and operation of an additional port infrastructure for fuel and distillates in Ashkelon, as part of the efforts to permit the development of competition in the fuel products market.

Eilat Ashkelon Pipeline Co. Ltd. and Oil Infrastructures Ltd. have constructed a port for distillates in Ashkelon. The port was operated in April 2000.

On August 22, 1999, the Government decided, for purposes of encouraging competition in the refining industry in Israel, to take steps to promote competition between the Haifa refinery and the Ashdod refinery while separating the ownership thereof, and to adopt a governmental policy with respect to the structure of the fuel industry and the rules for operating therein, after completion of the process of separation of the two refineries as stated above, among other things, in according with the following principles:

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

1. Operations of the refineries in the area of marketing of refined oil products will be permitted in the manner which is determined in that decision (among other things: principles will be defined which permit the refineries to gradually enter into activities in the marketing area while examining the consequences of the marketing activities of each of the refineries on the competition in the fuel industry and while reviewing and defining the different marketing channels and methods in and through which the refineries will be permitted to operate; activities of the refinery in the marketing area, if and when allowed, shall be through a company which is separate from the company operating in the refining area; the Government shall act to obligate the refineries to ensure equal access on the part of all of the oil companies to purchase refined products; permitting the refineries to operate in the area of marketing of refined oil products shall be oriented such that they will not adversely effect the continued existence of the competitive conditions in all areas of the fuel industry, and particularly in the area of marketing of refined oil products by the filling stations).

2. Price control:

   The matter of the gradual removal of price controls over distillates sold at the refinery gate and based on the degree of competition which will develop in the industry shall be examined, and at the same time, control over 95 octane and 96 octane gasoline being sold by the filling stations shall also be looked into.

3. The operation of the two refineries in the petrochemical area shall be permitted in such a way that will assure them both an equal opportunity to operate in the area. The activities of the refineries in the petrochemical area shall be carried out in a manner which will assure full transparency of their activities.

It was also decided to appoint a joint team of representatives of the Ministries of National Infrastructures, Finance, Justice and the Government Companies Authority, which will act to arrange the matters referred to above in the appropriate legal framework.

In November 1999, ORL received from the Government Companies Authority, (hereinafter – “the Authority”) the text of “A Draft Decision to the Ministerial Committee for Privatization” (hereinafter – “the Draft Decision”) the gist of which is, the privatization of ORL by way of its split-up, such that after the conclusion of negotiations, the refinery in Ashdod will be transferred to the Corporation as a going concern, and no shares or rights of any kind in ORL will be retained by the Corporation. The Authority requested that, in accordance with Section 59B(c) of the Government Companies Law, 1975, ORL shall submit to the Authority the position of ORL's Board of Directors to the above Draft Decision.

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

On November 23, 1999, ORL's Board of Directors considered the above request of the Government Companies Authority, and decided in connection with the letter of the Government Companies Authority dated November 3, 1999 regarding the Government's decision of August 22, 1999, and the decision of the Ministerial Committee for Privatization dated October 20, 1999, that ORL views favorably the reorganization of the oil refining and the fuel industries in Israel and that in order to permit ORL's Board of Directors to relate positively to the proposal for privatization by means of the splitting up ORL, and out of concern for the well being of ORL, its stability, its ability to operate under competitive conditions, and the welfare of its employees, it is necessary to clearly define certain vital matters, which follow from the proposed decision to privatize, and which are of supreme importance to ORL:

Principles relating to the structure of the fuel industry subsequent to the split-up of ORL; structure of the split-up transaction; the tax implications of the split-up; assurance of the rights of ORL's employees; the capital structure of ORL following the anticipated split-up; the immediate arrangement of the matter of ORL's concession which will apply after its expiration; assurance of the fulfillment of ORL’s undertakings, including its commitment regarding the supply of raw material to the petrochemical industry.

It was also decided that after the receipt of the necessary clarifications regarding these matters, ORL's Board of Directors will convene to consider the proposal, to formulate its position with respect thereto, and to communicate its position to the Government Companies Authority, as requested by it in its letter of November 3, 1999.

Following this decision of ORL's Board of Directors, three work groups were set up, at the initiation of ORL, consisting of representatives of ORL, the Government Companies Authority, the Ministry of Finance and the Ministry of National Infrastructures, for the purpose of examining the various matters raised by the Board of Directors. As at the signing date of the financial statements, no answers had yet been received to the matters raised by the Board of Directors of ORL.

During 2000–2001, a committee appointed by the Minister of Finance and the Minister of National Infrastructures, reexamined the issue of the split-up of ORL and in 2001 submitted its conclusions. The committee recommended not to wait until the end of the concession and to immediately arrange the matters related to the end of the concession. In respect of the structure of the fuel industry and the split-up of ORL, the committee does not see any reason for changing the policy of the Government regarding the future structure of the fuel industry, as reflected in the Government decision dated August 22, 1999. Nevertheless, if it becomes necessary, the Government's decision will be amended so as to make it possible for ORL, in the opinion of the Government, to enter into the marketing sector and the petrochemicals area, and to remove the control over prices. The committee recommended conducting discussions with ORL and the Israel Corporation for the purpose of arranging the relationship with them in a manner which will facilitate implementing the Government decision regarding the split-up of ORL, while arranging, among other things, the issue of the end of the concession and finding a solution for the matter of treatment of the Assets at the end of the concession.

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

In Appendix C to the arrangement, dated December 2, 2002, regarding the matter of ORL's concession, an appendix which was signed by the Government and the Israel Corporation, the Israel Corporation committed to cooperate to the extent required by the Government, for purposes of split-up of ORL into two separate refineries (Haifa and Ashdod). A mechanism was also determined for performance of valuations as well as a mechanism regarding for sale of the Israel Corporation's shares in ORL or, in the case of a split-up of ORL, acquisition by the Israel Corporation of one of the two refineries and sale of the balance of the Israel Corporation's holdings in ORL, to the Government. In this case, the Israel Corporation will pay to the Government or receive therefrom, the difference between the relative value of the Israel Corporation's share in ORL (26%) and the value of the split-up refinery which it shall choose, based on the valuations performed pursuant to the arrangement.

The arrangement provides that in the case of a split-up of ORL into two separate refineries, each of the split-up refineries shall pay the Government license fees based on the internal allocation and brackets, in accordance with a determination to be made in the framework of the split-up arrangements, provided that the total license fees to be received by the Government from the two refineries is not more than or less than the amount the Government would have received from ORL had the split-up not been executed.

In the period of the report, the two aggregate valuations were submitted. One from an appraiser on behalf of the Israel Corporation, pursuant to which the total value of ORL is NIS 2,234 million, and the other from an appraiser on behalf of the Government, pursuant to which the total value of ORL is NIS 2,143 million.

On August 5, 2003, the Israel Corporation notified the Government that in light of the fact that the negotiations with the Government regarding participation of the Israel Corporation in the split-up have not been completed, and due to the dates provided in the appendix to the arrangement, it has decided not to exercise the option it was granted in Appendix C to the arrangement, to participate in the split-up of ORL into two separate refineries and, therefore, the provisions of Section 4 of that Appendix shall apply, according to which the Israel Corporation shall sell to the Government or to a party which the Government shall instruct, all shares of ORL owned by the Israel Corporation, within 30 days, at a price which constitutes an average between the two aggregate valuations of ORL, this being subject to certain monetary adjustments.

Nonetheless, the Israel Corporation is prepared to continue the negotiations with the Government regarding its participation in the split-up.

The Government is permitted to instruct that the execution date of the sale transaction shall be postponed for an additional period which shall not exceed two years from June 6, 2003.

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

The Israel Corporation clarified, that at this point, it can not be known whether the transaction will ultimately be consummated, taking into account, among other things, the following items:

1. The results of the judicial decision with respect to the petition filed by the Israeli Society for Proper Government (as described above).
2. The need for approvals which according to the Government's position (with which the Israel Corporation disagrees) are required by law, including a tender exemption.
3. The results of the negotiations (if held) with the Government regarding the matter of the Israel Corporation's participation in the split-up of ORL into two separate refineries, one in the Haifa Bay and the other in Ashdod.

On September 15, 2003, the Government made the following decision: "Further to Government Decisions No. 126, dated August 22, 1999, and No. 2796, dated November 25, 2002, the decision of the Committee of Ministers for Privatization Matters DH/2, dated October 20, 2001, and the agreement signed between the Government and the Israel Corporation, dated December 2, 2002, which has not yet received all the required approvals (hereinafter – "the Agreement"), to advance the split-up of ORL and the privatization thereof, in the following manner:

1. To set up an inter-office team which will include representatives of the Ministry of Finance, Ministry of National Infrastructures, Ministry of Justice and the Supervisor of Restrictive Business Practices. The work of this team will be managed by the Ministry of Finance.

2. The team will examine all of the issues affecting ORL at this time, directing attention to the letters of the Attorney General, dated July 7, 2003 and August 13, 2003. At first, the team will examine the agreement and the alternatives thereto, including, postponement of the date of the option held by the Israel Corporation, the agreement's conditions, including the license fees determined therein, and the valuations performed by the Government and the Israel Corporation as a result of the agreement, and shall formulate its position. Thereafter, and in accordance with its positions, as stated, it shall examine, among other things, the most appropriate and efficient way for executing the split-up of ORL and the privatization thereof and arranging the holdings of each of the split-up refineries in investee companies, directly and indirectly by ORL. The team is authorized to make a decision regarding the matter of postponement of the date of the option, as stated, and there is no need to include this matter in the framework of the team's recommendations, as stated in Section 5.

3. Taking into account its conclusions in Section 2, the team is permitted to conduct negotiations with the Israel Corporation with respect to, among other things, split-up of ORL and the ownership structure in ORL and its investee companies, directly or indirectly, after the split-up.

Note 3 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

4. In addition, the team will make recommendations with respect to the target structure, including supervision of prices, the reciprocal relationships which will remain between the two oil refineries, including, principles regarding the transfer of input materials between them and between them and the petrochemicals industry and additional areas of activity for the separate refineries or for the controlling interests therein, including the dates from commencing the activities as stated.

5. The team is to submit its recommendations within 30 days for approval by the Committee of Ministers for Privatization Matters or approval by the Committee of Ministers for Society and Economic Matters, as will be determined by the Minister of Finance, and it is permitted to submit partial recommendations regarding urgent matters within 20 days. The team's recommendations regarding Section 4, may be submitted within 60 days.

6. Up to 30 days after submission of the team's conclusions, and taking such conclusions into account, the Manager of the Companies Authority shall submit, in coordination with the Supervisor of Budgets, the Attorney General, Ministry of National Infrastructures, Ministry of Justice and the Restrictive Business Practices Authority, a proposed decision to the Committee of Ministers for Privatization Matters regarding privatization of ORL by means of its split-up and sale of the Government's holdings after the split-up. The proposed decision is to relate to, among other things, to the extent necessary, the following matters:

   A. Split-up of ORL into two sister companies: ORL Haifa Ltd. (hereinafter – "ORL–Haifa") and ORL Ashdod Ltd. (hereinafter – "ORL–Ashdod"), such that all the assets, rights, liabilities and employees involved with the refining activities in Haifa shall remain in ORL–Haifa, and all the assets, rights, liabilities and employees involved with the refining activities in Ashdod shall be transferred to ORL–Ashdod.

   B Determination of the ways for privatization and the course for sale of the Government's holdings in ORL–Haifa and ORL–Ashdod after the split-up.

   Up to the publication date of the financial statements, the inter-ministerial team had not yet submitted its recommendations.

In the assessment of ORL, all that stated above regarding the arrangement, if it is decided on the implementation thereof and such implementation is, in fact, effected, will have a material impact on ORL, however, at this stage, ORL is not able to estimate and quantify such impact on its financial position and results of operations. The management of the Israel Corporation adopts the assessment of ORL.

Note 4 - Contingent Liabilities and Commitments

A. Beginning in 1994 and subsequent thereto, subsidiaries of ICL (hereinafter – the Bromine Group) received notifications of third and fourth party claims filed against them, by U.S. companies that were sued in U.S. Courts (among others, in the framework of two class actions), by approximately 30,000 plaintiffs contending to be former banana plantation workers, mainly from Central America, the Caribbean Islands, Africa and the Philippines (hereinafter – the plaintiffs). The plaintiffs claim that they suffered bodily injury in the past as a result of exposure to a chemical substance during the period of their employment, many years ago, which was produced by a number of producers, which included a substance produced by ICL, including large chemical companies, and which was supplied to companies engaged in the growing of bananas (hereinafter jointly – "the defendants") during an aggregate period of about thirty years (1960–1990).

A large part of the aforesaid proceedings have been transferred by the U.S. Court to the countries of plaintiffs' domicile, however, appeals regarding various aspects of the relevant judicial decisions are still pending before a number of U.S. appellate courts. In most of the above-mentioned proceedings, the Bromine Group companies were named as direct defendants.

In the framework of the hearings being held at various judiciary levels of the U.S. courts, the U.S Supreme Court recently ruled that ICL, due to its not being a first level subsidiary of the State of Israel, is not entitled to Federal jurisdiction. At this stage, ICL is unable to assess the impact of this decision on the proceedings or other proceedings involving possible claims regarding the chemical substance mentioned above.

During the time that the aforementioned proceedings have been carried on, most of the plaintiffs have reached compromise arrangements with most of the defendants. The Bromine Group is mentioned in these compromise arrangements, as a party that is included in the claims release documents of the above claims. At this stage, it is not possible to estimate the effect of the abovementioned compromise arrangements on the claims for indemnification and reimbursement that were lodged against the Bromine Group. It should be noted that there are claims of approximately 5,000 plaintiffs (possibly even more), who are not parties to the aforementioned compromise arrangement.

The Bromine Group companies maintain that there is an absence of responsibility or liability on their part. They also maintain that there is a lack of jurisdiction with respect to them regarding these legal proceedings. In addition, the Bromine Group estimates, that the quantities of chemicals supplied by it, if any, was small as compared to the quantity supplied by the other producers being sued in the abovementioned proceedings.

In the opinion of the management of the Bromine Group, in the relevant time periods, the Group had a certain amount of insurance coverage covering the events which are the subject of the claims, although there are disagreements, with at least some of the insurers regarding the coverage and its extent. The Bromine Group is presently engaged in a legal proceeding that was submitted against such insurers in respect of that mentioned above.

Note 4 - Contingent Liabilities and Commitments (cont'd)

A. (Cont'd)

In January 2003, The Bromine Group was informed of six claims filed in Nicaragua by 350 claimants, apparently for alleged damages from use of the aforementioned chemical product. The defendants also include a subsidiary of ICL. Since the process has not yet been served to the subsidiary, it is not required to issue a response. The statement of claim has also not been submitted to the subsidiary and, accordingly, the exact nature of the claim is not known.

Since the claims in question are for personal injury, they do not stipulate any amounts. Nevertheless, since there are thousands of plaintiffs, if they are successful in their claims, the amounts the Bromine Group will have to pay, net of the amounts recognized and paid by the insurers, could be substantial.

Management of the Bromine Group and its legal counsel are unable to estimate the effect of these claims at this stage. Therefore, no provision has been made in the financial statements in respect of the possible outcome of these claims.

B. Contrack-Line Ltd. (hereinafter – Contrack) has filed a suit in the Tel-Aviv District Court against Dead Sea Works Ltd. (hereinafter – DSW) and against others, for infringement of a patent regarding a dredge which was designed for crushing salt mushrooms and with respect to the violation of other alleged rights of the plaintiff regarding the dredge.

The District Court ruled that DSW had violated the patent. In respect of this ruling an appeal was submitted to the Supreme Court, which held a hearing thereon in October 2002. The Court transferred the matter for mediation, with the consent of the parties. Mediation proceedings between the parties were not successful and the case is pending hearing of the appeal.

Concurrent with the appeal and on the basis of the aforementioned ruling, Contrack filed a financial claim with the District Court against DSW in the amount of $52 million in respect of the damages/loss it incurred. Contrack requested an exemption from the court fee and the Court permitted Contrack to pay a token fee in the amount of NIS 10 thousand in respect of a claimed amount of up to $20 million. Both sides have submitted appeals on this decision. Rendering of a decision on these appeals has been deferred until after the decision on the appeals which are in the Supreme Court.

DSW has recorded a provision in its books which, in its estimation, based on the opinion of its legal counsel and taking into account the above-mentioned development in the proceedings, is sufficient to cover any exposure arising from such proceedings.

Note 4 - Contingent Liabilities and Commitments (cont'd)

C. On May 29, 2001, a class action suit was filed against Fertilizers and Chemicals Ltd. (hereinafter – Fertilizers) and other defendants, under the Abatement of Environmental Nuisances Law (Civil Actions), 1992. In the claim, the plaintiffs contend that the defendants are polluting the Kishon stream. The plaintiffs request that the Court issue an order to cease the discharge of wastes into the Kishon and to restore the stream to its condition prior to discharge of the wastes.

On June 13, 2001 and on May 22, 2002, December 31, 2002, and March 20, 2003, monetary claims in the total amount of $30 million were filed against Fertilizers and many other defendants regarding the dumping of wastes into the Kishon stream, which allegedly caused the plaintiffs to contract cancer. These claims are in addition to other claims filed against Fertilizers with respect to bodily injuries and economic damages allegedly caused to the plaintiffs as a result of pollution of the Kishon stream, for which the plaintiffs claim that Fertilizers is also responsible. In the opinion of the management of Fertilizers, based on the opinion of its legal counsel handling the claims, it is not yet possible to evaluate the risk inherent in the claims and, therefore, no provision has been included in the financial statements in respect thereof.

D. In addition to the contingent liabilities mentioned above, there are a number of claims pending against ICL and some of its subsidiaries (including legal claims). Regarding some of the claims there is insurance coverage and partial provisions have been recorded on the books. In the opinion of the managements of the companies, based on the opinion of its legal advisors, the provisions included in the financial statements are adequate. With respect to claims regarding which it is not possible at this point to estimate the amounts thereof or to predict their outcomes, no provisions have been including in the financial statements.

E. For additional details in connection with the contingent liabilities, see Note 21B of the Corporation's financial statements as at December 31, 2002.

F. In July 2003, certain shareholders of Tower filed a claim in a U.S. court against Tower, certain of its directors, certain Wafer partners and main investors, including the Israel Corporation. The plaintiffs, which have requested, among other things, that their claim be certified as a class action, have raised contentions under the U.S. Securities Law from 1934, in connection with inaccurate reports and omission of information by the defendants in material sent to the shareholders of Tower in April 2002 relating to approval of the amendment of Tower's investment agreements with its Wafer partners and main investors in capital.

Tower and the Corporation believe that the claim has no basis and they intend to vigorously oppose it.

Note 5 - Business Segment Information

	Fertilizers													
	Potash	Phosphate	Eliminations	Total	Industrial products	Agricultural products*	Performance products	Metallurgy	Shipping	Energy	Technology & communication	Other activities	Eliminations & unrelated expenses	Total consolidated
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the nine month period ended September 30, 2003														
Segment sales	**2,555**	**1,701**	**(77)**	**4,179**	**1,598**	**262**	**1,675**	**250**	**-**	**-**	**-**	**341**	**(604)**	**7,701**
Segment results*	**549**	**26**	**2**	**577**	**7**	**69**	**122**	**(42)**	**63**	**43**	**(52)**	**20**	**(21)**	**786**
For the nine month period ended September 30, 2002														
Segment sales	2,100	1,592	(78)	3,614	1,773	297	1,568	276	-	-	-	300	(549)	7,279
Segment results*	454	61	3	518	26	92	150	(46)	(34)	(38)	(66)	14	2	618
For the three month period ended September 30, 2003														
Segment sales	912	707	(30)	1,589	539	138	602	81	-	-	-	120	(235)	2,834
Segment results*	182	-	-	182	(13)	41	40	(14)	51	(12)	(1)	7	(8)	273
For the three month period ended September 30, 2002														
Segment sales	807	598	(31)	1,374	581	157	550	92	-	-	-	95	(213)	2,636
Segment results*	148	33	1	182	9	61	50	(13)	-	(21)	(30)	(1)	1	238

* The results of each segment includes part of the results of affiliated companies and amortization of excess cost.

Note 5 - Business Segment Information (cont'd)

	Fertilizers													
	Potash	Phosphate	Eliminations	Total	Industrial products	Agricultural products*	Performance products	Metallurgy	Shipping	Energy	Technology & communication	Other activities	Eliminations & unrelated expenses	Total consolidated
	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)	(Audited)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Year ended December 31, 2002														
Segment sales	2,698	1,995	(99)	4,594	2,304	397	2,090	362	404	-	-	-	(748)	9,403
Segment results*	548	24	-	572	36	120	200	(62)	14	(21)	(28)	(99)	(5)	727

* The results of each segment includes part of the results of affiliated companies and amortization of excess cost.