Israel Corporation Limited

Financial Statements
As at September 30, 2004
(Unaudited)

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Contents

Directors' Report to the Shareholders of
Israel Corporation Ltd.

For the Nine Months Ended September 30, 2004

DESCRIPTION OF THE CORPORATION AND ITS BUSINESS ENVIRONMENT

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 57% by the Ofer Group, and 20% by Bank Leumi Le-Israel B.M.

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.

After three years of recession in the world economy, a turnaround is discernible in the international markets in areas in which the Corporation operates – the chemicals, shipping and energy fields.

The Corporation took advantage of the recession years to execute reorganization and efficiency measures, improve its cash flows and make strategic acquisitions in the fertilizers' and shipping areas.

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 fully controlled subsidiary, and is also actively involved in the strategic planning and business development of the investee companies.

This Directors' Report is submitted as part of the financial statements for the period ended September 30, 2004, and on the assumption that the reader is also in possession of the said financial statements. This report has been prepared in a condensed format for the aforementioned period on the assumption that the reader is also in possession of the Directors' Report and the financial statements for 2003.

CHANGES IN THE INVESTMENT PORTFOLIO

A. Tower Semiconductor Ltd. (hereinafter – Tower)

(1) In January 2004, Tower issued, by means of a prospectus published to the public in the United States, approximately 11.4 million ordinary shares at a price of $7 per share for a net consideration of $75.1 million (including partial execution of the options granted to the underwriters).

In addition, Tower issued shares to Israel Corporation Technologies (I.C. Tech) Ltd. (hereinafter – "I.C. Tech"), the primary Wafer partners, and an additional partner in Tower (hereinafter – "the Investors") based on a price of $7 per share for a consideration of $16.4 million, which was transferred to Tower in December 2003.

As a result of the public issuance, and after issuance of the share capital to the investors, I.C. Tech's share in Tower declined to 21.7%, and the Group realized a capital gain of NIS 29 million.

(2) In November 2003, Tower reached agreement with the banks regarding amendment of its credit facility agreements for the financing of FAB2. In the framework of amendment of the agreements, Israel Corporation gave the banks a letter of commitment as part of the arrangements required by them for the granting of a security net by Tower's main shareholders as a condition for the continued provision of financing by the banks to Tower.

The total amount of the Corporation's liability to invest in Tower pursuant to the letter of commitment shall not exceed $50 million.

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).

As at the signing date of the financial statements, the balance of the Corporation's liability under the above-mentioned letter of commitment is $36 million.

Regarding Tower's compliance with financial covenants, see the section in this report dealing with Tower.

B. On February 5, 2004, the Corporation acquired all of the State's shares in ZIM Integrated Shipping Services Ltd. (formerly – "ZIM Israel Navigation Co. Ltd.") (hereinafter – "ZIM") and, in addition, during the period of the report the Corporation acquired part of the holdings of the other shareholders in ZIM. In total, the Corporation acquired 49% of ZIM's shares at a cost of NIS 517 million. As at the balance sheet date, the Corporation holds approximately 98% of ZIM's share capital.

The excess of the cost over the net asset value totaled NIS 22 million, and was allocated to the fleet of ships and its equipment that is included in the fixed assets category.

Up to December 31, 2003, the Corporation presented its investment in ZIM based on the equity method. As of January 1, 2004, ZIM's financial statements were consolidated for the first time. The Corporation's share in ZIM's results was calculated for the period from the acquisition date to the end of the period of the report.

C. In the second quarter of the period of the report, ZIM sold two ships, for a consideration of $70 million. The two ships will be leased to ZIM for a period of five years. The after-tax capital gain created to ZIM totals $22 million, and Israel Corporation's share of the gain is approximately NIS 95 million.

D. ZIM signed agreements for sale of five ships that will enter into effect upon delivery of the ships (2 ships in November 2004 and 3 ships in January 2005). The proceeds from sale of the ships amounts to $180 million and the after-tax capital gain to be realized by ZIM will total $20 million in the fourth quarter of the year of account and $32 million in the first quarter of 2005. The Corporation's share of the gain is approximately NIS 88 million and NIS 140 million, respectively. The ships are to be leased to ZIM for a period 5–6 years.

E. In the second quarter of the period of the report, Israel Chemicals Ltd. (hereinafter – "ICL") sold its investment in Negev Industrial Minerals Ltd. (as well as in a sister company related thereto), for a consideration of $20 million. ICL's after-tax capital gain totals NIS 21 million and Israel Corporation's share is approximately NIS 11 million.

F. In the period of the report, the amount of the Corporation's investment in Oil Refineries Ltd. (hereinafter – "ORL") based on the equity method of accounting increased above the exercise price of the option. The exercise price of the option derives from the Corporation's notification to the Government on August 4, 2003, according to which, the Corporation decided, by virtue of the provisions of Appendix C of the Arrangement, to exercise the option to sell all its shares of ORL at a price constituting an average between the two overall valuations of ORL, subject to certain adjustments (see also Effect of External and Other Factors).

Pursuant to the above, the Corporation set its investment in ORL at the exercise price of the option, in the amount of NIS 596 million, which is NIS 88 million less than the amount of the investment based on the equity method of accounting.

G. In the third quarter of the period of the report, PSINet Europe B.V. and Sorbie Holding BVI, subsidiaries of the Corporation held at the rate of 62% (hereinafter – "the PSI Group"), sold a number of their investee companies in Europe, in two separate transactions, for an aggregate consideration of $112 million. Up to the balance sheet date, $90 million was received in cash. Part of the balance of the consideration is scheduled to be received during 2005 and part thereof is contingent on adjustments and conditions spelled out in the agreements. The Corporation's share in the after-tax gain realized amounts to NIS 201 million.

The companies sold constituted a separate component and operated in the communications area. Upon sale of the companies, the Corporation no longer has activities in the communications area. Therefore, the investment in the PSI Group is presented in accordance with Accounting Standard No. 8 – "Discontinued Operations". The assets and liabilities attributable to the discontinued activities have been presented in separate categories, after the fixed assets category and the minority interest category, respectively. In the statement of earnings, the earnings from the discontinued activities are presented after the share of the minority interest (including the capital gain realized from the sale as stated above). In addition, the cash flows from the discontinued activities are classified separately in the statement of cash flows from the cash flows from continuing activities.

The impact of discontinuance of the activities on the Corporation's financial-statement categories is not significant, except for the capital gain as stated above.

FINANCIAL POSITION

The total assets, as at September 30, 2004, amounted to NIS 21,897 million, compared with NIS 15,446 million, as at September 30, 2003. The increase derives mainly from the first time consolidation of the financial statements of ZIM.

The balance of the long-term investments, loans and receivables as at September 30, 2004 amounted to NIS 1,356 million, compared with NIS 1,533 million as at September 30, 2003.

The long-term liabilities, as at September 30, 2004, amounted to NIS 9,400 million, compared with NIS 6,410 million, as at September 30, 2003. The increase derives mainly from the first time consolidation of the financial statements of ZIM.

The Corporation's working capital as at September 30, 2004 amounted to NIS 851 million, compared with working capital of NIS 583 million as at September 30, 2003.

The Corporation's shareholders' equity as at September 30, 2004 amounted to NIS 3,238 million, compared with NIS 2,069 million as at September 30, 2003, and NIS 2,170 million as at December 31, 2003.

The cash flows from operating activities in the period of the report amounted to NIS 1,805 million, compared with NIS 1,629 million in the corresponding period last year.

The cash flows in third quarter of the period of the report amounted to NIS 611 million, compared with NIS 421 million in the corresponding quarter last year.

SOURCES OF FINANCING OF THE CORPORATION AND THE HEADQUARTERS COMPANIES

As at September 30, 2004, the total financial liabilities of the Corporation and its wholly-owned and controlled headquarters companies (hereinafter – "the Headquarters Companies"), amounted to NIS 2,588 million.

As at September 30, 2004, the Corporation and the Headquarters Companies had investments in liquid assets of NIS 699 million, invested, primarily, in treasury bills and corporate debentures in CPI-linked and unlinked channels, and in medium-term dollar debentures.

During the period of the report, the Corporation received a long-term loan in the amount of $60 million, which it used to finance acquisition of ZIM's shares from the State.

During the period of the report, the Corporation issued non-marketable debentures to institutional investors, in the amount of NIS 200 million, which are repayable in one lump-sum payment in 2009. This liability was swapped from a shekel CPI-linked liability to a dollar liability.

During the period of the report, the Corporation and the Headquarters Companies repaid current maturities of long-term loans in the amount of NIS 222 million (including NIS 42 million which were scheduled to be repaid up to December 2004).

During the period of the report, NIS 26 million par value of debentures (Series 1) were converted into 37,481 ordinary shares of the Corporation and, correspondingly, the Corporation's liabilities were reduced by NIS 26.5 million.

RESULTS OF OPERATIONS

The Corporation ended the period of the report with earnings of NIS 1,051 million, compared with earnings of NIS 250 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 $168.7 million compared with earnings of $89.3 million in the corresponding period last year.

B. ZIM Integrated Shipping Services Ltd. (hereinafter – "ZIM") finished the period of the report with earnings of $115.2 million compared with earnings of $28.8 million in the corresponding period last year.

C. Oil Refineries Ltd. (hereinafter – "ORL") finished the period of the report with earnings of NIS 554.8 million, compared with earnings of NIS 162.4 million in the corresponding period last year. The Corporation reduced its share in ORL's earnings by NIS 88 million (see Section on Changes in the Investments Portfolio).

D. Tower Semiconductor Ltd. (hereinafter – "Tower") finished the period of the report with a loss of $114.4 million, compared with a loss of $68.3 million in the corresponding period last year.

   In the period of the report, the Corporation included its share of Tower's losses in the amount of NIS 110 million and, at the same time, it reduced the provision for decline in value of the investment in Tower (which was recorded in 2002) by NIS 106 million.

E. The results for the period of the report include non-recurring income, in the net amount of NIS 459 million, compared with non-recurring expenses of NIS 10 million in the corresponding period last year.

   The non-recurring income is composed mainly of capital gains, in the amount of NIS 348 million, and from a change in the Companies Tax rates, in the amount of NIS 120 million (See also Section on Events Occurring during the Period of the Report and Thereafter).

   In the period of the report, the Corporation's earnings without non-recurring items amounted to NIS 592 million, compared with earnings of NIS 260 million in the corresponding period last year.

The Corporation finished the third quarter, with earnings of NIS 491 million, compared with earnings of NIS 94 million, in the corresponding quarter last year.

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

A. ICL – finished the third quarter with earnings of $61.8 million compared with earnings of $29.0 million in the corresponding quarter last year.

B. ZIM – finished the third quarter with earnings of $39.4 million compared with earnings of $23.1 million in the corresponding quarter last year.

C. ORL – finished the third quarter with earnings of NIS 219.1 million, compared with a loss of NIS 47.7 million in the corresponding quarter last year. The Corporation decreased its share in ORL's earnings by the amount of NIS 51 million. (See Section on Changes in the Investments Portfolio).

D. Tower – finished the third quarter with a loss of $39.4 million, compared with a loss of $37.1 million in the corresponding quarter last year. The Corporation included its share in Tower's losses in the third quarter, in the amount of NIS 38 million while, on the other hand, it reduced the provision for decline in value of its investment in Tower by NIS 34 million.

E. The results for the third quarter include non-recurring income, in the net amount of NIS 208 million. In the corresponding quarter last year there were no non-recurring income or expenses. The non-recurring income is composed mainly of capital gains, in the amount of NIS 212 million.

As an investments company, the Corporation's financial results are affected by the results of its investee companies as well as from non-recurring income/expenses.

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 $168.7 million, compared with earnings of $89.3 million in the corresponding period last year.

In the period of the report, a significant recovery was visible in most of ICL's target markets, mainly due to the improvement in economic growth in North America and Asia. ICL also enjoyed an increase in demand in the fertilizers and industrial products segments, as well as a strengthening of the euro, the British pound and the Japanese yen against the dollar compared with the corresponding period last year.

The ICL Group has endeavored to take full advantage of the market potential, particularly in improving the balance of demand versus supply in most of the target markets, and enjoyed rising prices in almost all areas of its activities. As a result, in the period of the report there was a sharp improvement in the earnings from the ICL Group's activities, this being despite the continued struggle with the high marine bulk shipping prices, from the upward revaluation of the shekel–dollar exchange rate, the high prices of some of its raw materials and the sharp increase in fuel prices.

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 measures.

Sales of the ICL Group totaled $1,969 million in the period of the report, compared with $1,707 million in the corresponding period last year, an increase of 15.3%.

The increase in the sales of the ICL Group reflects an increase in turnover in all of the Group's areas of activities, both as a result of a quantitative increase as well as due to an increase in prices The upward revaluation of the euro and the British pound against the dollar also contributed to the increase in revenues from sales in Europe.

There was an increase in the selling and marketing expenses in the period of the report by 12.6% compared with the corresponding period last year, this being mainly due to an increase in the marine bulk shipping prices of products in the fertilizers sector owing to an increase in world tariffs, and due to the upward revaluation of the shekel and the euro against the dollar.

The administrative and general expenses increased by 9.2% in the period of the report over the corresponding period last year. The increase stems mainly from the upward revaluation of the shekel and the euro against the dollar, as well as from non-recurring expenses to outside consultants and other expenses, including for reorganization of activities.

Due to the changes in the Companies Tax rates, ICL's tax expenses decreased by $18 million, such change being reflected in the second quarter of the period of the report. The tax expenses in the period of the report also include an adjustment of amounts of the losses for tax purposes which are expected to be utilized in the upcoming years.

ICL finished the third quarter of the period of the report with earnings of $61.8 million, compared with earnings of $29.0 million in the corresponding period last year, an increase of 113%.

Sales of the ICL Group in the third quarter of the period of the report amounted to $678 million, compared with $587 million in the corresponding quarter last year, an increase of 15.5%.

The increase sales reflects an increase in turnover in all of the ICL Group's areas of activities, stemming from an increase in prices along with an increase in sales in some of the segments. The increase in the exchange rate of the euro compared with the dollar also contributed to the increase in revenues from sales in Europe.

There was an increase in selling and marketing expenses in the third quarter of the period of the report, due to an increase in bulk shipping costs relating to products in the fertilizers sector owing to an increase in tariffs globally, and an upward revaluation of the exchange rate of the euro compared with the dollar. The administrative and general expenses remained at about the same level as in the corresponding period last year, this being despite the upward revaluation of the euro against the dollar, this being thanks to efficiency and savings measures taken by the ICL Group.

Severe flooding in the stream channels, which took place on October 29, 2004, caused the flooding of a large section of the premises of part of ICL's facilities in Sdom and the entry of water and large-scale drainage into the evaporation pools at the Dead Sea. As a result of the flooding, the work at the power and production station in part of ICL's facilities in Sdom was halted for a number of days. Due to the floods, ICL sustained property damage and also suffered a loss of profits. At this stage, ICL is unable to estimate the extent of the damage, however, beyond the insurance deductible, in the net amount of $8.5 million, insurance coverage exists in connection with the damages.

Subsequent to the balance sheet date, a company in the ICL Group received an approval in principle from the Minister of National Infrastructures, for the granting of a license for the production of electricity by means of power and heat facilities (line – generator). The facilities that are the subject of the approval will operate at a production level of between 400 and 700 megawatts. Granting of a private producer's license pursuant to the approval is conditioned on construction of a power station and compliance with additional milestones that have not yet been obtained.

ZIM INTEGRATED SHIPPING SERVICES (FORMERLY – ZIM ISRAEL NAVIGATION CO. LTD.)

ZIM finished the period of the report with earnings of $115.2 million compared with earnings of $28.8 million in the corresponding period last year.

ZIM's revenues in the period of the report amounted to $1,818 million compared with $1,502 million in the corresponding period last year, constituting an increase of 21%. The increase in revenues reflects an increase of 10% in the average shipping price per container and an increase of 8.2% in the quantity of containers shipped, compared with the corresponding period last year.

The leasing expenses in the period of the report increased by 45% and the fuel prices rose by 54% over the corresponding period last year.

The tax expenses amounted to $26.4 million in the period of the report, compared with expenses of $15.0 million in the corresponding period last year.

The cash generated by operating activities amounted to $149 million compared with $92 million in the corresponding period last year.

ZIM finished the third quarter of the period of the report with earnings of $39.4 million compared with earnings of $23.1 million in the corresponding quarter last year. The sales in the quarter increased by 25% over the corresponding quarter last year.

During the period of the report, Zim entered into an agreement for acquisition of three ships. The ships were delivered to ZIM in the months March to July 2004. Pursuant to the agreement, the ships will be leased to the seller for a period of two years. After the lease period, the ships are expected to be integrated into ZIM's fleet of ships.

In the second quarter of the period of the report, ZIM sold two ships, for a consideration of $70 million. The two ships were leased to ZIM for a period of five years. The after-tax capital gain created to ZIM will total $22 million.

ZIM entered into agreements for sale of 5 ships, which will enter into effect upon delivery of the ships (2 ships in November 2004 and 3 ships in January 2005). The proceeds from sale of the ships amounts to $180 million. The after-tax capital gain that ZIM will realize totals $20 million in the fourth quarter of the year of account and $32 million in the first quarter of 2005. The ships are to be leased to ZIM for periods of 5–6 years.

During the period covered by the report, there was a work strike at Israel's ports. The strike affected ZIM's operational and commercial activities. The timetables for the scheduled voyages of the ships operated by ZIM were interrupted, and a shortage of containers was created in various regions. As a result, the regular service to customers throughout the world was adversely affected. A small portion of the additional expenses caused by the strike was collected from ZIM's customers. In addition, owing to the strike, ZIM was unable to transport cargo due to the unavailability of ships and equipment that, in turn, caused a loss of income.

Regarding the plan for equipping 12 ships, see the Section on Various Activities in the Period of the Report and Thereafter.

TOWER SEMICONDUCTOR LTD.

During the period of the report, Tower's sales totaled $96.0 million, compared with $41.6 million in the corresponding period last year.

The cost of sales in the period of the report amounted to $162.2 million, compared with $75.8 million in the corresponding period last year. The increase in the cost of sales is explained mainly by recording of the depreciation and amortization of FAB2. Tower placed FAB2 into service in the third quarter of 2003, and beginning with this date it commenced recording depreciation expense.

Tower finished the period of the report with a loss of $114.4 million, compared with a loss of $68.3 million in the corresponding period last year.

In the period of the report, the financing expenses totaled $20.9 million, compared with $4.3 million in the corresponding period last year.

Tower finished the third quarter of the period of the report with a loss of $39.4 million, compared with a loss of $37.1 million in the corresponding quarter last year.

The sales in the third quarter amounted to $35.1 million, compared with $16.1 million in the corresponding quarter last year. The cost of sales also increased due to the increase in depreciation and amortization expenses relating to FAB2.

During the period of the report, Tower raised the amount of $75.1 million, net, through the public issuance of 11.4 million shares on the NASDAQ.

During 2003, Tower requested that the Investments Center approve the revised 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, based on discussions held with the Investments Center, that the reaching of a satisfactory arrangement regarding this matter is probable.

According to the Facility Agreement with the banks, Tower is required to comply with certain financial ratios and covenants. As at the balance sheet date, Tower was in full compliance with these financial ratios and covenants. Due to the recent and current slowdown in the semiconductor markets, Tower's Management estimates that it is possible that Tower will not comply with certain of the financial ratios and covenants.

Tower is presently preparing an updated work plan for 2005 for FAB2 which will be based on the prevailing and Tower's forecast of the market conditions. Accordingly, if required, Tower's Management intends to request its banks to agree to amend the financial ratios and covenants in order to align them with the updated work plan for FAB2 for 2005. Tower's Management estimates that it probable that satisfactory agreements with the banks will be achieved. According to the Facility Agreement, satisfying the financial ratios and covenants is a material provision. Achieving arrangements with the banks is essential to the continued equipping, operation and construction of FAB2.

The Facility Agreement provides that if as the result of any default whatsoever, the banks were to accelerate Tower's obligations Tower would be obligated, among other things, to immediately repay all loans made by the banks (which as at the balance sheet date amount to $497 million), and the banks would be entitled to exercise the remedies available to them under the Facility Agreement, including realization of the liens recorded on Tower's assets.

Subsequent to the balance sheet date, Tower reported that it is taking a series of efficiency measures the goal of which is to conform the level of its capital and operating expenses to the current market conditions and to those conditions that are expected in the near future. Tower is planning to reduce its work force by 12%. Completion of implementation of the efficiency measures is expected to take place by December 31, 2004 and is expected to save $20 million in 2005, compared with the current level of expenses.

Regarding the Corporation's share in Tower's results, see the Section on Results of Operations.

OIL REFINERIES LTD.

ORL finished the period of the report with earnings of NIS 555 million, compared with earnings of NIS 162 million in the corresponding period last year.

The refining sector finished the period of the report with operating earnings of NIS 630 million, compared with operating earnings of NIS 88 million in the corresponding period last year.

The accelerated economic growth in China and India that joined the growth in the United States resulted in an increase in the demand for fuel products. The terrorist activities in Saudi Arabia, the continued lack of American control in Iraq, the lack of stability in Nigeria and the hurricanes in the Gulf of Mexico, all contributed to the significant increase in crude oil prices. The average price of one barrel of crude oil during the period of the report increased to approximately $41.6.

As at the signing date of the financial statements, the global fuel production and refining systems are operating at almost full capacity.

Margin on refining activities ($ per ton):

	January – March	April – June	July– September	January– September
2004	25.0	35.7	46.8	35.1
2003	23.0	17.5	16.5	19.0

For the entire 2003 year, the average margin per ton was $19.7.

In the period of the report, ORL's total sales amounted to NIS 13,655 million compared with NIS 10,448 million in the corresponding period last year, an increase of 31%.

In the period of the report, there was an increase in the cost of manufacturing and in the administrative and general expenses over the corresponding period last year, mainly due to the concession fees which were not included in the corresponding period last year, as well as due to a provision for future salary expenses.

During the period of the report, the financing expenses amounted to NIS 158 million, compared with financing income of NIS 66 million in the corresponding period last year. The large fluctuations in the financing expenses between the reported periods derive mainly from the impact of the devaluation or real upward revaluation of the shekel versus the dollar. In the period of the report, there was a devaluation of the shekel exchange rate by 2.4% versus the dollar, compared with a real upward revaluation of 4.8% in the corresponding period last year.

ORL finished the third quarter of the period of the report with earnings of NIS 219 million, compared with earnings of NIS 48 million in the corresponding quarter last year.

The gross profit in the third quarter amounted to NIS 417 million, compared with gross profit of NIS 96 million in the corresponding quarter last year.

In the third quarter of the period of the report, the financing expenses amounted to NIS 25 million, compared with financing income of NIS 107 million in the corresponding period last year.

Reduction of the Companies Tax rates caused a decline in ORL's tax expenses of NIS 134 million in the second quarter of the period of the report.

During the period of the report, ORL raised NIS 648 million by means of a private issuance of debentures (mostly index-linked).

Regarding the Corporation's share in ORL's results, see the Section on Results of Operations.

EXPOSURE TO MARKET RISKS AND RISK MANAGEMENT

During the period of the report, there was no sugnificly material change with respect to market risks and their management as they were reported in the Directors' Report as at December 31, 2003.

EFFECT OF EXTERNAL AND OTHER FACTORS

A. <u>The ORL concession</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 ended in October 2003.

On December 2, 2002, an arrangement was signed between ORL, the Government and 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 these 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).

A. The ORL concession (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.

Upon expiration of the original concession and in accordance with the arrangement, ORL began paying license fees under the arrangement. In the period of the report, ORL recorded a provision of NIS 42 million in its financial statements for the first nine months of the year. 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 in the name of the Government after all the required approvals had been received by the parties authorized on behalf of the Government to sign it, and after it was signed, approvals of the Board of Directors of ORL and the Board of Directors of Israel 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 date of the arrangement (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 2003, 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, which believes that the correct solution is establishment of a local industrial council in the area, requested to present its position to the Minister of the Interior. The Minister of the Interior rejected ORL's request for a hearing and a decision has not yet been made regarding the municipal allocation. Upon inclusion of lands belonging to ORL within the boundaries of any local authority, it is expected that ORL will begin paying Municipal Tax for the Haifa refinery as well. In the period of the report, ORL received a charge for Municipal Tax relating to the 2004 year. Pursuant to a legal opinion received by ORL, as at the signing date of the financial statements ORL was not subject to an obligation to pay Municipal Tax in accordance with the charge notification it received. In 2003, ORL prepared and submitted a site plan for the Haifa refinery site.

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 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 Israel Corporation.

A. <u>The ORL concession</u> (cont'd)

On June 4, 2003, 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 Director of the Government Companies Authority, ORL, 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 that will prevent realization of the arrangement up to the time of the decision on the petition.

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 Israel Corporation in ORL and to prepare a new agreement or revisions to the arrangement.

On January 19, 2004, the Supreme Court, at the invitation of all the parties to the proceeding, including the Corporation, decided, among other things, that "the respondents are permitted to continue negotiations among themselves to change the conditions of the agreement which is being attacked by the petition and even to sign a new agreement, provided that up to the time the matter is brought before the Court for the second time no irreversible actions shall be taken and that the present situation shall continue".

On March 28, 2004, May 5, 2004 and July 12, 2004, the Government requested and received additional extensions from the Court for provision of its position regarding the petition.

On August 9, 2004, the Government submitted a notice to the Court wherein was stated, among other things, that on July 29, 2004, the Ministerial Committee for Society and Economic Matters (Social and Economic Cabinet) made a decision determining the manner in which the split up of ORL and its privatization are to be executed, which imposes on the Accountant General the responsibility to amend, up to October 15, 2004, "Appendix C of the Agreement", in accordance with the principles detailed in the decision (for the sake of good order it is noted that the "Agreement" is the arrangement signed on December 2, 2002, between Israel Corporation and ORL and the Government, as detailed at the beginning of this note, whereas "Appendix C of the Agreement" was signed between Israel Corporation and the Government relating to the relationship between the shareholders of ORL, as will be explained in this note below). It was also determined in the Government's notice that if Israel Corporation does not agree to amendment of "Appendix C of the Agreement", in accordance with the principles of the decision, the "Agreement" will be cancelled and unilateral steps will be taken by the Government. (Detail of the content of the decision of the Ministerial Committee of July 29, 2004, is presented in this note below). At the end of its notification, the Government added the following language:

"8. Therefore, the respondents request that the decision of the Honorable Court of January 19, 2004 be applied such that the petitioner will submit an amended petition or reference to the decision within 20 days, based on the date fixed in the decision. The case was scheduled for hearing, pursuant to the decision, and the respondents will be able to submit their response to the amended petition at the time of the hearing.

9. The respondents do not object to scheduling an urgent hearing of the petition. However, in the opinion of the respondents the hearing should be scheduled for the end of October, since then it will possible to present to the Honorable Court a signed appendix, or it will be possible to give notice of cancellation of the Agreement."

A. The ORL concession (cont'd)

On August 11, 2004, the Court decided that: "taking into account the Government's decision of July 29, 2004, the petitioner is requested to respond to the decision of the respondents dated August 9, 2004, primarily to that stated in Section 8 of such notice. In any similar case, it would seem, that the petition should be amended based on the Government's aforementioned decision".

In a preliminary response, dated August 8, 2004, Israel Corporation notified the Court that it takes the position that the provisions of the "Agreement" must be honored, since it is a binding agreement duly signed, including the provisions of "Appendix C of the Agreement", this being for the reasons well detailed in the Corporation's response to the petition. In this response, the Corporation once again clarified its position that there is no and will be no legal basis that can serve as a foundation (not even in the first instance) for cancellation of the "Agreement", in whole or in part, as well as any of its appendices – with all that deriving and implied thereby. Nonetheless, Israel Corporation notified that it was and continues to be ready to negotiate with the Government with respect to "Appendix C of the Agreement", and it will consider its position regarding this matter, after taking into account, among other things, the content of the decision of the Ministerial Committee dated July 29, 2004.

On August 26, 2004, the petitioner received permission from the Court to submit an amended petition. Up to the signing date of the financial statements, the Israeli Corporation has not been notified regarding the filing of an amended petition by the petitioner.

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 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 4 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 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 Israel Corporation, 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 Israel Corporation's shares in ORL or, in the case of a split-up of ORL, optional acquisition by Israel Corporation of one of the split-up two refineries. In this case, Israel Corporation will pay to the Government or receive therefrom, the difference between the relative value of 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.

B. The splitting of ORL's facilities into separate ownerships (cont'd)

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

In June 2003, the two aggregate valuations were submitted. One from an appraiser on behalf of 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 4, 2003, Israel Corporation notified the Government that in light of the fact that the negotiations with the Government regarding participation of 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 Israel Corporation shall sell to the Government or to a party which the Government shall instruct, all ORL shares owned by 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, 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 September 6, 2003.

Israel Corporation clarified, in the framework of an Immediate Report, that at this point, it cannot 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 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 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 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.

B. The splitting of ORL's facilities into separate ownerships (cont'd)

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 30, 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 Israel Corporation, the agreement's conditions, including the license fees determined therein, and the valuations performed by the Government and 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 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 Accountant 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.

As a result of the recommendations of the inter-office team appointed by the Government, the Committee of Ministers for Social and Economic Matters made the following decision on July 29, 2004: "Further to Government Decisions No. 126, dated August 22, 1999, No. 2796, dated November 25, 2002, and No. 787, dated September 15, 2003, the decision of the Committee of Ministers for Privatization Matters MH/2, dated October 20, 1999, the agreement signed between the Government and Israel Corporation Ltd. (hereinafter – "Israel Corporation") and Oil Refineries Ltd. (hereinafter – "ORL") dated December 2, 2002, which has not yet received all the required approvals (hereinafter – "the Agreement"), as follows:

B. The splitting of ORL's facilities into separate ownerships (cont'd)

1. To execute the split-up and privatization of the refineries during the years 2004–2005, in accordance with the outline detailed below:

   1.1 In the first stage, the refinery in Ashdod will be sold as activities, or in a private sale as a subsidiary or a separate company with an ownership structure identical to the ownership of ORL, and immediately thereafter a public issuance of ORL will be made.

   1.2 The refinery in Ashdod will be sold as a "going concern". In the framework of the process of sale of the refinery in Ashdod the purchaser will undertake to operate the refinery for a period of not less than 10 years from the acquisition date.

   1.3 If necessary, principles for reciprocal relationships will be formulated during the split-up process that will apply between the refineries, including with respect to sale of intermediate products and feedstock materials between them, and between them and the petrochemicals industry.

2. To impose on the Accountant General in the Ministry of Finance the responsibility of amending Appendix C to the Agreement in the framework of a new agreement with Israel Corporation, which will be approved in accordance with Section 16 of the Agreement, such that Sections 3, 4, and 5 of Appendix C to the Agreement will be amended and superseded pursuant to the principles attached as Appendix A to the Government's decision, and the rest of the Sections will remain unchanged, all of this up to October 15, 2004. In the framework of amendment of Appendix C, the following principles, among others, will be expressed:

   2.1 Israel Corporation will sell together with the Government all the holdings of the refineries.

   2.2 The accountings with Israel Corporation shall be made after completion of privatization of ORL, as will be detailed in the new agreement that amends Appendix C to the Agreement.

3. To impose on the Supervisor of the Government Companies Authority to submit to the Ministerial Committee for Privatization, no later than October 15, 2004, a proposal for split-up and privatization of the refineries on the basis of the outline as stated in Section 1, above. The process of split-up and sale of the refineries will be conducted and executed by the Government Companies Authority as is customary, including by means of mechanisms it determines for purposes of execution of the split-up and advancement of the privatization. In addition, provisions and limitations were determined in the privatization decision regarding ownership of the split-up refineries, among other things, as detailed in notification of the Supervisor of Restrictive Business Practices, as stated in Section 5, below. Commencing from the date that will be determined in the privatization decision, ORL will move to operating based on a separate optimization model for the two refineries, as will be detailed therein.

4. In the framework of the split-up and privatization process, issues relating to ORL employees will be handled, and to the extent necessary this will be reflected in the privatization decision.

5. To record the notification of the Supervisor of Restrictive Business Practices regarding his position with respect to matters within the scope of his responsibility in the area of regulation of the fuel industry, which are attached as Appendix B to the Government's decision. In addition, to record the notification of the Minister of National Infrastructures regarding his intention to enact the Fuel Industry Law, which will deal with, among other things, arrangement of the regulation in various sectors of the fuel industry.

B. The splitting of ORL's facilities into separate ownerships (cont'd)

6. To impose on the Minister of Finance and the Minister of National Infrastructures to amend the Order for Supervision of Prices of Goods and Services, 1992, no later than October 15, 2004, in such a manner that after the split-up and privatization of the refinery in Ashdod, the supervision of refined oil products at the refinery gate will be removed, except for supervision of the prices of refined oil products where more than 50% of their total consumption in the local market is sold by one of the refineries and, at the same time, less than 15% of their total consumption in the local market is sold by the other refinery. After removal of the supervision as stated, re-imposition of supervision of the price of any refined oil product at the refinery gate will be examined in light of the competitive conditions existing in the refining sector in the fuel industry, and in accordance with all law.

7. After sale of the refinery in Ashdod, in principle there is nothing preventing operating of a refinery in the area of production of electricity and desalination of water, in accordance with and subject to all law.

8. If Israel Corporation does not agree with the principles stated in Section 2 – to cancel the agreement, and to take unilateral steps available to the Government in connection with split-up and privatization, among other things in light of the Government's position regarding ownership of ownership of ORL's in the area of the concession.

Regarding this matter, see above also the report regarding the petition filed against the agreement dated December 2, 2002.

Up to the signing date of the financial statements, the Israel Corporation has not yet been informed that a proposal to split up and privatize the oil refineries on the basis of the outline stated in Section 1 to the Decision of the Committee of Ministers for Welfare and Economics, dated July 29, 2004, has been submitted to the Committee of Ministers.

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 and the results of its operations.

The management of Israel Corporation adopts the assessments of ORL, and believes, based on legal opinions, that the agreement dated December 2, 2002, is a valid agreement.

C. Montreal Protocol

Pursuant to the treaty known as the Montreal Protocol, to which Israel is a party (and which was also adopted during the period of the report in the Regulations accompanying Israeli domestic law), production and consumption of methyl bromine for soil fumigation in developed countries are being gradually reduced to zero by the year 2005. Recently, discussions are being carried on between the countries that are parties to the Protocol regarding the possibility of changes in the rate and timing of the reduction of the manufacture and consumption of methyl bromine in the developed countries as explained above. At the end of March 2004, a special meeting of the parties to the Protocol was held, where decisions were made regarding approval of quantities for manufacture and consumption of methyl bromine for soil fumigation purposes in developed countries, which are defined as "critical uses", for 2005. The quantities approved for manufacture and sale in 2005 are about the same as the quantities approved in 2003 and 2004. During 2004, discussions are to be held regarding "critical uses" for 2006 and 2007. Sales of methyl bromine for soil fumigation to developing countries, is expected to continue until 2015, however they are to be reduced by 20% commencing with 2005. Sales during the period of the report, to which the prohibition will apply in 2006, if there are no changes in the rate of the reduction of the manufacture for critical uses in 2006 and 2007, as stated above, were $39 million and the operating earnings in respect thereof came to $13 million.

C. Montreal Protocol (cont'd)

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.

ICL's strategy is to remain in the area of soil fumigation even after the prohibition against use of methyl bromine for soil fumigation, as stated, goes into effect. Therefore, in the past several years efforts have been made to develop, license and market new and substitute uses of methyl bromine in this important market. In the third quarter of the period of the report, ICL received a license in Israel and in the United States for an initial product in a new family of products in the area of soil fumigation, and ICL is getting ready to begin selling the product in 2005.

Sales of the agricultural products in the industrial products sector during the period of the report for uses and to customers which, to the extent currently known, will not be covered by the production and marketing prohibition in 2006, amounted to $34 million. The operating earnings with respect to these sales were $11 million.

D. One of ICL's subsidiaries, Fertilizers and Chemical Products Ltd (hereinafter – "Fertilizers") is located close to the Haifa port. Over the course of many years, Fertilizers as well as local authorities and other factories, have dumped waste into the Kishon stream which is located near Haifa. In the 1980's, operation of a purification facility was started, which reduces the concentration of certain contaminating agents in waste dumped by the said factories.

In 2001, a class action suit was filed against Fertilizers and 3 other defendants, wherein it is claimed 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 stream and to restore the stream to its condition prior to discharge of the wastes. The State of Israel and many factories and local authorities were joined to the claim as third parties.

In 2000, due to reports that soldiers of the Israel Defense Forces that trained in the Kishon stream developed cancer, the Chief of the General Staff appointed a committee to examine the existence of dangerous substances in the area of the Kishon stream and whether such materials as stated were likely to cause the development of cancer by soldiers who trained in the stream. Despite the fact that the committee determined that most of the said soldiers have no proofs indicating a circumstantial connection between contamination of the stream and the cancer, in the view of the minority there was a circumstantial connection as stated. This report, which was published in 2003, is not admissible in the court in Israel.

Additional claims were filed against various other parties, including the State of Israel, local authorities and government agencies, as well as against Fertilizers. The claims are in the aggregate amount of $138 million and are for bodily injury and property damage, and include additional damages that were not estimated in cash in the statement of claim, such as, future loss of wages and medical expenses as a result of the alleged contamination of the Kishon stream.

In the opinion of ICL, at this stage it is not possible to quantify the financial exposure in the framework of the circumstances relating to the Kishon stream, as described above, since the claims are pending and are in the initial stages and ICL is likely to be a third party to additional claims. Nonetheless, the cost of restoration of the Kishon stream and the liabilities for bodily injury and property damage could be very high. Should Fertilizers be required to participate in the cost of the restoration or the cost of the damage payments as stated, its operating results may be adversely affected to a significant extent.

E. An affiliated company, ORL, is a defendant in some of the claims enumerated in Section D., above. See Note 18B2 to the financial statements as at December 31, 2003.

During the period of the report, 94 plaintiffs, former soldiers in the Israel Defense Forces, filed claims against ORL and three other parties, in respect of bodily injuries which they allege were caused to them, as a result of activities within the framework of their military service, in the Kishon stream, after their request to join the claim of a soldier in the Navy was not accepted. One of the defendants filed a third-party notification against ORL. A statement of defense has not yet been filed, and due to the early stage of the proceeding it is not possible, in ORL's opinion, based on its legal advisors, to predict the claim's chances of success.

F. In February 2004, ICL became aware that the Prosecutor of Environmental Crimes of Catalonia, Spain, initiated a criminal proceeding, in the framework of which an account was filed with the Magistrate's Court in Messarat, Spain, against present and former managers in a company in ICL's fertilizers sector, which operates mines in Spain, wherein it is alleged that managers violated the local law and caused contamination of subterranean water due to permeation of salt compounds which were dumped from the mine sites during the course of many years, partly prior to acquisition of the company by ICL Fertilizers. The Court was also requested to issue an order forbidding the continued dumping of the salt compounds. As at the date of the report, no order, as stated, was issued. ICL Fertilizers estimates, based on the opinion of its legal advisors, that the probability of such an order, as aforesaid, being issued, as this stage, is low. If an order, as stated, is issued and it is not changed during the legal process – such matter will have a material impact on the mining activities in the site.

G. 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 Israel Corporation and I.C. Tech. 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 and Exchange Act of 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. In August 2004, the claim was summarily dismissed in full by a court in New York. In September 2004, one of the leading plaintiffs gave notice of his intention to file an appeal against the decision. The U.S. court determined timetables in connection with the appeal.

Tower and the Corporation intend to vigorously oppose the claim.

EVENTS OCCURRING DURING THE PERIOD OF THE REPORT AND THEREAFTER

A. In January 2004, Prof. Itzhak Ben-Israel was appointed as a director of the Company.

B. In March 2004, Mr. Ohad Marani commenced serving the Chairman of the ORL's Board of Directors.

C. In April 2004, Ms. Anat Keynan, ceased serving as a director of the Company.

D. In August 2004, Ms. Yocheved Dvir was appointed as an external director of the Company.

E. Pursuant to a collective agreement signed in 1978 with employees of Dead Sea Works (DSW), Sdom employees leave on early retirement upon reaching the age of 58, provided they worked at Sdom for 25 years, or at the age of 60, provided they worked at Sdom for 20 years. On September 16, 2001, a judgment was handed down by the District Labor Court in Be'er Sheva with respect to the claim of an employee of DSW which held that the "early retirement" clause in the collective agreement between the company and its employees should be viewed as conveying to the employees a right to retire and not as imposing on them an obligation to retire. DSW appealed the District Labor Court's decision to the National Labor Court. On March 18, 2004, the decision on the appeal was rendered. The National Labor Court accepted DSW's appeal in part and reversed the District Labor Court's determination pursuant to which DSW's employees have a right to take early retirement in place of an obligation to retire. The decision ruled that the existing early retirement arrangement is null and void, however it held that this ruling will become effective 6 months after the date the decision was rendered in order to allow the parties to determine during such period a new and detailed arrangement covering early retirement of the Sdom employees on a basis which conforms with the requirements of law and the existing case law. Since the six-month period ended but the negotiations have not yet been completed, it was agreed between the parties that during another period of six months ending March 17, 2005, DSW will permit Sdom employees regarding which the conditions for early retirement stipulated in the cancelled retirement section are fulfilled during the said additional period, to take early retirement. The parties agreed that the said agreement will cease to apply and to automatically control at the end of the additional period.

F. In the second quarter of the period of the report, Tower and the chipmaker, Siliconics Incorporated (hereinafter – "Siliconics"), an 80.4% subsidiary of Vishay Intertechnology, signed a long-term agreement for the manufacture of semiconductors.

Siliconics is to order semiconductor wafers from Tower that are to be manufactured in the Tower's FAB1 factory, in the aggregate amount of $200 million, during a period of 7 to 10 years. Of this amount, Tower is to supply Siliconics semiconductor wafers having a value of $53 million within the first three years from the date of transfer of the technology.

In August 2004, Siliconics transferred to Tower an advance deposit, in the amount of $20 million, mainly for acquisition of the equipment necessary in order to manufacture the products. This amount will serve as a credit against Siliconics' future purchases of the products.

G. On September 29, 2004, the Law for Amendment of the Income Tax Ordinance (No. 140 and Temporary Order), 2004 (hereinafter – "the Amendment") was passed by the Knesset. The Amendment provides for gradual reduction of the tax rates for companies, from the rate of 36% to the rate of 30%, in the following manner: in the 2004 tax year the tax rate will be 35%, in the 2005 tax year the tax rate will be 34%, in the 2006 tax year the tax rate will be 32%, and in the 2007 tax year and thereafter the tax rate will be 30%.

The current taxes and balances of deferred taxes as at September 30, 2004, are computed in accordance with the new tax rates as determined in the Amendment. The effect of the change in the consolidated financial statements in the period of the report is a decrease of tax expenses of NIS 161 million. The impact on the net income amounts to NIS 120 million.

H. On August 30, 2004, the Audit Committee and the Corporation's Board of Directors, decided to approve a transaction of ZIM regarding equipping by ZIM of additional ships, a transaction that is related the controlling shareholders in the Corporation.

The subject of the transaction is the acquisition by ZIM of 12 ships, including 8 container ships having a capacity of 4,250 containers each, that are scheduled to be delivered to ZIM during 2006 and 2007 and 4 container ships having a capacity of 6,350 containers each, that are scheduled to be delivered to ZIM during 2008 and 2009. 2 out of the 8 ships having a capacity of 4,250 containers will be acquired by ZIM by means of assignment of the rights to acquire the ships of a foreign company controlled by a foreign trust related to the family of Mr. Sami Ofer (hereinafter – “Zodiac”). 4 out of the 8 ships having a capacity of 4,250 containers will be acquired by means of assignment of the rights to acquire the ships, by 4 joint foreign companies (in equal shares) of ZIM and Ofer Shipping Ltd. (a company controlled by the Corporation’s controlling shareholders (hereinafter – “the Joint Transaction”). The ships will be acquired at a price of $54.21 million per ship, this being at the same price and on the same terms (back to back) that the ships were acquired. Out of the 8 ships having a capacity of 4,250 containers, ZIM will lease 2 ships from Zodiac for a period of 10 years, for a lease fee of $23,000 per day per ship. ZIM will also lease 4 ships that are to be acquired by the Joint Transaction for a period of 10 years, for a lease fee of $23,000 per day per ship. Out of the 4 ships having a capacity of 6,350 containers, ZIM will purchase 2 ships from companies in the Zodiac Group, one for a price of $74.3 million and the other for a price of $74.1 million. Sale of the ships will be at the same price and on the same terms (back to back) that the companies in the Zodiac Group acquired the said ships. 2 of the 4 ships having a capacity of 6,350 containers will be leased by ZIM from companies in the Zodiac Group for a period of 10 years, for a lease fee of $31,500 per day per ship.

The Corporation’s Board of Directors decided to convene a General Meeting in order to approve the transaction.

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

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

We direct attention to that stated in Note 4 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 impacts which cannot be estimated at this stage, of the aforementioned matters on its financial position.

The Corporation's Board of Directors expresses its appreciation to the employees and officers of the Corporation and of the Group companies, in Israel and overseas, for their devoted service and contribution to the advancement of the Group's operations.

Idan Ofer	**Yossi Rosen**
Chairman of the Board of Directors	**Chief Executive Officer**

November 23, 2004

The Board of Directors
Israel Corporation Limited

Dear Sirs:

Review of the unaudited interim consolidated financial statements as at September 30, 2004

At your request, we have reviewed the interim consolidated balance sheet of Israel Corporation Ltd. as at September 30, 2004, 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 50.5% of the total consolidated assets as at September 30, 2004 and whose revenues constitute 66.9% and 68.1% of the total consolidated revenues for the nine-month and three-month periods then ended, respectively. Furthermore, we received reports of other auditors of affiliated companies, the investment in which, as at September 30, 2004, is approximately NIS 911 million and the Company's equity in their earnings is NIS 86 million and NIS 12 million for the nine-month and three-month periods ended on that date, respectively.

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 interim consolidated 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 direct attention to that stated in Note 4 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 impacts which cannot be estimated at this stage, of the aforementioned matters on its financial position.

Sincerely,

Somekh Chaikin
Certified Public Accountants (Isr.)

November 23, 2004

Consolidated Balance Sheets as at

	September 30 2004	September 30 *2003	December 31 *2003
	Reported amounts(1)	Adjusted amounts(2)	
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current assets			
Cash and cash equivalents	**893**	222	139
Marketable securities	**652**	625	697
Short-term loans and deposits	**386**	346	266
Trade receivables	**2,658**	1,070	1,193
Other receivables	**561**	840	692
Inventories	**2,335**	2,275	2,405
	7,485	5,378	5,392
Long-term investments, loans and receivables			
Investments in investee companies	**958**	1,133	1,200
Investments in other companies	**259**	248	246
Long-term deposits, loans and receivables	**69**	75	69
Inventories	**70**	77	63
	1,356	1,533	1,578
Fixed assets	**11,958**	7,676	7,608
Other assets and deferred expenses	**817**	850	830
Assets attributable to discontinued activity	**281**	9	414
	21,897	15,446	15,822

Idan Ofer	**Yossi Rosen**	**Avisar Paz**
Chairman of the Board of Directors	Chief Executive Officer	Chief Financial Officer

November 23, 2004

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.

* Reclassified - See Note 3H.

	September 30 2004	September 30 *2003	December 31 *2003
	Reported amounts(1)	Adjusted amounts(2)	
	(Unaudited)	(Unaudited)	(Audited)
	NIS millions	NIS millions	NIS millions
Current liabilities			
Short-term credit from banks and others	**3,274**	2,635	2,657
Trade payables	**1,566**	1,005	1,089
Other payables	**1,794**	1,119	1,326
Proposed dividend payable	**-**	36	-
	6,634	4,795	5,072
Long-term liabilities			
Long-term liabilities to banks and others	**6,446**	4,231	3,826
Provision for reclamation and disposal of waste	**116**	89	99
Debentures convertible into shares of the Corporation	**189**	187	253
Debentures	**200**	-	-
Deferred taxes, net	**1,393**	1,160	954
Liabilities for employee severance benefits, net	**1,056**	743	826
	9,400	6,410	5,958
Debentures convertible into shares of a subsidiary	**175**	315	314
Minority interest	**2,262**	1,857	1,895
Liabilities attributable to discontinued activity	**143**	-	413
Shareholders' equity	**3,283**	2,069	2,170
	21,897	15,446	15,822

(1) See Note 1.

(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.

* Reclassified - See Note 3H.

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

Consolidated Statements of Earnings for the

	For the nine month period ended		For the three month period ended		For the year ended
	September 30 2004	September 30 *2003	September 30 2004	September 30 *2003	December 31 *2003
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	Reported Amounts (1)	Adjusted Amounts (2)	Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Sales, shipping and services	**17,097**	7,670	**6,109**	2,823	10,101
Cost of sales, shipping and services	**13,265**	5,211	**4,647**	1,948	6,966
Gross profit	**3,832**	2,459	**1,462**	875	3,135
Selling, transport and marketing expenses	**1,404**	1,260	**466**	469	1,654
General and administrative expenses	**663**	346	**234**	129	465
Research and development expenses, net	**100**	98	**33**	33	128
	2,167	1,704	**733**	631	2,247
Operating earnings	**1,665**	755	**729**	244	888
Financing expenses, net	**(269)**	(117)	**(92)**	(53)	(117)
Other income (expenses), net	**186**	(18)	**6**	(3)	(194)
Earnings before taxes	**1,582**	620	**643**	188	577
Income tax	**(401)**	(240)	**(226)**	(71)	(145)
Earnings after taxes	**1,181**	380	**417**	117	432
Group's equity in earnings of affiliates, net	**86**	62	**12**	36	110
Minority interest in earnings of subsidiaries, net	**(391)**	(182)	**(139)**	(59)	(203)
Net earnings from continued operations	**876**	260	**290**	94	339
Income (loss) from discontinued operations, net	**175**	(10)	**201**	-	(14)
Net earnings for the period	**1,051**	250	**491**	94	325
	NIS	**NIS**	**NIS**	**NIS**	**NIS**
Basic and diluted earnings per share of NIS 1 par value					
Income from continuing operations,	**126.15**	37.64	**41.59**	13.51	48.99
Income (loss) from discontinued operations	**25.18**	(1.45)	**28.77**	-	(2.02)
Earnings per share	**151.33**	36.19	**70.36**	13.51	46.97

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.
* Reclassified - See Note 3H.

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

Statements of Changes in Shareholders' Equity

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Dividend proposed subsequent to the balance sheet date	Retained earnings	Total
			Reported amounts (1)			
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the nine-month period ended September 30, 2004 (unaudited)						
Balance as at the beginning of the period	**1,467**	**(10)**	**(82)**	**-**	**795**	**2,170**
Net earnings for the period	**-**	**-**	**-**	**-**	**1,051**	**1,051**
Adjustments from translation of financial statements	**-**	**-**	**49**	**-**	**-**	**49**
Conversion of debentures into shares	**26**	**-**	**-**	**-**	**-**	**26**
Issuance of capital	**(10)**	**10**	**-**	**-**	**-**	**-**
Realization of reserves due to realization of investment	**-**	**-**	**(13)**	**-**	**-**	**(13)**
Change in accounting in method in an affiliated company (3)	**(3)**	**-**	**7**	**-**	**(4)**	**-**
Balance as at the end of the period	**1,480**	**-**	**(39)**	**-**	**1,842**	**3,283**

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Dividend proposed subsequent to the balance sheet date	Retained earnings	Total
			Adjusted amounts (2)			
	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	1,470	(13)	(70)	98	506	1,991
Net earnings for the period	-	-	-	-	250	250
Dividend	-	-	-	(98)	-	(98)
Dividend proposed subsequent to the balance sheet date	-	-	-	-	(36)	(36)
Adjustments from translation of financial statements	-	-	(38)	-	-	(38)
Issuance of capital	(1)	1	-	-	-	-
Balance as at the end of the period	1,469	(12)	(108)	-	720	2,069

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.
(3) See Note 3K.

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

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

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Dividend proposed subsequent to the balance sheet date	Retained earnings	Total
			Reported amounts [1]			
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the three-month period ended September 30, 2004 (unaudited)						
Balance as at the beginning of the period	**1,485**	**(5)**	**(37)**	**-**	**1,355**	**2,798**
Net earnings for the period	**-**	**-**	**-**	**-**	**491**	**491**
Adjustments from translation of financial statements	**-**	**-**	**5**	**-**	**-**	**5**
Conversion of debentures into shares	**3**	**-**	**-**	**-**	**-**	**3**
Issuance of capital	**(5)**	**5**	**-**	**-**	**-**	**-**
Realization of reserves due to realization of investment	**-**	**-**	**(14)**	**-**	**-**	**(14)**
Change in accounting in method in an affiliated company (3)	**(3)**	**-**	**7**	**-**	**(4)**	**-**
Balance as at the end of the period	**1,480**	**-**	**(39)**	**-**	**1,842**	**3,283**

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Dividend proposed subsequent to the balance sheet date	Retained earnings	Total
			Adjusted amounts [2]			
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the three-month period ended September 30, 2003 (unaudited)	1,469	(12)	(158)	36	626	1,961
Balance as at the beginning of the period						
Net earnings for the period	-	-	-	-	94	94
Proposed dividend subsequent to the balance sheet date	-	-	-	(36)	-	(36)
Adjustments from translation of financial statements	-	-	50	-	-	50
Balance as at the end of the period	1,469	(12)	(108)	-	720	2,069

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.
(3) See Note 3K.

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

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

	Share capital and capital reserves	Shares of the Corporation held by a subsidiary	Adjustments arising from translation of financial statements of investee companies	Dividend proposed subsequent to the balance sheet date	Retained earnings	Total
	Adjusted amounts [(1)]					
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
For the year ended December 31, 2003 (audited)						
Balance as at the beginning of the year	1,470	(13)	(70)	98	506	1,991
Net earnings for the year	-	-	-	-	325	325
Dividend	-	-	-	(98)	(36)	(134)
Adjustments from translation of financial statements	-	-	(12)	-	-	(12)
Issuance of capital	(3)	3	-	-	-	-
Balance as at the end of the year	1,467	(10)	(82)	-	795	2,170

(1) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.

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

Consolidated Statements of Cash Flows for the

	For the nine month period ended		For the three month period ended		For the year ended
	September 30 2004	September 30 *2003	September 30 2004	September 30 *2003	December 31 2003
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	Reported Amounts (1)	Adjusted Amounts (2)	Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
Cash flows generated by operating activities:					
Net earnings for the period	**1,051**	250	**491**	94	325
Adjustments to reconcile net earnings to net cash flows generated by operating activities (A)	**768**	1,389	**120**	327	1,615
Net cash inflow generated by continuing operating activities	**1,819**	1,639	**611**	421	1,940
Net cash outflow generated by discontinued operating activity	**(14)**	(10)	**-**	-	(26)
Net cash inflow generated by operating activities	**1,805**	1,629	**611**	421	1,914
Cash flows generated by investing activities:					
Investments in investee and other companies	**(26)**	(28)	**(19)**	(16)	(49)
Acquisition of fixed assets and other assets	**(1,477)**	(437)	**(669)**	(129)	(605)
Long-term loans granted	**(21)**	(36)	**(12)**	(29)	(56)
Sale (acquisition) of marketable securities, net	**45**	89	**(154)**	(16)	46
Investment grant in respect of fixed assets	**12**	35	**1**	22	44
Proceeds from sale of fixed and other assets	**372**	7	**27**	4	15
Collection of long-term loans	**36**	16	**4**	7	19
Granting of short-term loans and deposits in banks, net	**(72)**	(273)	**172**	(257)	(193)
Proceeds from sale of investments in investee and other companies	**13**	36	**-**	24	38
Acquisition of newly consolidated subsidiaries (B)	**(19)**	-	**-**	-	-
Proceeds from realization of investments in previously consolidated subsidiaries (C)	**89**	-	**-**	-	-
Net cash outflow generated by continuing investing activities	(1,048)	(591)	(650)	(390)	(741)
Net cash inflow generated by discontinued investing activity	373	-	378	-	54
Net cash outflow generated by investing activities	**(675)**	(591)	**(272)**	(390)	(687)

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.
* Reclassified – see Note 3G.

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

Consolidated Statements of Cash Flows for the (cont'd)

	For the nine month period ended		For the three month period ended		For the year ended
	September 30 2004	September 30 *2003	September 30 2004	September 30 *2003	December 31 *2003
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	Reported Amounts (1)	Adjusted Amounts (2)	Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)
	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	**2,219**	502	**579**	312	1,005
Repayment of long-term liabilities	**(1,544)**	(1,458)	**(392)**	(370)	(2,249)
Receipt (repayment) of short-term loans, net	**(746)**	228	**135**	152	303
Proceeds from exercise of options of employees in the Corporation and in a subsidiary	**2**	3	**-**	-	3
Acquisition of shares of subsidiary by its subsidiary	**-**	(9)	**-**	-	(9)
Dividend paid	**-**	(98)	**-**	-	(134)
Issuance of capital to minority interest in subsidiaries	**-**	-	**-**	-	1
Issuance of debentures	**200**	-	**-**	-	-
Dividend paid to minority shareholders of subsidiaries	**(194)**	(129)	**(140)**	(78)	(129)
Net cash inflow (outflow) generated by continuing financing activities	**(63)**	(961)	**182**	16	(1,209)
Net cash outflow generated by discontinued activities	**(44)**	-	**(40)**	-	(1)
Net cash inflow (outflow) generated by financing activities	**(107)**	(961)	**142**	16	(1,210)
Translation differences of cash balances in autonomous investees	**(1)**	(2)	**15**	5	6
Increase in cash and cash equivalents	**1,022**	75	**496**	52	23
Less – increase in cash and cash equivalents allocable to discontinued activities	**(268)**	-	**(276)**	-	(31)
Increase (decrease) in cash and cash equivalents allocable to continuing activities	**754**	75	**220**	52	(8)
Balance of cash and cash equivalents at the beginning of the period	**139**	147	**673**	170	147
Balance of cash and cash equivalents at the end of the period	**893**	222	**893**	222	139

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.
* Reclassified - See Note 3G.

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

Consolidated Statements of Cash Flows for the (cont'd)

	For the nine month period ended		For the three month period ended		For the year ended
	September 30 2004	September 30 *2003	September 30 2004	September 30 *2003	December 31 *2003
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	Reported Amounts (1)	Adjusted Amounts (2)	Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
A. Adjustments to reconcile net earnings to net cash flows generated by continuing operating activities					
Income and expenses not involving cash flows:					
Group's equity in results of affiliates, net, less dividend	**(72)**	(45)	**(11)**	(40)	(88)
Minority interest in earnings of subsidiaries, net	**391**	182	**139**	59	201
Depreciation and amortization	**866**	590	**301**	204	859
Deferred taxes, net	**39**	177	**57**	78	(35)
Capital gains, net	**(248)**	(53)	**(61)**	(9)	(44)
Erosion of short and long-term loans granted and increase in value of marketable securities, net	**(2)**	(34)	**4**	8	(58)
Erosion of loans received and of short-term and long-term liabilities, net	**10**	(24)	**(5)**	(27)	(19)
Increase (decrease) in liability for employee severance benefits, net	**79**	39	**30**	(5)	102
Loss (income) from discontinued activity	**(175)**	10	**(201)**	-	14
	888	842	**253**	268	932
Changes in asset and liability items:					
Decrease (increase) in trade and other receivables	**(313)**	511	**(38)**	(15)	598
Decrease (increase) in inventories	**130**	(37)	**(4)**	32	(127)
Increase in uncompleted voyages, net	**(119)**	-	**(127)**	-	-
Increase in trade and other payables	**169**	73	**31**	44	195
Increase (decrease) in provision for reclamation and disposal of waste	**13**	-	**5**	(2)	17
	(120)	547	**(133)**	59	683
	768	1,389	**120**	327	1,615

* Reclassified.
(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.
* Reclassified – see Note 3G.

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

Consolidated Statements of Cash Flows for the (cont'd)

	For the nine month period ended		For the three month period ended		For the year ended
	September 30 2004	September 30 *2003	September 30 2004	September 30 *2003	December 31 *2003
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Audited)
	Reported Amounts (1)	Adjusted Amounts (2)	Reported Amounts (1)	Adjusted Amounts (2)	Adjusted Amounts (2)
	NIS millions	NIS millions	NIS millions	NIS millions	NIS millions
B. Acquisition of newly consolidated subsidiaries					
Working capital (excluding cash and cash equivalents)	**671**	-	**-**	-	-
Investment in affiliated company that became a subsidiary	**485**	-	**-**	-	-
Fixed assets, other assets and long-term receivables	**(3,913)**	-	**-**	-	-
Minority interest	**26**	-	**-**	-	-
Deferred taxes	**407**	-	**-**	-	-
Long-term liabilities	**2,305**	-	**-**	-	-
	(19)	-	**-**	-	-
C. Proceeds from realization of previously consolidated subsidiaries					
Working capital (excluding cash and cash equivalents)	**10**	-	**-**	-	-
Fixed assets, net	**54**	-	**-**	-	-
Deferred taxes	**9**	-	**-**	-	-
Long-term liabilities	**(5)**	-	**-**	-	-
Capital gain from realization of investment	**21**	-	**-**	-	-
	89	-	**-**	-	-
D. Non-cash transactions					
Acquisition of fixed assets on supplier credit	**50**	25	**50**	25	10

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.
* Reclassified - See Note 3G.

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 in accordance with Standard No. 14 of the Israeli Accounting Standards Board.

2. The significant accounting policies applied in the preparation of these financial statements are consistent with those applied in the financial statements as at December 31, 2003, except as stated in this Note.

3. These financial statements have been prepared in a condensed format as at September 30, 2004 and for the nine-month and three-month periods then ended. The financial statements should be read in conjunction with the annual financial statements as at December 31, 2003 and for the year then ended and the related notes.

B. Definitions

In these financial statements –

Adjusted amount –	The nominal historical amount adjusted in accordance with the provisions of Opinions 23, 34, 36 and 37.
Reported amount –	The adjusted amount as at the date of transition (December 31, 2003), with the addition of amounts in nominal values that were added after the transition and less amounts eliminated after the date of transition.
Adjusted financial report –	The financial report based on the provisions of Opinions 23, 34, 36, 37 and 50.
Nominal financial report –	The financial report based on reported amounts.

C. Discontinuance of adjustment of financial statements

In October 2001 the Israeli Accounting Standards Board published Accounting Standard No. 12, "Discontinuance of Adjustment of Financial Statements". Pursuant to this Standard and in accordance with Accounting Standard No. 17 that was published in December 2002, the adjustment of financial statements will be discontinued as of January 1, 2004. Up to December 31, 2003, the Corporation continued to prepare adjusted financial statements in accordance with Opinion No. 36 of the Institute of Certified Public Accountants in Israel. The Corporation has implemented the provisions of the Standard and has accordingly discontinued the adjustment as of January 1, 2004.

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

D. Financial statements in reported amounts

1. In the past the Corporation prepared its financial statements on the basis of historical cost adjusted for the changes in the Consumer Price Index (CPI). The adjusted amounts included in the financial statements as at December 31, 2003 constitute the starting point for the nominal financial report as of January 1, 2004. Any additions made during the period are included according to their nominal values.

2. Amounts of non-monetary assets do not necessarily reflect their realizable value or updated economic value but, rather, only the reported amounts of such assets.

3. The term "cost" in these financial statements means the reported amount of cost.

4. All the comparative data for prior periods is stated after being adjusted to the CPI of December 31, 2003.

5. Balance sheets:

   a. Non-monetary items are stated at reported amounts.
   b. Monetary items are stated in the balance sheet at their nominal historical values as at balance sheet date.

6. Statements of operations:

   a. Income and expenses deriving from non-monetary items or from provisions included in the balance sheet are calculated as the difference between the reported amount of the opening balance and the reported amount of the closing balance.
   b. All other operating items are stated at their nominal values.

7. Statements of changes in shareholders' equity:

   A dividend declared in the period of the report is presented in nominal values.

E. First time application of new accounting standards

Accounting Standard No. 13, Effects of Changes in Exchange Rates of Foreign Currency

As of January 1, 2004, the Corporation applies Accounting Standard No. 13, regarding the "Effects of Changes in Exchange Rates of Foreign Currency". The Standard deals with the translation of transactions in foreign currency and the translation of financial statements of foreign activities for purposes of the inclusion thereof with the financial statements of the reporting entity. The Standard provides principles for classification of foreign activities as an autonomous investee entity overseas or as an integrated extension based on the indicators enumerated in the Standard and the use of discretion, as well as the manner of translation of the financial statements of autonomous investee entities as stated.

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

E. First time application of new accounting standards (cont'd)

The balance of goodwill created on acquisition of an autonomous investee entity overseas is treated as an asset of that autonomous investee entity overseas and is translated based on the closing exchange rate as of January 1, 2004, this being different than the principles applied in the past pursuant to which the translation of goodwill was based on the rate at the time of execution of the transaction.

Translation of statements of operations of an autonomous investee entity overseas is executed based on the rate of exchange at the time of execution of the transaction or for practical reasons based on the average rate of exchange in the period commencing January 1, 2004, this being different than the principles applied in the past pursuant to which the translation of the statements was executed based on the closing rate.

A reduction in the value of an investment in an autonomous investee entity overseas does not constitute a partial realization and, therefore, no part of the translation differences are recorded on the statement of earnings at the time of recording the reduction in value.

Translation of financial statements of an autonomous investee entity overseas, which is required to present financial statements adjusted for inflation, in accordance with generally accepted accounting principles in a hyper-inflationary economic environment, is executed based on the closing rate.

F. Disclosure of accounting standard in the period prior to its application

In July 2004, the Israeli Accounting Standards Board published Accounting Standard No. 19, "Taxes on Income". The Standard provides that a liability for deferred taxes is to be recorded for all temporary differences subject to tax, except for a limited number of exceptions. In addition, a deferred tax asset is to be recorded for all temporary differences that may be deducted, losses for tax purposes and tax benefits not yet utilized, if it is anticipated that there will be taxable income against which they can be offset, except for a limited number of exceptions. The new Standard applies to financial statements for periods beginning on January 1, 2005. The Standard provides that it is to be implemented by means of a cumulative effect of a change in accounting method. In the Corporation's estimation, the impact of the Standard on its results of operations, financial position and cash flows are not expected to be material.

Note 2 - Rates of Changes in the Consumer Price Index and the Dollar Exchange Rate

Presented below is the rate of change in the Consumer Price Index and the representative rate of exchange of the U.S. dollar in the reported periods:

	CPI %	Representative exchange rate of the U.S. $ %
During the nine-month period ended September 30, 2004	1.21	2.35
During the nine-month period ended September 30, 2003	(1.49)	(6.25)
During the three-month period ended September 30, 2004	(0.20)	(0.33)
During the three-month period ended September 30, 2003	(0.98)	2.99
During the year ended December 31, 2003	(1.89)	(7.56)

Note 3 - Investments and Supplementary Information

A. Tower Semiconductor Ltd. (hereinafter – Tower)

(1) In January 2004, Tower issued, by means of a prospectus published to the public in the United States, approximately 11.4 million ordinary shares at a price of $7 per share for a net consideration of $75.1 million (including a partial exercise of the options granted to the underwriters).

In addition, Tower issued shares to Israel Corporation Technologies (I.C. Tech) Ltd. (hereinafter – "I.C. Tech"), the primary Wafer partners, and an additional partner in Tower (hereinafter – "the Investors") based on a price of $7 per share for a consideration of $16.4 million, which was transferred to Tower in December 2003.

As a result of the public issuance, and after issuance of the share capital to the investors, I.C. Tech's share in Tower declined to 21.7%, and the Group realized a capital gain of NIS 29 million.

(2) In November 2003, Tower reached agreement with the banks regarding amendment of its credit facility agreements for the financing of FAB2. In the framework of amendment of the agreements, Israel Corporation gave the banks a letter of commitment as part of the arrangements required by them for the granting of a security net by Tower's main shareholders as a condition for the continued provision of financing by the banks to Tower.

The total amount of the Corporation's liability to invest in Tower pursuant to the letter of commitment shall not exceed $50 million.

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).

As at the signing date of the financial statements, the balance of the Corporation's liability under the above-mentioned letter of commitment is $36 million.

Note 3 - Investments and Supplementary Information (cont'd)

(3) During 2003, Tower requested that the Investments Center approve the revised 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, based on discussions held with the Investments Center, that the reaching of a satisfactory arrangement regarding this matter is probable.

(4) According to the Facility Agreement with the banks, Tower is required to comply with certain financial ratios and covenants. As at the balance sheet date, Tower was in full compliance with these financial ratios and covenants. Due to the recent and current slowdown in the semiconductor markets, Tower's Management estimates that it is possible that Tower will not comply with certain of the financial ratios and covenants.

Tower is presently preparing an updated work plan for 2005 for FAB2 which will be based on the prevailing and Tower's forecast of the market conditions. Accordingly, if required, Tower's Management intends to request its banks to agree to amend the financial ratios and covenants in order to align them with the updated work plan for FAB2 for 2005. Tower's Management estimates that it probable that satisfactory agreements with the banks will be achieved. According to the Facility Agreement, satisfying the financial ratios and covenants is a material provision. Achieving arrangements with the banks is essential to the continued equipping, operation and construction of FAB2.

The Facility Agreement provides that if as the result of any default whatsoever, the banks were to accelerate Tower's obligations Tower would be obligated, among other things, to immediately repay all loans made by the banks (which as at the balance sheet date amount to $497 million), and the banks would be entitled to exercise the remedies available to them under the Facility Agreement, including realization of the liens recorded on Tower's assets.

Subsequent to the balance sheet date, Tower reported that it is taking a series of efficiency measures the goal of which is to conform the level of its capital and operating expenses to the current market conditions and to those conditions that are expected in the near future. Tower is planning to reduce its work force by 12%. Completion of implementation of the efficiency measures is expected to take place by December 31, 2004 and is expected to save $20 million in 2005, compared with the current level of expenses.

(5) In the period of the report, the Corporation included its share of Tower's losses in the amount of NIS 110 million and, at the same time, it reduced the provision for decline in value of the investment in Tower (which was recorded in 2002) by NIS 106 million.

Note 3 - Investments and Supplementary Information (cont'd)

B. On February 5, 2004, the Corporation acquired all of the State's shares in ZIM Integrated Shipping Services Ltd. (formerly – "ZIM Israel Navigation Co. Ltd.") (hereinafter – "ZIM") and, in addition, during the period of the report the Corporation acquired part of the holdings of the other shareholders in ZIM. In total, the Corporation acquired 49% of ZIM's shares at a cost of NIS 517 million. As at the balance sheet date, the Corporation holds approximately 98% of ZIM's share capital.

The excess of the cost over the net asset value totaled NIS 22 million, and was allocated to the fleet of ships and its equipment that is included in the fixed assets category.

Up to December 31, 2003, the Corporation presented its investment in ZIM based on the equity method. As of January 1, 2004, ZIM's financial statements were consolidated for the first time. The Corporation's share in ZIM's results was calculated for the period from the acquisition date to the end of the period of the report.

Set forth below is condensed financial statement data of ZIM:

	September 30 2004
	NIS millions
Balance sheet	
Current assets	2,010
Fixed assets, investments and long-term receivables	4,606
Current liabilities	(2,016)
Long-term liabilities	(3,110)
Minority interest	(1)
	1,489

	For the nine months ended September 30 2004	For the three months ended September 30 2004
	NIS millions	NIS millions
Statement of earnings		
Sales	8,196	3,044
Cost of sales	7,364	2,660
Net income	521	177

C. In the second quarter of the period of the report, ZIM sold two ships, for a consideration of $70 million. The two ships will be leased to ZIM for a period of five years. The after-tax capital gain created to ZIM totals $22 million, and the Corporation's share of the gain is approximately NIS 95 million.

Note 3 - Investments and Supplementary Information (cont'd)

D. ZIM signed agreements for sale of five ships that will enter into effect upon delivery of the ships (2 ships in November 2004 and 3 ships in January 2005). The proceeds from sale of the ships amounts to $180 million and the after-tax capital gain to be realized by ZIM will total $20 million in the fourth quarter of the year of account and $32 million in the first quarter of 2005. The Corporation's share of the gain is approximately NIS 88 million and NIS 140 million, respectively. The ships are to be leased to ZIM for a period 5–6 years.

E. In the second quarter of the period of the report, Israel Chemicals Ltd. (hereinafter – "ICL") sold its investment in Negev Industrial Minerals Ltd. (as well as in a sister company related thereto), for a consideration of $20 million. ICL's after-tax capital gain totals NIS 21 million and Israel Corporation's share is approximately NIS 11 million.

F. On September 29, 2004, the Law for Amendment of the Income Tax Ordinance (No. 140 and Temporary Order), 2004 (hereinafter – "the Amendment") was passed by the Knesset. The Amendment provides for gradual reduction of the tax rates for companies, from the rate of 36% to the rate of 30%, in the following manner: in the 2004 tax year the tax rate will be 35%, in the 2005 tax year the tax rate will be 34%, in the 2006 tax year the tax rate will be 32%, and in the 2007 tax year and thereafter the tax rate will be 30%.

The current taxes and balances of deferred taxes as at September 30, 2004, are computed in accordance with the new tax rates as determined in the Amendment. The effect of the change in the consolidated financial statements in the period of the report is a decrease of tax expenses of NIS 161 million. The impact on the net income amounts to NIS 120 million.

G. In the period of the report, the amount of the Corporation's investment in Oil Refineries Ltd. (hereinafter – "ORL") based on the equity method of accounting increased above the exercise price of the option. The exercise price of the option derives from the Corporation's notification to the Government on August 4, 2003, according to which, the Corporation decided, by virtue of the provisions of Appendix C of the Arrangement, to exercise the option to sell all its shares of ORL at a price constituting an average between the two overall valuations of ORL, subject to certain adjustments (see also Note 4).

Pursuant to the above, the Corporation set its investment in ORL at the exercise price of the option, in the amount of NIS 596 million, which is NIS 88 million less than the amount of the investment based on the equity method of accounting.

H. In the third quarter of the period of the report, PSINet Europe B.V. and Sorbie Holding BVI, subsidiaries of the Corporation held at the rate of 62% (hereinafter – "the PSI Group"), sold a number of their investee companies in Europe, in two separate transactions, for an aggregate consideration of $112 million. Up to the balance sheet date, $90 million was received in cash. Part of the balance of the consideration is scheduled to be received during 2005 and part thereof is contingent on adjustments and conditions spelled out in the agreements. The Corporation's share in the after-tax gain realized amounts to NIS 201 million.

Note 3 - Investments and Supplementary Information (cont'd)

(H) (cont'd)

The companies sold constituted a separate component and operated in the communications area. Upon sale of the companies, the Corporation no longer has activities in the communications area. Therefore, the investment in the PSI Group is presented in accordance with Accounting Standard No. 8 – "Discontinued Operations". The assets and liabilities attributable to the discontinued activities have been presented in separate categories, after the fixed assets category and the minority interest category, respectively. In the statement of earnings, the earnings from the discontinued activities are presented after the share of the minority interest (including the capital gain realized from the sale as stated above). In addition, the cash flows from the discontinued activities are classified separately in the statement of cash flows from the cash flows from continuing activities.

The impact of discontinuance of the activities on the Corporation's financial-statement categories is not significant, except for the capital gain as stated above.

I. Severe flooding in the stream channels, which took place on October 29, 2004, caused the flooding of a large section of the premises of part of ICL's facilities in Sdom and the entry of water and large-scale drainage into the evaporation pools at the Dead Sea. As a result of the flooding, the work at the power and production station in part of ICL's facilities in Sdom was halted for a number of days. Due to the floods, ICL sustained property damage and also suffered a loss of profits. At this stage, ICL is unable to estimate the extent of the damage, however, beyond the insurance deductible, in the net amount of $8.5 million, insurance coverage exists in connection with the damages.

J. On August 30, 2004, the Audit Committee and the Corporation's Board of Directors, decided to approve a transaction of ZIM regarding equipping by ZIM of additional ships, a transaction that is related the controlling shareholders in the Corporation.

The subject of the transaction is the acquisition by ZIM of 12 ships, including 8 container ships having a capacity of 4,250 containers each, that are scheduled to be delivered to ZIM during 2006 and 2007 and 4 container ships having a capacity of 6,350 containers each, that are scheduled to be delivered to ZIM during 2008 and 2009. 2 out of the 8 ships having a capacity of 4,250 containers will be acquired by ZIM by means of assignment of the rights to acquire the ships of a foreign company controlled by a foreign trust related to the family of Mr. Sami Ofer (hereinafter – "Zodiac"). 4 out of the 8 ships having a capacity of 4,250 containers will be acquired by means of assignment of the rights to acquire the ships, by 4 joint foreign companies (in equal shares) of ZIM and Ofer Shipping Ltd. (a company controlled by the Corporation's controlling shareholders (hereinafter – "the Joint Transaction"). The ships will be acquired at a price of $54.21 million per ship, this being at the same price and on the same terms (back to back) that the ships were acquired. Out of the 8 ships having a capacity of 4,250 containers, ZIM will lease 2 ships from Zodiac for a period of 10 years, for a lease fee of $23,000 per day per ship. ZIM will also lease 4 ships that are to be acquired by the Joint Transaction for a period of 10 years, for a lease fee of $23,000 per day per ship. Out of the 4 ships having a capacity of 6,350 containers, ZIM will purchase 2 ships from companies in the Zodiac Group, one for a price of $74.3 million and the other for a price of $74.1 million. Sale of the ships will be at the same price and on the same terms (back to back) that the companies in the Zodiac Group acquired the said ships. 2 of the 4 ships having a capacity of 6,350 containers will be leased by ZIM from companies in the Zodiac Group for a period of 10 years, for a lease fee of $31,500 per day per ship.

Note 3 - Investments and Supplementary Information (cont'd)

(J) (cont'd)

The Corporation's Board of Directors decided to convene a General Meeting in order to approve the transaction.

K. An affiliated company of Oil Refineries Ltd. adjusted its financial statements by means of a restatement in order to retroactively reflect therein a change in the adjustment basis to a basis based on the changes in the Consumer Price Index instead of a basis based on the changes in the exchange rate of the U.S. dollar, as was the previous practice. The impact of the change on the Corporation's financial statements is not material.

Note 4 - Concessions

Oil Refineries Ltd.

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 ended in October 2003.

On December 2, 2002, an arrangement was signed between ORL, the Government and 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 these 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.

Note 4 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

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.

Upon expiration of the original concession and in accordance with the arrangement, ORL began paying license fees under the arrangement. In the period of the report, ORL recorded a provision of NIS 42 million in its financial statements for the first nine months of the year. 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 in the name of the Government after all the required approvals had been received by the parties authorized on behalf of the Government to sign it, and after it was signed, approvals of the Board of Directors of ORL and the Board of Directors of Israel 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 date of the arrangement (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 2003, 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, which believes that the correct solution is establishment of a local industrial council in the area, requested to present its position to the Minister of the Interior. The Minister of the Interior rejected ORL's request for a hearing and a decision has not yet been made regarding the municipal allocation. Upon inclusion of lands belonging to ORL within the boundaries of any local authority, it is expected that ORL will begin paying Municipal Tax for the Haifa refinery as well. In 2003, ORL prepared and submitted a site plan for the Haifa refinery site.

Note 4 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

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 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 Israel Corporation.

On June 4, 2003, 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 Director of the Government Companies Authority, ORL, 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.

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 Israel Corporation in ORL and to prepare a new agreement or revisions to the arrangement.

On January 19, 2004, the Supreme Court, at the invitation of all the parties to the proceeding, including the Corporation, decided, among other things, that "the respondents are permitted to continue negotiations among themselves to change the conditions of the agreement which is being attacked by the petition and even to sign a new agreement, provided that up to the time the matter is brought before the Court for the second time no irreversible actions shall be taken and that the present situation shall continue".

On March 28, 2004, May 5, 2004 and July 12, 2004, the Government requested and received additional extensions from the Court for provision of its position regarding the petition.

Note 4 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

On August 9, 2004, the Government submitted a notice to the Court wherein was stated, among other things, that on July 29, 2004, the Ministerial Committee for Society and Economic Matters (Social and Economic Cabinet) made a decision determining the manner in which the split up of ORL and its privatization are to be executed, which imposes on the Accountant General the responsibility to amend, up to October 15, 2004, "Appendix C of the Agreement", in accordance with the principles detailed in the decision (for the sake of good order it is noted that the "Agreement" is the arrangement signed on December 2, 2002, between Israel Corporation and ORL and the Government, as detailed at the beginning of this note, whereas "Appendix C of the Agreement" was signed between Israel Corporation and the Government relating to the relationship between the shareholders of ORL, as will be explained in this note below). It was also determined in the Government's notice that if Israel Corporation does not agree to amendment of "Appendix C of the Agreement", in accordance with the principles of the decision, the "Agreement" will be cancelled and unilateral steps will be taken by the Government. (Detail of the content of the decision of the Ministerial Committee of July 29, 2004, is presented in this note below). At the end of its notification, the Government added the following language:

"8. Therefore, the respondents request that the decision of the Honorable Court of January 19, 2004 be applied such that the petitioner will submit an amended petition or reference to the decision within 20 days, based on the date fixed in the decision. The case was scheduled for hearing, pursuant to the decision, and the respondents will be able to submit their response to the amended petition at the time of the hearing.

9. The respondents do not object to scheduling an urgent hearing of the petition. However, in the opinion of the respondents the hearing should be scheduled for the end of October, since then it will possible to present to the Honorable Court a signed appendix, or it will be possible to give notice of cancellation of the Agreement."

On August 11, 2004, the Court decided that: "taking into account the Government's decision of July 29, 2004, the petitioner is requested to respond to the decision of the respondents dated August 9, 2004, primarily to that stated in Section 8 of such notice. In any similar case, it would seem, that the petition should be amended based on the Government's aforementioned decision".

In a preliminary response, dated August 8, 2004, Israel Corporation notified the Court that it takes the position that the provisions of the "Agreement" must be honored, since it is a binding agreement duly signed, including the provisions of "Appendix C of the Agreement", this being for the reasons well detailed in the Corporation's response to the petition. In this response, the Corporation once again clarified its position that there is no and will be no legal basis that can serve as a foundation (not even in the first instance) for cancellation of the "Agreement", in whole or in part, as well as any of its appendices – with all that deriving and implied thereby. Nonetheless, Israel Corporation notified that it was and continues to be ready to negotiate with the Government with respect to "Appendix C of the Agreement", and it will consider its position regarding this matter, after taking into account, among other things, the content of the decision of the Ministerial Committee dated July 29, 2004.

Note 4 - Concessions (cont'd)

Oil Refineries Ltd. (cont'd)

On August 26, 2004, the petitioner received permission from the Court to submit an amended petition. Up to the signing date of the financial statements, the Israeli Corporation has not been notified regarding the filing of an amended petition by the petitioner.

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 4 - 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 refineries 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 4 - 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, 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 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 4 - 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 Israel Corporation, 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 Israel Corporation's shares in ORL or, in the case of a split-up of ORL, optional acquisition by Israel Corporation of one of the split-up two refineries. In this case, Israel Corporation will pay to the Government or receive therefrom, the difference between the relative value of 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 June 2003, the two aggregate valuations were submitted. One from an appraiser on behalf of 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 4, 2003, Israel Corporation notified the Government that in light of the fact that the negotiations with the Government regarding participation of 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 Israel Corporation shall sell to the Government or to a party which the Government shall instruct, all ORL shares owned by 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, 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.

Israel Corporation clarified, in the framework of an Immediate Report, that at this point, it cannot be known whether the transaction will ultimately be consummated, taking into account, among other things, the following items:

Note 4 - Concessions (cont’d)

Oil Refineries Ltd. (cont'd)

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

2. The need for approvals which according to the Government's position (with which 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 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 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 30, 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 Israel Corporation, the agreement’s conditions, including the license fees determined therein, and the valuations performed by the Government and 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 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 4 - Concessions (cont'd)

A. 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 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 Accountant 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.

   As a result of the recommendations of the inter-office team appointed by the Government, the Committee of Ministers for Social and Economic Matters made the following decision on July 29, 2004: "Further to Government Decisions No. 126, dated August 22, 1999, No. 2796, dated November 25, 2002, and No. 787, dated September 15, 2003, the decision of the Committee of Ministers for Privatization Matters MH/2, dated October 20, 1999, the agreement signed between the Government and Israel Corporation Ltd. (hereinafter – "Israel Corporation") and Oil Refineries Ltd. (hereinafter – "ORL") dated December 2, 2002, which has not yet received all the required approvals (hereinafter – "the Agreement"), as follows:

Note 4 - Concessions (cont’d)

Oil Refineries Ltd. (cont'd)

1. To execute the split-up and privatization of the refineries during the years 2004–2005, in accordance with the outline detailed below:

   1.1 In the first stage, the refinery in Ashdod will be sold as activities, or in a private sale as a subsidiary or a separate company with an ownership structure identical to the ownership of ORL, and immediately thereafter a public issuance of ORL will be made.

   1.2 The refinery in Ashdod will be sold as a “going concern”. In the framework of the process of sale of the refinery in Ashdod the purchaser will undertake to operate the refinery for a period of not less than 10 years from the acquisition date.

   1.3 If necessary, principles for reciprocal relationships will be formulated during the split-up process that will apply between the refineries, including with respect to sale of intermediate products and feedstock materials between them, and between them and the petrochemicals industry.

2. To impose on the Accountant General in the Ministry of Finance the responsibility of amending Appendix C to the Agreement in the framework of a new agreement with Israel Corporation, which will be approved in accordance with Section 16 of the Agreement, such that Sections 3, 4, and 5 of Appendix C to the Agreement will be amended and superseded pursuant to the principles attached as Appendix A to the Government’s decision, and the rest of the Sections will remain unchanged, all of this up to October 15, 2004. In the framework of amendment of Appendix C, the following principles, among others, will be expressed:

   2.1 Israel Corporation will sell together with the Government all the holdings of the refineries.

   2.2 The accountings with Israel Corporation shall be made after completion of privatization of ORL, as will be detailed in the new agreement that amends Appendix C to the Agreement.

3. To impose on the Supervisor of the Government Companies Authority to submit to the Ministerial Committee for Privatization, no later than October 15, 2004, a proposal for split-up and privatization of the refineries on the basis of the outline as stated in Section 1, above. The process of split-up and sale of the refineries will be conducted and executed by the Government Companies Authority as is customary, including by means of mechanisms it determines for purposes of execution of the split-up and advancement of the privatization. In addition, provisions and limitations were determined in the privatization decision regarding ownership of the split-up refineries, among other things, as detailed in notification of the Supervisor of Restrictive Business Practices, as stated in Section 5, below. Commencing from the date that will be determined in the privatization decision, ORL will move to operating based on a separate optimization model for the two refineries, as will be detailed therein.

Note 4 - Concessions (cont’d)

Oil Refineries Ltd. (cont'd)

4. In the framework of the split-up and privatization process, issues relating to ORL employees will be handled, and to the extent necessary this will be reflected in the privatization decision.

5. To record the notification of the Supervisor of Restrictive Business Practices regarding his position with respect to matters within the scope of his responsibility in the area of regulation of the fuel industry, which are attached as Appendix B to the Government’s decision. In addition, to record the notification of the Minister of National Infrastructures regarding his intention to enact the Fuel Industry Law, which will deal with, among other things, arrangement of the regulation in various sectors of the fuel industry.

6. To impose on the Minister of Finance and the Minister of National Infrastructures to amend the Order for Supervision of Prices of Goods and Services, 1992, no later than October 15, 2004, in such a manner that after the split-up and privatization of the refinery in Ashdod, the supervision of refined oil products at the refinery gate will be removed, except for supervision of the prices of refined oil products where more than 50% of their total consumption in the local market is sold by one of the refineries and, at the same time, less than 15% of their total consumption in the local market is sold by the other refinery. After removal of the supervision as stated, re-imposition of supervision of the price of any refined oil product at the refinery gate will be examined in light of the competitive conditions existing in the refining sector in the fuel industry, and in accordance with all law.

7. After sale of the refinery in Ashdod, in principle there is nothing preventing operating of a refinery in the area of production of electricity and desalination of water, in accordance with and subject to all law.

8. If Israel Corporation does not agree with the principles stated in Section 2 – to cancel the agreement, and to take unilateral steps available to the Government in connection with split-up and privatization, among other things in light of the Government’s position regarding ownership of ownership of ORL’s in the area of the concession.

   Regarding this matter, see above also the report regarding the petition filed against the agreement dated December 2, 2002.

Up to the signing date of the financial statements, the Israel Corporation has not yet been informed that a proposal to split up and privatize the oil refineries on the basis of the outline stated in Section 1 to the Decision of the Committee of Ministers for Welfare and Economics, dated July 29, 2004, has been submitted to the Committee of Ministers.

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 and the results of its operations.

The management of Israel Corporation adopts the assessments of ORL, and believes, based on legal opinions, that the agreement dated December 2, 2002, is a valid agreement.

Note 5 - Contingent Liabilities and Commitments

A. One of ICL's subsidiaries, Fertilizers and Chemical Products Ltd (hereinafter – "Fertilizers") is located close to the Haifa port. Over the course of many years, Fertilizers as well as local authorities and other factories, have dumped waste into the Kishon stream which is located near Haifa. In the 1980's, operation of a purification facility was started, which reduces the concentration of certain contaminating agents in waste dumped by the said factories.

In 2001, a class action suit was filed against Fertilizers and 3 other defendants, wherein it is claimed 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 stream and to restore the stream to its condition prior to discharge of the wastes. The State of Israel and many factories and local authorities were joined to the claim as third parties.

In 2000, due to reports that soldiers of the Israel Defense Forces that trained in the Kishon stream developed cancer, the Chief of the General Staff appointed a committee to examine the existence of dangerous substances in the area of the Kishon stream and whether such materials as stated were likely to cause the development of cancer by soldiers who trained in the stream. Despite the fact that the committee determined that most of the said soldiers have no proofs indicating a circumstantial connection between contamination of the stream and the cancer, in the view of the minority there was a circumstantial connection as stated. This report, which was published in 2003, is not admissible in the court in Israel.

Additional claims were filed against various other parties, including the State of Israel, local authorities and government agencies, as well as against Fertilizers. The claims are in the aggregate amount of $138 million and are for bodily injury and property damage, and include additional damages that were not estimated in cash in the statement of claim, such as, future loss of wages and medical expenses as a result of the alleged contamination of the Kishon stream.

In the opinion of ICL, at this stage it is not possible to quantify the financial exposure in the framework of the circumstances relating to the Kishon stream, as described above, since the claims are pending and are in the initial stages and ICL is likely to be a third party to additional claims. Nonetheless, the cost of restoration of the Kishon stream and the liabilities for bodily injury and property damage could be very high. Should Fertilizers be required to participate in the cost of the restoration or the cost of the damage payments as stated, its operating results may be adversely affected to a significant extent.

B. An affiliated company, ORL, is a defendant in some of the claims enumerated in Section A., above. See Note 18B2 to the financial statements as at December 31, 2003.

During the period of the report, 94 plaintiffs, former soldiers in the Israel Defense Forces, filed claims against ORL and three other parties, in respect of bodily injuries which they allege were caused to them, as a result of activities within the framework of their military service, in the Kishon stream, after their request to join the claim of a seaman in the Navy was not accepted. One of the defendants filed a third-party notification against ORL. A statement of defense has not yet been filed, and due to the early stage of the proceeding it is not possible, in ORL's opinion, based on its legal advisors, to predict the claim's chances of success.

Note 5 - Contingent Liabilities and Commitments

C. 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 Israel Corporation and I.C. Tech. 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 of 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.

In August 2004, the claim was summarily dismissed in full by a court in New York. In September 2004, one of the leading plaintiffs gave notice of his intention to file an appeal against the decision. The U.S. court determined timetables in connection with the appeal.

Tower and the Corporation intend to vigorously oppose the claim.

D. For additional details in connection with the contingent liabilities, see Note 18B of the Corporation's financial statements as at December 31, 2003.

Note 6 - Business Segment Information

	Fertilizers									Eliminations	
	Potash	Phosphate	Eliminations	Total	Industrial Products	Performance products	Shipping	Energy	Other activities	& unrelated expenses	Total consolidated
	(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
	Reported Amounts [1]										
For the nine month period ended September 30, 2004											
Segment revenues	**3,012**	**1,897**	**(86)**	**4,823**	**1,907**	**1,935**	**8,196**	**-**	**1,010**	**(774)**	**17,097**
Segment operating earnings	**762**	**31**	**(1)**	**792**	**68**	**189**	**551**	**-**	**93**	**(28)**	**1,665**
Share in earning (losses) of affiliates	**1**	**1**	**-**	**2**	**-**	**-**	**41**	**57**	**(14)**	**-**	**86**

	Fertilizers									Eliminations	
	Potash	Phosphate	Eliminations	Total	Industrial Products	Performance products	Shipping	Energy	Other activities	& unrelated expenses	Total consolidated
	(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
	Adjusted Amounts (2)										
For the nine month period ended September 30, 2003											
Segment revenues	2,545	1,694	(77)	4,162	1,592	1,668	-	-	850	(602)	7,670
Segment operating earnings	560	30	2	592	16	122	-	-	47	(22)	755
Share in earning (losses) of affiliates	(1)	(1)	-	(2)	-		62	43	(41)	-	62

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.

Note 6 - Business Segment Information (cont'd)

	Fertilizers									Eliminations	
	Potash	Phosphate	Eliminations	Total	Industrial Products	Performance products	Shipping	Energy	Other activities	& unrelated expenses	Total consolidated
	(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
	Reported Amounts [(1)]										
For the three month period ended September 30, 2004											
Segment revenues	**1,026**	**691**	**(35)**	**1,682**	**625**	**656**	**3,044**	**-**	**383**	**(281)**	**6,109**
Segment operating earnings	**289**	**34**	**(2)**	**321**	**16**	**77**	**280**	**-**	**64**	**(29)**	**729**
Share in earning (losses) of affiliates	**-**	**-**	**-**	**-**	**-**	**-**	**16**	**6**	**(10)**	**-**	**12**

	Fertilizers									Eliminations	
	Potash	Phosphate	Eliminations	Total	Industrial Products	Performance products	Shipping	Energy	Other activities	& unrelated expenses	Total consolidated
	(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
	Adjusted Amounts (2)										
For the three month period ended September 30, 2003											
Segment revenues	908	704	(30)	1,582	537	600	-		338	(234)	2,823
Segment operating earnings	186	1	-	187	(11)	40	-		34	(6)	244
Share in earning (losses) of affiliates	-	-	-	-	-	-	50	(13)	(1)	-	36

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.

Note 6 - Business Segment Information (cont'd)

	Fertilizers									Eliminations	
	Potash	Phosphate	Eliminations	Total	Industrial Products	Performance products	Shipping	Energy	Other activities	& unrelated expenses	Total consolidated
	(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
	Adjusted Amounts (2)										
Year ended December 31, 2003											
Segment revenues	3,352	2,177	(124)	5,405	2,092	2,263	-	-	1,139	(798)	10,101
Segment operating earnings	663	13	5	681	14	156	-	-	63	(26)	888
Share in earning (losses) of affiliates	(1)	(1)	-	(2)	-	-	100	58	(46)	-	110

As a result of the first time consolidation of ZIM and discontinuance of the activities in the communications area, as stated in Note 3, the metallurgy, agricultural products and technology and communications sectors do not meet the quantitative threshold requirements for a reportable sector and they are presented as part of the "other activities" category. As a result, the comparative data was reclassified accordingly.

(1) See Note 1.
(2) Amounts adjusted for the effect of inflation in terms of shekels of December 2003.