AZRIELI GROUP

Azrieli Group Ltd.

Periodic Report

As of December 31, 2011

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CHAPTER A

Description of the Corporation's Business

December 31, 2011

All chapters of the report and the annexes hereto constitute a single whole and complement one another

CONVENIENCE TRANSLATION FROM HEBREW

Important Notice

Set out below for your convenience is a convenience translation into English of the periodic report for Year 2011 and the financial statements annexed thereto (the "**Report**") of the Azrieli Group Limited. Please note that this document should not be regarded as a substitute for reading the original Hebrew version of the Report in full.

This document is a convenience translation into English of the Hebrew language Report, and the financial reports annexed thereto, of the Azrieli Group Limited (The "Company") (the "Report"). The binning version of the Report for all purposes is the original Hebrew version filed by the Company with the Israel Securities Authority through the MAGNA website (www.magna.isa.gov.il**). Nothing in this translation constitutes a representation of any kind in connection with the Report nor should it be regarded as a source of interpretation of the Report. In the event of a contradiction or inconsistency between this translation and the Hebrew version of the Report, the provisions of the Hebrew version shall prevail.**

This translation was not carried out by the Company, nor checked by it, and accordingly, the Company does not undertake that the translation fully, correctly or accurately reflects the Report and its contents. The full and legal version of the Report, in Hebrew, was released by the Company on March 21, 2012 and may be inspected on the MAGNA website.

The translation of the financial statements annexed to the Report (the "Financial Statements") was not carried out by Brightman, Almagor, Zohar and Co., Accountants (the "Company's Auditors"), and was not checked by the Company's Auditors, and accordingly, they do not undertake that the translation of the Financial Statements fully, correctly or accurately reflects their contents, and the Company's Auditors' report on the financial statements relates solely to the Hebrew language financial statements of the Company. The full and legal version of the Financial Statements was released by the Company as part of the Report on March 21, 2012 and may be viewed on the MAGNA website.

CHAPTER A: BUSINESS DESCRIPTION OF THE COMPANY

General

Azrieli Group Ltd. hereby respectfully files the Description of the Corporation's Business Report as of December 31, 2011 (the "**Date of the Report**"), reviewing the description of the Group and development of business thereof, in 2011 (the "**Report Period**") until the Report Publication Date. The Report is prepared pursuant to the provisions of Regulation 8a of the Securities Regulations (Periodic and Immediate Reports), 5730-1970 and in accordance with the directives of the Israel Securities Authority pertaining to disclosure in respect of investment property segment published on January 11, 2011. Figures appearing in the Report are true as of the Date of the Report. However, in certain cases details appear in the Report reviewing events which occurred subsequent to the Report Date and soon before the date of publication thereof on March 21, 2012 (the "**Report Publication Date**") and in such cases the Company states that these are provided as of the Report Publication Date.

Materiality

The materiality of the information included in this Report, including a description of the material transactions and/or material projects, is evaluated from the point of view of the Company. It should be clarified that, in a part of the cases, the Company, in its exclusive discretion, decided to expand the description necessary, in order to give a more comprehensive picture of the subject being discussed.

Forward-Looking Information

The Description of the Corporation's Business in this Chapter A contains in part forward-looking information as defined in the Securities Law. Such information presented below and referred to as forward-looking information, includes forecasts, estimates, evaluations or other information which are uncertain information addressing a future event and which relies, *inter alia*, on the publications of the Central Bureau of Statistics, the publications of the Bank of Israel, publications of other relevant professional entities and also on internal evaluations of the Company which are based on the collection of statistics, experience and information accumulated by the Company along the years. The actual results may be significantly different from those predicted within the forward-looking information as aforesaid, as a result of a multitude of factors, including as a result from the risk factors, in whole or in part, as described in Section 25 below, all as shall be specified in the specific references to forward-looking information further along the chapter. Sentences containing expressions such as: "projected", "intends", "estimates", "forecasts", "expects" and similar expressions indicate that such is forward-looking information. Such information reflects the Company's current point of view, in respect of future events based on evaluations which are therefore subject to risks and uncertainty.

Definitions

In this Chapter, the following terms will be ascribed the meaning listed next thereto:

TASE	The Tel Aviv Stock Exchange Ltd.;
"**Granite Hacarmel"**	Granite Hacarmel Investments Ltd.;
"**Financial Statements**"	The consolidated financial statements of the Company as of December 31, 2011;
"**Company**"	Azrieli Group Ltd.;
"**Companies Law**"	The Companies Law, 5759-1999;
"**Securities Law**"	The Securities Law, 5728-1968;
"**Nadav Investments**"	Nadav Investments Inc., a private company incorporated under Canadian Law, fully owned and controlled by Azrieli Holdings Inc., a private company incorporated under Canadian Law, which is fully owned and controlled by Mr. David Azrieli and his family members.
"**Azrieli Group**" or the **"Group**"	The Company and/or subsidiaries and/or companies affiliated thereto;
"**Prospectus**"	A public offering prospectus published by the Company on May 12, 2010 as amended on May 25, 2010.;
"**IC**"	International Consultants (Iconsult) Ltd.

PART ONE: DESCRIPTION OF THE GENERAL DEVELOPMENT OF THE COMPANY'S BUSINESS

1. Business of the Company and description of the business development thereof

1.1. General

The Company was incorporated on January 6, 1983 as a private company according to the laws of the State of Israel under the name of Canit-Investments and Finances Management Ltd. On February 23, 1983, it changed its name to Canit-Investments and Financing Management Ltd. On December 1, 2009, the Company changed its name to its present name.

On June 3, 2010, the Company's shares were issued to the public for the first time, and the Company became a public company, within the meaning thereof in the Companies Law. Trade in the Company's shares on TASE began on June 7, 2010.

As of the Date of the Report, the controlling shareholder of the Company is Azrieli Holdings Inc. ("**Azrieli Holdings**"), a private company, incorporated under Canadian law, which holds the entire share capital of Nadav Investments, the direct controlling shareholder of the Company. Azrieli Holdings is fully controlled and owned by Azrieli family members: Mr. David Azrieli, Chairman of the Company's Board of Directors, holds directly and indirectly, approx. 40% of the issued and paid-up share capital in Azrieli Holdings, and his four children each holding, directly and indirectly, approx. 15% of Azrieli Holdings' issued and paid-up share capital. As of the Date of the Report and as of the Report Publication Date, Azrieli held holdings in 73.66% of the share capital and the voting rights of the Company in practice, on a fully diluted basis. For further details see immediate report on interested party holdings dated October 6, 2011, reference 2011-01-295410).

As of the Date of the Report, the Company is engaged, both on its own and through its subsidiary and investee companies, primarily in the income-producing property segment, with most of the business operations of the Company being in the commercial center and mall segment in Israel and in the office and other space for lease segment both in Israel and overseas. In addition, the Company is engaged, through its holdings in Granite Hacarmel, in an additional segment, which comprises, as an intrinsic part, the direct marketing of petroleum distillates, fuelling and commerce complexes, painting and building-finishing, water and sewage etc. and also, the holding of minority interests in financial entities, all of which will be specified below.

As mentioned, the Company belongs to Azrieli Group and its business has developed, *inter alia*, on the basis of the substantial know-how and experience accumulated thereby over many years in the income-

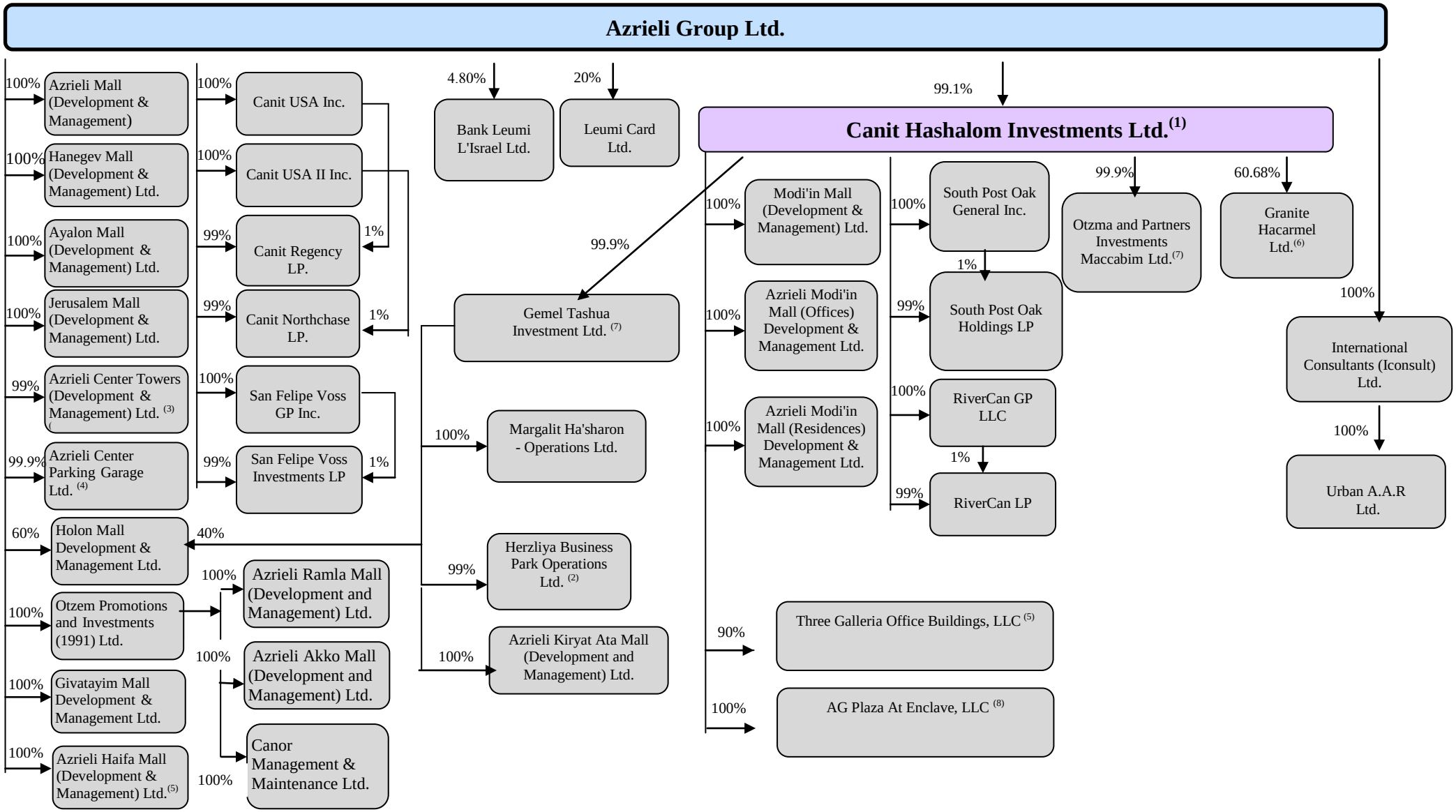
producing property industry in Israel, while using the experience and expertise of its principal controlling shareholder, Mr. David Azrieli, who founded and established the Company from the beginning of its business. Mr. David Azrieli and Ms. Dana Azrieli undertook, in connection with the management agreements for providing services to the Company, not to operate in part of the Company's operating segments, namely, in the commercial center and malls segment and in the office and other space for lease segment in Israel, subject to the size of the area of the leasable properties and the rate of their holdings in such properties. It should be clarified that the aforementioned undertaking does not apply to operations in additional segments in which the Company is active, including operations in the foreign real estate segment. See Section 22 of Chapter D of this Report for further details.

The operations of the Group are carried out by means of a managerial headquarter that is comprised of professionals having a great deal of seniority and managerial experience, most of whom have been associated with the Company and the Group's companies for many years. See Section 15 of this Chapter for additional details in connection with the human capital of the Company.

Commencing from 2008 (transition date January 1, 2007), the Company's financial statements have been prepared according to International Accounting Rules (IFRS), according to which, inter alia, the investment property is presented at its fair value.

1.2. A diagram of the structure of holdings of the Group Companies prior to the Report Publication Date[1]

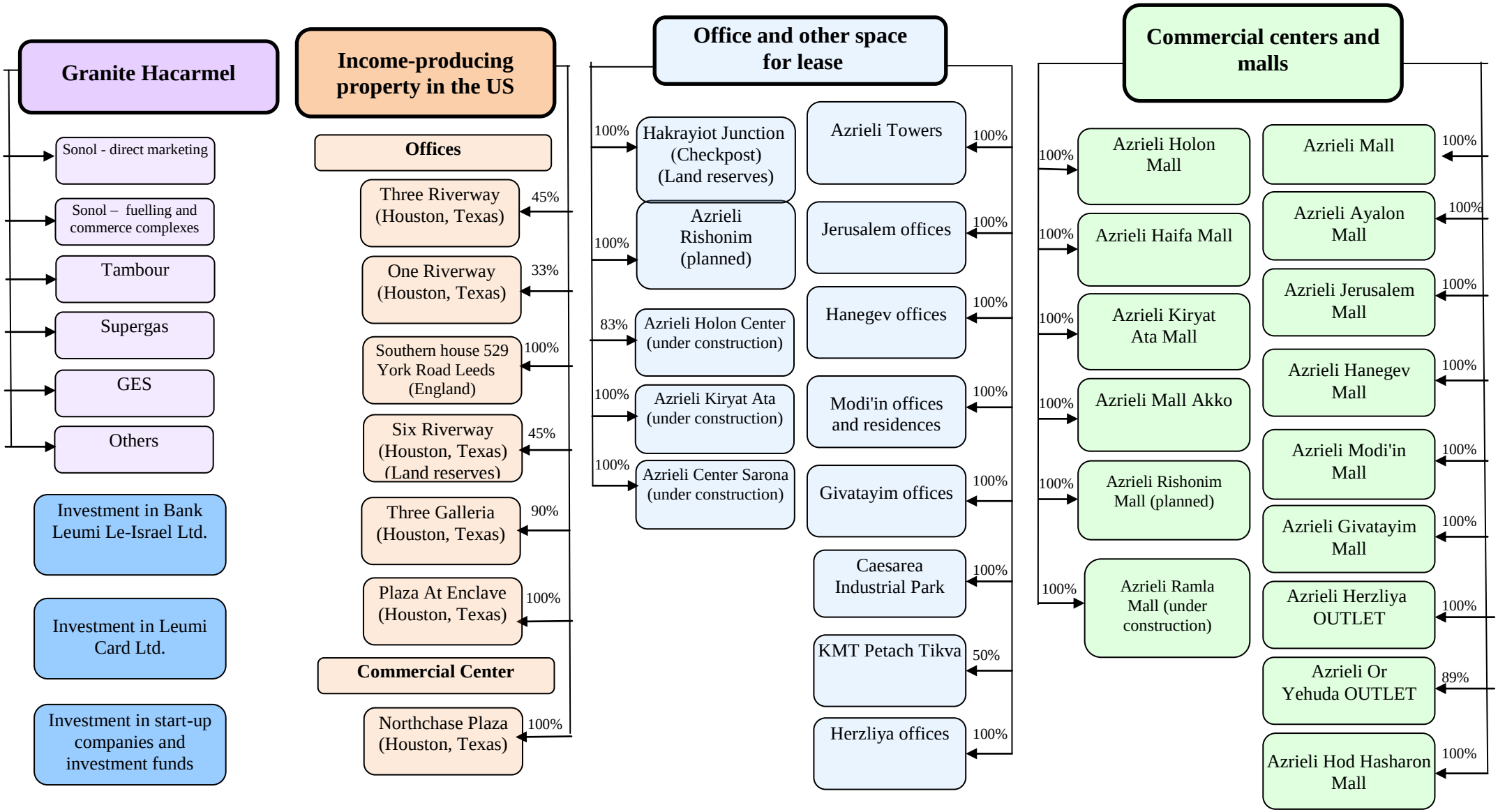
As of the Report Publication Date, the diagram of the structure of holdings of the Company and the Group Companies is as follows:



[1] The diagram does not include inactive companies as of the Report Publication Date.

(1) Approx. 0.9% held by Mr. David Azrieli.
(2) 1% held by IC.
(3) 1% held by Nadav Investments.
(4) 0.01% held by Nadav Investments.
(5) Indirectly. 0.9% is held by Canit Hashalom.
(6) For a description of Granite Hacarmel's holdings in the subsidiaries, see Section 10.1 of the Report.
(7) 0.051% of such companies held by IC.
(8) Indirectly through other companies wholly owned by the Company.

As of the Report Publication Date, the diagram of the holdings of the Group in the properties in final succession(*) is as follows:



(*) In some of the properties the holding is close to 100%. For details, see diagram above.

1.3. **Main developments occurring in the Company's structure and business until the Report Publication Date**

1.3.1. Acquisition and/or Sale of Income-Producing Properties

As a company whose primary business is in the income-producing property segment, the Company engaged in acquisition transactions of income-producing properties and/or lands for development and construction of income-producing properties:

- Three Office Towers, Houston U.S.A.: In February 4, 2011, Three Galleria Office Buildings, LLC, a U.S. company indirectly held (90%) by the Company, completed the purchase of three office towers in Houston, Texas, U.S.A. (the "**Agreement**") in consideration for a sum total of U.S. $176 million. For details see Section 10.9 below.

- Azrieli Center Sarona: On May 30, 2011, the Company won a tender on behalf of the Israel Land Association for the acquisition of the lease rights in a lot of an area of approx. 9.4 dunams in Southern Hakirya in Tel Aviv (the "**Lot**"). The Lot is intended for the construction of an office and commercial project at a scope of approx. 125 thousand sqm of above-ground built-up area (gross) and approx. 61 thousand sqm of underground floors. In consideration for the lease of the Lot, the Company paid the Israel Land Association the sum of NIS 522 million (exclusive of V.A.T) and approx. NIS 39 million as development expenses. For details see Section 7.8 below.

- Azrieli Ramla Mall: In May 2011, Otzem Initiation and Investments (1991) Ltd. completed the acquisition of the rights in a lot of an area of approx. 31,650 sqm in Ramla, which is intended for the construction of a commercial center, in consideration for approx. NIS 100 million. For details see Section 7.8 below.

- Office Building, Houston, U.S.A.: On January 10, 2012, after the date of the statement of financial position, AG Plaza at Enclave, LLC, a U.S. corporation indirectly held at a rate of 100% by the Company, completed the purchase of an office building with a 100% occupancy rate in Houston, Texas, U.S.A., in consideration of a sum total of approx. U.S. $107.5 million (in addition to transaction expenses and financing costs of approx. U.S. $750 thousand). For details see Section 10.10 below

1.3.2 Further Events:

- The Opening to the public of two new malls in Kiryat Ata and in Akko: At the beginning of Q3/2011 the Group opened to the public the "Azrieli Akko Mall" at an overall area for marketing of approx. 12,640 sqm and the "Azrieli Kiryat Ata Mall" at an overall area for marketing of approx. 9,180 sqm. As of the Date of the Report, the occupancy rate at Azrieli Akko Mall was approx. 98% and at Azrieli Kiryat Ata Mall approx. 94%. See Section 19 below for details regarding an appeal filed by the Ministry of Environmental Protection against the resolution of the local use and zoning committee in Akko to grant the Akko Mall an occupancy

permit without requiring the approval of the Ministry of Environmental Protection.

- "Ir Yamim" Mall, Netanya: On August 15, 2011 and on September 11, 2011, the Company entered into contingent sale agreements for the acquisition of all of the rights in the "Ir Yamim" mall in Netanya (the "**Mall**"). The agreements set forth conditions precedent, including receipt of the Antitrust Commisioner's approval. On January 8, 2012, the Company withdrew the merger application filed thereby with the Israel Antitrust Authority for the approval of the acquisition of the Mall, in light of the Company's disagreement with the conditions presented by the Israel Antitrust Authority for the approval of the acquisition thereof. In accordance with the aforesaid, the condition precedent for the completion of the transactions to purchase the Mall was not fulfilled.

2. Main operating segments of the Group

As of the Date of the Report, the business operations of the Group are focused primarily on the income-producing property market in Israel, and the Group also operates in the income-producing property segment overseas, as well as on additional segments, *inter alia*, by means of the subsidiary, Granite Hacarmel.

In light of the expansion in the Group's activity in the U.S.A. during 2011, starting with the Financial Statements as of December 31, 2011, the Company's activity in the income-producing property segment outside of Israel (including comparison figure adjustment) shall be reported as a separate segment, which includes several office properties and one commercial center. For details, also see Note 41 of the Consolidated Financial Statements as of December 31, 2011. In addition, this activity shall be presented as an operating segment in the framework of this Chapter A of the Company's periodic report, as specified in Section 10 below.

Therefore, starting with the Company's Financial Statements as of December 31, 2011,

The operating segments of the Group which are reported as reportable operating segments in the Company's Financial Statements are as follows:

(1) **The commercial centers and malls segment in Israel -** in this operating segment, the Group focuses, primarily, on promoting, constructing, acquiring, renting, managing and maintaining malls and commercial centers in Israel. As of the Date of the Report, the Group owns 13 malls and commercial centers in Israel, in a total leasable area of approx. 256 thousand sqm that are leased (the Company's share – approx. 255 thousand sqm) to about 1,750 tenants, with most of the malls and commercial centers spread throughout the large cities in Israel. In the framework of this operating segment, the Company provides management services to the commercial centers and malls maintained thereby, with the management being performed by the Company and/or designated management companies in relation to each mall or commercial center that is owned by the Group, which enters into management agreements with the lessees. All of the malls and commercial centers also include car parks (above or underground) which serve the visitors and the potential tenants.

See Section 8 of the Report for additional details regarding the commercial centers and malls segment.

(2) **The office and other space for lease segment in Israel -** in this operating segment, the Company focuses, primarily, on promoting, constructing, acquiring, renting, managing and maintaining office buildings and parks for offices and high-tech industry in Israel. As of the Date of the Report, the Group owns 9 income-producing properties in the office and other space for lease segment in Israel, in a total leasable area of approx. 282 thousand sqm (the Company's share is approx. 280 thousand sqm) that are leased to about 500 tenants. Most of the Group's income-producing areas in this operating segment constitute part of the Group's projects which integrate commercial areas, as portrayed in the commercial centers and mall segment, and area designated for office and other space for lease.

See Section 9 of the Report for additional details regarding the office and other space for lease segment in Israel.

(3) **The Income-Producing Property Segment in the U.S.A.** – As of the Report Publication Date, the Group's companies own five office properties for lease outside of Israel, in a total leasable area of approx. 166 thousand sqm (the Company's share is approx. 155 thousand sqm) that are leased to about 270 tenants, as well as one commercial center in a total leasable area of approx. 13 thousand sqm, fully owned by the Company, with about 10 tenants.

For further details regarding the income-producing property segment in the U.S.A., see Section 10 of the Report.

Granite Hacarmel segment - Granite Hacarmel is a public company incorporated in Israel whose shares are registered for trading on the TASE. Most of the business of Granite Hacarmel is in the following operating segments, in accordance with the companies held thereby: (1) Sonol fuelling and commerce complexes and direct marketing; (2) Supergas; (3) Tambour; (4) GES (water and sewage); (5) others. It should be emphasized that the results of Granite are reviewed in total, as one segment and, accordingly, decisions are taken for the allotment of resources to this segment, *inter alia*, while considering the volume of the investment in Granite in relation to the value of all of the Group's assets.

See Section 11 of the Report for additional details regarding Granite Hacarmel and its business.

Other properties and business:

In addition, The Group has other businesses, including, *inter alia*, investments in entities in the banking and financial segment, investments in venture capital, start-up companies and investment funds, and investments in other income-producing properties. See Section 12 of this Chapter for additional details.

3. Investments in the Company's capital and transactions in its shares

To the best of the Company's knowledge, no investments have been made in the Company's capital over the past two years and no other material transaction has been executed in the Company's shares by an interested party outside of the TASE during the two years preceding December 31, 2011, as well as until this Report Publication Date, except as specified below:

3.1. On May 4, 2010, the general meeting of the Company's shareholders approved a resolution whereby the Company's share capital was consolidated such that every 100

shares of par value NIS 0.001 each in the Company's share capital, were consolidated into one share of par value NIS 0.1 each, as specified below:

- 150,000 ordinary shares of par value NIS 0.001 each which are registered in the Company's authorized capital, have been converted into 1,500 ordinary shares of par value NIS 0.1 each of the Company.

- 83,720 ordinary shares of par value NIS 0.001 each, held by Nadav Investments Inc., were converted into 837 ordinary shares of par value NIS 0.1 each of the Company.

- 250,000,000 ordinary Class A shares of par value NIS 0.001 each, which are registered in the Company's authorized capital were converted into 2,500,000 ordinary shares of par value NIS 0.1 each of the Company.

- 204,278,159 ordinary Class A shares, which were held by Nadav Investments Inc., were converted into 2,042,781 ordinary shares of par value NIS 0.1 each of the Company.

According to the capital consolidation as aforesaid, the Company's authorized capital was NIS 250,150 divided into 2,501,500 ordinary shares. After consolidation of the capital as aforesaid, all of the preferred rights attached to ordinary Class A shares have expired, and the Company has no undertakings in respect thereof.

3.2. On May 4, 2010, the Company's general meeting of the shareholders approved a resolution on an increase in the Company's authorized capital in the amount of NIS 12,500,000, which were divided into 125,000,000 ordinary shares. After the increase in capital as aforesaid, the Company's authorized capital is in the amount of NIS 12,750,150 divided into 127,501,500 ordinary shares.

3.3. On May 4, 2010, the Company's general meeting of the shareholders approved a resolution whereby an allotment for no consideration was performed to Nadav Investments Inc., the Company's only shareholder prior to the offering to the public thereof, of 88,897,383 additional ordinary shares of NIS 0.1 each, as stock dividends, such that in respect of each ordinary share of par value NIS 0.1, 43.5 stock dividends will be allotted, such that at the end of the allotment the Company's issued share capital will be 90,941,001 shares of par value NIS 0.1. The issue of the stock dividends shall be performed against the capitalization of NIS 8,889,738 from surplus to equity.

3.4. On May 6, 2010, the Company's general meeting of the shareholders approved a resolution whereby an allotment for no consideration was performed to Nadav Investments Inc., the Company's only shareholder prior to the offering to the public thereof, of 999 additional ordinary shares of NIS 0.1 each, as stock dividends, such that at the end of the allotment the Company's issued share capital will be 90,942,000 shares of par value NIS 0.1. The issue of the stock dividends shall be performed against a capitalization of NIS 99.9 from surplus to equity.

3.5. On June 3, 2010, the Company completed the issue of 24,161,440 ordinary shares in the framework of the Prospectus at a price of NIS 83.25 per share. The gross amount of the consideration in respect of the allotment of the shares was the sum of NIS 2,011,440 thousand. After completion of the said issue, the Company became a public company. On June 7, 2010 the Company’s shares began to be traded on TASE.

3.6. On June 14, 2010 the Company completed a private placement of 6,169,320 ordinary shares to accredited investors. The gross amount of the consideration in respect of the private placement was the sum of NIS 513,595,890 which reflected, at that time, a price per share of NIS 83.25.

3.7. On June 23, 2011, Nadav Investments Inc., which is the direct controlling shareholder of the Company, transferred 1,605,354 Company's shares owned thereby, for no consideration, to a registered charity fund located in Canada and whose properties are designated for donations and the financing of philanthropic activities in Israel and Canada (the "**Fund**").

As the Company was informed, neither Mr. David Azrieli nor any of his relatives are considered as holders of control in the Fund, and therefore the Fund shall not be considered an interested party or holder of control in the Company. For further details see the Company's immediate report dated June 23, 2011 (reference no.: 2011-01-192156), which is included in this Report by way of reference.

3.8. Since July 1, 2010, the Company's shares have been included in the TA-25 index.

4. Dividends

4.1. On May 25, 2010, the Company's Board of Directors adopted a policy for dividend distributions, subject to any law and the Company's needs, whereby on an annual basis, upon publication of the Company's annual financial statements or subsequently, the Company shall distribute dividends to its shareholders in the amount of 35% of the Company's net profit, based upon such annual statements, subject to the Company's cash flows situation, the extent of its need for cash in order to finance its business as being at that time and/or its anticipated and/or planned future business, all as will be evaluated according to the exclusive discretion of Company's Board of Directors.

On March 29, 2011, the Company's Board of Directors determined that until the adoption of another resolution, in view of the Company's main business being in income-producing property, subject to any law and the needs of the Company, a dividend would be distributed from the Company's net profit, net of revaluations and net of the tax effects thereon, and in consideration of additional indexes that are characteristic of income-producing property companies such as the FFO index.

For the avoidance of doubt, it is clarified that the sum of the dividend to be distributed in the future is anticipated to be affected by the Company's profits and its business needs, including investment and business opportunities where an investment therein may reduce liquidity thereof. The Company shall include in its periodic and quarterly reports, as the case may be, disclosure with respect to every decision in connection with the implementation of this policy. The Company's Board of Directors may reevaluate and change the dividend distribution policy at any time, all according to its exclusive discretion.

4.2. The Company undertook, in the context of the issuance of Series A Bonds, not to distribute dividends to its shareholders, to the extent that such distribution will cause a decline in the rating of the Series A Bond, as specified in Section 17.5.2 of the Report. See Section 17.7 below for details concerning the Company's undertaking *vis-à-vis* the banking corporations to comply with certain credit restrictions.

4.3. On March 29, 2011, the Company’s Board of Directors approved, after having received the finance committee's recommendation, a cash distribution in the total amount of NIS 240 million constituting approx. 48% of the Company's net profit to the shareholders net revaluation and net of the tax effects in respect thereof. On April 27, 2011, the Company distributed to its shareholders the aforesaid amount (1.9790099 per share). For further details, see the Company’s immediate report as of March 30, 2011, reference: 2011-01-098883, which is included in this Report by way of reference.

4.4. On March 21, 2012, the Company’s Board of Directors approved, after having received the finance committee's recommendation, a cash distribution in the total amount of NIS 240 million constituting approx. 48% of the Company's net profit to the shareholders net revaluation, net of the tax effects in respect thereof and net of the effect of a change in the corporate tax rate (following recommendations of the Trajtenberg Committee), which constitutes 36% of the FFO for the income-producing property business, as specified in Section 1.1.7 of the Board of Directors' Report. For further details see immediate report as of March 22, 2012, which is released concurrently with this Report.

4.5. According to the Company’s Financial Statements as of December 31, 2011, the Company has a balance of retained earnings in the sum of approx. NIS 8.4 billion.

PART TWO: OTHER INFORMATION

5. Financial data regarding the Company's operating segments

The following is financial data of the Company, as specified in the Company's financial statements (in NIS thousands) for the years 2009 to 2011:

In view of the expansion of the Group's activity in the U.S. in 2011, commencing from the Financial Statements as of December 31, 2011, the Company's income-producing property activity overseas shall be presented in a separate reportable segment, as stated in Section 2 above. The data below with respect to years 2009-2010 were restated due to update of the operating segments as aforesaid.

Y2011:

	Commercial centers and malls in Israel	Office and other space for lease in Israel	Income-producing property in the U.S.A	Granite Hacarmel	Adjustments*	Consolidated
Revenues						
Revenues from outsiders	813,847	325,382	102,244	6,304,842	955	7,547,270
Revenues from other Group operating segments	---	---	---	---	---	---
Total	813,847	325,382	102,244	6,304,842	955	7,547,270
Attributed costs						
Costs not representing revenues from other Group operating segments	152,389	53,513	53,859	6,104,112	72	6,363,945
Cost representing revenues from other Group operating segments	---	---	---	---	---	---
Total	152,389	53,513	53,859	6,104,112	72	6,363,945
Profits from operations attributed to operating segment (NOI in the income-producing property segments)	661,458	271,869	48,385	200,730	883	1,183,325
Variable costs attributed to operating segment	152,389	53,513	53,859	5,425,789	72	5,685,622
Fixed costs attributed to operating segment				678,323		678,323
Rise (decline) in fair value of investment property	554,600	217,987	76,051	221	---	848,859
Profits from operations attributed to owners of parent company	659,250	269,621	45,353	120,735	883	1,095,842
Profits from operations attributed to rights which do not confer control	2,208	2,248	3,032	79,995	---	87,483
Total assets attributed to operating segment	9,424,443	4,279,980	1,091,725	5,497,368	---	20,293,516

* Adjustments to consolidated derive from business in the insurance segment, see Section 12.3 of the Report.

Y2010:

	Commercial centers and malls in Israel	Office and other space for lease in Israel	Income-producing property in the U.S.A	Granite Hacarmel	Adjustments*	Consolidated
Revenues						
Revenues from outsiders	754,137	301,641	35,032	5,252,470	642	6,343,922
Revenues from other Group operating segments	---	---	---	---	---	---
Total	754,137	301,641	35,032	5,252,470	642	6,343,922
Attributed costs						
Costs not representing revenues from other Group operating segments	139,823	54,870	14,399	5,074,980	49	5,284,121
Costs representing revenues from other Group operating segments	---	---	---	---	---	---
Total	139,823	54,870	14,399	5,074,980	49	5,284,121
Profits from operations attributed to operating segment (NOI in the income-producing property segments)	614,314	246,771	20,633	177,490	593	1,059,801
Variable costs attributed to operating segment	139,823	54,870	14,399	4,330,577	49	4,539,718
Fixed costs attributed to operating segment				744,403		744,403
Rise (decline) in fair value of investment property	775,703	109,096	6,977	(1,080)	---	890,696
Profits from operations attributed to owners of parent company	612,349	244,734	20,505	106,756	593	984,937
Profits from operations attributed to rights which do not confer control	1,965	2,037	128	70,734	---	74,864
Total assets attributed to operating segment	8,445,171	3,437,387	281,321	4,921,319	---	17,085,198

* Adjustments to consolidated derive from business in the insurance segment, see Section 12.3 of the Report.

Y2009:

	Commercial centers and malls in Israel	Office and other space for lease in Israel	Income-producing property in the US	Granite Hacarmel	Adjustments*	Consolidated
Revenues						
Revenues from outsiders	659,019	286,152	38,130	4,546,674	---	5,529,975
Revenues from other Group operating segments	---	---	---	---	---	---
Total	659,019	286,152	38,130	4,546,674	---	5,529,975
Attributed costs						
Costs not representing revenues from other Group operating segments	128,289	53,777	15,810	4,364,729	---	4,562,605
Costs representing revenues from other Group operating segments	---	---	---	---	---	---
Total	128,289	53,777	15,810	4,364,729	---	4,562,605
Profits from operations attributed to operating segment (NOI in the income-producing property segments)	530,730	232,375	22,320	181,945	---	967,370
Variable costs attributed to operating segment	128,289	53,777	15,810	3,692,808	---	3,890,684
Fixed costs attributed to operating segment	---	---	---	671,921	---	671,921
Rise (decline) in fair value of investment property	172,676	95,582	(46,173)	(4,399)	---	217,686
Profits from operations attributed to owners of parent company	(**)528,648	(**)230,177	22,163	(**)109,300	---	890,288
Profits from operations attributed to rights which do not confer control	(**)2,082	(**)2,198	157	(**)72,645	---	77,082
Total assets attributed to operating segment	7,266,457	3,268,305	284,498	4,356,715	---	15,175,975

* Adjustments to consolidated derived from the residential complex of the Modi'in project were reclassified to the office and other space for lease segment.

** The split between profit from business attributed to rights which do not confer control and profit from business attributed to the owners of the parent company was restated.

See the Company's Board of Directors' Report in Chapter B of this Report for the explanations of the Board of Directors with relation to the financial data of the Company as it appears in its Consolidated Financial Statements.

6. General environment and effect of external factors on the Company's business

Following are the assessments of the Company as to the major trends, events and developments in the macroeconomic environment of the Company, which to the best of its knowledge and belief, have or are anticipated to have an effect on the business results or the developments in the Group's operating segments.

The estimates of the Company below in this section and in this Report are based, *inter alia*, on data published and not independently examined by the Company. Every reference appearing in this section should be considered data not under the control of the Company and indefinite, and it is based, *inter alia*, on data published by the Bank of Israel, as specified below.

6.1 The business in Israel

As a company operating in the Israeli market, with its various industries, the Company is exposed to changes in the condition of the economy in general and in the real estate industry, in particular. The central factors affecting the business of the Company and the Group companies in Israel are specified below.

Israel	For the Year Ended on		
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2009
Macroeconomic parameters *			
Gross Domestic Product (PPP)	NIS 864 billion	Approx. NIS 813 billion	**Approx. NIS 768 billion**
Product per Capita (PPP)*	NIS 111,286	NIS 106,669	NIS 102,414
Growth rate in the Domestic Product (PPP)*	4.8%	4.8%	0.8%
Growth Rate in the Product per Capita (PPP)*	2.9%	2.9%	**(0.9%)**
**Inflation Rate ** **	2.17%	2.66%	3.91%
Return on long term domestic governmental debt * **	5%	4.68%	**5.06%**
Rating of long term governmental debt ** **	A1	A1	A1
Exchange Rate of domestic currency compared to the Dollar as of the last day of the year*	**3.821**	**3.549**	**3.775**

* Source: The site of the Central Bureau of Statistics in Israel - http://www.cbs.gov.il

** Source: Bank of Israel website - http://www.bankisrael.gov.il *** Source: The OECD website - http://www.oecd.org

**** Source: Ministry of Finance website – the Government Debt Management Unit (by the global rating company – Moody's) - http://www.ag.mof.gov.il/AccountantGeneral/GovDebt.

6.1.1 Global economic crisis - During 2011, the world experienced a financial crisis in some of the countries members of the Eurozone. The events related to the financial crisis affect the capital market and the financial system in Israel, *inter alia*, their liquidity, the state of their businesses and the ability of Israeli corporations that are either directly operating in the Eurozone countries and/or invest in entities and corporations operating in these countries (including investment in governmental bonds issued by Eurozone countries), to obtain financing for their on-going and long-term business. In light of this crisis, during the last months the international credit rating of a considerable number of central Eurozone countries was reduced (sometimes by more than one international rating agency), including France, Spain, Italy, Ireland, Greece, Portugal, Belgium, Cyprus and Slovenia.

Since the Israeli economy and banking system are exposed to the global economy, the development of the financial crisis may have a certain influence

on the Group's accessibility to resources for financing for its business both in the Israeli capital market and in the banking systems in Israel and overseas.

However, due to the Group's policy to focus its business mainly in the Israeli market (a policy expressed in a relatively low exposure to properties in the U.S.A. and negligible exposure to properties in Europe), the Group's management estimates that the direct influence of the development of the European debt crisis along with its consequences, value of properties and/or financial situation thereof is limited.

Furthermore, in light of high cash balances and cash equivalents, a strong cash flow, low leverage (that finds expression in conservative financial ratios) and the scope of income-producing properties that are not significantly pledged – the Group's management believes that negative developments in the global economy could have a low influence on its ability to raise financing resources from both the Israeli banking system and the Israeli capital market. However, as of the Date of the Report, the scope of the direct and indirect economic implications of the crisis, and its consequences, cannot be fully estimated.

6.1.2 Condition of the Israeli economy - In real terms, in 2011 the improvement trend in the Israeli market continued, and the real activity attests to the continuation in growth. The gross domestic product (GDP) increased by approx. 4.7% in 2011, the business product increased by approx. 5.2%, the private consumption increased by approx. 3.6% and a significant improvement in the employment condition had occurred. Nonetheless, the effects of the crisis in the Euroblock are evident also in the Israeli market, both from the standpoint of the slowdown in the growth rate of real activity and from financial standpoint, versus 2010. The growth in the domestic economic activity in 2011 encompassed most of the industries in the market and derived mainly from increase in the expense for private consumption (growth of approx. 3.6% in 2011) and growth in export (which was halted in the second half of 2011).[2]

According to the publications of the Bank of Israel, the growth forecast for 2012 is approx. 2.8%[3] and a moderate decrease of the interest is also expected deriving from the deterioration in the global conditions (specifically the damage to global demand for Israeli exports, the influence of the global slowdown on local demands (for private consumption and investments), and the expected downgrade of interest rate in the world). The Bank of Israel interest rate is expected to be 2.2% at the end of 2012[4].

From the financial aspect, the global crisis is reflected mainly through decreases in the prices of shares and corporate bonds. In 2011 the fluctuation in the capital markets continued, which found expression in a decline of 18% and 20% in the TA-25 Index and the TA-100 Index, respectively.

6.1.3 The income-producing property segment in Israel - Despite the negative trends that accompanied the global economy in the last two years, the negative

[2] Website of the Central Bureau of Statistics, press release, March 8, 2012, National Accounts for Israel for 2011 http://www.cbs.gov.il/reader/newhodaot/hodaa_template.html?hodaa=201208056.

[3] Bank of Israel, press release December 26, 2011, update to the macroeconomic forecast for the years 2011-2012, the Bank of Israel website http://www.bankisrael.gov.il/press/heb/111226/111226t.htm.

[4] Bank of Israel, press release, December 26, 2011, the Bank of Israel interest for the month of January shall remain unchanged. http://www.bankisrael.gov.il/press/heb/111226/111226maafn.htm

influence on the income-producing property segment in Israel, in the standpoint of the level of demand, the occupancy and the cash flows was, to the Company's belief, immaterial, contrary to most of the European markets in which the crisis left its mark to a substantial extent also on the income-producing property segment, being a segment reliant to a great extent on financing properties.

During 2010-2011, an increase occurred in the Group's business in the commercial centers and malls segment and in the office and other space for lease segment, as specified in this Chapter below. Transactions performed in the the income-producing property segment in Israel during the last year reflect low yield rates compared with the yield rates in previous years. To the Company's belief, the yield rates mainly reflect the low financing costs for certain bodies in the market due to the low interest environment that made, for some of the companies in the economy, the investment in income-producing property an attractive alternative in comparison to other investments, *inter alia* due to the historically high capitalization rates, compared to most of the European markets and in relation to the local interest rate.

For further details in connection with each of the Company's operating segments, see Sections 8, 9 and 10 of the Report.

6.1.4 The capital market in Israel – the local capital market serves as a source for raising funds for the financing of the Company's business activity, whether through shares or through bonds. In 2011, the TA-100 Index declined by approx. 20% to a level of 978 points, and approx. NIS 3.3 billion were raised on the share market in Tel Aviv, compared with an amount of NIS 8.5 billion in 2010[5]. The business sector raised in 2011 through issuances and allotments of ordinary bonds and special bonds to institutional investors, an amount of NIS 40.6 billion compared with an amount of NIS 41.9 billion in 2010. In 2011 the TA RealEstate-15 Index declined by approx. 23.2% to a level of 267.1 points. To the Company's management belief, the continuation of this trend may make difficult the possibility of raising funds on the capital market.

6.1.5 Political-security situation - The Company's business is affected by the political-security situation in Israel. The Company's management estimates that deterioration in the political security situation may cause a decline in the business in malls and commercial centers, decline in demands and a decrease in prices in the income-producing property segment.

6.1.6 Credit availability and cost - Changes in financing cost and availability and the scope of available credit in the banking and non-banking system affect the real estate industry and the profitability thereof. As a result of the implementation of structural reforms implemented in recent years in the capital market (such as the Bachar Reform, the pension reform and the tax reform) the banks ceased being the main credit providers to the business sector, and a non-banking credit market had developed, constituting an alternative for financing assets and projects. At the end of 2011, the issuances of the business (non-finance) sector totaled in approx. NIS 26 billion, from which approx. 78% in marketable bonds on TASE. In the second half of 2011 private non-financial sector's bond raising

[5] The Tel Aviv Stock Exchange Annual Review 2011, from the TASE website http://www.tase.co.il/TASE/Statistics/ResearchReviews/2010/Research_2010_12_164825.htm.

rate decreased to approx. NIS 8 billion compared with approx. NIS 18 billion in the first half of the year[6].

In light of this market condition and due to the financial strength of the Company, its accessibility to sources of bank financing, and the relatively low scope of pledges on properties, taking into consideration the extent of business thereof, the Company estimates that no material difficulties are anticipated in raising the financing required thereby.

6.1.7 Fluctuations in the inflation rate, the Consumer Price Index and the interest rates - The real estate industry is exposed to risks deriving from changes in the inflation rate, the Consumer Price Index and interest rates. The Company finances most of its business operations by means of loans linked to the Consumer Price Index and linked to the prime interest or to the Bank of Israel interest. In addition, most of the Company's revenues from rent are also linked to the Consumer Price Index. The Consumer Price Index increased during the years of 2010 and 2011 by 2.7% and by 2.2%, respectively. The Research Department in the Bank of Israel published a forecast, whereby in 2012 the inflation shall be at a rate of 2.1%[7]. The prime interest increased in 2011 at a rate of 0.75% (from 3.5% as of December 31, 2010 to 4.25% as of December 31, 2011). The Bank of Israel interest increased in 2011 at a rate of 0.75% (from 2.0% as of December 31, 2010 to 2.75% as of December 31, 2011).

6.1.8 Fluctuations in the exchange rate of the U.S. dollar - Changes in the exchange rate of the dollar have a marginal effect on the growth rate of the Consumer Price Index in Israel and on the economic results of the Company, as to which, for the most part, its functional currency for operations outside of Israel is in dollars. In 2011, the exchange rate of the dollar rose at the rate of approx. 7.7%.

6.1.9 Changes in global petroleum prices – In 2010-2011 and until the Date of the Report, a rise occurred in the global petroleum price, *inter alia* due to uncertainty in connection with the regular supply of petroleum as a result of the political instability and security situation in oil producing Arab countries, and in view of international sanctions that were imposed on Iran, which may harm the supply of petroleum from the gulf countries. The rise in petroleum prices has a direct effect on the results of Granite Hacarmel, and causes an increase in the receivables of Granite Hacarmel, in the value of the inventory balances, and accordingly an increase in the scope of banking credit, which increases the financing expenses of Granite Hacarmel, as well as a decline in the demand for the petroleum products. The increase in the scope of the receivables may also cause an increase in the credit risks of Granite Hacarmel as a result of exposure to doubtful debts. On the other hand, an increase in the petroleum prices causes profits in respect of the operating inventory of Granite Hacarmel, once used.

6.1.10 Increase of the excise on diesel oil and gasoline – Excise tax is imposed in a fixed amount on every liter of fuel, in accordance with the type of fuel, and the rate thereof is a significant component in the final consumer price. In recent years, government policy has been to raise the excise on diesel oil and gasoline, which has led to an increase in the price thereof. Such increase raises the price

[6] Bank of Israel, press release January 25, 2012, the development of the debt of the business sector November-December 2011. http://www.bankisrael.gov.il/press/heb/120125/120125h.htm

[7] Bank of Israel, press release, January 23, 2012, the interest of the Bank of Israel for February 2012 will decline by 0.25% to a level of 2.5%, the website of the Bank of Israel http://www.bankisrael.gov.il/press/heb/120123/120123awar.htm

of the diesel oil and gasoline, and as a result thereof causes an increase in Granite Hacarmel's receivables and the scope of the financing required thereby, due to the gap between the date of remittance of the excise to the tax authority and collection of the debt from the customer.

6.1.11 Privatizations in the fuel market – Privatization of the refineries in Israel may have repercussions on Granite Hacarmel's business, both due to new regulation as a result of these privatizations and from the perspective of ORL's ability to engage in direct marketing of fuels so long as its market share in the fuel segment shall not exceed 20% of the marketing business in Israel. ORL's privatization, including the various implications thereof, may have adverse effects on Granite's results of operations. In addition, privatization of the fuel terminals at Pi Glilot may confer upon Delek, The Israel Fuel Corp. Ltd. a relative advantage over its competitors, mainly in the storage and trade of fuels, and therefore may adversely affect Granite's results.

6.2 The business in the U.S.A.

U.S.A.	For the Year Ended on		
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2009
Macroeconomic parameters			
Gross Domestic Product (PPP) (1) (U.S. $ in billions)	15,065	14,527	**13,939**
Product per Capita (PPP) (1) (U.S. $)	48,147	46,860	**45,348**
Growth rate in the Domestic Product (PPP) (1)	3.71%	4.22%	**(2.47%)**
Growth Rate in the Product per Capita (PPP) (1)	2.75%	3.33%	**(3.31%)**
Inflation Rate (2)	3%	1.5%	**2.7%**
Return on long term domestic governmental debt (3)	1.89%	3.3%	**3.85%**
Rating of long term governmental debt (4)	AA+/Negative	AAA/Stable	AAA/Stable
Exchange Rate Shekel to U.S. Dollar (5)	3.821	**3.549**	**3.775**

(1) The product data is based on a publication of the International Monetary Fund ("**IMF**") of September 2011 (http://www.imf.org). .
(2) According to publications of the US Department of Labour.
(3) According to the US Department of Treasury with respect to bonds for a period of 10 years from December 31, 2011.
(4) According to the rating of S&P (www.standardandpoor.com).
(5) According to data of the Bank of Israel.

The Company's business in the U.S.A. is influenced mostly by the economic situation in the U.S. economy in general, and in the income-producing commercial property segment, in particular, the demand and supply in the area in which the Company's properties are located and the volume of its rent.

Just like in 2010, during 2011 too, the U.S. economy continued to recover from the recession that had haunted it more than two years before, although in 2011 a slowdown in the said recovery was evident, as well as a slowdown in the financial activity in the U.S. compared to 2010. In accordance with the figures of the IMF, the growth in the second half of 2010 in the U.S. decreased from an annual rate of 2.75% to 1% in the first half of 2011, *inter alia* due to the shift of most of the demand from the public market to the private market.

To the best of the Company's knowledge, in accordance with IMF figures, household and business confidence declined and market volatility rose significantly due to the concerns with respect to the lukewarm recovery, the decline in the credit rating of the U.S., and the fears regarding the financial situation in Europe.

In the area of financing and access to capital, in 2010 and 2011, the liquidity level in the commercial mortgage-backed securities (CMBS) market improved, even though high volatility in this market during 2011 caused providers of credit of this type to act cautiously upon giving new loans[8].

The City of Houston, Texas

The Houston metropolis, with a population of approx. 5.9 million people, and in which most of the Group's properties in the operating segment are located, presented a higher than U.S. average rise in population growth in the last 30 years. In addition, on the basis of an examination of the last results of the population censuses in the U.S. in 2000 and 2010 that was carried out by the Kinder Institute for Urban Research of Rice University, the growth in the number of residents in Houston during this decade is the highest from among the other urban areas of the U.S. Even though New York, Los Angeles and Chicago continue to top the list of the U.S. cities with the highest population, high quality of life, limited government and attractive cost of living contributed to the population growth in Houston.

While the continuing national recovery from the recession was not uniform in most of the U.S., it is evident that the recovery process in Houston is one of the fastest in the U.S., and statistics show that Houston has begun to restore the majority of the jobs that were lost at the beginning of the last crisis. Thus, in Houston, a general increase in the number of jobs was recorded at the rate of 3% in 2011 compared with the previous year[9], which figure is much higher than the average in the U.S. After delaying large projects in 2008 and 2009, many energy companies began increasing their investment budgets, leading to growth in the number of jobs in the city of Houston, which significantly relies on energy companies and bodies. In addition to expansion in the gas and energy sector, Houston's economy is expected, to the best of the Company's knowledge, to also be affected by growth in the activity of Houston's port and its large medical center[10].

See Section 25 of the Report for discussions of the risk factors to which the Group is exposed.

The above information in Sections 6.1 and 6.2 concerning the general environment and the external factors that affect the Company's business, includes information based on subjective estimates and approximations of the Company in consideration of past experience, as well as publications and surveys written by professionals in connection with the condition of the Israeli economy, the real estate industry, and the condition of the economy in countries in which the Company operates, as detailed above in this section. The above data are only approximations and it is possible that they are incomplete, but, in the Company's estimation, are able to provide a general picture, even if inexact, of the markets in which it operates in the various operating segments. In view of the above, and due to the existence of causes beyond the control of the Company, the actual results may vary from the estimates specified above and below if a change should take place in one of the factors which were taken into account in these estimates or the economic crisis shall aggravate, the condition of the economy and/or the security situation shall become worse or due to the realization of any of the risk factors specified in Section 25 of the Report, and mainly the world financial crisis, the

[8] In accordance with publications of real estate consulting company Cushman and Wakefield.
[9] In accordance with the National Office Market Summary and Highlights 2011 HFF - of January 2012.
[10] The data is from publications of real estate consulting company Cushman and Wakefield.

condition of the economy in Israel and in the U.S. and the security situation in Israel, changes in relevant interest rates and indices, decline in demand for space for lease and in rent prices, deterioration of strength of primary tenants and costs of financing sources.

PART THREE: DESCRIPTION OF THE GROUP'S BUSINESS IN THE INVESTMENT PROPERTY SEGMENT - AGGREGATE

7. Aggregate disclosure with respect to the investment property segment (disclosure is made jointly for the commercial centers and malls segment in Israel and for the office and other space for lease segment in Israel and for the income-producing property segment in the U.S.)

7.1 General

The Group began its activity in the income-producing investment property segment in 1983 and since then and as of the Date of the Report the Company operates in development, construction, acquisition, lease, management and maintenance of malls and commercial centers in Israel as well as office and hi-tech parks, office and industry, light industry and storage buildings in Israel. Commencing from 2001 the Company began to operate in these segments also overseas (U.S.A. and UK). For details on two transactions for acquisition of office towers in Houston Texas, U.S.A. during the Report Period and subsequently, see Sections 10.9 and 10.10 of this Chapter.

Underlying the Company's policy is the basic assumption whereby the property's location is the most important factor for its success. Accordingly, upon examination of the location of a potential property, the Company ascribes significant weight to the population growth potential in the examined area and the urban development anticipated therein, based, *inter alia*, on urban research, segmentation of the existing and anticipated population and the unique or typical commercial needs of such area.

The Company's properties in the commercial centers and malls segment are located in the center of residential neighborhoods in developed cities characterized by a population whose socio-economic level ranges from average to high, and at entrances to developed urban areas, insofar as possible, on main traffic arteries. Due to the location of the properties, their accessibility, spacious car parks, tenant mix and variety of activities therein, they attract a large and diverse target audience. Some of the commercial centers include office space for lease designated to provide a supplementary response for the target audience's needs, according to the nature of the commercial center and its location.

According to its policy and profit maximization, the Company acts, insofar as necessary, to upgrade its properties, while using the existing and potential commercial, office and other areas, improving the tenant mix and adjusting the same to the target audience.

The Group's strategy and business in the investment property segment is performed both through initiation, development and construction of new properties and acquisition of existing income-producing property, upgrading the same and maximizing potential thereof.

The Group, by itself (through companies which are entirely controlled thereby), manages and operates the properties, their construction and betterment while using the know-how and experience accrued by the Group, in order to give added value to its properties, tenants and the public visiting the properties.

Set forth below are aggregate figures regarding investment property owned by the Group[11]. The figures will be presented jointly with regard to properties from the three operating segments of investment property owned by the Company, namely: commercial centers and malls segment in Israel, the office and other space for lease segment in Israel and the income-producing property segment overseas. For further details regarding the operating segments and regarding material properties and very material properties, see Sections 8 and 9 of this Chapter.

7.2 Summary results in the investment property segments

7.2.1 Summary of the aggregate results in the Group's three investment property segments

Parameter	For the Year ended on		
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2009
	NIS in millions		
Total business revenues (consolidated)	1,241	1,091	983
Profit/loss from revaluations (consolidated)	849	892	222
Business profits (consolidated)	1,831	1,774	1,007
Same property NOI (consolidated)	903	852	---
Same property NOI (corporation's share)	896	848	---
Total NOI (consolidated)	982	882	785
Total NOI (corporation's share)	974	878	781

* The figures do not include the investment properties component appearing in Granite Hacarmel which does not constitute a part of the income-producing property segment of the Company.

7.2.2 Summary of the results in the commercial centers and malls in Israel segment

Parameter	For the Year ended on		
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2009
	NIS in millions		
Total business revenues (consolidated)	814	754	659
Profit/loss from revaluations (consolidated)	555	776	173
Business profits (consolidated)	1,217	1,390	704
Same property NOI (consolidated)	612	584	---
Same property NOI (corporation's share)	610	582	---
Total NOI (consolidated)	662	614	531
Total NOI (corporation's share)	659	612	529

[11] The figures in this Section 7 will be disclosed in accordance with the disclosure directives for the investment property industry that was published on the Israel Securities Authority's website on January 11, 2011.

7.2.3 Summary of the results in the office and other space for lease in Israel segment

Parameter	For the Year ended on		
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2009
	NIS in millions		
Total business revenues (consolidated)	325	302	286
Profit/loss from revaluations (consolidated)	218	109	95
Business profits (consolidated)	490	356	327
Same property NOI (consolidated)	272	247	---
Same property NOI (corporation's share)	270	245	---
Total NOI (consolidated)	272	247	232
Total NOI (corporation's share)	270	245	230

7.2.4 Summary of the results in the income-producing property in the U.S. segment

Parameter	For the Year ended on		
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2009
	NIS in millions		
Total business revenues (consolidated)	102	35	38
Profit/loss from revaluations (consolidated)	76	7	(46)
Business profits (consolidated)	124	28	(24)
Same property NOI (consolidated)	19	21	---
Same property NOI (corporation's share)	16	21	---
Total NOI (consolidated)	48	21	22
Total NOI (corporation's share)	45	21	22

7.3 The geographic regions in which the Group operates in the investment property segments

As of the Date of the Report, the Company operates in two main geographic regions, Israel and the U.S.A. Most of the Company's business is in Israel, where the Company operates throughout the country, including North, Center, South and other urban areas, with no preference of specific areas and without investing special managerial inputs in specific areas. In the U.S.A. the Company operates, as of the Date of the Report, mainly in Houston, Texas, in the U.S.

For details regarding the macroeconomic parameters affecting the business in Israel and the U.S.A., see Section 6 above.

7.4 Segmentation of the investment property business

Set forth below are details of the Company's investment property business, in the three investment property operating segments, namely, the malls and commercial centers in Israel, the office and other space for lease in Israel and income-producing property in the U.S.A., in a consolidated manner, segmented according to the various uses of the space of each segment. All of the figures in the following tables do not contain the investment property component appearing in Granite Hacarmel, which does not constitute part of the income-producing property segment of the Company. The commercial use in Israel in the tables below is attributed to the commercial centers and malls operating segment, whereas the office, industrial and residential uses are attributed in Israel to the office and other space for lease operating segments (and do not constitute operating segments in themselves). All of the figures of the income-producing property segment in the U.S.A. appear under the U.S.A. region, in accordance with the various segmentations, which also do not constitute operating

segments in themselves. The segmentation of uses below is in the format in which the information is presented to the Group's management. As a rule, the Company does not deem the car parks as an income-producing property of the Company, and therefore in properties whose main use is commerce, the car park was attached to such use, whereas in properties whose main use is offices, the car park was attached to such use. As for the Tel Aviv Azrieli Center, for the purpose of the Report, the car park space is divided equally between the commercial and office uses, due its being a car park common to both uses.

In the Report below, the following terms shall have the meanings set forth beside them:

"**Space**"/"**Area**" – the space/area for which rent is paid, with the addition of unleased areas (excluding areas sold or acquired after the Date of the Report, if any).

"**Revenues**" – all payments made by the tenant, including rent, management fees, profit from electricity, parking fees and other payments, if any.

(1) Segmentation (aggregate) of income-producing property space by regions and uses, as of December 31, 2011 (in sqm)

Regions	Uses	Office	Industrial	Commercial	Residential	Parking lots	Total	% of total property area
Israel	Consolidated	254,844	18,635	255,814	8,698	389,449	927,440	82%
	Corporation's share	252,734	18,635	254,915	8,622	387,055	921,960	83%
U.S.A.	Consolidated	133,561	-	12,973	-	55,345	201,879	18%
	Corporation's share	123,395	-	12,973	-	55,023	191,391	17%
Total	Consolidated	388,405	18,635	**268,787**	8,698	444,794	**1,129,319**	100%
	Corporation's share	376,129	18,635	**267,888**	8,622	442,078	**1,113,351**	100%
% of total property area	Consolidated	**34%**	**2%**	**24%**	**1%**	**39%**	**100%**	
	Corporation's Share	**34%**	**2%**	**24%**	**1%**	**39%**	**100%**	

(2) Segmentation (aggregate) of income-producing property space by regions and uses, as of December 31, 2010 (in sqm)

Regions	Uses	Office	Industrial	Commercial	Residential	Parking lots	Total	% of total property area
Israel	Consolidated	252,657	18,635	228,755	8,698	374,100	882,845	90%
	Corporation's share	250,549	18,635	228,058	8,622	371,840	877,704	90%
U.S.A.	Consolidated	34,674	--	12,973	--	55,345	102,992	10%
	Corporation's share	34,397	--	12,973	--	55,023	102,393	10%
Total	Consolidated	287,331	18,635	241,728	8,698	426,863	985,837	100%
	Corporation's share	284,946	18,635	241,031	8,622	426,501	980,097	100%
% of total property area	Consolidated	**29%**	**2%**	**25%**	**1%**	**43%**	**100%**	
	Corporation's Share	**29%**	**2%**	**25%**	**1%**	**43%**	**100%**	

(3) Segmentation (aggregate) of fair value of income-producing property, by regions and uses, as of December 31, 2011 (NIS in thousands)[12]

Regions	Uses	Office	Industrial	Commercial	Residential	Total	% of total property area
Israel	Consolidated	3,499,490	79,550	9,143,580	102,190	12,824,810	92%
	Corporation's share	3,469,896	79,550	9,111,740	101,294	12,762,480	93%
U.S.A.*	Consolidated	1,027,762	---	42,986	---	1,070,748	8%
	Corporation's share	951,115	---	42,986	---	994,101	7%
Total	Consolidated	4,527,252	79,550	9,186,566	102,190	13,895,558	100%
	Corporation's share	4,421,011	79,550	9,154,726	101,294	13,756,581	100%
% of total property area	Consolidated	32%	1%	66%	1%	100%	
	Corporation's Share	**32%**	**1%**	**66%**	**1%**	**100%**	

* Amounts are translated into NIS in accordance with exchange rate of $1=NIS 3.821.

[12] The fair value of all of the Group's income-producing properties is in accordance with valuations that the Group has received which were performed by licensed land appraisers, independent of the Company or of the Group's companies as of December 31, 2011.

(4) Segmentation (aggregate) of fair value of income-producing property, by regions and uses, as of December 31, 2010 (in NIS thousands)

Regions	Uses	Office	Industrial	Commercial	Residential	Total	% of total property area
Israel	Consolidated	3,219,375	77,280	8,221,578	102,190	11,620,423	98%
	Corporation's share	3,192,037	77,280	8,195,704	101,294	11,566,315	98%
U.S.A.*	Consolidated	233,898	--	43,830	--	277,728	2%
	Corporation's share	232,179	--	43,830	--	276,009	2%
Total	Consolidated	3,453,273	77,280	8,265,408	102,190	11,898,151	100%
	Corporation's share	3,424,216	77,280	8,239,534	101,294	11,842,324	100%
% of total property area	Consolidated	29%	1%	69%	1%	100%	
	Corporation's Share	29%	1%	69%	1%	100%	

* Amounts are translated into NIS in accordance with exchange rate of $1=NIS 3.549.

(5) Segmentation (aggregate) of income-producing property NOI, by regions and uses, for the year ended on December 31, 2011 (in NIS thousands)

Regions	Uses[1]	Office	Industrial	Commercial	Residential	Total	% of total NOI of the properties
Israel	Consolidated	262,229	6,392	661,458	3,248	933,327	**95%**
	Corporation's share	260,009	6,392	659,250	3,220	928,871	**95%**
U.S.A.*	Consolidated	45,856	---	2,529	---	48,385	**5%**
	Corporation's share	42,824	---	2,529	---	45,353	**5%**
Total	Consolidated	308,085	6,392	663,987	3,248	981,712	**100%**
	Corporation's share	302,833	6,392	661,779	3,220	974,224	**100%**
% of total NOI of the properties	Consolidated	31%	1%	68%	---	100%	
	Corporation's Share	31%	**1%**	**68%**	**---**	**100%**	

(1) The car park NOI was attached to the main use of the property, see note in this Section 7.4 above.

*Amounts are translated into NIS in accordance with exchange rate of $1=NIS 3.578.

(6) Segmentation (aggregate) of income-producing property NOI, by regions and uses, for the year ended on December 31, 2010 (NIS in thousands)

Regions	Uses[1]	Office	Industrial	Commercial	Residential	Total	% of total NOI of the properties
Israel	Consolidated	237,530	6,146	614,314	3,095	861,085	98%
	Corporation's share	235,520	6,146	612,349	3,068	857,083	98%
U.S.A.*	Consolidated	17,333	--	3,300	--	20,633	2%
	Corporation's share	17,205	--	3,300	--	20,505	2%
Total	Consolidated	254,863	6,146	617,614	3,095	881,718	100%
	Corporation's share	252,725	6,146	615,649	3,068	877,588	100%
% of total NOI of the properties	Consolidated	29%	1%	70%	0%	100%	
	Corporation's Share	29%	1%	70%	0%	100%	

(1) The car park NOI was attached to the main use of the property, see note in this Section 7.4 above.
*Amounts are translated into NIS in accordance with exchange rate of $1=NIS 3.733.

(7) Segmentation (aggregate) of income-producing property NOI, by regions and uses, for the year ended December 31, 2009 (in NIS thousands)

Regions	Uses[1]	Office	Industrial	Commercial	Residential	Total	% of total NOI of the properties
Israel	Consolidated	223,728	6,123	530,730	2,524	763,105	97%
	Corporation's share	221,555	6,123	528,648	2,499	758,825	97%
U.S.A.*	Consolidated	18,424	--	3,896	--	22,320	3%
	Corporation's share	18,267	--	3,896	--	22,163	3%
Total	Consolidated	242,152	6,123	534,626	2,524	785,425	100%
	Corporation's share	239,822	6,123	532,544	2,499	780,988	100%
% of total NOI of the properties	Consolidated	31%	1%	68%	0%	100%	
	Corporation's Share	31%	1%	68%	0%	100%	

(1) The car park NOI was attached to the main use of the property, see note in this Section 7.4 above.

(8) Segmentation (aggregate) of income-producing property revaluation profits (losses), by regions and uses, for the year ended December 31, 2011 (in NIS thousands)

Regions	Uses[1]	Office	Industrial	Commercial	Residential	Total	% of total revaluation profits
Israel	Consolidated	215,392	2,350	554,600	245	772,587	91%
	Corporation's share	213,314	2,350	551,565	243	767,473	92%
U.S.A.*	Consolidated	80,735	---	(4,684)	---	76,051	9%
	Corporation's share	75,080	---	(4,684)	---	70,396	8%
Total	Consolidated	296,127	2,350	549,916	245	848,638	100%
	Corporation's share	288,394	2,350	546,881	243	837,868	100%
% of total revaluation profits	Consolidated	35%	---	65%	---	100%	
	Corporation's Share	35%	---	65%	---	100%	

(1) The car park revaluation profits (losses) were attached to the main use of the property, as stated in this Section 7.4 above.
*Amounts are translated into NIS accordance with exchange rate of $1=NIS 3.578.

(9) Segmentation (aggregate) of income-producing property revaluation profits (losses), by regions and uses, for the year ended December 31, 2010 (in NIS thousands)

Regions	Uses[1]	Office	Industrial	Commercial	Residential	Total	% of total revaluation profits
Israel	Consolidated	88,042	2,254	775,703	18,800	884,799	99%
	Corporation's share	87,355	2,254	772,736	18,635	880,980	99%
U.S.A.*	Consolidated	9,182	--	(2,205)	--	6,977	1%
	Corporation's share	9,064	--	(2,205)	--	6,859	1%
Total	Consolidated	97,224	2,254	773,498	18,800	891,776	100%
	Corporation's share	96,419	2,254	770,531	18,635	887,839	100%
% of total revaluation profits	Consolidated	11%	0%	87%	2%	100%	
	Corporation's Share	**11%**	**0%**	**87%**	**2%**	**100%**	

*Amounts are translated into NIS accordance with exchange rate of $1=NIS 3.733.

(10) Segmentation (aggregate) of income-producing property revaluation profits (losses), by regions and uses, for the year ended December 31, 2009 (in NIS thousands)

Regions	Uses[1]	Office	Industrial	Commercial	Residential	Total	% of total revaluation profits
Israel	Consolidated	97,293	790	172,676	(2,501)	268,258	121%
	Corporation's share	96,336	790	172,319	(2,476)	266,969	121%
U.S.A.*	Consolidated	(44,203)	--	(1,970)	--	(46,173)	(21%)
	Corporation's share	(43,697)	--	(1,970)	--	(45,667)	(21%)
Total	Consolidated	53,090	790	170,706	(2,501)	222,085	100%
	Corporation's share	52,639	790	170,349	(2,476)	221,302	100%
% of total revaluation profits	Consolidated	24%	0%	77%	(1%)	**100%**	
	Corporation's Share	**24%**	**0%**	**77%**	**(1%)**	**100%**	

(1) The car park revaluation profits (losses) were attached to the main use of the property, as stated in this Section 7.4 above.
*Amounts are translated into NIS accordance with exchange rate of $1=NIS 3.933.

(11) Segmentation of actual average monthly rent per sqm by regions and uses

Uses	Office		Industrial		Commercial		Residential	
	For the year ended on							
	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Israel (in NIS)	74	73	32	32	*208	*215	34	33
Maximum	(**)91	(**)90	-	-	316	315	-	-
Minimum	44	44	-	-	78	63	-	-
U.S.A. (in US$)	17	17	--	--	7	7	--	--
Maximum	--	--	--	--	--	--	--	--
Minimum	--	--	--	--	--	--	--	--

Maximum represents the average rent per sqm in a property of which the rent average is the highest, while the minimum represents the average rent per sqm in which the average rent is the lowest.

* The extensive range of rent in all of the uses derives, *inter alia*, from the diversity in the nature of the leased property, in the type of the leased unit in the property even in the same building, and in other parameters that are not expressed in this table.

The decrease in the average rent in 2011 compared to 2010 derives from the opening of the malls in Akko and in Kiryat Ata, the rent in which is lower than the average rent of the Group's other malls.

** The maximum represents the average rent per sqm of Azrieli Center towers, and does not include the rent of the hotel. If the average would have included the rent of the hotel, then the average for 2011 would have been approx. NIS 88 per sqm, and for 2010 approx. NIS 86 per sqm.

(12) Segmentation of average monthly rent per sqm with respect to the contracts signed in the period of the Report by regions and uses*

Uses	Office		Industrial		Commercial		Residential	
	For the year ended on							
	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Israel (in NIS)	79	70	41	--	**189	229	37	33
U.S.A. (in $)	16	13	--	--	--	172	--	--

* The figures do not include contracts signed due to storages and stalls and are due to new contracts only, excluding renewals of options.
** The decrease in 2011 derives from the opening of the Akko Azrieli mall and the Kiryat Ata Azrieli mall in 2011 at a lower rent than the average of the Group's other malls.

(13) Segmentation of average occupancy rates by regions and uses*

Uses	Office			Industrial			Commercial			Residential		
	In Percentages (%)											
	As of 31.12.11	As of 2011	As of 2010	As of 31.12.11	As of 2011	As of 2010	As of 31.12.11	As of 2011	As of 2010	As of 31.12.11	As of 2011	As of 2010
Israel	99%	96%	91%	100%	100%	100%	**99%	~100%	100%	100%	100%	100%
U.S.A.	87%	82%***	88%	--	--	--	69%	77%	85%	--	--	--

* The average occupancy rate was calculated based on the lease agreements' data for the beginning of the period and for the end of each period. During the Report Period no material changes occurred in the occupancy rate.
** The decrease in the occupancy rate derives from the opening of Akko Azrieli mall and Kiryat Ata Azrieli mall in 2011, whose population has not yet been completed. For information regarding the occupancy rate of these malls, see Section 1.3.2.
*** The decrease in the occupancy rate derives from the acquisition of office towers in Houston, Texas in February 2011. For details regarding the acquisition, see Section 10.9.

(14) Segmentation of number of income-producing properties, by regions and uses*

Uses	Office		Industrial		Commercial		Residential	
	For the year ended on							
	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Israel	7	7	1	1	13	11	1	1
U.S.A.	4	3	--	--	1	1	--	--
Total no. of income-producing properties	11	10	1	1	14	12	1	1

* Some properties have several different uses, and in such cases the properties were classified in the table under each of such uses.
* After the date of the statement of financial position, the Company had completed the acquisition of an additional income-producing property in Houston, U.S.A. For details, see Section 10.10.

(15) Segmentation of average actual yield rates (according to year-end value), by regions and uses*

The rate of the yield is a division of the actual NOI by the value of the property as of end of year. In the event of the acquisition of properties or completion of construction of malls in the course of the year, the index does not reflect the rate of the annual yield from these properties. The rate of the yield in practice does not constitute the CAP rate that the Group used for revaluation of its properties.

Uses	Office		Industrial		Commercial		Residential	
	For the year ended on (in %)							
	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Israel	**7.49%**	7.38%	**8.04%**	7.95%	**7.23%**	7.47%	**3.18%**	3.03%
U.S.A.	4.46%	**7.41%**	---	---	5.88%	**7.53%**	---	---

***** During 2011, office towers were acquired in Texas, U.S., and the Azrieli Akko and Kiryat Ata malls were opened. At the end of 2010, the properties used for commerce include the Haifa Mall that was acquired in February 2010. In addition, the properties leased for offices include the E Tower in Herzliya, whose population began in September 2010.
The figures do not represent representative yield but rather the division of actual NOI by the value of the properties, and do not take into account other influences, such as properties populated, properties purchased during the period and revenues expected from vacant space.

7.5 Projected revenues due to signed lease contracts (NIS in thousands)

Period of Revenue Recognition		Revenues from Fixed Components	Number of Contracts Ending	**Space Contemplated in the Ending Agreements (sqm in thousands)**
Y2012	Q/1	300,457	76	9
	Q/2	297,130	123	18
	Q/3	286,444	141	21
	Q/4	278,298	207	26
Y2013		980,672	728	142
Y2014		719,697	743	96
Y2015		487,676	759	134
Y2016 and forth		789,178	495	213
Total		4,139,552	3,272	659

The revenues figures in the above table were calculated based on the basic amounts determined in the lease agreements, linked to the Consumer Price Index known on December 31, 2011, and based on the following assumptions: (1) The exercise of the lessees' options to extend the lease periods included in the lease contracts, was not taken into account, since the main operating decision maker does not review, on a regular basis, the expected revenue figures under the assumption of the exercise options granted to the lessees to the extend the lease period; (2) Lease contracts, the lease period under which has ended, and new lease contracts have not yet been signed with the lessees, were not taken into account; (3) The possibility of sale of the properties or the purchase of new income-producing property, was not taken into account; (4) Fines due to early termination, if any, were not taken into account; (5) The increments to the rent due to percentages of the sales were not taken into account for calculation of the rent, and (6) No change has occurred in the management fees advance payments per tenant in respect of 2011.

The Company's revenues from variable components pertain to additional revenue from sales alone. The Company does not prepare estimates for revenues from variable components which are immaterial in relation to the Company's revenues from its income-producing properties, and therefore it does not have the information.

The revenue figures specified in the above table are under the assumption that the options for extending the lease periods included in the lease contract will not be exercised, although many of the tenants in the Company's space usually tend to extend the lease agreements upon the termination thereof.

The above figures are based on the Company's belief considering signed agreements as of the Date of the Report and constitute forward-looking information, as this term is defined in the Securities Law. Actual results may significantly differ from the above specified estimates and the implications thereof, for various reasons, including early termination of lease contracts or a business crisis of any of the lessees.

7.6 Main tenants

In 2011 the Company did not have a tenant, the revenue from whom constituted 10% or more of its total revenues.

7.7 Exposure to a specific industry in the tenants' business

To the Company's belief, as of the Date of the Report, the Company has no material exposure to a specific industry from among the businesses of the tenants in its income-producing properties. For details regarding trends that characterize the industries of the tenants in the Company's commercial properties, see Section 8.1.2 below.

7.8 Properties under construction In Israel (aggregate level) by uses*

Uses****	Parameters	For the Year Ended on		
		December 31, 2011	**December 31, 2010**	**December 31, 2009**
Commercial	Number of properties under construction at the end of the period	3	4	**4**
	Total space under (planned) construction at the end of the period (sqm in thousands)**	80	83	**83**
	Total costs invested in the current period (consolidated) (NIS in thousands)	2,036	66,665	**27,459**
	The amount at which the properties are presented in the statements at the end of the period (consolidated) (NIS in thousands)	177,242	223,593	**92,803**
	Construction budget in the consecutive period (estimate) (consolidated) (NIS in thousands)	87,000-92,000	185,000-240,000	**70,000 – 60.000**
	Total estimated balance of construction budget for completion of the construction work (consolidated) (estimate as of the end of the period) (NIS in thousands)	657,500-737,500	690,000-805,000	**740,000-835,000**
	Rate of built-up area in respect of which lease contracts have been signed (%)	13%	6%	**0%**
	Projected annual income from projects that will be completed in the consecutive period (consolidated) (estimate) (NIS in thousands)***	--	--	**---**
Offices	Number of properties under construction at the end of the period	3	2	**3**
	Total space under (planned) construction at the end of the period (sqm in thousands) (****) (**)	249	122	**135**
	Total costs invested in the current period (consolidated) (NIS in thousands)	96,953	32,094	**66,824**
	The amount at which the properties are presented in the statements at the end of the period (consolidated) (NIS in thousands)	680,801	20,742	**133,425**
	Construction budget in the consecutive period (estimate) (consolidated) (NIS in thousands)	365,000-383,000	170,000-193,000	**15,000-25,000**
	Total estimated balance of construction budget for completion of the construction work (consolidated) (estimate as of the end of the period) (NIS in thousands)*	1,080,000-1,175,000	600,000-643,000	**628,000-671,000**
	Rate of built-up area in respect of which lease contracts have been signed (%)	0.13%	0%	**---**
	Projected annual income from projects that will be completed in the following period (consolidated) (estimate) (NIS in thousands)(***)	--	**--**	**--**

*The Company has no properties under construction outside of Israel.

** Space for marketing.

*** As of the end of the period, contracts for leasing 50% or more of the projects' spaces included in this table have not yet been signed.

***** Uses were determined according the main use of the property.

The construction of Tower E in Herzliya was completed during 2010. The construction of Azrieli Akko Mall and of Azrieli Kiryat Ata Mall was completed during 2011.

Properties Under Construction – Further Details:

Set forth below is a specification regarding the main new properties under construction as of the Date of the Report in the operating segments of investment property (for further details see Section 1.1.3 of the Board of Directors' Report in Chapter B of this Report):

The construction of Azrieli Ramla Mall

As of the Report Publication Date, the Group, through Otzem Initiation and Investments (1991) Ltd. ("**Otzem**"), holds all of the lease rights in a lot of an area of approx. 31,650 sqm in Ramla (the "**Lot**") and started the construction of Azrieli Ramla Mall of a gross area of 31,500 sqm (main areas and service areas). The Lot was purchased by Otzem in May 2011 in consideration for NIS 100 million (plus VAT), which as of the Date of the Report was fully paid. For further details see Note 14h to the consolidated financial statement which constitutes Chapter C hereto. As of the Report Publication Date, Otzem has submitted documents that are required for the purpose of modification of a zoning plan under local authority and for the purpose of arranging issues in connection with the Project, has received a permit for fencing of the Lot and destruction of the buildings therein, and has commenced the development work. In March 2012, a permit was received for the construction of a supermarket building (Stage A) and two parking levels. The Israel Antiquity Authority has completed its tests in the Lot, and released the Lot for performance of the work, and shall return for further testing upon demolition of the existing Shufersal building on the Lot and the relocation of the access road to the site. Otzem estimates that the sum total of the additional investments required for the construction of the mall on the Lot is NIS 210-230 million. For further details, see the Company's immediate reports as of January 2, 2011 (reference: 2011-01-000081) and May 26, 2011 ((reference: 2011-01-162048), which are included in this Report by way of reference.

Sarona Azrieli Center, Tel Aviv

As of the Report Publication Date, the Company fully owns the lease rights in a lot of an area of approx. 9.4 dunams in Southern Hakirya in Tel Aviv (the "**Lot**"), after having won a tender on behalf of the Israel Land Association for the acquisition thereof, in consideration for a sum of NIS 522 million (exclusive of V.A.T), approx. NIS 39 million as development expenses and approx. NIS 27 million as purchase tax. The Lot is intended for the construction of an office and commercial project at a scope of approx. 125 thousand sqm of above-ground built-up area (gross) and approx. 61 thousand sqm of underground floors. The Company estimates, as a preliminary estimate, that the sum total of the planning costs, licensing and development expenses and construction costs required for the construction of the project on the Lot ranges at approx. NIS 900 to 950 million . The Company financed the acquisition of the Lot from its own sources and through short-term bank financing and it intends to finance the construction from the Company's own sources and/or through bank financing. In the tender documents, the Company undertook to complete the construction of the project within 60 months and some of the work within 36 months. On March 1, 2012, a building permit was received for the construction of basements. The permit determines, *inter alia*, that the Company is required to complete, within 60 days, approvals that are required by the Ministry of the Environment, the Water Authority and the Fire Department. For further details, see Note 14 of the financial statements – Chapter C of this Report as well as the Company's reports dated May 29, 2011 and May 30, 2011 (ref. no.: 2011-01-165339 and 2011-01-167994, respectively) which are included in

this Report by way of reference.

Azrieli Holon Center

The Group, through Canit Hashalom, is entitled to receive lease rights in a plot of land owned by the City of Holon with an overall area of approx. 34 dunams in the eastern industrial area of Holon by virtue of an agreement signed between the City of Holon and Canit Hashalom on June 5, 2008, whereby the Project shall be constructed and operated as an income-producing property (leasable) by means of a joint venture. According to the agreement, the Project is designated for the construction of a business park in which framework (with no more than four sub-stages) buildings for high-tech industries, offices, exhibition halls and commerce, service areas and parking space, as well as additional uses will be constructed (the "**Project**").

Canit Hashalom will be entitled to receive 83% of the space to be built in such Project while the City of Holon will be entitled to receive 17% of the space to be built as aforementioned (the "**Rate of the Partnership in the Transaction**"). As of the Report Publication Date, the excavation and shoring work were completed, and the Group began construction of the foundations of the buildings and construction of the basements and the buildings, in accordance with the comprehensive building permit received for Stage A of the Project. For further details regarding the agreement and the terms and conditions thereof, see Note 34B(3) to the Financial Statements in Chapter C of this Report.

Azrieli Rishonim Mall

The Group, through Canit Hashalom, is the owner of a plot of land of an area of approx. 19 dunams in Rishon Lezion (the "**Site**"). Since the Site constitutes part of a larger plot of land which is jointly owned by Canit Hashalom and third parties, an agreement for division of the land was signed between Canit Hashalom and the said third parties, and a perpetual long-term lease on those parts of the land which constitute the Site was also registered in favor of Canit Hashalom. A corresponding lease is supposed to be registered in favor of the third parties in relation to other parts of the land which do not constitute part of the Site.

Part of the Site is currently used as an above-ground, ground-level car park, which is held and operated by the City of Rishon Lezion and is being used by the "Harishonim" train station until the plan which will allow construction on the land shall take effect, as stated below.

On August 24, 2009, a plan with respect to the Site was deposited, the approval of which will allow construction of leasable areas at a scope of approx. 48,000 sqm (commerce and offices) and 82,095 sqm of above-ground and underground parking spaces. In December 2010 the district committee's decision was received whereby the plan has been approved for deposit for validation subject to receipt of final approvals and performance of the coordination included in such decision, and the Company is acting for receipt of the approvals required in order to allow the publication of the plan for validation.

Canit Hashalom has assumed an undertaking whereby, should the plan be approved, Canit Hashalom will build, at its own expense, 600 parking spaces to be used as a car park for the benefit of the train users. On January 8, 2012, an administrative petition that was filed against the district committee, Canit Hashalom and others due to the

approval of the plan at such conditions, was rejected for being premature, since the Ministry of Transport had not yet provided its response in connection with the approval of the plan. To the best of the Company's knowledge, the petitioners have the right to petition again against the approval of the plan upon its final approval. As of the Date of the Report, the Company has begun construction of a temporary parking lot in the Site after receiving a building permit for a temporary parking lot as aforesaid.

Azrieli Kiryat Ata Mall

After the completion and opening to the public of the Azrieli Kiryat Ata Mall, during the Report Period, the Group is acting for the construction of an additional building within the project, at a total leasable area of 4,000 sqm, which will be used mostly as office space and will also include a commercial space that is to be leased to a food chain. The completion of the additional building is expected in Q1/2013. As of the Date of the Report, the Company has begun advancing the excavation and shoring work of the additional building, and has carried out various tasks on the land, in accordance with undertakings that were given thereby to the authorities, according to an agreement with the Ministry of the Environment.

The Company's estimates with respect to the expected investments and costs for properties under construction, the manner of financing of the projects and the dates of completion of the construction in this Section 7.8 are forward-looking information, as defined in the Securities Law, which is based on subjective estimates of the Company as of the Date of the Report, and the materialization thereof, in whole or in part, is uncertain, or they may materialize in a significantly different manner, inter alia, due to factors which are beyond its control, including changes in market conditions, the period of time that shall be required for approval of the building plan for performance and the construction input prices.

7.9 Land (aggregate)

The table below presents a summary of figures on the Company's land reserves:

Region	Parameters	For the year ended on	
		December 31, 2011	**December 30, 2010**
Israel	The amount at which the lands are presented in the financial statements at the end of the period (NIS in thousands) (*)	21,570	17,800
	Total area of the lands at the end of the period (sqm in thousands) (**)	20.33	19.1
U.S.A.	The amount at which the lands are presented in the financial statements at the end of the period (NIS in thousands) (*)	3,869	3,593
	Total area of the lands at the end of the period (sqm in thousands) (**)	1.5	1.5

* All of the Company's lands in Israel are presented in the Company's financial statements in the office and other space for lease segment, while the land in the U.S. is designated for offices and presented in the income-producing property in the U.S. segment.
** As of the Date of the Report, the construction in the Company's land reserves is impossible due to planning and other restrictions.
*** There are no building rights according to approved plans in these lands.

7.10 Purchase and sale of properties (aggregate)

Region	Parameters		Period (Year ended on)		
			December 31, 2011	**December 31, 2010**	**December 31, 2009**
Israel	Properties Sold	Number of properties sold in the period [1]	-	1	-
		Consideration from realization of properties sold in the period (consolidated) (NIS in thousands)	-	1,858	-
		Area of properties sold in the period (consolidated) (sqm in thousands)	-	1	-
		NOI of properties sold (consolidated) (NIS in thousands) [2]	-	(13)	-
		Profit / loss recorded due to realization of the properties (consolidated) (NIS in thousands)	-	584	-
	Properties Purchased	Number of properties purchased in the period	[6]2	1[3]	**3[4]**
		Cost of properties purchased in the period (consolidated) (NIS in thousands)	661,000	300,000	**826,988**
		NOI of properties purchased (consolidated) (NIS in thousands)	Under construction	29,515	**46,750**
		Area of properties purchased in the period (consolidated) (sqm in thousands)	147	28.6	**40**
U.S.A.	Properties Sold	Number of properties sold in the period	-	-	-
		Consideration from realization of properties sold in the period (consolidated) (NIS in thousands)	-	-	-
		Area of properties sold in the period (consolidated) (sqm in thousands)	-	-	-
		NOI of properties sold (consolidated) (NIS in thousands)	-	-	-
		Profit / loss recorded in respect of realization of the properties (consolidated) (NIS in thousands)	-	-	-
	Properties Purchased	Number of properties purchased in the period	[7]1	-	-
		Cost of properties purchased in the period (consolidated) ($ in thousands)	176,000	-	-
		NOI of properties purchased (consolidated) ($ in thousands)	[8]13,645	-	-
		Area of properties purchased in the period (consolidated) (sqm in thousands)	99	-	-

(1) In January 2010 Otzma Holdings sold its full rights in the office floor on Y.L. Peretz St. in Haifa in consideration for an amount which is immaterial to the Group.

(2) The negative NOI results from a settlement of accounts for past expenses that were not paid.

(3) During Q1/2010 the Company consummated the purchase of Azrieli Haifa Mall, in consideration for an amount of approx. NIS 300 million (not including purchase tax and related expenses). The mall extends over a lot area of approx. 48 dunams (before expropriations), while the project (commerce and parking spaces) is in a gross built-up area of approx. 95,000 sqm, out of which 3 commercial floors and a car park.

(4) In 2009 the Group purchased the following properties:

i. Azrieli Givatayim Mall – the mall was opened to the public in 2005 and operates on an overall built-up area of approx. 88,481 sqm gross, including an underground car park, commerce areas (in three floors), an entertainment floor (which includes cinemas and a gym), office space and clinics.

ii. Azrieli Or Yehuda outlet Mall – the mall extends over a lot area of approx. 4.5 dunams, while the project (commerce areas, service areas and a car park) is at a gross built-up area of approx. 9,568 sqm (out of which the Company's share is 8,516 sqm) which includes three commercial floors.

iii. Land reserve in Kiryat Ata, on which the Company built the "Azrieli Kiryat Ata mall" on a built-up area according to a plan of 33,000 sqm.

(5) The costs do not include purchase taxes and transaction closing costs.

(6) In 2011, the land for the development of Ramla Azrieli mall and Sarona Azrieli Center was purchased. For details, see Section 1.3.1.
(7) In 2011, office towers were purchased in Houston, Texas. For details, see Section 1.3.1.
(8) The NOI is according to a forecast in a representative year, and according to which the purchase price was determined.

For details on another property which the Company acquired, after the Report Period, see Section 10.10 below.

7.11 Fair value adjustments of values in the Statement of Financial Position required at the corporation level

		As of (Consolidated) (NIS in Thousands)	
		December 31, 2011	**December 31, 2010**
Presentation in the Description of the Corporation's Business Report	Total Value of the Investment Property whose Construction has Ended (as presented in the total column in the income-producing properties fair value by regions and uses tables as of December 31, 2011 and December 31, 2010)	13,895,558	**11,898,151**
	Total Investment Property under Construction (as presented in the total column in table 7.8)	858,043	**244,335**
	Total Land classified as Investment Property (as presented in the total column in the table 7.9)	25,439	**21,393**
	Total	**14,779,040**	**12,163,879**
Adjustments	Adjustments to value deriving from receivables items	(30,092)	**(26,443)**
	Advance payments on account of real estate acquired in 2012	17,108	**--**
	Other adjustments[13]	73,514	**72,827**
	Total adjustments	60,530	**46,384**
	Total, After Adjustments	**14,839,570**	**12,210,264**
Presentation in the Statement of Financial Position	Investment Property Item in the Statement of Financial Position **(Consolidated)**	**13,981,528**	**11,969,647**
	Investment Property under Construction Item in the Statement of Financial Position **(Consolidated)**	**858,042**	**240,617**
	Total	**14,839,570**	**12,210,264**

As aforesaid, the holding of investment property deriving from Granite Hacarmel was not specified in this Chapter, since the Company's management does not consider this property as part of the Company's investment property activity and examines Granite Hacarmel as a whole, as is reflected in the segments' note and in the Company's Extended Standalone Financial Statement.

7.12 Adjustments to FFO profits

The Company is not required to perform FFO disclosure since the total revenues of the Company from investment properties are lower than 90% of the Company's total revenues during the report year and year preceding it. In view thereof, the Company calculates FFO profits for the income-producing property business only with the necessary adjustments. For details and a calculation of the FFO profits for the Company's income-producing properties business, see Section 1.1.7 of the Board of Directors' Report in Chapter B of this Report.

[13] The investment properties of Granite Hacarmel (consolidated company) were not included within the description of the Company's investment properties and were recorded in the adjustments item as a sum total. The Company deems all of Granite's business as one segment which is not part of the Company's income-producing properties segments.

Part Four: Description of the Group's Business - Description of the Group's Business per Operating Segment and Material Properties

8. The commercial centers and malls segment in Israel

8.1 General information on the operating segment

8.1.1 General

Most of the Group's malls and commercial centers are spread out throughout the central cities of Israel and are located close to the main traffic thoroughfares which enable easy access and open parking. The commercial centers and malls are planned to the utmost degree according to the needs of the population of the area in which the mall is located, and they offer a wide and varied mix of shops in the fields of fashion, footwear, jewelry, gifts, housewares, communications, electronics and computers, optical devices, entertainment and food centers for the wellbeing of the visitors, easy access and a large number of parking spaces. The Company puts an emphasis on tenants' mix in each one of the malls and commercial centers owned thereby, which it believes shall constitute a center of public attraction to each one of them, in accordance with the characteristics of the local public. The Company did not have a main tenant, the rent paid by whom for 2011 accounted for 10% or more of the total revenues of the Company in its Financial Statements for year 2011.

Most of the Group's lease contracts in Israel are for periods of three (3) to five (5) years and for the most part, include an option for additional lease periods (usually additional three to five years), other than agreements in respect of a relatively large scope of space for lease, which are generally signed for longer lease periods of between 8 to 25 years (including extensions and exercise of options). The lease agreements include rent that is composed of a fixed rent or rent derived as a percentage of the tenant sales in the leasehold, whichever is higher, but in most cases, the actual rent payable to the Company are the fixed rent, and the Company's revenues from sales dependant rent are at an immaterial scope. The occupancy rate of the Group's properties in this operating segment, from the date of populating the commercial centers and malls in Israel, and as of the Date of the Report, is close to 100%.

The Group's commercial centers and malls in Israel are managed, with relation to each mall or commercial center, in most cases, by designated management companies owned by the Group, which enter with the lessees into management agreements. Most of the management agreements determine that the management fees will be paid based on the cost of the management services, plus overhead expenses. Most of the management agreements with crowd attracting tenants determine management fees at a fixed amount. The management services include, *inter alia*, marketing services of the mall and/or the commercial center, both to visitors and to potential tenants, security services, cleaning of public areas, gardening, maintenance of elevators and public systems. The management companies collect from the tenants the management fees or the maintenance fees, which are used, *inter alia*, for financing the maintenance of public areas. The management company leases from the Group companies, as the case may be, in each of the malls and commercial centers, an area of approx. 45 to 350 sqm located in a non central area of the mall or commercial center, to serve as the offices and storage rooms

of the management company, in consideration for fixed rent. In most of the management agreements between the management companies and the tenants, the management companies undertake to maintain and operate the public areas in the malls and commercial centers, including cleaning, security, renewal, advertising, insurance, under conditions and to the extent that will be determined by the management companies from time to time.

All of the Group's commercial centers and malls include also car parks (above or underground) which serve the visitors and the potential tenants, with some of the car parks being open to the general public and some requiring payment.

Over the commercial areas of some of the malls and commercial centers there is an area designated for office space for lease. See Section 9 of the Report for additional details on the office and other space for lease segment.

8.1.2 The structure of the operating segment and changes occurring therein

The commercial centers and malls segment in Israel is affected by the business activities in the economy and its recovery is influenced both by the political and security situation and from the improvement in the economic condition in Israel. Various entities operate in the commercial centers and malls segment which locate, plan, construct, lease and maintain properties designated for lease for various uses.

To the best of the Company’s knowledge, based, *inter alia*, on publicly-available information, at the outset, most of the malls relied on large anchor tenants (such as supermarkets, department stores and movie theatres), which were considered to be crowd attracting. However, in recent years, the concept has changed for the malls in Israel and an opposite trend has begun, of the withdrawal or contraction of the space of the anchors, due to the low rent per square meter that are received from them and for the large space occupied thereby.

Additional trends in the commercial centers and malls segment is the strengthening of branded fashion chains at the expense of single, local type shops, including international fashion chains, the construction of low-prices power centers outside of the cities, which compete with the malls, as well as the process of consolidation among large companies in the Israeli economy that own commercial centers and malls, such as the Company, which represents an advantage for size over smaller competitors, while creating operational efficiency.

It shall be stated that in recent years, there has been an increase in the commercial areas designated to the fashion industry in the malls in Israel segment and in the Company's properties in the operating segment, and in the last two years, revenues of this industry constitute approx. 40%-45% of the revenues of the commercial centers and malls in Israel segment.

8.1.3 Restrictions, legislation, standards and special constraints applying to the operating segment

This operating segment is subject mainly to the land laws and the land use and zoning laws. In addition, the business in this segment is affected by legislative

updates in the field of business licensing, land taxation and municipal taxation. See Section 20 of the Report for details on the matter of the restrictions, legislation, standards and additional constraints applying to the Group.

8.1.4 Changes in the volume of business and profitability of the segment

During recent years, the volume of operations of the Group in the of commercial centers and malls segment grew, mainly due to the construction of income-producing properties (the construction of the Modiin Azrieli mall, the Akko Azrieli mall, the Kiryat Ata Azrieli mall) as well as the acquisition of existing income-producing properties (primarily the purchase of the Azrieli Givatayim Mall, the purchase of the Azrieli Haifa Mall and the purchase of the full control of the Azrieli Hod Hasharon Mall).

During 2011, a trend of stability was felt in the Israeli market in the real estate industry, which was mainly expressed in the preservation of high occupancy rates in the Company's properties. In addition, a trend of increase was evident in revenues from commercial areas, which is mainly attributed to the entry of international chains to the Group's properties. To the best of the Company's knowledge, in 2011, a nominal rise in revenues occurred in the commercial centers market, which is mainly attributed to growth in the economy.

8.1.5 Critical success factors in the operating segment and changes occurring therein

The Company estimates that the main success factors in the segment are, *inter alia*, locating commercial centers and malls in areas where there is a high level of demand, the right geographic location of commercial centers and malls as a response to the needs of the residents in each area, expertise in development and architectural planning, management and construction of commercial centers and malls through the professional management team employed by the Group, the creation of a mix of diverse, quality tenants with financial strength, know-how and experience in marketing, property management and operation, the positive goodwill of the Company, its business positioning and financial strength which allows immediate response to attractive business opportunities.

8.1.6 Changes to the system of suppliers and raw materials for the operating segment

In the framework of the maintenance and management of income-producing properties segment, the Company has no material suppliers with which it engages.

8.1.7 Main barriers to entry and exit of the operating segment and changes occurring therein

Barriers to Entry - To the Company's belief**,** entities operating in the commercial centers and malls segment require, primarily, equity and financial strength which allow them to operate in the development segment at relatively low financing cost. The main barrier to entry for the development and construction of a commercial center is financing of the construction and finding a suitable land in the required area. Additionally, required mostly are professional knowledge, experience in development segment, positive reputation in the industry, availability of financing sources at good terms and land reserves available and planned in areas with high levels of demand for

leasable space for commercial purposes. In addition, entities operating in the commercial centers and malls segment are required to meet high regulatory requirements, *inter alia*, regulation in the land use and zoning and environments fields. It shall be noted, that despite the high barriers to entry, it is possible to indicate a significant increase in the construction and development of many commercial centers, all over Israel, in recent years. In addition, it is possible to operate in the commercial centers and malls segment in lower costs through acquiring commercial centers from single developers, extending existing commercial areas, upgrading and renovating commercial centers as well as through managing commercial centers without the acquisition thereof.

To the Company's belief, the malls' barriers to entry are significantly higher than those of the power centers outside of the cities, due to the high construction costs that characterize the malls (including the cost of the land, which is more expensive since the locations of the malls are closer to the city centers).

Barriers to Exit - exiting this operating segment is conditional, mostly, on the ability to realize properties, which is a direct result of the location of the properties, their physical condition and the condition of the economy, as well as various costs, including in connection with land taxation.

8.1.8 Structure of competition in the operating segment and changes occurring therein

The income-producing property industry in general, and the commercial centers and malls segment in particular, are characterized by the high level of competition. As of the Date of the Report, there are approx. 300 various and diverse commercial centers in Israel (malls, power centers, neighborhood centers, managed complexes (such as the Hatachana complex and the Tel Aviv Port complex), etc.), in a total area of approx. 2.85 million sqm. Each commercial center is adjusted in its structure, size and business mix to the characterizations of the demands of its consumers who lease space in the geographic area where it is located. The competition in this segment revolves around a number of parameters, the main ones are; (1) the geographic location of the properties and the level of demand for the space for lease in that area; (2) the amount of the rent and the management and maintenance costs; (3) the quality of construction of the leased buildings; (4) the level of auxiliary services; and (5) the reputation of the lessor. See Section 8.3 of the Report for a description of the structure of competition in the operating segment.

8.1.9 The manner of executing purchases or construction of properties

8.1.9.1 The Company's management does not have a fixed policy with regard to the purchase of properties, and each case is examined on its merits, in light of the business opportunity carried therewith. The Company examines from time to time, business opportunities in Israel and overseas, in respect of expansion of the business thereof mainly in the real estate segment, including through the purchase of land reserves, purchase of additional properties and betterment of the existing properties.

8.1.9.2 As a general rule, the Company may acquire its rights to the properties, at times by direct acquisition of the property rights, at times by acquisition of shares of companies owning rights to properties and at

times, by issuance of shares in these companies. As of the Date of the Report, most of the rights to the properties were acquired by the Company by means of the acquisition of rights to properties. The considerations for the acquisition or construction of new income-producing properties are based, *inter alia*, on the following parameters: the yield from the property; properties generating a cash flow and fixed revenues while emphasizing preference for financially strong tenants; improvement potential in the acquired property.

8.1.9.3 The malls and commercial centers of the Group are owned or leased for long periods from the Israel Lands Administration (the "**Administration**") or leased for long periods from the local authorities in whose jurisdiction the property is located.

8.1.9.4 In transactions in which the completion of registration of the rights to the acquired property and its transfer to the name of the Company and/ or the Group companies is not executed until the date of closing the transaction, the Company includes mechanisms in its agreements in order to secure the compliance with obligations by the seller, including those connected with the registration of the rights to the property and their transfer to the name of the Company, by means of depositing part of the consideration in trust as well as by means of recording warning notices and/or pledges in favor of the Company, to the extent possible, and as the case may be.

8.1.9.5 The policy of the Company at the time of acquiring new properties as to which there are obligations vis-à-vis third parties to manage and operate them, is to release the properties that it acquires from the management and operating rights and to provide the management services by itself or by Group companies. As of the Date of the Report, there are no undertakings towards third parties in the Group’s properties in connection with the management and operation thereof.

8.1.9.6 In the income-producing property industry, in acquisition transactions with partners, the system of relationships is arranged, for the most part, by means of an undertakings in a partnership agreement, which includes, *inter alia*, provisions related to transfer of the rights in the mall or commercial center, including prohibited periods, as well as provisions in relation to mechanisms of right of priority, right of refusal and severance (Buy Me Buy You).

8.1.9.7 The professional management team employed by the Group accompanies the construction of all of the Group's projects, beginning from the stage of locating the property, through preparation of a cost estimate and time schedule for each project, architectural planning for the project, execution of tenders for contractors, and finally continuous follow up of construction of the project, with emphasis on the stages of finishing and completing the project and populating each project by the various tenants.

8.1.9.8 The Company does not deem the disposal of its assets as part of the business strategy thereof, but it may operate for disposal of existing income-producing properties, in case that they are not strategic for the

Company and are not within the core of the business thereof. The Company's management has not presented a fixed criterion of yield required in cases of disposals or purchases, and each case is examined on the merits thereof, in light of the circumstances, designation, location and characteristics of the property.

8.2 Material properties in the commercial centers and malls in Israel segment

Set forth in the table below is a concentration of figures pertaining to material properties of the Group in the commercial centers and malls segment as of December 31, 2011 which constituted 5% or more of the total company's consolidated properties, and were evaluated by the valuator Mr. Ronen Katz, a partner at Greenberg Olpiner & co (**) through the income capitalization method[14]:

Name and characteristics of property			Year	Information item									Additional figures required according to Regulation 8b(i) (as applicable)
				Fair value at end of period (NIS thousands)	Revenues from rent during the period (NIS thousands)	Actual NOI during the period (NIS thousands)	Rate of Yield (&)	Adjusted Rate of Yield (%)	Revaluation profits (consolidate) (NIS thousands)	Occupancy rate as of the end of the period (%)	Average monthly rent per sqm (in NIS)	Ratio of average revenue per sqm and average rent per sqm	**Other assumption in the basis of the valuation**
Azrieli Mall (1)	Region	Israel	**2011**	1,821,792	105,833	129,120	7.1%	7.42%	93,878	99%	296	12%	**Weighted cap rate 7.42%**
	Functional currency	NIS											
	Main use	Commerce	**2010**	1,726,786	101,509	124,379	7.2%	7.46%	176,261	100%	270	12%	**Weighted cap rate 7.46%**
	Construction cost (NIS millions)*	512	**2009**	1,548,530	95,616	115,579	7.5%	7.63%	25,693	100%	256	14%	**Weighted cap rate 7.63%**
	Corporation's share (%)	99.1%											
	Area [sqm]	32,864											
Azrieli Ayalon Mall (2)	Region	Israel	**2011**	1,269,640	89,030	93,600	7.3%	7.41%	29,142	100%	316	14%	**Weighted cap rate 7.41%**
	Functional currency	NIS											
	Main Use	Commerce	**2010**	1,240,500	84,329	91,152	7.3%	7.43%	87,645	100%	304	14%	**Weighted cap rate 7.43%**
	Construction cost (NIS millions)*	176	**2009**	1,151,800	81,292	87,094	7.6%	7.63%	56,517	100%	295	14%	**Weighted Cap rate 7.63%**
	Corporation's share (%)	100%											

[14] Azrieli Givatayim Mall is a "Complementary Asset" as defined in the directive of the Israel Securities Authority pertaining to disclosure in respect of investment property business, which constitutes approximately 3.8% of the Company's total consolidated properties.

	Area [sqm]	23,265											
Azrieli Jerusalem Mall (without the office component)	Region	Israel		1,690,345	113,323	122,024	7.2%	7.42%	92,976	100%	261	11%	**Weighted cap rate 7.42%**
	Functional Currency	NIS	**2011**										
	Main Use	Commerce	**2010**	1,596,675	107,301	116,652	7.3%	7.44%	143,907	100%	234	11%	**Weighted Cap Rate 7.44%**
	Construction Cost (NIS millions)*	447	**2009**	1,447,474	100,624	108,282	7.5%	7.72%	32,237	100%	226	10.5%	**Weighted Cap Rate 7.72%**
	Corporation's share (%)	100%											
	Area [sqm]	39,127											
Azrieli Givatayim Mall (w/o the office component) (3)	Region	Israel	**2011**	889,593	59,997	64,432	7.2%	7.47%	13,767	100%	238	13%	**Weighted cap rate 7.47%**
	Functional Currency	NIS											
	Main Use	Commerce	**2010**	875,720	58,573	61,831	7.1%	7.51%	80,623	100%	234	12%	**Weighted Cap Rate - 7.51%**
	Original Cost (NIS millions)*	795	**2009**	798,440	47,021	44,560	***5.6%	7.64%	(26,938)	100%	231	12%	**Weighted Cap Rate 7.64%**
	Corporation's share (%)	100%											
	Space [sqm]	**21,678**											

* Including investments in adjusting the leased properties and renovation of systems until the Date of the Report.

** Mr. Ronen Katz is a certified real estate appraiser, with B.A. in Agricultural Economy and Administration in the Agriculture Faculty from the Hebrew University of Jerusalem, and is experienced since 1997 as a real estate appraiser.

*** The mall was purchased during 2009.

**** The datum is to the Company's best knowledge. It does not include lease agreements which do not include rent from sales and is given based on information received from the tenants or from other third parties (as the case may be), and therefore the Company cannot verify that this information is indeed true.

(1) For further details see the valuation attached to this Report.

(2) The Company is registered in the Land Registration Bureau as a lessee of Azrieli Ayalon Mall for a 49-year period ending on August 1, 2031, with an option for an additional 49-year period. The City of Ramat Gan owns the adjacent car park, which includes approx. 2,350 parking spaces. The City of Ramat Gan has undertaken (and an easement therefor has been registered) to enable a right of passage for vehicles and pedestrians, as well as an open parking right for the public, including the Mall's visitors, in the parking spaces that were arranged (excluding 250 space use of which shall cease insofar as the City realizes building rights thereon) and so long as the Company continues leasing and operating the Azrieli Ayalon Mall. As of the Date of the Report, approval has been granted for the new zoning plan submitted by the Company, with the aim of allowing construction of up to 7,500 sqm of additional main areas as a second commercial floor at Ayalon Mall (approx. 9,500 sqm of area planned for leasing for commerce (including loaded public areas). For further details see Section 1.1.3 of the Board of Directors' Report.

(3) The rights in the land were purchased by the Company in March 2009. The sellers of the property undertook to arrange to obtain the Minister of the Interior's approval for the lease of one of the car parks (244 parking spaces), which is built below a public area, complete the licensing the areas, including stalls and further changes and registration of the rights to the land. The Company's rights in the property are charged in favor of Bank Leumi. To the best of the Company's knowledge, there is a dispute between the City of Givatayim and the sellers with respect to the amount of the payments that are due to the City in connection with the payment of additional rent in respect of parking fees whose collection has begun, and the parties' appraisers are negotiating to settle the amount of the payment. The agreement provided, *inter alia*, for a full indemnification duty in respect of any loss, damage or expense to be incurred by the Company, insofar as the Company shall bear such payments, including payments required to obtain the Minister of the Interior's approval.

On October 31, 2011, the lease rights in Givatayim Mall were registered in the Company's name (except for the Company's rights in the car parks) as well as an undertaking to register the mortgage in favor of Bank Leumi.

8.3 Competition

To the Company's belief, over recent years, the commercial centers and malls segment in Israel has been characterized with high competitiveness, and to the best of the Company's knowledge, there are approx. 300 commercial centers in Israel. As of the Date of the Report, the Company operates in that operating segment principally in the development and construction of commercial centers, and focuses on discovering reserves of land in attractive locations and with the potential for high revenues, and therefore the competition vis-à-vis bodies which concentrate primarily on acquisitions of existing commercial centers is lower. In commercial complexes and centers located in residential areas a competition could also develop with local developers. The market trends over the recent years and the attempt to adjust the characteristics of the commercial center accurately to local demands and to the substitutes available to the consumer, dazed the border lines between the different commercial centers.

To the best of the Company's knowledge, a number of entities operate in Israel which hold significant portions of properties in the commercial centers and malls segment, including Reit 1 Ltd., Gazit Globe Ltd., Melisron Ltd. (which, to the best of the Company's knowledge, is also due to hold all of the capital of British Israel Investments Ltd.), Industrial Properties Ltd., Amot Investments Ltd., Jerusalem Economy Ltd. and Big Shopping Centers (2004) Ltd.

To the Company's belief, the geographic location of the commercial center and its differentiation directly affect its characteristics and its tenant mix since each center adjust itself to the sizes of the geographic market in which it is located in order to create a

center of attraction which is unique therefor and deal with centers existing in the area which created the consumers' purchase habits. For the most part, the tenants will consider the benefit of space in a commercial center with a better geographic location and a mix conforming to its business operations versus its cost.

The competition vis-à-vis the private consumer is also characterized mostly by the geographic location, and vis-à-vis other centers such as power centers as well as shops in the city streets. Most of the commercial centers and malls serve the population which resides or is employed in the geographic district in which the commercial center is situated. Nonetheless, the Azrieli Center in Tel Aviv, due to its location, its accessibility and proximity to the train station and major junctions, serves consumers from all over Israel.

The Company also believes that the tenant mix in the commercial center influences the competition vis-à-vis the private consumer - the types of the shops and their branding, the atmosphere and shopping experience, benefits to consumers, events initiated in the framework of the commercial center, access to the commercial center and available parking (free or paid) – all of these are branding the commercial center and create a competitive advantage. The main parameters that support the attractiveness of the commercial center for the consumer are, *inter alia*, location, size, innovative look and business mix adjusted to the needs of the customers in the area. The malls and commercial centers are therefore required to renovate, upgrade and adjust the tenant mix therein.

To the Company's belief, the volume of its business in the commercial centers and malls segment in Israel is large, and it is one of the companies with the greatest number of malls and commercial centers in Israel. As of the Date of the Report, approx. 1,750 tenants that are active in retail and commerce operate in the Group's commercial centers and malls. To the Company's belief, the factors and methods that help the Group to face competition in the segment are as follows:

- ☒ Most of the commercial centers and malls of the Group are characterized by quality planning and prestigious branding, which the Company carefully maintains over the years and that contribute to its competitive advantage and offer to the visitors to the commercial centers and malls a quality shopping experience;

- ☒ The volume of the Company's business in the segment allows the Company to engage with chains and service providers at beneficial terms;

- ☒ The volume of the Company's business in the segment allow the Company to specialize in the management of commercial centers and malls in an efficient manner in order to lead to savings in costs and in manpower;

- ☒ Most of the Company's tenants are large chains and/or companies with superior financial strength and the lease agreements therewith are for a relatively long period;

- ☒ The Company's commercial centers and malls are located in high-demand areas, enabling the Company to lease the properties to numerous and diverse types of tenants.

- ☒ The expertise of the Group in the planning and construction of commercial centers and malls according to the needs of the tenants and visitors in the commercial center and/or mall.

8.4 Goals and business strategy for the segment

See Section 23 of the Report for the Company's goals and the Group’s strategy.

9. Office and other space for lease segment

9.1 General information on the operating segment

9.1.1 General

In this operating segment, the Group operates, as of the Date of the Report, in the development, construction, acquisition, lease, management and maintenance in Israel of parks for offices and the high-tech industry, office buildings and industrial buildings, workshops and storage. The parks for offices and office buildings are designated primarily for businesses in the segments of liberal professions, service providers and high-tech industry, which are characterized by a large number of personnel and a demand for adjacent parking spaces.

Most of the Group's lease agreements are for periods of about five years, with the tenant given an option for additional lease periods of about five years. The rent is at a fixed amount per each square meter of the leased space.

The Group's office space is managed with relation to each office building or office park, in most cases, through the Company or through designated management companies owned by the Group, which enter with the lessees into management agreements. The management companies collect from the tenants the management fees or the maintenance fees, which are used, *inter alia*, for financing the maintenance of public areas, whereas in most of the management agreements between the Company or the management companies and the lessees, the management companies undertake to maintain and operate the public areas, including cleaning, security, renewals, advertising and insurance, under terms and in the scopes as shall be determined by the management companies from time to time.

All of the Group's office and other space for lease properties in Israel include also car parks (above or underground) which serve the tenants and their customers.

In this operating segment, the Group's income-producing space that are leased to third parties are mainly divided into two types:

a. Business parks for the high- tech industries- The Group specializes in responding to the special needs of the high-tech industries and the construction of purpose-built buildings fitted in advance to the needs of the tenants. The purpose-built construction provides a comprehensive and complete solution to tenants, that includes the guidance of the tenant beginning from the stage of preparing the working plans for purposes of the design requested by the tenants, the planning and construction of the building in full cooperation with the tenant and through responding to all of the tenant's demands as to the interior of the leasehold. The business parks present a quality and clean working environment in a central location, quality infrastructure, green areas and parking spaces.

b. Office towers - The Group has office towers that are leased, in most cases, with high occupancy to numerous and diverse tenants for long lease periods.

The office and other space for lease segment of the Group in Israel is managed with relation to each office building or office park through the Company or designated management companies owned by the Group, which engage with the tenants in management agreements[15]. Most of the management agreements determine that the management fees will be paid on the basis of the cost of the management services plus overhead expenses. In most management agreements, with large tenants, the management fees have been set at a fixed amount. The management services include, *inter alia*, security services, cleaning the public areas, gardening, maintenance of elevators and public systems.

9.1.2 The structure of the operating segment and the changes occurring therein

The office and other space for lease segment is affected by the economic activities in the market and its recovery is affected both by improvement in the political-security situation as well as the economic situation in Israel. Various entities are active in this operating segment which locate, plan, construct, lease and maintain properties designated for lease for various uses. There are many companies in Israel in the office and other space for lease segment, including large, veteran and leading companies, which own properties in large volumes, as well as smaller, local developers who operate in specific geographic areas. The business in this segment is generally characterized by the fact that part of the costs of construction or acquisition is financed by independent sources and the remainder is financed by credit from outside sources.

To the best of the Company's knowledge, in 2010 and 2011, growth was evident in the offices market in the center of Israel, which was expressed in a rise in the development and supply of new projects, a rise in demand for office space and an increase in the rent in many projects. The Company estimates that, due to the supply of new office buildings in the center of Israel in the coming years there may be a slight decline in rent prices in less sought after areas.

9.1.3 Restrictions, legislation, standards and special constraints applying to the operating segment

This operating segment is subject mainly to the land laws and the land use and zoning laws. In addition, the business in this segment is affected by legislative updates in the field of business licensing, land taxation and municipal taxation. See Section 20 of the Report for details on the matter of the restrictions, legislation, standards and additional constraints applying to the Group.

9.1.4 Changes in the volume of business and profitability of the segment

The Company estimates that it appears that the trend of slowdown that haunted the market of office rentals in the center of Israel in 2008-2009 has been halted, and as of the Date of the Report, the Group has preserved very high occupancy rates in its income-producing properties and even increased its revenues from

[15] Except for the property in Petach Tikva and the property in Caesarea that are managed by third parties unrelated to the Company.

rent, due to its financial strength, the strength of the Company's tenants, some of which constitute the leading firms in the economy (AAA tenants) high liquidity and standing in the financial market. See the Board of Directors' Report in Chapter B of this Report for details concerning the development of the revenues from this operating segment. In addition, in recent years, the Company has acted to expand its business in this operating segment, *inter alia* through the construction of the Sarona Azrieli project and Holon Azrieli center and population of vacant office space in existing properties, thus preserving and even increasing the high occupancy rates that characterize the Group.

9.1.5 Critical success factors in the operating segment and changes occurring therein

The Company estimates that the main success factors of the Company in the segment are, *inter alia*, the wide dispersion and location of the income-producing properties in the areas where there is a high level of demand throughout Israel for offices, commerce and industry, expertise in development and architectural planning, management and construction of properties conforming to potential tenants, in relation to which the Company had engaged in advance in lease contracts through the professional management team employed by the Group, the level of demand and supply of properties of a similar type which dictate the terms of the lease contracts and the potential changes thereto, know-how and experience in marketing, property management and operation, the positive goodwill of the Company, its business positioning and financial strength which allows immediate response to attractive business opportunities.

9.1.6 Changes to the system of suppliers and raw materials for the operating segment

Within the framework of this segment, the Group does not purchase raw materials.

9.1.7 Main barriers to entry and exit of the operating segment and the changes occurring therein

Barriers to Entry - To the Company's belief, entities operating in this operating segment require mainly equity and financial strength which allow them to operate in the development segment at relatively low financing costs. In addition, professional know-how, experience in the development segment, positive reputation in the industry and available and planned land reserves in areas with high demand for office buildings space for lease bear great importance.

Barriers to Exit - exiting this operating segment is conditional, mostly, on the ability to realize properties, which is a direct result of the location of the properties, their physical condition and the condition of the economy, as well as various costs, including in connection with land taxation.

9.1.8 Structure of competition in the operating segment and changes occurring therein

The income-producing property industry, in general, and the office and other space for lease segment, in particular, are characterized by a high level of competition. The competition in this segment revolves around a number of parameters, of which the principal ones are: (1) the geographic location of the

properties and the level of demand for space for lease in that area; (2) the amount of the rent and the management and maintenance costs; (3) the quality of construction of the leased buildings; (4) the level of the auxiliary services; and (5) the reputation of the lessor. The competition in this industry takes place both at the stage of locating the land for purposes of entrepreneurship, developing and constructing properties, as well as at the stage of leasing the properties. See Section 9.3 of the Report for a description of the structure of competition in this operating segment.

9.1.9 Manner of executing acquisitions of the Company

See Section 8.1.9 of this Chapter for a description of the manner of acquisition and exercise of the Group's rights in properties.

9.2 Details on the very material properties of the Group in the office and other space for lease segment

9.2.1 General – Azrieli Tel Aviv Towers

The following tables include data regarding the office towers in Azrieli Center, which, as of the Date of the Report, constitute 10.7% of the Company's total properties and complies with the definition of a very material property. The valuation of this property is attached to this Report as Annex C of the Board of Directors' Report, Chapter B of this Report.

The Group, through Canit Hashalom, is the holder of all of the lease rights in the center named "Azrieli Center". Azrieli Center extends over a land block at a total area of 32,894 dunam, located in the center of Tel Aviv, on a junction which is a main transport route and in proximity to the main transport routes of Tel Aviv (Ayalon Highways, Derech Hashalom, Haifa Road) and HaShalom train station, located on Hashalom intersection.

To the best of the Company's knowledge, as of the Date of the Report, Azrieli Center is the largest business center in Israel, with an overall built-up area (gross) of approx. 326,233 sqm, comprising an underground car park and storage rooms (at an area of 122,255 sqm), a mall including 3 commercial floors and a public floor (at an area of 58,649 sqm), two office towers, the Round Tower (at an area of 55,710 sqm) and the Triangle Tower (at an area of 47,680 sqm) as well as the Square Tower which is a tower of mixed uses of offices and a hotel (at an area of 40,574 sqm) as well as public passage bridges (over Petach Tikva Road and HaShalom Railway) (at an area of 1,365 sqm). The office buildings of the Group at Azrieli Center comprise the three towers: the Round Tower, which includes 38 office floors and another roof floor serving as an observatory and a restaurant; the Triangle Tower, which includes 35 office floors and 2 more service floors; and the Square Tower, including 18 office floors above the 13 hotel floors.

9.2.2 Presentation of the property

	Specification as of December 31, 2011
Property name:	**Azrieli Towers**
Property location:	**Tel Aviv**
Property areas – split by uses; (according to leasable area)	**Offices – 131,392 sqm** **Hotel – 18,000 sqm** **Offices used by the Group – 1,520 sqm**
Company's share in the property:	**99.1%**
Structure of holding in the property:	**Through Canit Hashalom Investments of which 99.1% is held by Azrieli Group Ltd.**
Corporation's effective share in the property:	**99.1%**
State the names of the partners in the property*:	**0. 9% are held directly by Mr. David Azrieli**
Date of acquisition of the property:	**The land was acquired in August 1992.**
Specification of legal rights in the property (ownership, lease etc.):	**Capitalized leasing.**
Status of registration of legal rights:	**As of the Date of the Report, the process of registration of Canit Hashalom's lease rights in the Square Tower has not yet been completed.**
Special issues (material building code violations, soil contamination, etc.):	**There are no special material issues. For further details, see the valuation attached hereto**
Method of presentation in the Financial Statements:	**Consolidation**

For details on the registration of rights in the property, pledges and guarantees, pertaining to Azrieli Center towers, see Section 9.2.8 of this Chapter. It shall be noted that all of Azrieli Center's space is designated for lease on the free market, other than space for self use by Canit Hashalom and the Group's companies (on the top floor of the Round Tower and other negligible areas, such as archives, gallery, storeroom, etc.), and other than an area of approx. 5,500 sqm, which is located in the project's basement which is designated for building of an IEC sub-station which was sub-leased in 2006 to the Israel Electric Corp. Ltd. in consideration for a one-time amount of approx. NIS 14 million, for the entire lease period of Canit Hashalom (such area was not taken into account in the valuation of the center which is attached to this Report).

Yarden Hotels M.H.Y. Ltd. who operates the hotel, which is located in the Square Tower of Azrieli Towers, has a temporary permit for the operation of the hotel that as of the Date of the Report, is effective until July 11, 2012. The position of the Licensing Division in the City of Tel Aviv is that the receipt of permanent business license for the hotel is contingent, *inert alia*, also in issuing a building permit to the changes made in the Square Tower until august 23, 2012. As of the Date of the Report the Company is acting for completion of the proceedings in the matter.

9.2.3 Main figures

Figures per 100%. The Company's share in the property – 99.1%	Y2011	Y2010	Y2009		On date of purchase of the property
Fair value at end of the period (NIS in thousands)	2,484,608	2,287,214	2,176,570	Cost of construction (NIS in millions) (**)	**1,292**
Revaluation profits (NIS in thousands)	186,655	98,205	82,824	Date of purchase of the land	**August 1992**
Average occupancy rate (%)	~100%	99%	99%		_____
Leased space (sqm)	149,392	148,395	148,125		_____
Total income (NIS in thousands) (*) per month	220,472	211,933	205,419		_____
Average rent per sqm per month (NIS) (***)	91	90	89		_____
Average rent per sqm per month in contracts signed during the period (NIS)	100	93	105		_____
NOI (NIS in thousands)	186,461	176,896	172,499		_____
Adjusted NOI (NIS in thousands)	193,070	184,105	172,746		_____
Actual yield rate (%)	7.5%	7.7%	7.9%		_____
Adjusted yield rate (%)	7.8%	8%	7.9%		_____
Number of tenants at end of reporting year (#)	**178**	**156**	**156**		_____

(*) The revenues and NOI include 50% of the car park's NOI revenues.
(**) Including adjustment costs for the tenants and renovations until the Date of the Report.
(***) Does not include the hotel's rent. Should the average include the hotel's rent, then the average for 2011 would have been approx. NIS 88 per sqm, for 2010 approx. NIS 86 per sqm and for 2009 approx. NIS 85 per sqm.

9.2.4 Segmentation of revenues and cost structure

Figures per 100%. The Company's share in the property – 99.1%	Y2011	Y2010	Y2009
Revenues:	**(NIS in thousands)**		
From rent – fixed	158,331	152,978	**149,076**
From rent – variable*	-	-	**-**
From management fees	38,187	36,011	**35,300**
From car park	23,781	22,847	**20,983**
Others	173	97	**60**
Total Revenues	220,472	211,933	**205,419**
Costs:			
Management, maintenance and operation	34,011	35,037	**32,920**
Depreciation	103	92	**58**
Other expenses	-	-	**-**
Total Costs:	34,114	35,129	**32,978**
Profit:	186,358	176,804	**172,441**
NOI:	**186,461**	**176,896**	**172,499**

(*) No sales increment for lease of offices.

9.2.5 Main tenants at the property

The Company does not have a main tenant at the property the revenues from whom produces 20% or more of the property's revenues.

9.2.6 Projected revenues due to signed lease contracts

	Year ending December 31, 2012	Year ending December 31, 2013	Year ending December 31, 2014	Year ending December 31, 2015	Year ending December 31, 2016, forth
	NIS in thousands (Figures according to 100%. Corporation's share in the property – 99.1%)				
Fixed components	196,802	161,763	125,489	106,835	**41,108**
Variable components (estimate)*	-	-	-	-	-
Total	**196,802**	**161,763**	**125,489**	**106,835**	**41,108**

(*) No sales increment for lease of offices.

The revenue amounts in the above table, were calculated based on the basic amounts set forth in the lease agreements while linked to the consumer price index known on December 31, 2011, and based on the following assumptions: (1) The exercise of options for extension of the lease periods included in the lease contracts was not taken into account; (2) Lease contracts which the lease period pursuant thereto has ended and new lease contracts have not yet been signed with the tenants were not taken into account; (3) The possibility of sale of the properties or purchase of new income-producing properties was not taken into account; (4) Early termination fines, if any, were not taken into account; and (5) no change occurred in the advance payments of management fees for each tenant for year 2011.

The amounts of revenues specified in the aforesaid table are under the assumption that the options for extension of the lease periods included in the lease contracts would not be exercised. That is, in spite of the fact that many of the tenants in the Company's premises usually tend to extend the lease agreements upon their termination.

The above figures are based on the estimates of the Company considering the signed agreements as of the Date of the Report and constitute forward-looking information, within the definition thereof in the Securities Law. Actual results may significantly differ from the above specified estimates and the implications thereof, for various reasons, including early termination of lease contracts or a business crisis of any of the tenants.

9.2.7 Specific financing for the property

Specific Financing			Loans(*):
Balances in the Statement of Financial Position	December 31, 2011 (NIS in thousands)	**Presented as current costs:**	**52,834**
		Presented as long-term costs:	**529,851**
	December 31, 2010 (NIS in thousands)	**Presented as current costs:**	**47,986**
		Presented as long-term loans:	**561,155**
Fair value as of December 31, 2011 (NIS in thousands)			**617,192**
Original date of taking the loan			**August 2001-January 2002**
Original amount of loan (NIS in thousands)(**)			**771,969**
Effective Interest Rate as of December 31, 2011 (%)			**5.94%**
Dates of repayment of principal and interest			**The interest and principal are retuned in quarterly payments until August 2013 except for a principal balance in the sum of approx. NIS 495 million (linked to November 2011 index) which is due in August 2013.**
Main financial covenants			**Canit Hashalom's undertaking not to create a floating charge**
Other main covenants			**-**
Statement of whether main covenants or financial covenants have been breached as of the end of the reporting year			**No**
Is it non-recourse			**No**

(*) The loans are for building the towers and the mall with no specific separation. The loans amount was split between the components according to the fair value ratio of the properties, such that in December 31, 2011, 57.7% of the loans were attributed to the towers (56.98% as of December 31, 2010).
(**) The split was made according to the ratio determined in December 31, 2011 for the sake of convenience.

9.2.8 Pledges and material legal restrictions on the property

Type		Specification	The amount secured by the pledge December 31, 2011 (NIS in thousands)
Pledges	First ranking	The property is pledged by a fixed charge to banking corporations	**582,685**

(1) Canit Hashalom has provided the City of Tel Aviv with a guarantee in the amount of NIS 8 million, linked to the Residential Construction Input Price Index (standing, as of December 31, 2011 at approx. NIS **22** million), which is designed to assure Canit Hashalom's compliance with its obligations in connection with the performance of the development and construction work for the project. This guarantee is expected to be returned to Canit Hashalom upon the issuance of a certificate of completion for the project. As of the Date of the Report, Canit Hashalom is acting towards obtaining the aforesaid certificate of completion, and does not expect any part of the guarantee to be forfeited. The provisions of this section constitute forward-looking information which is based upon estimates of the Company in reliance on past experience and the actual results may be different, primarily due to requirements of the authorities which are unknown as of the Date of the Report.

(2) On February 28, 2008, Canit Hashalom signed a letter of undertaking addressed to the City of Tel Aviv and also provided an additional bank guarantee in the amount of approx. NIS 8 million, linked to the Consumer Price Index (standing, as of December 31, 2011 at approx. NIS **8.4** million), in connection with the granting of a Form 4 for the square tower of the project, in the context of which it undertook to act to establish a steering team to evaluate the need to build another tunnel underneath the Kaplan interchange, and further undertook to build the tunnel at its expense, to the extent determined as aforesaid. Insofar as the construction of the aforesaid tunnel will be required, Canit Hashalom estimates the cost of construction in the amount of approx. NIS **4** million.

(*) The loans are for the construction of the towers and the mall without specific distinction. The amount of the loans was split between the components according to the property fair value ratio, such that as of December 31, 2011, 57.7% of the loans were attributed to the towers.

9.2.9 Details regarding the valuation

		Y2011	Y2010	Y2009
The value determined (NIS in thousands)		2,484,608	2,287,214	**2,176,570**
Identity of the appraiser		Greenberg Olpiner & Co.	Greenberg Olpiner & Co.	**Greenberg Olpiner & Co.**
Is the appraiser independent?		yes	yes	**yes**
Is there an indemnification agreement?		Yes	yes	**yes**
Date of validity of the valuation (the date to which the valuation pertains)		Dec. 31, 2011	Dec. 31, 2010	**Dec. 31, 2009**
The valuation model		DCF	DCF	**DCF**
Main parameters used for the valuation[16]				
The valuation according to the	Gross leasable area used in the	149,392	149,184	**148,833**

[16] The valuation is attached as annex C to the Board Report in Chapter B of this Report.

Income Approach	calculation (sqm)[17]			
	Representative occupancy rate out of the leasable area for the purpose of valuation (%)[18]	100%	99.47%	**99.5%**
	Representative average monthly rent per leased sqm for the purpose of valuation i[19]	90.5	86.31	**87.33**
	Representative NOI for the purpose of valuation (NIS in thousands)[20]	193,070	184,105	**172,746**
	Annual average periodic expenses for preservation	**See in other main parameters below**		
	Weighted cap rate used for the valuation	7.59%	7.85%	**7.94%**
	Other main parameters	Projected investments in the property were depreciated, as well as investments due to undertakings to the City of Tel Aviv per contract. The overall depreciation of the property value due to the aforesaid totaled to approx. NIS 58 million.	Projected investments in the property were depreciated, as well as investments due to undertakings to the City of Tel Aviv per contract. The overall depreciation of the property value due to the aforesaid totaled to approx. NIS 59 million.	**Bezeq rent were depreciated for a period of 4 years, and an investment due to an undertaking to the City of Tel Aviv per contract was also depreciated. The total value of the property depreciation due to the aforesaid totaled at approx. NIS 12 million.**
Value sensitivity analyses		**Change in value in NIS in thousands**		
Cap rates	Rise of 0.25%	(81,020)	(71,798)	**(66,102)**
	Decline of 0.25%	86,536	77,171	**70,543**
Average rent per sqm	Rise of 5%%	109,625	101,582	**97,800**
	Decline of 5%	**(109,625)**	**(101,582)**	**(97,800)**

[17] Not including area for the Company's own use of approx. 1,520 sqm on the last office floor of the round tower.
[18] Represents the ratio of marketed area out of the total area, but in appraisal, value was taken for vacant areas too.
[19] In 2011 and 2010 including reduction of rent for Bezeq.
[20] Including 50% of representative NOI of the car park which is included in the property value. (The remaining 50% were included in the valuation of the mall).

9.3 Competition

The office and other space for lease segment in Israel is, in general, characterized by a high level of competition in all aspects pertaining to the rent, the building's accessibility, the finishing and other unique characteristics of the property. The Group is exposed in Israel to competition by numerous companies engaging in the lease of business property, in areas of demands similar to those in which the Group's properties are located, while in most cases, the competition is local competition. Thus, for example, the competition for the Azrieli Center are the high priced office buildings in Tel Aviv and the competition for the Herzlia Business Park are other alternate office buildings in that area.

To the best of the Company's knowledge, several bodies are active in Israel, holding significant shares of the office and other space for lease segment, including Reit 1 Ltd., Gav Yam Land Ltd., Nitzba Holdings 1995 Ltd., Industrial Buildings Ltd., British Israel Investments Ltd. and Amot Investments Ltd. In the Company's estimation, the scope of its business in the office and other space for rent in Israel segment is among the leading companies in the segment, particularly with completion of the projects which are, as of the Date of the Report, under construction.

The factors assisting the Company to deal with the competition in this segment are as follows:

- The Company's volume of operation in the segment enables the Company to communicate with companies and service providers at beneficial terms;

- The Company's volume of operation in the segment enables the Company to specialize in the management of commercial parks and office buildings in an efficient manner which leads to savings in costs and in manpower;

- Most of the Company's tenants are companies with high financial strength and the lease agreements therewith are for a relatively long period of time;

- The Company's office and other space for lease is located in areas of high demand, enabling the Company to lease the properties to numerous diverse types of tenants.

- The unique characteristics of the Group's properties, such as: a commercial center in proximity to the office space for rental, access to public transportation, including the railroad and underground car parks for the convenience of the tenants and their customers.

- Most of the Company's office space is characterized by its high quality and prestigious nature, which distinguishes the Company's property from those of the competing companies and strengthen its competitive ege.

9.4 Goals and business strategy in the segment

See Section 23 of the Report for details on the Company's goals and the Group's strategy.

10. The income-producing property in the U.S.A. segment

10.1 General

As of the Report Publication Date, the Group owns five office rental properties outside of Israel, of a total leasable area of approx. 166 thousand sqm (the Company's share is approx. 155 thousand sqm), which is leased to approx. 270 tenants, as well as one commercial center of a total leasable area of approx. 13 thousand sqm, wholly owned by the Company, containing approx. 10 tenants. The Company's properties in this operating segment do not amount to material properties or very material properties. For aggregate details regarding all of the Company's income-producing properties in this operating segment, see Part Three, Section 7 above, under the geographic region U.S.

The Group's office properties in this operating segment are Class A multi-tenant properties, which also include parking lots (above ground and underground) which are used by the tenants. The properties are located in high demand areas with more office building clusters. Unlike the Company's properties in Israel, in some of the Company's properties in the U.S., the Company holds the property together with one or more local partners.

The office buildings in the operating segment are mostly intended for businesses (*inter alia* from the energy industry) and service providers which are characterized by a large number of employees and demand for adjacent parking spaces.

Most of the Group's lease contracts in this operating segment are for periods of between three (3) and ten (10) years, while often the tenant is given an option for additional lease periods of up to five years. The rent is at a fixed amount per square meter (or the corresponding measure – SQF) of the leased area, while often the lease contract includes a rent increase during the term of the lease.

Unlike the Group's office properties in Israel, the Group's office space in the U.S. is managed by professional and local management companies with which the Company has engaged in agreements, and which the Group is entitled to terminate by advance notice of 30 days. The management companies collect from the tenants the rent, as well as current expenses, such as security, cleaning, maintenance, municipal taxes, insurance, gardening, maintenance of elevators and public systems.

10.2 The structure of the operating segment and changes occurring therein

During 2011 and 2012 until the Report Publication Date, the Company expanded its business in the U.S.A. through two purchase transactions, one of three office towers in the "Galleria" area of the city of Houston, Texas, and the other of an additional office building in the "Energy Corridor" area of the city of Houston, Texas (as specified in Section 10.10 below).

The income-producing property segment in the U.S.A is affected by the economic activity in the U.S. economy, and mainly by the economic business in Houston and its office lease market.

In recent years, the U.S. income-producing property market suffered an acute crisis and general sweeping deterioration. The occupancy of properties and rent decreased, the rate of available areas in the office market increased and as a result of liquidity and

credit problems, banks and other lenders have toughened the financing conditions for commercial properties, mostly by reducing the leverage rates and raising the required equity.

In order to assist in stabilizing the financial markets, the U.S. government launched several large scale programs to aid the real estate industry, and in December 2008 the Federal Reserve reduced the interest rate to 0.25%. In 2010, a positive trend began to become apparent in the real segment and in the U.S. economy, which also continued in 2011.

To the best of the Company's knowledge, the effect of the global economic crisis was clearly evident in the U.S. office market, although the effect in Houston was minor relative to other regions, both in the rates of the vacant space and in the decline in the rent prices. During 2011, there were increases in the rent prices in the various areas of the city of Houston in which the Company holds office buildings, and a trend of decrease in the rates of vacant space in properties was evident.

In 2011, there was a rise in the development of new projects in the sought after areas of Houston, after several years of an absolute standstill in the development of such projects.

10.3 Restrictions, legislation, standards and special constraints applying to the operating segment

This operating segment is subject mainly to the local planning and building laws and land laws. In addition, the business in this segment is affected by legislation and regulation of authorities in the fields of environmental protection, safety, business licensing, land taxation and municipal taxation. See Section 20 of the Report for details on the matter of the restrictions, legislation, standards and additional constraints applying to the entire Group.

10.4 Changes in the volume of business and profitability of the segment

As aforesaid, it appears that the slowdown trend that occurred in the income-producing property market in the U.S. in recent years came to a halt and stabilized in 2011. In the Houston metropolis, even more significant improvement was evident when in 2011, approx 3 million SQF more office space was rented than that rented in 2010[21]. The total rate of vacant space in the city of Houston decreased from 16% to 15%, while in Class A office buidlings, the rate of vacant space at the end of 2011 was 10.6%. In addition, to the best of the Company's knowledge, in 2011 there was a rise in rent prices in the office segment in some of the markets in the U.S., as well as in the city of Houston..

10.5 Critical success factors in the operating segment and changes occurring therein

The Company estimates that the main success factors in this operating segment are its know-how, expertise and experience in the location and acquisition of attractive properties that will yield a high return, and the location of local management companies specializing in the local market and in property, for the purpose of management of the properties and marketing of the space therein. The Company estimates that the success factors in the acquisition of such properties in the operating segment are, *inter alia*,

[21] According to figures appearing in Market Outlook, Houston Texas, which was published by CBRE in February 2012.

location of worthwhile transactions and identification of opportunities in the market with a fast response capability, acquisition of properties in attractive, high demand locations with improvement potential, acquisition of properties of a high building and finishing standard, acquisition of properties with a range of related services that are not available in nearby properties which are competing for new contracts, performance of meticulous due diligence investigations, *inter alia* with respect to the expected expense structure in the property and the profit increase potential, the strength of the tenants in the property and the nature of the collateral, as well as knowledge of the financial markets and the various players therein for the purpose of achieving attractive financing.

10.6 Main barriers to entry and exit in the operating segment and changes occurring therein

Barriers to Entry - To the Company's belief**,** entities operating in this operating segment require mainly equity and financial strength which allow the acquisition of existing properties at relatively low financing costs. In addition, professional know-how, experience in the segment of acquisitions and management of income-producing properties, as well as know-how and experience in the credit and financing sector are important. Positive goodwill is another important element, both during tenders for the acquisition of income-producing properties and in order to attract attractive tenants to the properties.

Barriers to Exit - exiting this operating segment is conditional, mostly, on the ability to realize properties, which is a direct result of the location of the properties, their physical condition and the condition of the economy, as well as various costs, including in connection with land taxation.

10.7 Structure of competition in the operating segment and changes occurring therein

The income-producing property industry, in the U.S. and in Houston in particular, is characterized by a high level of competition. Competition in this segment revolves around a number of parameters, of which the principal ones are; (1) the geographic location of the properties and the level of demand for the space for lease in that area; (2) the amount of the rent and the management and maintenance costs; (3) the granting of incentives to new tenants or upon renewal of a lease agreement, such as improvements in the leased premises or a certain lease period in which rent will not be charged; (4) the quality of construction of the leased buildings; (5) the level of auxiliary services; and (6) the reputation of the lessor. The competition in this sector exists both at the stage of acquisition of the properties and at the stage of the leasing of the properties. See Section 10.11 below for a description of the structure of competition in this operating segment.

10.8 Manner of executing acquisitions of the Company

For the purpose of the Group's development in this operating segment, the Group focuses, as of the Date of the Report, on the acquisition of existing and populated income-producing properties, and is not building new properties itself. In addition, the Company usually enters into financing agreements with different financing bodies for the purpose of the acquisition of the properties in this operating segment, usually under non-recourse terms (with exceptions standard in the U.S.). See section 8.1.9 of this Chapter for a description of the manner of acquisition and exercise of the entire Group's rights in properties.

10.9 Properties acquired during the Report Period – acquisition of office towers in Houston

On February 4, 2011, Three Galleria Office Buildings, LLC, a U.S. company indirectly held at the rate of 90% by the Company (in this section: the "**Buyer**") completed the acquisition of three office towers in Houston, U.S. (the "**Agreement**") in consideration for the total sum of U.S. $176 million.

In accordance with the Agreement, the Buyer acquired all of the rights in three towers that are used for offices, of a total area of approx. 99,000 sqm (1,065,789 SQF) (without additional building rights), which are situated in the Galleria area of Houston, Texas, in the U.S. (the "**Property**"). The three towers are located in part of a complex that includes commercial areas, two luxury hotels and parking lots. Approx. 3,775 parking spaces serve the towers according to a long-term agreement with the owners of the commercial property.

In addition, the Company provided the partner in the Property (10%) with a loan in the sum of approx. U.S. $2.5 million, which was required for the financing of part of the partner's share in the equity required for the acquisition, and which bore annual interest at the rate of 6.998% and was repaid in full as of the Date of the Report. Concurrently, the pledge that was imposed on the partner's rights expired and the guarantee that it provided was cancelled. For further details regarding the Property and the Agreement for its acquisition and for its financing, see the Company's reports of January 30, 2011 (ref. 2011-01-031650) and of February 6, 2011 (ref. 2011-01-039024), which are included herein by way of reference.

10.10 Properties purchased after the date of the Statement of Financial Position – **purchasing an office building in Houston**

On January 10, 2012, AG Plaza at Enclave, LLC, a U.S.A. corporation indirectly held at a arte rate of 100% by the Company (in this Section: the "**Buyer**"), completed the purchase of an office building with a 100% occupancy rate in Houston, Texas, U.S.A. (the "**Agreement**") in consideration for the sum of approx. U.S. $107.5 million (in addition to transaction costs (including financing costs) in the sum of approx. U.S. $750 thousand).

As per the Agreement, the Buyer had purchased the full rights to an office building on a total area of about 31,986 sqm (344,296 sqf), (including some 1,500 parking spaces located in a separate parking building), which is located in a central business district in the Houston, Texas, U.S.A., whose construction was completed in 2008 (the "**Office Building**").

The property has four (4) tenants, as follows:

- ✓ A main tenant (87%) which is one of the world-leading agrochemical companies by the name of Dow Chemical Company, which is traded on NYSE, which has a long-term lease agreement expiring in May 2026, with no early termination option. The lease agreement includes an option to extend the agreement for additional terms.

- ✓ Three lessees (13% in total) have lease agreements for periods ranging between 6 and 7 years from the date of acquisition of the property, with some of the tenants having an early termination option after about 5 years, and all having an option to extend the agreement for additional terms.

The lease agreements include fixed mechanisms for rent increase throughout the terms of the agreements, such that the total annual average NOI[22] for all of the contracts, throughout all of the lease periods will be approx. U.S. $8 million, constituting a yield of approx. 7.5%. For further details regarding the property and its purchase agreement, see the Company's reports dated January 1, 2012 (reference no.: 2012-01-000444) and January 11, 2012 (reference no.: 2012-01-01253). As to the way of financing the property, see Section 17.9 of this Chapter.

The information regarding the projected total average annual NOI is forward-looking information, as defined in the Securities Law, and is based on the Company's estimates and the lease agreements existing as of the Date of the Report. The actual results may be materially different to the estimates specified above, and the implications thereof, for various reasons including due to modification or early termination of lease contracts or a change in the relevant market conditions.

10.11 Competition

The income-producing property segment in the U.S.A. is, in general, characterized by a high level of competition in all aspects pertaining to the rent, the quality of the finishing of the building and other unique characteristics of the property. The Group is exposed in the U.S.A. to competition by numerous companies engaging in business property lease, in areas of demands similar to those in which the Group's properties are located. The market of leasable offices in Houston, Texas, constitutes approx. 191 million sqf of leasable office space (of which approx. 93 million SQF is defined as Class A), and includes a large number of properties. To the best of the Company's knowledge, several bodies are active in Houston, holding significant shares of the office lease areas segment[23], and the Group's share in the income-producing property segment in the U.S. is negligible.

The factors assisting the Company to deal with the competition in this segment are as follows: (1) The Company's office lease areas are located in high demand attractive areas, enabling the Company to lease the properties to numerous and diverse types of lessees; (2) most of the Group's properties in this operating segment have special characteristics, including: a "Leed Gold Certificate" rating of the Green Building Council, tenants with a high rating, attractive location adjacent to large commercial centers, as well as a high parking space ratio relative to the size of the property; (3) most of the Company's office space in this operating segment is characterized by a high building and finishing standard and has been granted the highest rating level of office properties (Class A).

The Group engages in this operating segment in management agreements with strong local entities which have vast experience in and deep knowledge of the local market, for the purpose of management and lease of the properties.

[22] The Buyer will step into the shoes of the seller, who committed in the lease agreements to a five (5) months free rent period. Assuming full rent (based on the agreements in effect) in 2012 the annual representative NOI would have been expected to be approx. U.S. $7.1 million.

[23] According to figures appearing in Market Outlook, Houston Texas, which was published by CBRE in February 2012.

10.12 **Goals and business strategy in the segment**

See Section 23 of the Report for details on the Company's goals and the Group's strategy.

Part Five - Granite Segment

11. Granite Segment

On October 30, 2006, Canit Hashalom purchased approx. 53.99% of the issued and paid-up capital of Granite Hacarmel, a public company whose shares are listed for trade on the TASE, in consideration for the sum of approx. NIS 631 million (reflecting a value for Granite at that time in the sum of NIS 1,666 million) (the "**Purchase Agreement**").

On December 13, 2006, Canit Hashalom purchased from an interested party in Granite Hacarmel approx. additional 10% of Granite Hacarmel's issued and paid-up capital, in consideration for the sum of approx. NIS 109 million (reflecting a value for Granite at that time in the sum of NIS 1,092 million). As a result of the purchase, the rate of Canit Hashalom's holdings in Granite Hacarmel went up to 63.83% at that time.

As of March 29, 2011, the Canit Hashalom holds some 60.68% of the issued equity capital and the voting rights in Granite Hacarmel Investments Ltd. ("**Granite**"), which is incorporated in Israel and traded on the TASE. As of June 30, 2011, following the expansion of the organ of the Chief Operating Decision Making team ("**CODM**"), and due to the increasing focus on Supergas's operations in the natural gas and solar energy segments, the reporting format was updated so that, as of the said date, Granite issues public reports in five operating segments, in accordance with the Core Companies, which also constitute the financial segments in Granite's financial statements. They are: (a) Sonol fuelling and commerce complexes; (b) Sonol direct marketing; (c) Supergas; (d) Tambour; (e) GES and Other segment. Accordingly, information concerning Granite's operating segment shall be provided for each of the five operating segments reported by Granite. For details regarding general information with respect to the Granite group in its entirety, see Sections 11.74 to 11.81 below.

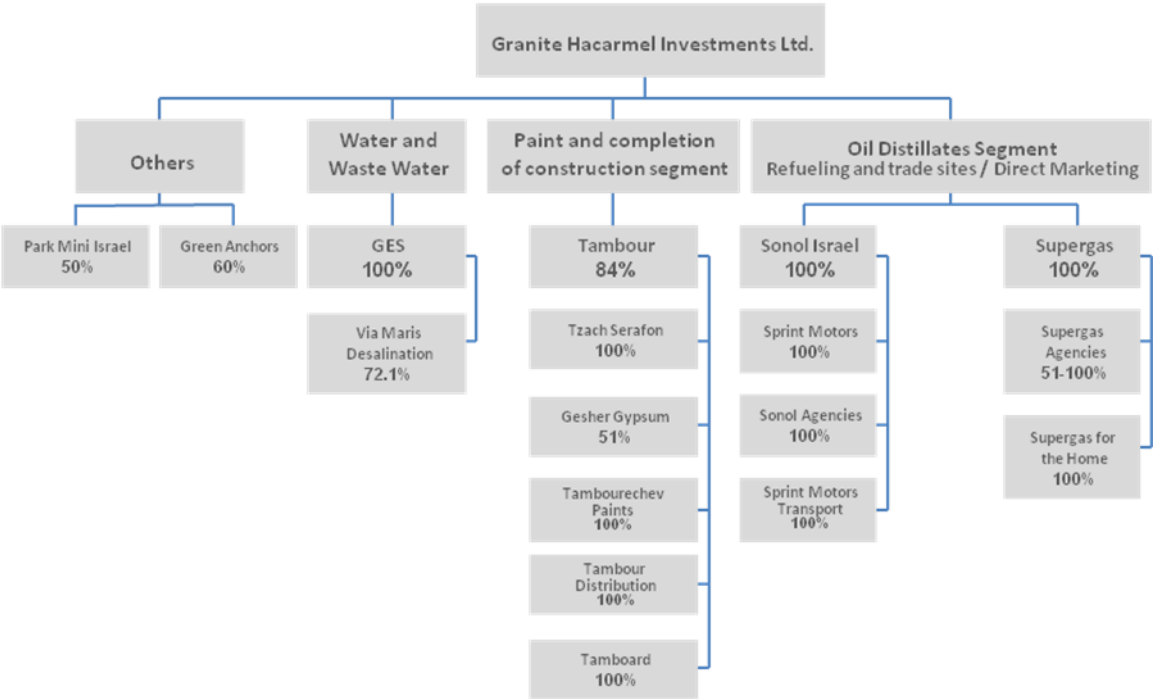
For the sake of convenience, in this Section 11, the following abbreviated terms shall have the meanings set forth beside them:

Granite -	Granite Hacarmel Investments Ltd.;
The Granite Group or the Group -	Granite and its consolidated companies;
Reported Shekels -	Shekels adjusted for the transition date (December 31, 2003), with additional sums in nominal values added after the transition date;
The Fuel Administration -	The Fuel Administration at the Ministry of Energy & Water Resources;
Granite Properties -	Granite Hacarmel Properties (1993) Ltd. – A wholly owned (100%) subsidiary of Granite and its consolidated companies;
Tambour -	Tambour Ltd. – A public company traded on the TASE, in which Granite holds some 84% of the shares (without dilution) and its consolidated companies;
Sonol -	Sonol Israel Ltd. – A subsidiary company wholly owned (100%) by Granite and its consolidated companies;
Supergas -	Supergas Israel Gas Distribution Company Ltd. – A fully-owned (100%) subsidiary of Granite and its consolidated companies;
GES -	GES Global Environmental Solutions Ltd. – A subsidiary

	wholly owned (100%) by Granite and its consolidated companies;
Magal -	Magal Israel Oil and Gas Enterprises Ltd.;
Pi-Glilot -	Pi-Glilot Petroleum Terminal and Pipelines Ltd.;
HBO -	Haifa Basic Oils factory.;
BAZA or ORA -	Paz Oil Refinery Ashdod Ltd.;
BAZAN or ORL -	Oil Refineries Ltd.;
Oil Distillates -	The various types of fuels, including Liquefied Petroleum Gas ("LPG");
LPG	Liquefied Petroleum Gas;

11.1. Holdings structure

The following diagram illustrates Granite's principal holdings on the Date of the Report.



11.2. Financial data on Granite's operating segments

Below is financial data on Granite's various operating segments:

Financial data on Granite's operating segments for the year ended December 31, 2011 (NIS in thousands)

	Sonol									
	Fuelling complexes	**Direct marketing**	**Not associated(1)**	**Total**	**Supergas**	**Tambour**	**GES**	**Other**	**Adjustments(2)**	**Consolidated**
Revenues										
From external parties	3,014,440	1,774,174	-	4,788,614	499,740	769,270	233,062	14,156	-	6,304,842
From other operating segments	12,401	8,366	-	20,767	14,961	1,535	1,621	337	(39,221)	-
Total	3,026,841	1,782,540	-	4,809,381	514,701	770,805	234,683	14,493	(39,221)	6,304,842
Attributed costs										
Costs that do not constitute revenues in other operating segment	2,970,860	1,721,839	34,799	4,727,498	454,224	681,508	201,884	12,317	19,099	6,096,530
Costs that constitute revenues in other operating segment	471	1,210	-	1,681	3,391	30,367	5,779	(246)	(40,972)	-
Total	2,971,331	1,723,049	34,799	4,729,179	457,615	711,875	207,663	12,071	(21,873)	6,096,530
Operating profit attributed to the operating segment	55,510	59,491	(34,799)	80,202	57,086	58,930	27,020	2,422	(17,348)	208,312
Fixed costs attributed to the operating segment	293,565	35,877	33,760	36,202	108,061	139,170	54,765	2,978		
Variable costs attributed to the operating segment	2,677,295	1,685,962	-	4,363,257	346,560	544,917	154,020	6,472		
(Rise) Fall in value of investment property, net	-	-	(2,015)	(2,015)	-	-	-	1,794		

Other expenses (revenues), net	-	-	3,054	3,054	(397)	(2,579)	(6,901)	1,073
Operating profit attributed to the owners of the parent company	55,510	59,491	(34,799)	80,202	56,839	47,086	23,180	836
Operating profit attributed to rights which do not confer control	-	-	-	-	247	11,844	3,840	1,586

Financial data on Granite's operating segments for the year ended December 31, 2010 (NIS in thousands)

	Sonol									
	Fuelling Complexes	Direct marketing	Not associated	Total	Supergas	Tambour	GES	Other	Adjustments(2)	Consolidated
Revenues										
From external parties	2,518,206	1,411,520	-	3,929,726	419,912	683,647	205,202	13,982	-	5,252,469
From other operating segments	7,433	19,489	-	26,922	7,668	551	1,755	499	(37,395)	-
Total	2,525,639	1,431,009	-	3,956,648	427,580	684,198	206,957	14,481	(37,395)	5,252,469
Attributed costs										
Costs that do not constitute revenues in other operating segment	2,400,652	1,380,064	48,901	3,829,617	367,262	612,990	194,283	10,999	26,142	5,041,293
Costs that constitute revenues in other operating segment	-	1,472	-	1,472	14,851	17,178	3,878	39	(37,418)	-
Total	2,400,652	1,381,536	48,901	3,831,089	382,113	630,168	198,161	11,038	(11,276)	5,041,293
Operating profit attributed to the operating segment	124,987	49,473	(48,901)	125,559	45,467	54,030	8,796	3,443	(26,119)	211,176
Fixed costs attributed to the operating segment	268,277	35,401	71,157	374,835	110,596	177,151	54,577	2,422		
Variable costs attributed to the operating segment	2,132,375	1,344,663	-	3,477,038	257,688	439,900	142,159	7,934		
(Rise) Fall in value of investment property, net	-	-	(165)	(165)	-	-	-	1,246		

Other expenses (revenues), net	-	-	(22,091)	(22,091)	(1,022)	(4,061)	(2,453)	(603)
Operating profit attributed to the owners of the parent company	124,987	49,460	(48,901)	125,546	45,522	44,657	8,043	2,610
Operating profit attributed to rights which do not confer control	-	13	-	13	(55)	9,373	753	833

Financial data on Granite's operating segments for the year ended December 31, 2009 (NIS in thousands)

	Sonol									
	Fuelling complexes	**Direct marketing**	**Not associated(1)**	**Total**	**Supergas**	**Tambour**	**GES**	**Other**	**Adjustments(2)**	**Consolidated**
Revenues										
From external parties	2,111,393	1,292,175	-	3,403,568	393,032	572,028	141,863	36,183	-	4,546,674
From other operating segments	4,019	15,989	-	20,008	-	333	286	4,419	(25,046)	-
Total	2,115,412	1,308,164	-	3,423,576	393,032	572,361	142,149	40,602	(25,406)	4,546,674
Attributed costs										
Costs that do not constitute revenues in other operating segment	1,970,713	1,252,915	55,581	3,279,209	333,696	521,803	130,015	47,755	20,089	4,332,567
Costs that constitute revenues in other operating segment	-	354	-	354	13,885	6,409	1,356	4,095	(26,099)	-
Total	1,970,713	1,253,269	55,581	3,279,563	347,581	528,212	131,371	51,850	(6,010)	4,332,567
Operating profit attributed to the operating segment	144,699	54,895	(55,581)	144,013	45,451	44,149	10,778	(11,248)	(19,036)	214,107
Fixed costs attributed to the operating segment	263,216	36,523	69,245	368,984	109,161	112,453	47,110	11,345		
Variable costs	1,707,497	1,216,392	-	2,923,889	224,746	413,125	91,081	29,914		

attributed to the operating segment								
(Rise) Fall in value of investment property, net	-	-	292	292	-	-	-	4,107
Other expenses (revenues), net	-	-	(13,956)	(13,956)	(211)	(3,775)	(8,176)	2,389
Operating profit attributed to the owners of the parent company	144,699	54,582	(55,581)	143,700	45,484	35,757	11,503	(11,182)
Operating profit attributed to rights which do not confer control	-	313	-	313	(33)	8,392	(725)	(66)

(1) In Note 5 to Granite Hacarmel's financial statements, clarifications were provided in respect of a change in the attribution of unattributed expenses.
(2) The adjustments include adjustments to a segment's revenues and profits due to intersegment transactions as well as companies which do not comply with the definition of the operation segment.

Sonol Direct Marketing and Fuelling Stations and Commerce Complexes Segment

11.3. **General**

In view of the great similarities between most of the characteristics of the Sonol direct marketing segment and the Sonol fuelling stations and commerce complexes segment, the following description refers to both operating segments jointly, with explicit reference to dissimilarities between the two operating segments or to matters relevant to only one of them.

11.3.1. Granite Group holds 100% of the rights in Sonol Israel Ltd. Within the business segments of Sonol direct marketing and fuelling stations and commerce complexes the Granite Group is involved in the following fields: (1) local purchase, import, storage, marketing and distribution of Oil Distillates; (2) production, storage, marketing and distribution of lubrication oil, engine oil, transmission oil, oil for industry, additives and other auxiliary products; (3) Transport of Oil Distillates and oils; (4) marketing of various products in Sonol's chain of convenience stores. It shall be noted that on March 21, 2012, Granite Group announced that following the request of various entities to explore the possibility of acquiring Granite's holdings in Sonol, Granite allowed such entities to inspect certain information in writing in connection with Sonol, subject to an undertaking to maintain the information in confidence and subject to the provisions of the law. At this stage, it is unclear whether such inspection will lead to negotiations, and even if and insofar as negotiations will be held, there is no certainty that agreements will be reached between the parties in connection with the terms and conditions of the transaction and in connection with engagement in an agreement in respect thereof.

11.3.2. In the Sonol direct marketing segment, the sales of Oil Distillates and oils is made to institutional, governmental, commercial and business customers, including to transportation companies, airlines, industry and agriculture. Sales of fuels and oils to such customers do not involve the public fuelling stations operated by the Granite Group and/or any other operator.

11.3.3. The characteristics common to direct marketing customers are *inter alia*, sales on a relatively large scale, coupled with relatively high discounts and relatively long credit periods (end-of-month + 30 days to end-of-month+ 90 days), all of which is standard practice in this market as well as

transactions conducted through a system of agreements for defined periods. Therefore, Granite categorizes those customers as high commercial and credit risks. For most of these customers, Sonol transports the Oil Distillates directly to their premises, where they are stored in tanks.

11.3.4. In the Sonol fuelling stations and commerce complexes segment, Oil Distillates and oils are sold to individual customers and to commercial customers operating fleets of vehicles with automatic fuelling systems installed for fuelling at fuelling stations in the Sonol Chain. Oil Distillates and oils are also sold to distributors and public fuelling stations not operated by the Granite Group. At fuelling stations operated by a subsidiary company, Sonol also sells other consumer products, both in convenience stores and at the pump docks.

It shall be noted that the gross margins from sales to customers at fuelling station and commerce complexes are higher than from direct sales customers. However the nature of those sales (sales at fuelling stations operated by the Granite Group) makes the cost of sales higher.

11.3.5. The Granite Group has a dependency upon BAZAN – see also Section 11.13.4 below.

11.3.6. Changes in global oil prices and the rate of tax imposed on diesel fuel have an effect on Granite customers' profit. In 2009, 2010 and 2011 crude oil prices went up and taxes on both gasoline and diesel fuels also went up, which caused a rise in customers' profits. Granite's business in these operating segments is subject to a range of legislative and regulatory limitations, including environmental regulation. In reference to this matter see also Section 11.16.1 below.

11.3.7. Granite's operating segments are characterized by intense competition. For further details, see Section 11.10 below.

11.3.8. In September 2006, Paz bought BAZA from the State of Israel and thereby, Paz became the first fuel company to control the entire customer supply chain in Israel's fuel market. The synergy between the refinery owned by Paz and the marketing of petroleum products by Paz provides that company with an advantage over other fuel companies involved solely in the marketing of petroleum products. That advantage might become especially prominent in the direct marketing segment.

Moreover, BAZAN became entirely privately owned in February 2007. The Government Corporations Order (Declaration of Essential State Interests in The Oil Refinery

Company Ashdod, Ltd.), 5766-2005 (the "**Interests Order**"), states that anyone declared by the Commissioner of the Antitrust Authority as involved in the national marketing of Oil Distillates at fuelling stations in Israel shall not be permitted to hold 5% or more in BAZAN. Furthermore, BAZAN is entitled to be engaged in marketing fuels but its market share in the fuel marketing segment may not exceed 20% of the Israeli market (the Minister of National Infrastructures is empowered to increase that percentage at the end of 2011). Marketing fuels by BAZAN, if and when it happens, will constitute the entry of another strong competitor achieving total control on the entire customer supply chain and might have a substantial effect on competition in the direct marketing segment.

Following the privatization of BAZAN, it may also begin to operate in the Oil Distillates marketing segment, which it has been prevented from doing until now. The entry of another strong competitor controlling the entire chain of supply to the customer might have a material effect on competition in the Oil Distillates direct marketing segment.

In 2007, after the sale of BAZA to Paz, regulation of the prices at which fuel companies buy Oil Distillates from refineries was terminated and regulation is now achieved through reporting of the refineries' profits and prices. In reference to this matter, see also Section 11.5 below.

11.3.9. Benzine 95 is a commodity which is supervised by the Fuel Administration. In September 2011, the fuel price's structure was changed, and within such structure change, the supervised margin decreased as did the level of operational costs recognized by the Fuel Administration, which caused a decrease in the fuel companies' profitability in selling Benzine as stated. The margin's decrease and the decrease in the profitability rate, negatively affected Sonol's financial results in the fourth quarter of 2011. It should be noted that Sonol took and takes several efficiency measures in order to reduce the force of the effect. Such actions have partially compensated for the decrease in revenues in the last quarter of 2011, as described above.

11.3.10. Some of Granite's products have potential alternatives, such as natural gas. Marketing of natural gas could reduce the scale of sales by Granite Group companies active in the Oil Distillates segment. As of the date of this Report, such alternatives are available to only some Granite customers, some of whom are transferring over to the consumption of natural gas instead of fuel oil, diesel fuel and LPG. It should be noted that in the course the years 2010 and 2011 the volume of sales of fuel oil to plants in the south of the

country significantly decreased. However, that alternative is not yet available to most Granite customers. However, to the best of the Company's knowledge, based on Granite's management best knowledge, preparations for the marketing of natural gas to the Israeli economy are expanding. It should be noted that, due to the riots in Egypt and the change of government there, the natural gas supply from Egypt had been substantially disrupted, which compelled industrial companies, which had switched to using natural gas, to revert to using Oil Distillates once again, which in turn caused an unforeseeable increase in the demand for fuel oil in the second half of 2011. In Granite's estimations, this trend will stop insofar as the gas supply from Egypt is arranged or when the discovered Israeli gas reserves are operational, but these are Granite's estimations and there is no certainty with respect to their materialization.

11.3.11. The critical success factors in the Sonol fuelling stations and commerce complexes segment are the finding of new, strategic locations for the establishment of public fuelling stations; growth in the national coverage of fuelling stations in the Granite Group's chain; dealing with the surrounding competition and optimal exploitation of fuelling station land to establish a chain of convenience stores and mini-malls at fuelling stations, while maintaining the standards of safety, quality of the environment and the quality of customer service. Additionally, the Company's management deems operational efficiency and cutting back on expenditures as essential measures, which aid in the improvement of its profitability and in overcoming the decrease in the marketing margin as stated.

The critical success factors in the direct marketing segment are principally better service; professional response to customer needs and an increase in the range of commercial and institutional customers, achieved *inter alia*, by winning large tenders.

11.4. **Main products**

The main products and services in the two operating segments are as follows:

11.4.1. White fuels

The Granite Group markets and distributes different types of white fuels (**"White Fuels"**). White fuels are, principally, the following products:

Gasoline and diesel fuel for transportation – Most of the types of gasoline and diesel fuel for transportation are used to power vehicles.

In the direct marketing segment, the Granite Group markets a number of different types of gasoline (95 octane (Gold 95) and 98 octane) and diesel fuel, mainly to distributors, industrial plants, the agriculture industry, infrastructure contractors and Private Fuelling Stations at moshavim, kibbutzim and factories (the "**Private Fuelling Stations**"). These customers are direct commercial customers for Sonol or its subsidiaries.

In the fuelling station and commerce complex segment, the Granite Group markets the types of gasoline and diesel fuel for transportation mentioned above to individual, spontaneous customers of the public fuelling stations operated thereby (the "**Fuelling Stations Operated by the Granite Group"**), operators of Sonol Chain's public fuelling stations not run by the Granite Group (the **"External Operators"**) and to customers who own vehicle fleets.

Diesel fuel for heating – In the direct marketing segment, diesel heating fuel is used to fire ovens in industry and agriculture, for the institutional market and it is sold to commercial resellers. Diesel heating fuel is also used for private household heating and to fire various types of ovens.

Heating Oil – Heating oil is used for residential heating and to fire various types of heating ovens.

Jet **Fuel** – Jet fuel is used only in the direct marketing segment to fuel jet aircraft.

Kerosene – In terms of its technical specifications, **kerosene** is a product similar to jet fuel and it is available only in the direct marketing segment. Principally, **kerosene** is used for heating uses similar to diesel heating fuel.

Naphtha – Naphtha is used mainly as feedstock in the petrochemical industry. Naphtha is sold in the direct marketing segment.

11.4.2. Black fuels

The Granite Group markets and distributes different types of black fuels, solely to the direct marketing customers. Black fuels include, primarily, bitumen and different types of fuel oils (**"Black Fuels"**).

Principally, Black Fuels are used for pavement, sealing (bitumen), as heating fuels and feedstock in industrial applications (mainly heavy industry), shipping, electricity and steam generation and other uses.

11.4.3. Oils

As a rule, the various types of oil comprise base oils with additives. Base oils are produced by the petroleum industry and they are manufactured mainly at HBO (Haifa Basic Oil Ltd.) in which, until March 2010, Granite held some 14% of the equity. Most of the various additives and some of the oils are imported from foreign suppliers.

The Granite Group manufactures, stores, markets and distributes various types of oils, marketed to institutional and commercial customers through direct marketing and for privately owned vehicles at fuelling station and commerce complexes, including automotive and engine oils. Furthermore, the Granite Group markets other auxiliary products (various additives). In addition, the Granite Group manufactures and markets transmission oils, lubricants, marine oils, industrial oils and various additives, marketed solely through direct marketing.

11.4.4. Consumer products sold at fuelling stations

At the fuelling stations chain operated by the Granite Group, the Granite Group sells a range of consumer products in convenience stores and at the pump docks. As of the Date of this Report, the Group operates 164 convenience stores under the brand name: "Sogood" (as of December 31, 2010 and 2009, 151 and 140 stores operated in the chain, respectively), while Sonol's intention is to construct 10 additional stores in 2012, and all subject to Sonol's resolutions, the competition in the market and Sonol's situation. from the sales turnover of various products (except fuels) reached NIS 240 million in 2011, compared with NIS 206 million and NIS 164 million in the years 2010 and 2009, respectively. It should be noted that the increase rate in 2011 compared with 2010 in the sales turnover of stores that operated in both years is approx. 9.4%. Granit's gross profit from the sales of the convenience stores as aforesaid amounted in 2011 to the sum of approx. NIS 70 million compared to a gross profit of NIS 60 million and NIS 46.9 million in the years 2010 and 2009, respectively. It must be mentioned that the scale of revenues generated by the sale of those products is not significant when compared with the overall revenues generated by the Oil Distillates segment. As pertains to the convenience stores in the chain, including the intention to increase their number, see Section 11.6 below.

11.5. **Determining the price of products for customers**

Until January 2007, the Fuel Administration determined the prices of most of the Oil Distillates sold by BAZAN, a price that was known as the "ORL Gate Price". Such price was adjusted once a month according to the price at Labra Port (an average price of the relevant Oil Distillate in the Mediterranean basin region based on the five days of publication towards the end of the preceding month, except for ORL price to LPG, which was determined according to the average import price in the preceding month). During 2007, supervision of prices for oil products at the refinery gate was lifted and from that date, prices for Oil Distillates have been determined in negotiation between the refineries and their customers, although the ORL Gate Price, calculated as aforesaid, was still used as basis. Negotiations are influenced by the prices paid by the fuel companies for directly imported Oil Distillates, which constitute the alternative to purchasing from BAZAN. Lifting regulation of Oil Distillates prices on the one hand while maintaining regulated maximum prices for 95 octane gasoline on the other, has a negative effect on the fuel companies' situations.

The maximum consumer price for 95 octane gasoline is determined by the Fuel Administration (for details of products under regulation, see also Sections 11.17.7-11.17.9 below), based on the price for those products at the ORL Gate plus taxes, costs incurred for infrastructure, financing costs and transportation and the fuel companies' marketing margin, which are supposed to compensate those companies for the cost of infrastructure, financing and transportation including, *inter alia*, the marketing margin for fuelling station operators. As aforesaid, in September 2011, the Fuel Administration reduced the overall marketing margin for the supervised gasoline. For details, see Section 11.17.9 hereunder.

As pertains to other Oil Distillates sold by the Granite Group, no maximum price is determined by the Fuel Administration. However, in most instances, Granite's consumer prices are also determined in accordance with the parameters mentioned above.

Prices for fuels sold by Sonol to the direct marketing's customers are derived by Sonol based on the Sonol price list, which is determined as explained above. The final price offered to each customer is considered on an individual basis and *inter alia*, takes into account the scale of the customer's purchases, the quality of the customer's guarantees, credit terms and the customer's potential contribution to overall sales.

Prices for fuels sold by Sonol at fuelling stations operated by the Granite Group are based on the Sonol price list, which is determined according to the parameters explained above. The price of the gasoline sold in Self service fuelling does not exceed the maximum supervised price and no extra price is charged therefor in accordance with that determined in the Regulatory Order. Furthermore, Sonol grants certain discounts to those fuelling at fuelling stations, as required to stay

competitive and discounts to vehicle fleets in view of their size. Prices for independent operators of fuelling stations in the Sonol Chain also take into account the nature of the agreement with the operator, Sonol's investments in the stations, the competition etc..

Oils manufactured by Sonol are priced based on, *inter alia*, the cost of the raw materials, the additives, labor and indirect costs.

11.6. **Material changes expected in the corporation's share and mix**

To the Company's belief, based on the best knowledge of Granite's management, no material change is expected in Sonol's share in the principal markets as such pertains to the products described above or the product mix. However, if Sonol does not win large tenders in the future, as have been won in the past, such could have an effect on the Company's share in the direct marketing segment. Moreover, the purchase of BAZA by Paz and the privatization of BAZAN, could affect Granite's share in both the direct marketing and the fuelling station and commerce complexes segments (see Section 11.3.8 below). As part of Granite's business in the fuelling station and commerce complexes, Granite intends to act through Sonol to establish Public fuelling stations and additional convenience stores at fuelling stations in order to increase sales of Oil Distillates and consumer products respectively. Furthermore, Sonol intends to establish mini-malls around the fuelling stations, which will expand the range of services and products available to its customers.

The information given in this Section constitutes prospective information as defined in the Securities Law. It is based on the information known to the Granite management on December 312011; on subjective estimates and assessments made by the Granite management that take into account past experience, its intentions and plans on the Date of the Report and which might not come to fruition. At this stage, there can be no certainty that there will be no significant changes in the markets in which Granite operates and its range of products. Furthermore, there can be no certainty that the additional convenience stores and the mini-malls shall indeed be established and the scope of sales will, consequently, increase as stated above. It is possible that the aforementioned information will not come to fruition, if there shall be changes to Granite's plans and intentions as stated above, including due to competition, global oil products prices, entry into new fields, Granite's intentions in this matter and Granite's assessment of the commercial feasibility of those aforementioned matters, or due to the realization of any one of the risk factors listed in Section 11.80 below.

11.7. **Segmentation of revenues from products**

The following table provides information pertaining to the segmentation of revenues from the products in Sonol's direct marketing

segment whose revenues constitute 10% or more of the Azrieli Group's total revenues:

Product Type	2011		2010		2009	
	Revenues in NIS Thousands	Percentage of Company's Revenues	Revenues in NIS Thousands	Percentage of Company's Revenues	Revenues in NIS Thousands	Percentage of Company's Revenues
Diesel Oil	870,399	10.2%	536,163	7.2%	390,463	6.7%

The increase in the rate of revenues from diesel oil in the direct marketing business segment out of the Company's total revenues in 2011, compared with their rate in 2010, and in 2010 compared with their rate in 2009, resulted from an increase in the prices and in the quantities sold.

The following table reports the distribution of revenues from the products in Sonol's fuelling stations and commerce complexes segment whose revenues constitute 10% or more of the Azrieli Group's total revenues:

Product Type	2011		2010		2009	
	Revenues in NIS Thousands	Percentage of Company's Revenues	Revenues in NIS Thousands	Percentage of Company's Revenues	Revenues in NIS Thousands	Percentage of Company's Revenues
Gasoline	**1,870,590**	**21.9%**	1,552,546	20.9%	1,270,240	21.7%
Diesel Fuel	**898,888**	**10.5%**	749,324	10.1%	663,691	11.4%
Total	**2,769,478**	**32.4%**	2,301,870	31.0%	1,933,931	33.1%

The rate of revenues from gasoline and diesel oil in the fuelling and commerce complexes' segment out of the Company's total revenues in 2011 has not changed compared with the 2010 rate. During 2011, there was a decrease in the quantities of gasoline and diesel oil sold at the fuelling complexes, but an increase in the products' price level brought about an increase in the total revenues. The increase in the gasoline sales' rate in the Oil Distillates segment at the fuelling complexes out of the total revenues of the Company in 2010 compared to 2009 resulted from an increase in prices and in the gasoline quantities that were sold. The change in the rate of diesel oil sales is negligible.

The gross profit of this operating segment in 2011 was NIS 537,618 thousand compared with the amount of NIS 578,497 thousand in 2010. The gross profit due to the fuel sale operation decreased by approx. NIS 41 million, resulting from a decrease in the quantities sold and margins' erosion, *inter* alia, as a result of a decrease in the marketing margin in the last quarter (for details see Section 11.17.9). On the other hand, the gross profit from the convenience stores increased by approx. NIS 10 million. The gross profit in 2009 was NIS 577,285 thousand. In other words, the gross profit from this operating segment in 2010

remained almost unchanged compared to 2009. The gross profit in 2010 included an increase of approx. NIS 13 million due to the retail business at the fuelling complexes and approx. NIS 12 million of reduction in the gross profit from fuel sale business resulting mainly from erosion of the marketing margins due to the intensification of the competition in this segment during the first half of 2010.

11.8. Customers of the operating segments

In Sonol's direct marketing segment, the Granite Group supplies its products to a broad range of commercial and business customers; to airlines, transportation companies, agriculture, industry, institutional customers and distributors. In this segment, the agreements through which Sonol contracts with commercial and institutional bodies are for varying periods. Occasionally, after winning a tender, such agreements are for periods from one to five years.

In Sonol's fuelling and commerce complexes segment, the Granite Group supplies its products to a broad range of spontaneous, individual customers, to customers who own fleets of vehicles, purchasing fuels through automatic fuel pumps or using magnetic cards (**"AVR – Automatic Vehicle Recognition"**) and to members of various customer clubs at the fuelling stations of the Sonol Chain as well as to external operators of fuelling stations. By using AVR, the vehicle fleets' customers can purchase fuels and oils in a computerized and automatic manner, without cash payment (the charge is made in aggregate once a month). Vehicle fleets' customers mostly include business and institutional customers, who usually benefit from a discount in the fuels' purchase price (as a result of a negotiation or tender). Therefore, the average gross profit of the Granite Group from sales through AVR is lower than the average gross profit from sales to random customers. In this segment, agreements with the external owners or operators of fuelling stations are for varying periods and each year, a number of agreements end, while a number of new agreements are signed. Customers with fleets of vehicles with AVR installed have signed agreements with the Granite Group for varying periods and usually, for no less than three years.

In each of these operating segments, Sonol is not dependent upon a single customer or a limited number of customers, the loss of which would have a material effect on these operating segments. Furthermore, Sonol has no single customer in either of these segments, with revenues from that customer constituting 10% or more of Granite's total revenues in the year of the Report.

Segmentation of sales in the operating segments per customer types

The following is a table describing the segmentation of sales in Sonol's direct marketing segment in the years 2011, 2010 and 2009, according to customer types as well as their percentage out of the total revenues from this operating segment in this period:

	2011		2010		2009	
Customer type	**Sales (NIS in thousands)**	**Percentage of total revenues of the operating segment**	**Sales (NIS in thousands)**	**Sales (NIS in thousands)**	**Sales (NIS in thousands)**	**Percentage of total revenues of the operating segment**
Institutional, governmental , commercial and business customers	980,154	55%	801,400	56%	802,428	61%
Airlines	214,617	12%	295,200	21%	232,202	18%
Other,	587,769	33%	334,409	23%	452,362273,534	21%
Total	1,782,540	100%	1,431,009	100%	1,308,164	100%

The following is a table describing the distribution of sales in Sonol's fuelling and commerce complexes segment in the years 2011, 2010 and 2009, distributed according to customer types as well as their percentage out of the total revenues from this operating segment in this period:

	2011		2010		2009	
Customer type	**Sales (NIS in thousands)**	**Percentage of total revenues of the operating segment**	**Sales (NIS in thousands)**	**Percentage of total revenues of the operating segment**	**Sales (NIS in thousands)**	**Percentage of total revenues of the operating segment**
Station operators in the Sonol Chain	496,491	16%	352,515	14%	160,096	8%
Owners of fleets of vehicles fuelling with AVR installed	1,168,777	39%	947,516	37%	828,210	39%
Other, including private LPG customers	1,361,573	45%	1,225,608	49%	1,127,106	53%
Total	3,026,841	100%	2,525,639	100%	2,115,412	100%

11.9. **Marketing and distribution**

11.9.1. Storage and supply of Oil Distillates

Sonol buys the Oil Distillates for its operations mainly from BAZAN and from there, they are pumped through pipes

belonging to the government owned company Fuel Products Pipeline Ltd. to the various tank fields (only one of which is owned by the Granite Group – all the others are in third party ownership, among them BAZA and Delek) for storage and provision to Granite Group customers. Payments made by the Granite Group for the pumping of Oil Distillates are based on information given in accordance with the Regulation of Consumer Prices and Services Notice (Infrastructure Tariffs in the Petroleum Industry) (Updating of Prices for Infrastructure Services) 5763-2003 and they are calculated based on the quantities pumped and the distance pumped. Storage fees are calculated based on the quantities stored.

The Jet Fuel marketed to airline companies is pumped from BAZAN to Ben Gurion Airport where it is stored in facilities owned by the Paz Group. Aircraft fuelling is carried out through underground pipes by companies wholly or partially owned by Paz or Dor-Alon (it should be noted that Paz and Dor-Alon are Sonol's main competitors), but payments for aircraft fuelling services are determined based on information given in accordance with the Regulation of Consumer Prices and Services Notice (Prices for Aircraft Refueling Services at Ben Gurion Airport),5770-2010.

11.9.2. Supply of Oil Distillates

The supply of Oil Distillates to the direct marketing customers and fuelling stations in the Sonol Chain is executed mainly by transportation in tanker trucks, with the exception of a small number of commercial and institutional customers, who receive their oil products through direct pipelines between BAZAN and their plants.

11.9.3. Marketing of Oil Distillates

In Sonol's direct marketing segment, marketing activities are conducted through marketing personnel, branches and distributors, all working to identify customers and reach agreements with them.

As of the date of the Report, Sonol has five distributing branches across the country, which are fully owned thereby. Beginning in 2009, most of the distribution activities were transferred from the agencies to Sonol’s central operation through Sprint Transport.

Sales to large institutional customers, usually accomplished through national tenders, or purchases made on a nationwide scale, are executed directly by Sonol. Furthermore, in this market, Sonol markets fuels directly to Private Fuelling

Stations, which then supply those fuels for their own internal use.

In Sonol's fuelling and commerce complexes segment, the marketing of fuels is conducted through the Public fuelling stations operated by the Granite Group (as pertains to the types of fuelling stations in the Sonol Chain see Section 11.9.5 below). Sales of fuels to owners of fleets of vehicles are usually conducted in accordance with direct agreements between Sonol and the vehicle fleet owners, with discounts and advantageous credit conditions which change according to the size of the transaction and the risk exposure it entails to the Granite Group. Discounts granted to the owners of fleets of vehicles are granted by Sonol or its subsidiary companies and in some cases, the owner of a fuelling station bears some of the cost. To recruit more vehicle fleet customers, Sonol has also signed with external recruiters who are paid according to the scale of sales to customers they have brought in.

11.9.4. Marketing of oils

Oils are marketed to direct marketing customers through distributors, agents and the Company's marketing personnel. Sales to spontaneous fuelling station and commerce complex customers are made at the fuelling stations.

11.9.5. Fuelling stations in the Sonol Chain

As of the Date of the Report, there are 232 public fuelling stations throughout Israel in the Granite Group chain of public fuelling stations (the "**Sonol Chain**"). To the best of the Company's knowledge, based on the best of Granite Group's management knowledge, there is a total of some 1,050 public fuelling stations operating in Israel. Additionally, Sonol sells to approx. 100 Private Fuelling Stations; their revenues are credited to the direct marketing segment.

As of the Date of the Report, 191 fuelling stations, constituting 82% of the Sonol Chain, are operated by Sonol or by operators acting on Sonol's behalf and the remaining fuelling stations are operated by external operators, and revenues therefrom are not included in the Granite Group's revenues.

Some 18% of the Public fuelling stations in the Sonol Chain are owned by Sonol. Sonol has other rights of possession or just the rights to supply fuels to the other fuelling stations in the chain. The supply of fuels to Public fuelling stations is executed in accordance with an array of agreements deriving from the type of right held by Sonol in the fuelling station. Public fuelling stations in the Sonol Chain can be divided up into three main categories: (A) Fuelling stations owned or on a

primary lease from the Israel Lands Authority (including "key money" contracts) (some 18%), most of which belong to Sonol; (B) Sub-leased or rented fuelling stations (some 69%), in which most of the buildings were erected by Sonol and the fuelling station equipment belongs to Sonol; (C) Fuelling stations at which Sonol has no rights of possession whatsoever and Sonol has contracted with the owners of those fuelling station through short terms agreements for the supply of fuels (some 13%). It must be noted that the fuelling stations in category C also display Sonol signs and in most of them, the above ground equipment belongs to Sonol and is maintained by Sonol.

Under certain circumstances, Sonol transfers the right to operate fuelling stations in the chain to external operators and sometimes, transfers the right to operate owned or leased fuelling stations. As of the date of this Report, some 82% of the fuelling stations in the Sonol Chain are operated by or operated on behalf of Sonol. Some 18% of the fuelling stations in the Sonol Chain are not operated by Sonol, but Sonol has an agreement to supply to those fuelling stations. It must be emphasized that revenues from customers at the pump in the fuelling stations not operated by Sonol, are not included as part of Granite Group's revenues and instead, they belong to the operators of those stations.

11.9.6. Dependence upon a marketing channel

Sonol's activities in the fuelling and commerce complexes segment do not depend upon any single marketing body whatsoever. However, the array of Public fuelling stations in the Sonol Chain is the main marketing channel through which the Granite Group sells fuels to its customers.

There is absolute dependency upon FRP (Fuel Products Pipeline Ltd.) for the flow of oil products from the refineries to the various terminals. However, FRP is a regulated government corporation and it is obliged to provide that service at fixed rates. Furthermore, there is absolute dependency upon Paz Aviation Assets Ltd, for the storage and supply of Jet Fuel. However, Paz Aviation Assets Ltd. is a regulated company, obliged to provide these services at fixed rates.

11.10. **Competition**

The Sonol fuelling and commerce complexes segment is characterized by relatively high barriers to entry, because of the need for considerable investment in the erection of fuelling stations, the need to comply with regulatory requirements, long processes for the receipt of licenses and a scarcity of suitable land. Therefore, there are only a few significant competitors in this market, but the competition between them is fierce.

In contrast, in Sonol's direct marketing segment, the barriers to entry are lower. Therefore, a large number of bodies are active in this segment under conditions of very fierce competition which is characterized, *inter alia*, on sizeable discounts and long term credit.

According to the Ministry of Energy and Water Resources statistics, as of the Date of this Report, in the fuel market there are some 40 authorized companies registered, whereas the principal market share is dominated by 4 of them (including Sonol).

To the Company's belief, based on the best of Granite management's knowledge, as of the Date of this Report Sonol's share of the fuels, diesel oil and gasoline alone market (the segments in direct marketing and in the fuelling and commerce complexes) in Israel is approx. 17.5% of total sales (including sales of fuels to the Israel Electricity Corporation and the Palestinian Authority). These estimations are based on data published by the Fuel Administration in reference to total sales of fuel and there can be no certainty that the said estimations are correct and accurate.

In the Company's estimation, based on the best of Granite management's knowledge, the Company's main competitors in the direct marketing of fuels segment and in the fuelling stations and commerce complexes segment are: The Paz Group, Delek and Dor-Alon. Furthermore, in the fuelling station and commerce complexes segment, there is also regional competition with the companies: Ten Petroleum Company Ltd.; Fuel and Oil Agents Ltd., which operate Public fuelling stations and with independent fuelling station owners.

In reference to the implications of the purchase of BAZA by Paz and the privatization of BAZAN on Granite's competitive status, see Section 11.3.8 above.

The Granite Group is dealing with competition in the direct marketing segment by granting discounts to customers, because the principal parameters taken into account by customers when choosing a supplier are product cost, payment terms and quality of service.

In the fuelling station and commerce complexes segment, location and quality of service are the main parameters in the customer's choice of where to fuel. Accordingly, Sonol is investing both efforts and means in the expansion of the Public Fuelling Station chain and its national coverage. In addition, efforts are invested to improve service, build convenience stores, expand services available at fuelling stations and promote sales at fuelling stations.

11.11. **Production capacity**

Given that the Granite Group only manufactures oils and supplementary products, reference to production capacity is relevant only in oils. Oil production capacity is higher than the quantities of oil

actually sold by Sonol and it is currently operating at approx. 60% of the maximum production capacity during a single shift. However, should the need arise, it shall be possible to produce oils working more than one shift a day.

11.12. **Fixed assets and facilities**

11.12.1. Storage and dispensing facilities

Sonol owns manufacturing, storage and supply facilities in Haifa extending over an area of some 80 dunam that mainly includes a tank field with a capacity of some 25 million liters and some of the area (about 28 hectares) houses the oil factory and the central distribution warehouse for oils and products.

11.12.2. Public Fuelling Stations

As mentioned above, as of the date of this Report, the Sonol Chain consists of approx. 232 public fuelling stations. A standard fuelling station has a building on an area ranging from 40 sqm to 120 sqm, which includes a convenience store, office, storeroom, washrooms, and also roofed over pump islands, lanes for traffic movement, an area for re-fuelling the underground tanks and parking areas.

Most of the equipment installed at Public fuelling stations in the Sonol Chain is owned by Sonol, including operating equipment at fuelling stations not owned by the Chain.

In the coming years, the Granite Group intends to continue constructing new fuelling stations and investing resources in design, rebranding and upgrading existing fuelling stations, all subject to Granite's decisions, the competition in the market and Granite's situation. It should be noted that most of the stations in the chain underwent a process of re-branding and upgrade in recent years, whereby convenience stores in the Sogood chain were constructed in most of the stations.

This Section includes forward-looking information, which is not in the Granite Group's control. Such information is uncertain about the future. Granite's intentions as stated above depend, inter alia, on regulation, internal estimates and work programs. At the end of the day, it is possible that those intentions will not reach fruition and actual results will be materially different from the anticipated, due to many factors, including due to the competitive environment, the need to invest resources in other matters and market conditions as such shall be extant from time to time. Moreover, actual results might be different from the estimates detailed above, due to deviation in one of the factors taking in consideration in those estimations, or due to the realization of any of the risk factors

listed in Section 11.80 below.

For details concerning the fuelling stations mortgaged to Granite's bond holder's trustee, see Section 11.76.5 below.

11.12.3. Office building in Netanya

Granite management and Sonol headquarters operate from an office building in Netanya, with an area of approx. 3,000 sqm and additional areas for parking and storage. The building is owned by Sonol and it was established on land leased from the Israel Land Administration. Granite has additional fixed assets in the building, including computers, furniture and office equipment.

11.12.4. Equipment at the direct marketing segment customers

The Granite Group customarily loans equipment to direct marketing segment customers, for the purposes of supplying Oil Distillates and oils to those customers. Customers are required to return the loaned equipment when the contract terminates.

11.12.5. Vehicles

The Granite Group owns a fleet of tanker trucks, trucks and commercial vehicles as well as other vehicles leased through long term operational leasing agreements.

11.12.6. Computing Systems

Sonol has an ERP system used for current management. Furthermore, Sonol has developed a unique system for the management and control of fuelling station forecourts, which has been installed at the fuelling stations in the Sonol Chain.

11.13. **Raw Materials and Suppliers**

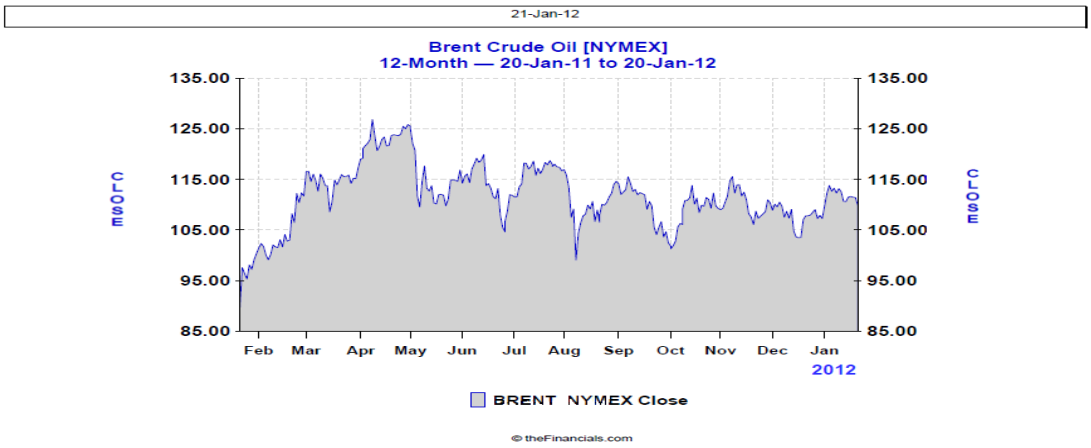
11.13.1. The principal raw materials used in the operating segments

The main raw material from which petroleum products are manufactured is crude oil. There are a number of different types of crude oil and they differ according to the source from which they were produced.

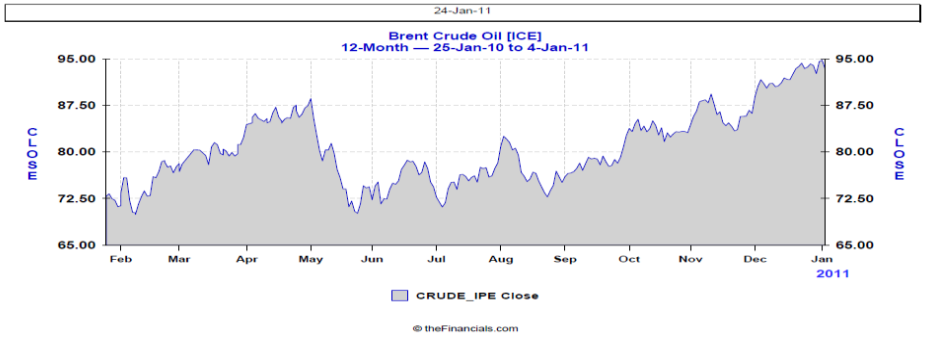
The following graph illustrates the fluctuations in crude oil prices in the years 2011, 2010 and 2009 (price for a barrel of “Brent” type oil in dollars)1:

[1] Oil prices as published in the http:/the financials.com website.

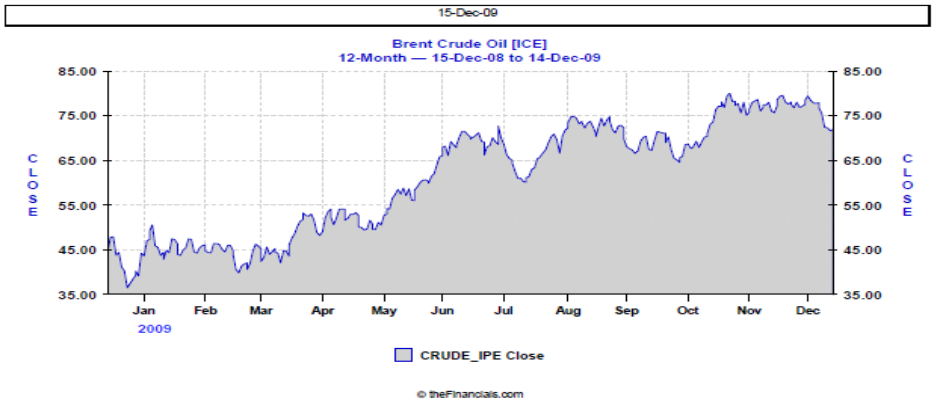
2011



2010



2009



After the splitting up of the refineries, the sale of BAZA to Paz and the privatization of BAZAN, Sonol now purchases Oil

Distillates from both refineries, but even so, BAZAN remains the main supplier to the Granite Group.

BAZAN is a monopoly in the field of petroleum product sales and therefore, it is obliged to sell its products to all the oil companies, including Sonol. For details of the removal of regulation of Oil Distillates prices and the transition to regulation through reporting, see Section 11.17.8 below.

Sonol also exploits opportunities to purchase petroleum products through independent imports, when such importing is cheaper than purchasing the same product at that time from the refineries and such is subject to operational limitations and Israeli standards.

During the years 2009 to 2011, Sonol purchased all its Oil Distillates from Israeli refineries, however in previous years Sonol imported Oil Distillates from time to time.

On December 20, 2011 the Antitrust Commissioner granted an exemption from approval as [not in Hebrew original – consider revising] a restrictive arrangement under Clause 14 of the Restrictive Trade Practices Law, 5748-1988 ("the Restrictive Trade Law"), whereby Sonol and Dor Alon are entitled to cooperate with respect to the import of Oil Distillates, including diesel oil and gasoline, including conducting joint negotiations and signing purchase agreements with Distillates' suppliers from abroad and conducting joint negotiations with carriers from abroad, to the extent required and on the conditions stipulated by the General Director, which compel, inter alia, Sonol and Dor Alon to allow interested fuel companies holding 5% or less of the total of public fuelling stations to join the venture and benefit from its terms. The aforesaid exemption from approval of a restrictive arrangement will remain in force for two years of the date of the General Director's decision.

The oils manufactured by Sonol are comprised of basic oils and additives. Most of the basic oil is manufactured by HBO (for further details, see Section 11.4.3 below) and Sonol imports the various additives from suppliers outside of Israel.

11.13.2. <u>Percentage of purchases by the Granite Group from principal suppliers</u>

In the years 2011, 2010 and 2009, the Granite Group purchased from BAZAN, approx. 91%, 89% and 75% respectively, of total petroleum products. During those years, approx. 9%, approx. 11% and approx. 25%, respectively, out of total petroleum products were purchased from BAZA. The decrease in the volume of purchases from BAZA in 2011 and 2010 results from the decrease in the consumption of Black Fuels by

consumers in the south of the country, as a result of a transition to natural gas. In recent years, Sonol has purchased the majority of its requirements for basic oil from HBO and most of the additives from suppliers outside of Israel.

11.13.3. Manner of engagement with principal suppliers

During 2009-2011, Sonol signed agreements with BAZAN, through which Sonol ordered annual quantities of Oil Distillates, which Sonol was obliged to purchase during those years, under specific commercial conditions. In accordance with those agreements, in reference to gasoline, a deviation of 10% was possible in the annual quantity purchased by Sonol. BAZAN makes no commitment to sell any additional quantities to Sonol but previous experience indicates that if BAZAN is in possession of the suitable stocks, BAZAN will sell additional quantities to Sonol under different commercial conditions. The agreement with BAZA is based on monthly orders.

The payment conditions for Granite's debts to BAZAN for the purchase of petroleum products are end-of-month + 15 days.

Purchases from the suppliers of other products purchased by Sonol are usually carried out generally undercurrent purchase orders.

11.13.4. Dependence on suppliers and the products for which there is dependence on suppliers

As is true for other fuel companies in Israel, Sonol is dependent on BAZAN as the major, central supplier of various petroleum products to the Granite Group and all the companies purchase most of their quantities of Oil Distillates from BAZAN.

In addition, the Granite Group is dependent on the Orpak Systems Company Ltd. for the supply of automatic vehicle identification and fuelling systems manufactured in accordance with the patent held by Sonol and Delek. If Sonol decides to replace those systems, such shall require a period of preparation and investment of high costs.

For details on Granite Group's dependence on marketing channels, see: Section 11.9.6 above.

11.14. **Working capital**

11.14.1. Policy for holding inventory of raw materials

Granite's oil facility holds an inventory of basic finished oils and additives in a quantity of approx. one month's production.

11.14.2. Policy for holding investment of finished goods

Due to the volatility in oil prices, Granite's policy is to hold in its storage plants an inventory of finished oil products for a period of a number of single days of supply, which facilitate ongoing operations..

According to the Arrangements in the State Economy Law, 5761-2001 and its regulations, the Granite Group is required to hold an emergency inventory of fuels in separate tanks at sites that have been determined. The inventory is guaranteed, in any event, by the State by determining compensation based on the exchange rate of the dollar at the time of sale. The costs and expenses related to the holding of the emergency inventory are covered by the State.

11.14.3. Policy of returning goods

Granite allows the return of goods only for the oil products in closed packages, and of products sold in conveniences stores and at fuelling station bays. These returns are not material.

11.14.4. Credit policy

A. Customer credit

In the direct marketing segment, Sonol provides its customers with credit ranging from 20 to 135 days, according to the type of product, the nature of the customer's characteristics, the purchase volume, the status of the securities and the type of engagement therewith.

In the fuelling and commerce complexes segment, most private customers pay Sonol in cash or through credit cards. Business customers in this segment, as well as Granite Group customers in the Oil Distillates direct marketing segment, receive credit from the Granite Group for periods ranging from 20 to 105 days, depending on the nature of the engagement with each customer.

The average period of credit to Sonol customers in 2009-2011 was 42 days, approx. 38 days and 41 days, respectively. The average amount of credit to customers in the aforesaid years amounted to approx. NIS1,037,026 thousand, approx. NIS 841,672 thousand and approx. NIS 810,148 thousand, respectively. The increase in credit balances is due to the increase in fuel prices and an increase in the quantities sold to customers of the direct marketing segment.

B. Suppliers credit

The main supplier of Sonol in these operating segments is ORL, which grants credit for a period of end-of-month + 15 days.

The excise component, levied within the price of the Oil Distillates which Sonol sells, is transferred thereby pursuant to the law to the Treasury after 10 days of supplying the fuels and before the funds are collected from the customer, which causes high financing costs to the Company, as the excise component in the price of Oil Distillates increases.

Other suppliers of Sonol grant it credit for a period of between current and 130 days. The average amount of credit from suppliers in 2011, 2010 and 2009 amounted to approx. NIS 495,523 thousand, approx. NIS 430,936 thousand and approx. NIS 364,756 thousand, respectively.

11.14.5. Corporation policy and its plans for dealing with working capital

As of December 31, 2011, Sonol has a negative working capital totalling approx. NIS 345,368 thousand, comprised of current assets in the amount of NIS 358,710 thousand, net of current liabilities of NIS 704,078 thousand. Until December 31, 2010,Sonol had negative working capital totalling approx. NIS 403,689 thousand, comprised of current assets of NIS 1,010,369 thousand, net of current liabilities of NIS 1,414,058 thousand. The decrease in the negative working capital is attributable, inter alia, to the conversion of a short-term credit in the sum of NIS 200 million to a long-term loan. Sonol examines, from time to time, the advisability of converting the short-term loans into long-term loans, in accordance with the changing market conditions.

11.15. **Investments**

11.15.1. Holdings of Granite Group in Pi-Glilot

Delek, Paz and the Granite Group hold 50% of the mixed company, “Pi-Glilot” (with the share of the Granite Group in Pi-Glilot being 13%). The balance of the equity of Pi-Glilot (50%) is held by the State.

As part of the privatization process of Pi-Glilot, Pi-Glilot sold in 2007 all of its business and properties as a going concern, with the exception of the land in Ramat Hasharon, which is due to pass to the direct ownership of the shareholders in Pi-Glilot relatively to their holdings. At the same time, upon signing the privatization agreement in 2005, the fuel companies and Pi-

Glilot signed their consent to the agreed order, which was approved by the Antitrust Tribunal, with regard to the cessation of all joint activity of the fuel companies at Pi-Glilot. As of the Date of the Report, Pi-Glilot holds land at Ramat Hasharon. The shareholders at Pi-Glilot have applied to the Government Corporations Authority and to the Antitrust Commissioner with a request to defer the liquidation of Pi-Glilot, in order to postpone the date of charging with the levies due upon liquidation until execution of the transfer of the said lands to the shareholders, in accordance with the privatization agreement. The shareholders of Pi-Glilot are negotiating with the State's authorities for the amendment of the privatization agreement and the agreed order. As of the date of the Report, documents stipulating a different agreement are yet to be signed and a proper application to the Restrictive Trade Practices Tribunal is yet to be filed.

11.15.2. Holdings of the Granite Group in HBO

In the years 2011 and 2010, Pi-Glilot did not distribute any dividends. The Granite Group has a 14% stake in HBO, which owns a facility for the production of basic oil. During 2010, some of the shareholders (including the Granite Group) sold their holdings in HBO, so that as of the Date of the Report, HBO is wholly owned by ORL. Regarding the capital gain generated for Granite from this sale, see Note 30 to the Financial Statements in Chapter C of this Report. In 2010, HBO paid a dividend totalling NIS 35 million, which was announced by HBO in 2009 (the share of the Granite Group in the said dividend was NIS 5 million and was recorded as revenues in 2009).

11.15.3. Income-Producing Properties and Surplus Properties

Except for properties used by Sonol for the current activity thereof, Sonol holds income-producing properties and surplus properties, which, in previous years, were included in other business segments of the Company. Upon the sale of most of the properties of Granite Group and due to the presentation of the business segments according to the Core Companies, the surplus properties of Sonol were included within the Sonol business segment.

The properties shall be described below:

The Property	The ownership rate	The property area in sqm	Value in the books as of December 31, 2011	Profits (losses) of valuation attributed to the property in 2011	Notes
Commercial building in Carmiel	100%	4,200	5,100	(66)	The area for rent (without parking) is 3,780 sqm out of which 2,584 sqm are leased, constituting occupancy of 84%.
Land attached to a fueling station in Be'er Sheba	100%	Approx. 17,000	5,537	-	Vacant Lot
Land at Pi-Glilot	100%	Approx. 6,400	17,491	3,396	Lot at the Pi-Glilot Complex in Ramat Hasharon which does not belong to the mixed company Pi Glilot
Land attached to a fueling station in Netanya (*)	100%	3,000	9,500	(1,315)	Vacant Lot

(*) Pledged in favor of the Company's bondholders, see Section 11.75.5 below.

11.16. **Environmental risks and ways of their management**

11.16.1. Main Legal Provisions pertaining to the Protection of the Environment

Sonol's business is subject to the provisions in legislation and regulation concerning environmental protection.

Following are the main legal provisions applicable to Sonol's various operating segments with respect to environmental protection. As specified in this section below, a breach of the environmental regulations may lead to third parties claims, such as: claims by the owners of property adjacent to facilities, customers, municipalities or organizations. In addition, violation of the law's provisions with respect to environmental

protection may lead to criminal sanctions or monetary sanctions.

Provisions referring to the fuelling stations

One of the obvious risks arising from the operation of a fuelling station is the contamination of the soil by fuels and oils, which could cause contamination of the soil and groundwater and health hazards due to exposure to toxic substances. To prevent those problems, standards have been determined for the establishment of fuelling stations.

Granite Group must comply with the various regulations and orders pertaining to environmental protection, inter alia, by dint of the Water Regulations (Prevention of Water Pollution) (Gasoline Stations), 5757-1997 (the "Water Regulations"). These standards and orders include a range of provisions and inter alia, provisions referring to prevention of soil pollution, the pollution of ground-water and air pollution.

To prevent pollution of the environment, Granite must comply with many requirements, the most important of which are listed below:

Maintenance of Cleanliness Law, 5754-1984 - This law imposes criminal liability on anyone disposing of waste, including fuels or dirt into the public domain. In accordance with the interpretation of this law by the Courts, public domain includes fuelling station land and areas adjacent to that land. Breach of the provisions to this law incurs a fine and the law grants the authority to oblige the polluting party to restore the situation to its previous condition, and if the polluting party fails to do so, the authorities may do it themselves and charge the polluting party with double payment of the incurred expenses.

The Hazardous Substances Law, 5753-1993 – Sonol's business segments involve handling hazardous substances. According to the law, the storage and supply facilities of these segments are required to obtain a toxic materials permit issued by the authorized inspector in the Ministry of Environmental Protection. For marketing and commerce, transportation and storage of fuels and for Sonol's supply facility in Haifa. As of the date hereof, Sonol holds the necessary toxic materials permits.

Environmental Protection Law (The Polluter Pays) (Means of Punishment) (Amendments to Legislation) 5768-2008

The Polluter Pays law that took effect on the July 29, 2008, strengthened the responsibility and punishment mechanisms in 13 environmental laws.

The Polluter Pays Law provides that if a person obtained, as a result of an environmental offense, any benefit or profit (including saved costs), that person may be fined in the sum of the benefit and/or profit, in addition to any other sanction. The Polluter Pays law also amended the Water Law, such that an offense thereunder was classified as strict liability while aggravating the penalty threshold. In addition, the law grants the Ministry of Environmental Protection the authority to impose financial fines when an offense is committed under the Law for Preventing Sea Pollution from Land-Based Sources, 5748-1988 and/or the Hazardous Substances Law.

The Water Law

The Water Law, 5719-1959 imposes responsibility on anyone causing or likely to cause pollution of water sources and allows the State authorities to impose fines on anyone breaching their provisions and to instruct anyone committing a breach to restore the situation to its previous state.

The Water Regulations (Preventing Water Pollution) (Fuel Stations), 5757-1997

The Water Regulations determine different provisions obliging fuelling station operators to take preventative measures in reference to a gamut of issues, both during fuelling station construction and during their operation. Furthermore, the provisions to the Water Law oblige a fuelling station operator to conduct periodic testing of sealing for the tanks and pipes. The provisions also determine the manner in which to deal with the reporting of and the treatment of a polluted site. In the event of a discovery of a leak, Sonol seeks approval from the Ministry of Environmental Protection for the appropriate action to be taken.

In the Company’s estimation, based on the best of Granite management’s knowledge and as of the date of this Report, the cost of conducting the aforementioned testing and the cost of adapting older fuelling stations to comply with the new provisions is not significant for Granit. The water regulations provide that the long-existing stations are to be adapted to some of the Regulations' provisions which apply to new stations. As of the date of the Report, most of Sonol's stations comply with the requirements of the water regulations to install the aforesaid

protective measures, subsequently to Sonol's performance of the regulations' requirements in a several-year process starting on the date when the regulations had entered into effect. In the remaining stations, which are yet to be completely adapted to the regulations, Sonol is acting for the completion of the required protective measures. It shall be noted that gaps have been discovered in the performance of impermeability tests in stations. As the repair of flaws in the stations that had been checked until 2010 has yet to be completed, Sonol acted during 2011, and plans to continue the activity for closing the gaps in 2012. The Company estimates, based on Granite's management's best knowledge, that the cost of completing the adjustment of the protective measures to the regulations is not substantial to the Company.

It should be noted that in December 2010, the Ministry of Environmental Protection filed an indictment against Sonol, and against persons who served as officers thereof, for a number of violations of such water regulations: non-performance of impermeability tests; non-delivery of results of impermeability tests; failure to report a fuel leak, including in aggravated circumstances; failure to repair an impermeable facility, including in aggravated circumstances; and failure to install a piezometer. These are violations that alleged to have been committed between 2000 and 2004. In October 2011 the parties filed preliminary arguments with the court. In the Company's estimation, at this preliminary stage, it is impossible to assess Granite’s level of exposure in the event that Sonol is convicted. In addition, following such indictment, in December 2010, a motion for class certification was filed against Sonol and other fuel companies for non-performance of impermeability tests on the fuel tanks and pipelines, failure to report leakage and/or failure to rehabilitate contamination, which according to the applicants caused contamination of groundwater.

<u>The Water Regulations (Prevention of Water Contamination) (Fuel lines), 5766-2006</u>

The Regulations require, *inter alia*, that a fuel line business license holder or a party under whose care, supervision or management a fuel line or part thereof operates, perform initial intactness and impermeability tests prior to operating a gas line, ongoing intactness and impermeability tests of the fuel line, and ongoing maintenance activities in order to properly preserve its intactness, while the line shall only be operated in the event that such tests prove that the fuel line is impermeable and intact. In the event that the operator learns of a leak to the soil of a volume exceeding one cubic meter, or a leak to water sources in a fuel concentration exceeding what is stated in any law, or

that the fuel line is not sealed – the operator must report this to the Commissioner, as defined in such Regulations, to the Water Commissioner, to the Health Authority, and to the local authority, in whose jurisdiction the leak occurred or a company providing water and sewer services, as defined in the Water and Sewer Corporations Law, 5761-2001, respectively. In the event that the fuel line is not impermeable, appropriate actions must be taken to seal it, as described in such Regulations, and it should be reported to the above-mentioned authorities. The year of the Report saw five events of leak, as stated, which are not substantial, for which Sonol delivered a report as required. In addition, the Regulations require the operator to be in possession of a map, pursuant to the requirements specified in the Regulations, marking the location of the fuel line and the water sources close to the line or protective areas of water sources, as defined in the Nation's Health Regulations (Sanitary Conditions for Drilling Potable Water), 5755-1995, and to provide it to the Commissioner, as defined in the Regulations, and to the Water Commissioner, if required. These Regulations are relevant to Sonol in the segment leading the fuel from the fuel line corridor, which belongs to ORL into Sonol's facilities in Haifa.

<u>The Water Rules (Treatment of Water Pollution from Fuel), 5770-2010</u>

The purpose of these Rules is to protect the quality of water sources in Israel from water pollution caused by fuel leaks, which may harm the overall usages of water due to the worsening of the quality thereof, to do all that is required in order to stop water pollution, reinstate the situation to the prior condition thereof and prevent the repetition of the water pollution. The Rules impose a duty on anyone under whose ownership, supervision, management and possession is a water pollution cause, provided that a water source was polluted due to fuel leakage, the duty to act for stopping the pollution and reinstating the situation to its prior condition, as well as a duty to report the leakage. Insofar as the commissioner of the water quality shall determine that a water source had been polluted, the Rules impose a duty to operate according to the provisions of the Rules, until the completion of the plan for stopping the pollution, removal from the water source and prevention of repetition thereof, as specified in the Rules.

Treating soil and water contamination

Sonol has a number of older fuelling stations, which are more likely to suffer from leaks. Those fuelling stations need heightened awareness of the need to find pollution and therefore, Sonol is exposed to higher treatment costs for the older fuelling stations. In October 2007, Sonol and the Ministry

of Environmental Protection agreed on a polluted soil rehabilitation program for fuelling stations constructed before January 1, 1998. Rehabilitation is carried out in accordance with a regulated process agreed by the two parties and spread out over a period of 6 years, beginning in 2008.

As of the Date of the Report, in coordination with the Ministry of Environmental Protection and the Water Authority, Sonol is dealing with approx. 90 fuelling stations, where ground-water and/or soil pollution has been discovered. The overall costs for tending to the fuelling stations in 2011 amounted to approx. NIS 6,200 thousand (compared to an amount of approx. NIS 3,500 thousand in 2010 and an amount of approx. NIS 2,000 thousand in 2009). Sonol continues to tend to the rehabilitation of said stations in coordination with the Ministry of Environmental Protection and the Water Authority. Sonol intends to begin tending to 14 additional stations in the course of 2012. In the Company's opinion, based on the best knowledge available to Granite management, in view of the program's progress, due to the intensity of the said activities at such fuelling stations, and due to the fact that additional stations where a contamination is found may be discovered, there will be a rise in the scope of investments required to deal with the fuelling stations. Accordingly, the estimate of costs and investments in the environment in these operating segments (is expected to amount, in the year 2012 and the years that will follow, to a total of approx. NIS 15 million, as stated.

That stated above in reference to anticipated costs and investments for the rehabilitation of fuelling stations is prospective information as defined in the Securities Law, and is based on the best of Granite management's knowledge as of the Date of this Report and its experience in this field. It is possible that Granite shall be required to invest more than the stated sums because it might be found that pollution is discovered in additional fuelling stations, or because additional demands may be made by the Ministry of Environmental Protection and/or the Water Authority.

The vast majority of Sonol fuelling stations comply with the standards described above. In reference to the other fuelling stations, Sonol is acting, investing resources and implementing a range of means for compliance with the standards as aforementioned.

Sonol has no insurance policy covering liability which the Group could incur for ongoing pollution of the environment as described above (as differentiated from accidental environmental pollution). The Granite Group has no way to assess the exposure, to the extent that it exists, to liability imposed on the Group due to ongoing pollution of the

environment, even though such exposure could be significant. As for the Clean Air Law, 5768-2008, see Section 11.17.15 below.

Preventing air pollution

Sonol is in the final phase (Stage I) of the process through which vapor recovery systems are installed at all its Public fuelling stations, as required for a business license. The vapor recovery system prevents the emission of gasoline fumes from the underground storage tanks when they are refilled by tanker trucks. It should be noted that the vast majority of the stations are equipped with a vapor recovery system, except for a very limited number of fuelling stations. According to Granite's estimate, the financial investment involved in the installation of a vapor recovery system (stage I) in these stations is not significant.

In accordance with the instructions published by the Ministry of Environmental Protection in March 2006, all fuelling stations at a distance of less than 40 meters from residential areas must install pumps, which draw in the vapor emitted from vehicle fuel tanks during fuelling and return that vapor to the fuelling station tanks (Stage II).

This requirement was added as another condition for the business license for fuelling stations.

It should be noted that in the past, the three fuel companies: Paz, Delek and Sonol were required to install a vapor recovery device in their facilities at Shemen Beach in Haifa. Said fuel companies did not meet the timetable that was fixed. Consequently, a fine was imposed on Sonol in an immaterial amount, pursuant to the judgment of the Haifa Magistrates Court of October 18, 2009. In addition, in the framework of such judgment of the Haifa Magistrates Court, the Court ordered each of the above-mentioned companies to install Stage II fuel vapor recovery systems, which, with respect to Sonol, refers to 35 fueling stations owned thereby, within 5 years.

In May 2010, the Minister of Environmental Protection announced new guidelines (whose provisions were incorporated into the business licenses of the fueling stations), according to which all of the fueling stations in Israel were required to install Stage II fuel vapor recovery systems, and not only fueling stations whose distance from residential areas is less than 40 meters as aforesaid. The timetable fixed for installation of these systems, as updated in January 2012, is as follows: in fueling stations, located at a distance of less than 40 meters from a residential area or from sensitive uses – until March 31, 2012, in fuelling stations located at a distance of 40

to 80 meters from a residential area and from other sensitive uses – until December 31, 2013, and in all of the remaining stations – until December 31, 2015. In 2011 Sonol was required to install systems, as aforesaid in 37 stations. Until the date of the report, Sonol installed the systems in 8 stations, and performed infrastructure work in 25 more stations. The delay derived from the fact that most of the dispensers in the possession of the Company did not have a technological solution which complied with the standards defined by the Ministry for Protection of the Environment. During the report year, a solution was developed, which matured into serial production towards the end of the year, was installed and approved in two fueling stations and these days Sonol is completing the installation according to the plan. As of the date of the report and according to the criteria set forth in the directive of the Minister for Protection of the Environment, the Sonol Chain still has a total of 145 stations in which Stage II fuel vapor recovery systems are required to be installed, as per the following: one fuelling station in which the system has to be installed by the end of March 2012, stations in which the said fuel vapor recovery systems are required to be installed by the end of 2013, and 111 stations in which installation must take place by the end of 2015.

To the Company's belief, based on the best of Sonol management's knowledge, the financial investment required for the installation of the vapor recovery systems (Stage I) at stations and for the implementation of the instructions of the Minister for Environmental Protection as amounts to a total of approx. NIS 35 million, approx. 7 million of which are expected in 2012.

That stated above is prospective information as defined in the Securities Law, which is uncertain and based on the Company's estimates, based on the estimates given by Granite's advisors, based on the information extant as of the Date of this Report. Actual costs might be significantly different from the Company's estimates as stated above for a variety of reasons, including: Regulation on this issue or the adoption of different methods for dealing with the prevention of air pollution.

Regulations pertaining to tanker trucks and facilities

Ministry of Transport regulations determine an obligation to install bottom fuelling systems in specific types of tanks. In coordination with the Ministry of Transport, bottom fuelling systems have been installed in those tanks for which they are required.

Regulations pertaining to facilities

Sonol has installed a vapor return system at the Haifa fuelling facility. The purpose of this system is to draw in fuel fumes emitted into the air when tanker trucks are filled with fuel. The system began operating during April 2007. Following the non-compliance of Sonol and other fuel companies with the timetable fixed by the Ministry for Environmental Protection for the installation of the vapor recovery system at the companies' facilities in Haifa, a proceeding as specified in this section was opened against Sonol. For further details concerning the number of fuelling stations at which Sonol installed vapor recovery systems, the fuelling stations at which Sonol is expected to install such systems and the related costs, see this section above.

In late-2008, additional conditions were received by Sonol for the business license for the facilities, which require Sonol to conduct a survey of fugitive (non-stack) emissions from its facilities, with the aim of preventing air pollution and neutralizing air pollution in accordance with Ministry of Environmental Protection guidelines through a regulated program approved by the Ministry. Such conditions also require the methodical performance of tanks' testing at the tank farm in the Haifa facilities as per Standards API-653 and the performance of reconditioning as necessary in accordance with the Standards. As of the Date of this Report, Sonol is in compliance with the timetables set in Ministry of Environmental Protection guidelines.

Business Licensing Regulations (Hazardous Plants), 5753-1993

Pursuant to said regulations, a business which stores, sells, processes or creates hazardous substances (Oil Distillates are included in this definition) requires a special license as a dangerous plant, and it must meet the safety provisions provided in the regulations. Up to the Date of this Report, the Company is not aware of a material breach of the provisions of the regulations.

11.16.2. Environmental Bills

For details see Section 1.17.6 below.

"The Green Taxation" Reform

The purpose of the Green Taxation Reform, is to create economic incentives for the reduction of the environmental pollution of automobiles, and promoting the purchase of automobiles with smaller engines which pollute less. The reform includes a number of changes in the area of taxation of

the automotive industry, including imposing a purchase tax on new automobiles that were registered for the first time on January 1, 2010, in accordance with the pollution level of the automobile, while 15 pollution levels have been established. According to this method, purchase tax benefits are granted according to the degree of polluting emissions of the automobile and the "green grade" of each model. It should be noted that this method has been implemented since 2009. To the Company's belief, based on Granite's management, the effect of the green taxation reform on the Company's operations and its results, in the short term, is expected to be insignificant. The Company is unable to estimate the effect of the green taxation reform on its operations and results in the long term. This Section includes forward-looking information that is not in the Company's control, and is uncertain. The Company's estimates that are included in this Section might not be realized, and the actual rights might be different from the aforesaid, if any of the underlying assumptions that were used by the Company in its stated estimations change, or if a change occurs in any of the risk factors detailed in Section 11.80 below.

11.16.3. Environmental risks with material effect on Granite

Sonol is exposed to various risks resulting from damage to the environment as a result of Sonol's business as specified below:

Criminal proceedings – The Granite Group is exposed to criminal proceedings for environmental violations against it and against former officers thereof, *inter alia*, as described above. Conviction for environmental violations means a criminal record, heavy penalties and financial sanctions, especially in light of the trend in environmental legislation of toughening the criminal punishment standard. It should be noted that the Polluter Pays Law amended a considerable part of the environmental protection laws (e.g.: the Water Law, the Prevention of Air Pollution from Land Sources Law and the Hazardous Substances Law) in a manner that the criminal punishment sections were made stricter, and administrative authority was granted to impose financial sanctions. In addition, it should be noted that the Clean Air Law and the Water Law impose strict responsibility on those responsible for the pollution, and the Clean Air Law also imposes criminal liability on directors.

Civil proceedings – Sonol is exposed to civil tort or other claims for damage to the environment (if any), e.g.: claims of property owners bordering on the facilities, authorities or organizations, and even class actions.

Closing of sites and cancellation of business licenses –The Granite Group is exposed to the risk that a judicial or administrative order will be issued for closure of the site where an environmental pollution is found (if any), e.g. pursuant to the provisions of the Clean Air Law or the Water Law. In addition, the Group is exposed to the risk of loss, suspension or conditioning on specific terms of its business license in a station where environmental pollution is found.

Employee safety – Since the work of the Granite Group's employees entails dealing with dangerous and flammable substances, there is a risk of damage to the safety of the Group's employees.

In addition, the Granite Group might be exposed in future to additional environmental risks which might occur as a result of ongoing events during the course of the Group's ordinary business, which it is not able to predict as of the Date of this Report.

11.16.4. Material consequences of the law on the Granite Group

To the Company's belief, based on Granite's management, the capital investments of Sonol in the year 2012 are expected to amount to approx. NIS 20 million, similarly to the amount in 2011, *inter alia*, as a result of the implications of the laws relating to environmental protection therefor. Nonetheless, to the Company's belief, the regulation and laws regarding the quality of the environment are not expected to influence the competitive status of the Granite Group, due to the fact that the provisions apply to all of the fuel companies.

The Company's said estimations are forward-looking information, as defined in the Securities Law, which is uncertain, and based on subjective estimations of the Company, as of the Date of the Report. The actual results might be materially different from the Company's stated estimations, *inter alia*¸ in light of the existing uncertainty regarding the future demands of the Ministry of Environmental Protection or other regulatory demands that are not in the Company's control.

11.16.5. Events and matters which caused or are expected to cause damage to the environment

To the Company's belief, based on Granite's management, there is no event or matter relating Sonol's operations, which caused or is expected to cause damage to the environment and would materially affect the Company. The Company's said estimation is a matter of forward-looking information, as defined in the Securities Law, which is uncertain, and based on

internal estimates of Granite's experts, based on the existing information as of the Date of the Report. Similarly, in the framework of Sonol's ordinary course of business, events may arise which could cause damage to the environment, which the Company is not able to predict in advance, e.g.: leakage of fuels from tanks in fueling stations, turning over of tanks containing fuels or damage to the environment as a result of another accident in the framework of transporting of hazardous substances, combustion of fuels which could cause a fire and similar fire risks, air pollution in fueling stating and the Company's facilities, etc.

11.16.6. Material legal or administrative proceedings relating to the environment

Criminal proceedings relating to the environment –In the past, the Ministry of Environmental Protection conducted investigations against Sonol for a small number of incidents of failure to connect the Stage I vapor recovery systems. Similarly, see Section 11.16.1 above, regarding the indictment filed by the Ministry of Environmental Protection against Sonol in December, 2010.

Civil proceedings relating to the environment – In December 2010, a Motion for Class Certification was filed against Sonol and other fuel companies regarding non-performance of impermeability tests on the fuel tanks and pipelines, failure to report leakage and/or failure to rehabilitate contamination, which caused contamination of groundwater, which was following a number of indictments that were filed against the fuel companies (see Section 11.16.1 above).

11.16.7. Sonol's policy for environmental risk management

Sonol takes many actions and invests considerable resources in order to prevent damage to the environment and prevent environmental risks. In this framework Sonol operates continuously to maintain quality systems, conduct various tests, increase the safety amongst the its employees, its customers, suppliers and third parties and to avoid accidents, *inter alia*, by enforcement of procedures, investment in equipment and devises to prevent soil and air contamination, and for safety and fire protection needs, in performing training, lectures and more.

It should be noted that Sonol acts according to a work plan agreed to by the Ministry of Environmental Protection, which was approved at the end of 2007, for the rehabilitation of contaminated soil in the fueling stations. Pursuant thereto, Sonol performs gas and soil surveys in each of the fueling stations that was erected prior to 1998, over a period of 6 years, in accordance with the procedures of the Ministry of

Environmental Protection, and in coordination therewith. Upon conclusion of the relevant surveys, Sonol performs a detailed soil rehabilitation plan, insofar as is required, which is submitted to the Ministry of Environmental Protection, for the purpose of receiving its opinion. The rehabilitation work apply to approx. 105 stations, which are dealt with. It should be noted that gaps have been discovered in the compliance with such plan. In this context, in early 2011, a meeting between Sonol and the Minister of Environmental Protection took place, where the current situation and a plan for the future were presented. In the year of the Report, Sonol expedited the plan's execution in order to close the gaps. To the Company's belief, based on the Granite company's management and based on Sonol's reports, most of the gaps have been reduced. In addition, Sonol has prepared an internal enforcement plan regarding environmental subjects, which includes coping with the environmental risks it is exposed to. In the framework of constructing such plan, Sonol is examining, *inter alia*, the application of the laws regarding the quality of the environment, and the application of the relevant safety and environmental procedures. Furthermore, during the year of the Report, Sonol was ISO 14001certified a standard which deals with ensuring environmental management and maximal protection of the quality of the environment. The enforcement plan focuses on Sonol's following activities: (1) the activity of transporting the fuels via Sprint Transportation; (2) the activity of retail sale of fuel by fueling stations operated by Sprint Motors; and (3) operation activities in the Company's facilities in Haifa. Additionally, a working plan was prepared for 2012, in order to close the gaps in accordance with each of the said three activities. It should be noted that the subject of environmental protection (including the aforesaid plans) is the responsibility of and supervised by Sonol's Chief Operations and Engineering Officer.

11.16.8. Amounts that were awarded regarding legal proceedings and other environmental costs

No proceedings as stated were finalized in the year of the Report.

Exposures regarding pending legal proceedings relating to the environment:

Criminal proceedings – At this stage, it is not possible to estimate the scope of Granite's exposure for the said proceeding in Section 11.16.1 above.

Civil proceedings - The amount of the claim in the proceeding of January 2011 stated in Section 11.16.1 above is estimated by the Plaintiffs in the total sum of NIS 200 million. Based on

Sonol's legal counselor's assessment, the Company estimates that prospects of certification of the aforesaid claim as a class action are lower than 50%. See also Note 36.c.5 to the financial statements in Chapter C of this Report.

It should be noted that no provision was made for such proceedings in Granite's financial statements for the year of the Report.

Environmental costs borne by Sonol – The environmental costs borne by Sonol in the year 2011 are in the amount of approx. NIS 19,100 thousand, out of which the amount of NIS 15,700 thousand was spent by Sonol for the purpose of preventing or reducing damages to the environment, and the amount of approx. NIS3,400 thousand was spent by Sonol for repairing damages caused to the environment. In 2010, Sonol spent a total of approx. NIS 8,145 thousand, of which an amount of approx. NIS 6,445 thousand was spent for prevention or reduction of damages to the environment and an amount of approx. NIS 1,700 thousand was spent for repairing damages caused to the environment.

Projected environmental costs – To the Company's belief, based on the information held by it at the Date of this Report, as was provided to it by Granite's management, the expected substantial environmental costs to Sonol in 2012 amount to approx. NIS 23,400 thousand. It should be noted that Sonol is expected to spend an amount of approx. NIS 20,000 thousand out of said amounts for the purpose of preventing or reducing damages to the environment, whereas the balance of those amounts is expected to be spent by Sonol for repairing damages caused to the environment and the rehabilitation thereof.

To the Company's belief, based on the information held by it at the Date of this Report, as was provided to it by Granite's management, the expected costs for the subject of environmental protection in each of the years following 2012 will be similar to the expected expenses for 2012, which is subject to the regulation that will apply at that time, and the agreements the Granite Group will reach with the Ministry of Environmental Protection. Nonetheless, it is clarified that the expected costs for the years after 2012 could change in accordance with the expenses actually spent in 2012, such that it is likely that expenses that will not be spent in 2012, if any, will be spent in the years thereafter.

This Section includes forward-looking information, as defined in the Securities Law, regarding the Company's estimations regarding the environmental risks and their consequences, and regarding costs, expenses and expected investments regarding the quality of the environment. The information, as stated, is

uncertain and based on information existing in the Company as of the Date of the Report, based on information that was provided to it by Granite's management, and including the subjective estimates and intentions of the Company as of the Date of the Report. The actual results and costs might be materially different from the Company's estimations, as stated, *inter alia*, in light of the existing uncertainty regarding future demands of the Ministry of Environmental Protection or other regulatory demands that the Company did not expect, if one or more of the underlying assumptions that were used by the Company in its estimations change, or if one or more of the risk factors stated in Section 11.81 below exist.

11.17. **Limitations and regulation of the corporation's business**

11.17.1. Operating segments subject to specific laws

The business of the Granite Group in these operating segments is subject to laws, regulations and orders pertaining to, *inter alia*, price control, determining standards of quality, safety, security, storage, packaging, labeling and identifying products, transport, proper business management and environmental protection. Following herein below is a review of the principal legislation.

11.17.2. Fuel Industry (Prohibition on Selling Fuel to Certain Fuelling Stations) Law, 5765-2005

As per this law, it is prohibited to sell fuel to a fuelling station, unless it is included in the list of stations managed by the Fuel Administration. Any fuelling station, which at some time had been given a construction permit, or at some time during the five years preceding the date of the application had been granted a business license, may be included in this list. As of the date of the Report, all of the public fuelling stations of the Sonol Chain are on the said list. A person selling or supplying fuel to a station which is not included in the list is committing a criminal offence and is subject to imprisonment or fine. The said law's objective is to cause the shut down of pirate fuelling stations by cutting-off their supply lines. It should be noted that the law does not apply to internal fuelling stations. To the Company's best knowledge, based on Granite's management's best knowledge, in view of the enforcement actions which have been taken, the operation of the pirate stations has been reduced.

11.17.3. Fuel Industry Bill, 5771-2011 (in this Section: the "**Bill**")

On January 9, 2007, the Ministry of Water and Energy Resources published the Bill, which was updated on January 23, 2011. It is aimed at arranging activity in the fuel industry

while determining a licensing regime in the fuel industry and appropriate regulation. The proposed control and regulation will including the entire chain of activities in the fuel industry, *inter alia*, to ensure the regular, consistent and reliable supply of fuel and LPG; to ensure a level of good service in all segments of the fuel industry; to safeguard competition, and to promote and create conditions of competition; and to ensure supply during emergencies and look after public welfare.

The principal points of the Bill concern the stipulation of the continuation of marketing and importing Oil Distillates, *inter alia*, by the Granite Group, following the law's entry into effect, on obtaining suitable licenses pursuant thereto. The Bill further determines restrictions regarding cross holdings in two refineries or cross holdings in a refinery and corporation that markets Oil Distillates or infrastructure services.

To the Report Publication Date, the Bill has not yet been passed.

11.17.4. Vehicle Operation (Engines and Fuel) Law, 5721-1960

Over the years orders were published by virtue of the aforesaid law, which determine that engine-powered vehicles may be operated solely with gasoline and diesel fuel that meet the criteria of the Israel Standards Institute stated in the same standards.

According to Amendment No. 4 to the law that entered into effect on April 10, 2008, there is a duty to perform periodic inspections of the suitability of the product. The law determines severe penalties to be imposed in respect to oil products that do not meet the standard, including orders for closure, fines and publicity. Instructions of the Amendment came into force on October 10, 2008.

According to the Vehicle Operation (Engines and Fuel) Distributing Fuel in Tankers Order, 5768-2007, the Minister of Energy and Water Resources directed that each of the fuel companies is to undertake all reasonable means in order to ensure that each fuel product it supplies to a fuelling station complies with the criteria of standards and the criteria of the Vehicle Operations Law. Furthermore, the fuel company is required to make certain that each fuel product shall be distributed from a tank in a registered distribution installation and that the tank shall have a certificate attesting that the fuel in the tank fulfills the criteria. In addition, the order requires the installation of an electronic stamp on the tankers that transport fuel to fuelling stations within the period of time set forth in the law.

11.17.5. Fuel Industry Promotion of Competition Law, 5754-1994

The Fuel Industry Promotion of Competition Law, 5754-1994 determines restrictions on the matter of a fuel company's agreement to set up a fuelling station, in order to promote competition within the fuel industry. Below are the principal points of the law:

A fuel company shall not enter into an agreement to set up a fuelling station or an exclusive agreement to operate a fuelling station, if, within the distances specified herein below from the place where the fuelling station subject of the agreement is situated or shall be set up, another fuelling station is situated, wherein fuel of the same fuel company is sold: a fuelling station on an urban road – 1 km; a fuelling station on another road – 10 km that are measured along the length of the roads. The aforesaid shall apply, *mutatis mutandis*, as well to the operator of a fuelling station. This provision has been extended for a period of an additional 10 years, commencing in July 2008. An exclusivity agreement on this matter is an agreement between the fuel company and an operator of a fuelling station, which grants the fuel company exclusivity regarding the sale of fuel or the supply thereof to fuelling stations, or the right to sell or supply it with more than three quarters of all the fuel sold at the station, provided that the fuelling station is not located on land owned by the fuel company or leased by the fuel company from the Israel Lands Administration or by an individual who is not the operator of the fuelling station. The aforesaid distance restrictions shall not apply to the renewal of an agreement for exclusivity between a fuel company and fuelling station operator who prior to the application of the aforesaid law were connected in an agreement for the sale of fuel.

According to this law, the officer in charge is authorized to approve the establishment of fuelling stations at more proximate distances than the aforesaid, and after persuaded that the matter will not significantly restrict competition in the same area.

In addition, the law, as aforesaid, determines that, during the years 1998 to 2000 (inclusive), the Israel Lands Administration shall market 200 lots to set up fuelling stations. Part of these lots, as aforesaid, shall be allocated to disabled ex-servicemen of the IDF in accordance with an arrangement for the occupational rehabilitation of disabled ex-servicemen of the IDF, as adopted in a government decision. To the best of the Company's management's knowledge, the Israel Lands Administration has failed to fulfill this provision. It shall be stated that the Fuel Industry Bill proposes to cancel the

provisions pertaining to the allotment of plots of land to IDF disabled veterans.

11.17.6. Fuel Industry Promotion of Competition Law, (Amendment 2) – 5768-2007 (the "**Amendment No. 2 of the Promotion of Competition Law**")

Amendment No. 2 of the Promotion of Competition Law, concerns the duty to display prices at fuelling stations. The law determines the rules for the advertisement of gas prices sold at the stations, the location of the sign, the form of the advertisement, the contents of the advertisement, etc. The law entered into effect on December 4, 2008.

A. Fuel Industry Law (Promotion of Competition) (Amendment Number 4 – Automatic Refueling Installation), 5770-2010 – On July 22, 2010, the Knesset passed Amendment No. 4 of the Promotion of Competition Law, pertaining to the imposition on fuel companies of the obligation to install a general automatic fuelling installation system, enabling fuelling with all of the fuel companies, whereby fuelling can be done at any company with which the customer has signed an engagement agreement. In this form, the customer can fuel at any of the companies, without having to replace the fuelling installation in his vehicle.

B. The Fuel Sector (Promotion of Competition)(Rules regarding general automatic fueling devices) Law, 5771-2011 – following Amendment number 4 of the Fuel Sector Law, described above, and for the purpose of implementation thereof, Regulations were published in the official gazette on October 23, 2011 which will gradually take effect, after the approval of a standard or the choice of a specification for general automatic fueling devices, as specified in the Regulations. Within the framework of the Regulations, rules were set forth, that prohibit the fuel companies from selling fuel through an automatic fueling device which is not general. Also, the fuel companies, may not refuse, an unreasonable refusal, to engage with a customer in an agreement for the purchase of fuel through a general automatic fueling device. The aforesaid Amendment of the Law, as well as the regulations thereunder, may cause Granite a significant financial expense, *inter alia*, from the conversion of its fuelling installations to general fuelling installations, computation adjustments in the fuelling stations, and from the effect of the amendment on market competition, the nature of

which is currently difficult to estimate. At this stage Granite is unable to quantify the effects that the aforesaid amendment will have on its business results (if and insofar as there will be any). The above information with respect to the costs that Granite may incur, as aforesaid, is forward looking and there is no certainty with respect to the occurrence thereof. The results in actual fact may be different from the aforesaid.

C. An Interoffice Committee for the Promotion of Competition - According to a government decision, an interoffice committee has been set up to promote competition and infrastructure in the fuel industry, which published a final report of its recommendations in January 2010. In the area of infrastructure development, the aforesaid committee's proposals concerned, *inter alia*, opening up the possibility of importing via the piers of the Israel Electric Corporation at Ashdod and the Haifa port. In the area of competition and regulation in the fuel industry segments, the committee advises, *inter alia*, the supervision of refineries and ensuring that there is no price discrimination among fuel companies, determining a controlled rate for the leasing of tanks from the infrastructure companies, Petroleum & Energy Infrastructures Ltd. (PEI) and Pi Glilot, and streamlining the process of setting up small public fuelling stations.

11.17.7. State Economy Arrangement Law (Legislative Amendments to Achieve Budgetary Objectives and Economic Policy for the Fiscal Year 2001), 5761-2001 (the "**State Economy Law**")

The State Economy Law determines that a fuel company shall register in the Companies' Registry for fuel companies prior to the commencement of the business thereof and shall continue with conducting the business thereof as long as it is registered in the Registry, managed by the manager. In addition, it has been determined that a fuel company must hold a reserve of fuel which it finances, required for the proper functioning of the civil fuel industry (in Section 11.17.6: the "**Civil Reserve**") as well as a reserve required for military purposes and security purposes (in Section 11.17.6: the "**Defense Reserve**"). It shall be noted that the State bears the costs of financing and storage of the aforesaid reserves. Furthermore, regulations have been enacted to arrange the duty of fuel companies to hold security reserves and civil reserves (the "**Arrangements Regulations**"). The Arrangements Regulations determine that a fuel company

which held, by virtue of the Regulation of Commodities and Services (Arrangements for the Fuel Industry) Order 5748-1988, emergency reserves of diesel or jet fuel, as specified in the Arrangements Regulations, shall continue to hold it as security reserves in accordance with and pursuant to the provisions of the Arrangements Regulations, and the Company is precluded from using the aforesaid reserves for its ongoing day-to-day requirements. In addition, a fuel company that has the duty to register in the Fuel Companies Registry is obligated to hold civil reserves of a quantity equivalent to 45 days supply of diesel fuel or a quantity of 1,700 tons of diesel fuel, whichever is the larger of the two. Nonetheless, in September 2001, a petition was filed with the High Court of Justice against the provisions of the State Economy Law and Arrangements Regulations relating to holding the civil reserves, as aforesaid. Within the confines of the claim, as aforesaid, the High Court of Justice determined that the situation be restored to its former state so that the fuel companies shall be obligated solely to hold defense reserves; however the State may amend this by way of advance notice of 60 days. It shall be stated that in the context of the Fuel Industry Bill it is proposed to cancel the aforesaid provisions in the State Economy Law, however, the Arrangements Regulations which were promulgated thereunder will remain in effect and will be deemed as having been promulgated by virtue of the Fuel Industry Law. It should be clarified that the aforementioned has no significant affect on Granit.

11.17.8. The Fuel Excise Law, 5718-1958 (the "**Excise Law**")

The Law determines that it is not possible to produce fuel or engage in the sale of fuel unless a license had been obtained therefor from the Customs and Excise Director. Sonol had been issued such a license and it acts to renew it annually. The excise is imposed on fuel upon its dispensing from the dispensing facilities or upon its release from the customs, in case of import. Therefore, only companies owning a production license may purchase oil products directly from the refineries in Israel or import them. According to the Order of Excise on Fuel (Exemption from the Duty to Receive License and Approval), 5720-1960, an exemption may be obtained from the duty of receiving a license, *inter alia*, for producers and holders of fuel who received the fuel after the excise had been paid therefor, upon the fulfillment of certain conditions. The Excise Order on Fuel (Imposing Excise), 5764-2004, determines specific rates of excise for each oil product. The Excise Order on Fuel (Imposing Excise) (Amendment no. 3 and Temporary Provision), 5764-2004, and the Excise Order on Fuel (Exemption), 5765-2005, including amendments thereof, according to which the rates of excise on diesel and oil would

be raised gradually from 2005 till 2009 and would be equaled to those imposed on fuel, entered effect in January 2005. It shall be stated, that following the increases which occurred in the excise prices, during 2011, 5 bills for amendment of the Excise Law were laid before the Knesset: one bill, from February 2011, proposed to amend the Excise Law so that orders of the Ministry of Finance regarding changes in the excise rates would enter effect only after approval thereof at the Knesset Finance Committee; another bill, from February 2011 as well, proposed that the Excise Law would prescribe a maximal consumer price per liter of fuel that would be at NIS 6.68 per liter in 2011; another bill, submitted in March 2011, proposed to limit the excise rate so that it would not exceed 30% of the fuel price; a similar bill from June 2011 proposed to limit the rates of excise and VAT together, so that they would not exceed 30% of the fuel prices, unless approval of the Knesset Finance Committee would be granted thereto; and a bill from July 2011 proposed to cancel the VAT on the excise component in the calculation of the fuel price, altogether. A similar bill from October 2011, proposed not to raise the excise rate beyond 30% of the fuel price, other than with a special approval of the Knesset Finance Committee by a majority of the members thereof. A bill from December 2011 proposed that orders for reduction or cancellation of customs and levies would be brought to the approval of the Knesset Finance Committee. To the best of the Company's understanding, such bills are at various preliminary stages of legislation and there is no certainty for the approval thereof as laws.

11.17.9. Price Control of Commodities and Services Law, 5756-1996 and the Regulations Pursuant Thereto

The Price Control of Commodities and Services Law 5756-1996 (the "**Price Control Law**") enables the minister in charge, *inter alia*, to apply, by way of an order, the provisions of this law to a certain commodity or service, where the grounds determined in the law as justifying price control are fulfilled. By virtue of the law, orders were issued to determine the maximum price for 95-octane gasoline and a method for updating prices and dates of updating was determined as well, subject to certain exceptions.

The Order further provided that it is permissible to charge an additional price, which was also fixed in the Order, for gasoline sold at full service, and also for sales at fueling stations at night and on rest days. Pursuant to the Order, the maximum price of gasoline is based on the price of fuel at the Oil Refineries Ltd. rate (which was also supervised until January 1, 2007) with a supplement of infrastructure costs, moving, financing and

marketing margin that is divided between the fueling station's operator and the fuel company.

The structure of such price is published monthly by the Fuel Administration. The update in the marketing margin of gasoline was done, until a year ago, once every six months, based primarily on the marketing margin customary in four European countries, however in any event, the margin will not be updated by more than 2.5%.

On August 1, 2011, a draft report for a hearing pertaining to the marketing margin of gasoline in fuelling stations and the additions added on top of the BAZAN rate price (the "**Draft Report**") was received from the Fuel Administration in the Ministry of Energy and Water Resources. Pursuant to the Draft Report, the Ministry of Energy and Water Resources has notified the fuel companies, including Sonol, of its intention to reduce the marketing margin of gasoline and the additions added on top of the BAZAN rate price by approx. 18.4 Agorot (without VAT).

On August 31, 2011 a Goods and Services Prices Order (Maximal Prices at Fueling Stations)(Amendment) 5771-2011 was released (hereinafter in this Section: the "**Amendment**"), according to which the marketing margin of the fuel companies and the additions added on the ORL gate price were reduced by approx. 16.1 Agorot per liter (without VAT). Upon the adoption of the Amendment, Sonol and other fuel companies filed appeals to the HCJ against the Minister of Finance, the Minister of Energy and Water, the Price Committee and the Price Commissioner, moving for an order to cancel the Amendment. On September 19, 2011, a hearing of the appeal took place. The Court decided, with the parties' consent, to return the issue of examining the margin for renewed hearing, on the basis of an updated database, and prescribed timetables of several months for completion of the proceeding. Such hearing took place after the date of the Report, on February 14, 2012. Until the completion of the proceeding, the Amendment for the Supervision Order shall remain in effect. As of the date of release of the Report the results of the hearing have not been obtained yet.

The reduction of the marketing margin had an adverse effect on Granite's financial results, as it causes a decrease in Sonol's gross profit from the sale of Benzine 95. In Q4/2011 such reduction caused a decrease of more than NIS10 million in Sonol's revenues. Sonol carries out various actions in order to minimize the said effect, by actions including: reduction of discounts for automobile fleets and customer club members, reduction of discounts given at the fueling stations to private customers and change of trade conditions. Also, Sonol operates

for reduction of expenses thereof, mainly reduction of the lease fees paid to the fueling station owners, reduction of manpower and compensation related costs and reduction of maintenance expenses, as well as other inter-organizational streamlining steps. Such actions partially compensated for the reduction in the revenues for Q4/2011, as described above. The Company, based on the best of the knowledge of Granite's and Sonol's managements, is of the opinion that once the initiation of the aforesaid steps will be completed and the results will be expressed, no material adverse effect is expected to Sonol's profitability, consequently to the reduction of the marketing margin.

The information provided in this Section is forward looking information, as defined in the Securities Law, and there is no certainty for the materialization thereof. It is possible, inter alia, that due to the results of the aforesaid hearing, or due to the inability of Sonol to complete all of the steps at the scopes planned, the influence of reduction of the marketing margin as aforesaid, shall be different than described above.

It shall be mentioned that within the framework of the Trachtenberg Committee Conclusions (see Section 11.17.7 below) it was recommended to expedite the proceeding of imposing supervision on diesel for transport. Sonol was requested by the Ministry of Energy and Water and the Ministry of Finance joint price committee, pursuant to the Law for Supervision of Goods and Services Prices, 5756-1996 to provide its opinion regarding the committee's intention to impose supervision on the marketing margin due to the sale of diesel for transport, and it had provided its opinion, as requested. As of the date of release of the Report, a hearing on the matter for the fueling companies had not taken place yet, and naturally the decision has not been published yet.

The imposition of such supervision on diesel for transport may have an adverse effect on the financial results of the Company, however, as of the date of the release of the Report, the Company is not able to quantify such influence. The information stated in this Section is forward looking information, as defined in the Securities Law and there is no certainty of the materialization thereof.

11.17.10. <u>ORL Price Control</u>

As aforesaid, to the best knowledge of Granite, ORL was recognized as a monopoly in sale of oil products segment in Israel. Accordingly, in the past and until the conclusion of 2006, prices of Oil Distillates sold by ORL were determined pursuant to the Price Stability of Commodities and Services Order (Temporary Order) (Maximum Prices for Oil Products at

the ORL Gate) 5753-1992, which determined maximum prices for a variety of Oil Distillates at the ORL Gate (save for 98-octane gasoline and low-sulphur crude oil). Commencing in January 2007, following the splitting of ORL, alterations occurred concerning price control of Oil Distillates sold by ORL and the control over ORL Gate was removed. With respect to these alterations, see section 11.17.13 herein below.

11.17.11. Price Regulation of Commodities and Services Order (Maximum Prices for Oil Products at the ORL Gate) (Amendment No. 2), 5766-2006 (the "**Regulation Order**")

In accordance with the Regulation Order, commencing on January 1, 2007, regulation by way of the determination of prices was removed and in place thereof regulation is performed by way of reports of the refineries on profitability and prices.

According to the conditions of the Order, maximum price at the rate of the refinery shall again apply in the event that the refinery fails to fulfill the duties of reporting, imposed thereon in relation to the quantities of oil products and prices thereof, or in the event that the controller determines that for 6 consecutive months one refinery sold more than 50% of the amount of consumption on the local market and less than 15% was sold by another refinery.

11.17.12. Price regulation of services that the Granite Group receives

According to the Notice of Price Regulation of Commodities and Services (Infrastructure Rates in the Oil Industry) (Update of Prices for Infrastructure Services) 5763-2008, there are rates for prices of infrastructure's services at various terminals.

Payment in respect of airplane fuelling services at Ben-Gurion International Airport was determined based on the Notice of Price Regulation of Commodities and Services (Prices of Refueling Services for Aircraft at Ben-Gurion Airport), 5765-2004.

11.17.13. Government Corporations Order (Declaration on Essential Interests of the State in Oil Refineries Ltd.), 5767-2007 (above and below, the "**Interests Order**")

In February 2007, as part of the privatizing process of BAZAN, the Interests Order which specifies essential interests of the State in connection with BAZAN, was published. *Inter alia*, the Essential Interests Order regulates the activity of the privatized BAZAN in the area of marketing Oil Distillates at fuelling stations by placing

certain limitations, including the limitations to be specified herein below.

BAZAN may hold the rights at fuelling stations in up to 20% of all fuelling stations in the country (on December 31, 2011 the government may increase this percentage, which has not been done). BAZAN will be permitted to acquire from one entity during the course of three years the rights at fuelling stations in up to 7.5% of all fuelling stations in Israel. If BAZAN holds the rights at fuelling stations that constitute 10% or more of all fuelling stations in Israel, it may not enter into an arrangement to receive the rights at a fuelling station that constitutes a proximate fuelling station, unless it receives the authorization of the Commissioner of Israel Antitrust Authority. In addition, the Order imposes additional restrictions on BAZAN's activity concerning a restriction on the acquisition of control or 5% or more of the means of control of a corporation which markets Oil Distillates or a port infrastructure for the import or export of oil products in Israel. A parallel order regulates the activity of Baza.

11.17.14. The Hazardous Substances Law, 5753-1993 (the "**Hazardous Substances Law**")

Sonol's business includes the handling of hazardous substances. In accordance with the Hazardous Substances Law, the dispensing and storage facilities are required to obtain a poison permit granted by the commissioner in the Ministry of Environmental Protection. Sonol possesses a poison permit as stated.

11.17.15. Clean Air Law, 5768-2008 (the "**Clean Air Law**")

In July 2008, the Knesset passed the Clean Air Law that shall enter into effect on January 1, 2011, which constitutes a framework for the regulation of air quality and the emission of pollutants, principally in relation to large industrial enterprises. For installations wherein the activities listed in the law are performed in accordance with a business license or in accordance with a personal order, pursuant to the Abatement of Nuisances Law 5721-1961 (the "**Abatement of Nuisances Law**"), a transitional provision was determined that sets forth a hierarchy of times for the submission of an application for "an emissions permit" for current sources of emission that were active prior to the date of the law entering into effect.

As test cases ahead of the commencement of the law, the Ministry of Environmental Protection already acts to apply additional conditions to the business licenses of two factory

groups – at Ramat Hovav and the Haifa Bay, where, *inter alia*, Sonol installations are located.

The Clean Air Law determines restrictions and prohibitions with respect to emission sources, mobile and stationary, and determines that provisions for the prevention and restriction of air pollution from emission sources shall be determined, in accordance with which a person will have to abide when creating, importing, marketing, operating and using an emission source. According to the law, a prohibition applies to installing an emission source that requires a permit, to hold it, operate it, or use it (also by means of another) without a valid emission permit and in accordance with the conditions thereof.

According to the law, the Minister for Environmental Protection shall determine provisions with respect to features, components and quality of types of fuel and fuel additives in order to reduce insofar as possible the emission of pollutants as a result of the consumption of fuel or fuel additives, and to preclude impairment of the effectiveness and functioning of an installation or system intended to reduce the emission of pollutants from an emission source that uses fuel or fuel additives. In addition, the law determines that the production of fuel or fuel additives, the sale thereof, the import or marketing thereof and operating an emission source by means of fuel or the use of fuel and fuel additives shall be performed in accordance with provisions to be determined in Regulations.

In terms of legal liability, the Clean Air Law determines three general types: civil liability, financial sanctions (of an administrative nature), and criminal liability.

In May 1992, the Clean Air (Air Quality) Regulations, 5752-1992 came into effect, defining severe or unreasonable air pollution. In May 2011, the Clean Air (Air Quality Values) Regulations (Provisional Directive), 5771-2011 came into effect, defining various pollution values. The major part of the aforesaid regulations is in force until March 2015, and the force of some of the values denoted in the second and third supplements of the said regulations is until the end of 2012.

11.17.16. Various Bills

As of the Report Publication Date, several bills are pending, each of which if passed has the capacity to adversely affect the profitability of Granite, and they are: the Encouragement of the Use of Vehicles Friendly to the Environment (Legislative Amendments) Bill 5766-2006 – the aforesaid bill proposes to amend the Purchase Tax Law (Goods and

Services), 5712-1952, such that from the tax year 2008, the rate of tax on an environmentally friendly vehicle in which an LPG system or hybrid technology was installed will not exceed the rate of 10% of its price. The bill has not yet been passed but on August 1, 2009, the Minister of Finance announced the green taxation reform as described in Section 11.16.2 above; the Planning and Construction (Amendment – Inspection of the Presence of Pollutants in the Ground, Air and Water Sources) Bill 5770-2009 – the bill proposes to amend the Planning and Construction Law, 5725-1965, such that it will not be possible to approve a plan on land which is suspected to be polluted, until an inspection of the presence of pollutants in the ground, air and water will be performed, and if pollution will be found, it will be required to remove the same. If the bill will be passed, an inspection of the presence of pollutants will be required before the re-designation of land which served as a fuelling station; the Business Licensing (Amendment – Imposing a Fine in respect of Violations of the Environmental Protection Regulations) Bill 5767-2007 – the bill proposes to increase punishment due to environmental violations; the Reduction of Greenhouse Gases Bill 5768-2008 – according to the bill, the State of Israel must decrease the greenhouse gas emissions by 25% by 2020 and by a further 25% by 2050, through a national plan. The bill may have a material effect on Granite's activity, since the main source of greenhouse gas emissions is the burning of oil products; and the Prevention of Soil Contamination and Rehabilitation of Contaminated Soils Bill 5771-2011 – the bill imposes a rehabilitation duty in respect of any land on which industrial activity took place. In the event that the land will not be rehabilitated, it will not be possible to transfer ownership thereof and/or renew a business license. In August 2011, the bill was approved in first reading. This bill, if approved, may have a significant impact on the Company; the Control of Prices of Commodities and Services (Amendment – Control of Diesel Oil for Transportation) Bill, 5771-2011 – On May 23, 2011, a bill was presented before the Knesset ,whereby the law would be amended so that the appointed minister and the Minister of Finance may, with the government's approval, reinstate the supervision of diesel oil for transportation, so that the maximum price permitted therefor will be determined in an order. On July 17, 2011, the Ministers' Committee for Legislative Matters decided to object to the said bill. On November 28, 2011, a similar bill was proposed – the Control of Prices of Commodities and Services (Amendment – Control of Diesel Oil Prices), 5772-2011, within which it is proposed that the ministers will set a maximum price for diesel oil for transportation in an order.

We shall indicate that some of the bills are in their initial stages and to the best of Granite's knowledge most of them have not yet been brought up for authorization at the Knesset and it is entirely uncertain whether the bills will be passed. In addition, it is entirely uncertain that, if and when the bills are passed, the conditions and provisions to be prescribed in the laws to be passed in accordance therewith shall be similar to the current bills pending. Accordingly, at this point, Granite is unable to evaluate whether and how the bills (if passed) will affect the fuel industry in general and the Granite Group in particular, except as aforesaid with respect to the bill concerning the Prevention of Soil Contamination and the Rehabilitation of Contaminated Soils, 5771-2011.

11.17.17. The Committee for Examination of an Economic Social Change Headed by Prof. Trachtenberg

In July and August 2011, a broad public protest developed across the country, expressed by pressuring the decision makers to act for the reduction of living costs in general and housing prices in particular, following which a committee, headed by Prof. Trachtenberg, was appointed, which examined various ways to alleviate the cost of living. In the report published thereby, the committee included several recommendations with respect to the fuelling stations, the principal ones of which are described hereunder: a recommendation to initiate a legislative process to immediately release several fuelling stations from obligation to fuel companies, including Sonol; Preferring independents, entities which are not one of the four major fuel companies, in planning processes, and instructing the Israeli Land Administration and the planning institutions to plan lands for 40 new fuelling stations within two years and market them to independents immediately upon the planning's finalization; expediting the implementation of regulations for a universal automatic vehicle identification and fuelling system, which will enable fuelling at all of the fuelling stations. It should be noted that the Fuel Industry (Promotion of Competition) (Rules for Automatic Fuelling Devices) Regulations, 5771-2011, were published and approved in the records on October 23, 2011. To implement immediate control over the prices of diesel oil for transportation, at the refineries' gate and at the fuelling stations. To assign the Ministry of Energy and Water Resources with mapping geographical areas where there is presence of the four major companies, emphasizing city centers, and in light of the level of competition, to determine a mechanism compelling the sale of stations to small companies of a lesser market share in order to encourage competition.

11.17.18. Transport Licenses

Within the framework of Sonol's operating segments, Sonol transports Oil Distillates considered to be hazardous substances. For the purpose of such business, Sonol holds a transport office license as well as a license to transport hazardous substances in accordance with the Traffic Regulations.

11.17.19. Essential Enterprise

Sonol holds an essential enterprise's authorization, obtained from the Ministry of Industry, Trade and Employment. In accordance with the authorization, as aforesaid, in an emergency, fleets of vehicles and the supply and fuelling facilities thereof, are mobilized in favor of the economy in a time of emergency to enable the regular supply of.

11.17.20. The Weights and Measures Ordinance

The Weights and Measures Ordinance 1947 prescribes a variety of standards for weights and measures. By virtue of this Ordinance, regulations were enacted to determine, *inter alia*, the manner of inspection of liquid fuel pumps and the calibration thereof and the duty to mark a calibration stamp on the pumps following the inspection thereof. In addition, the Regulations determine a variety of provisions with respect to instruments for the measurement of Oil Distillates carried on tanks as well as marking a calibration stamp on the same instruments. It is prohibited to use the instruments, as aforesaid, unless these have been calibrated and stamped in accordance with the Regulations.

11.17.21. Transition to fuelling with gas

Pursuant to an amendment to National Outline Plan 18 it is possible to obtain a permit for fuelling stations with LPG, on condition that certain conditions are fulfilled and authorization of the Director is obtained. Based on the best knowledge of Granite’s management, the Company estimates that fuelling vehicles with gas is anticipated to occur solely in the initial phases and Granite does not anticipate that it will significantly affect, if at all, its earnings and/or profitability in the near future.

This section includes forward-looking information as defined in the Securities Law, which relies on internal assessments of the Company based on the best knowledge of Granite’s management. It will be noted that it is entirely uncertain whether in the near future the transition to fuelling with gas will commence. Nonetheless, even if it does commence, it

will be solely in preliminary stages. Moreover, it is possible that the Company's assessments, based on the best knowledge of Granite's administration as regards anticipated costs that will be required for the adaptation of its fuelling stations to such a transition, will turn out to be erroneous.

11.17.22. Business licenses

The sites wherein Sonol operates, including the fuels' filling installations and fuelling stations, require a business license pursuant to the Licensing of Businesses Order (Businesses Requiring Licensing) 5755-1995, issued by virtue of the Licensing of Businesses Law, 5728-1968. At the Date of the Report, the majority of Sonol's business licenses are in effect or it is handling the renewal of their validity. It should be noted that in most cases wherein Sonol replaces the operator of a station with another operator, even if the new operator is a company under its full ownership, it is necessary to obtain a new business license, even if no change has occurred in the same station. Obtaining a new business license involves, *inter alia*, obtaining authorizations from the various authorities, including the Ministry of Environmental Protection, which generally stipulates its authorization on the performance of a comprehensive inspection of the state of the station, conducting surveys of the soil and making a variety of demands to upgrade the station. The aforesaid is true also with respect to new fuelling stations which are required to reapply and obtain again all the authorizations of the authorities that permitted the establishment thereof. Sonol takes steps to reduce, insofar as possible, the duration of time to obtain a new business license. Principally due to the aforesaid, with respect to some of the sites there are still no business licenses and Sonol is acting to obtain such. The business licenses are valid either permanently or for a fixed period, in which case it is necessary to renew the licenses on the expiration of the period of the license.

Operating the convenience stores of Sonol within the fuelling complexes requires obtaining a business license. Most of the convenience stores have a valid business license or Sonol is taking steps to obtain such.

The Licensing of Businesses Law prescribes criminal sanctions vis-à-vis an individual and/or a corporation which conduct a business requiring a license without a business license. In addition, the court may order the cessation of a business conducting business without a license, as aforesaid.

As of the Date of the Report, a small number of indictments are pending against Sonol and several of its officers pertaining to the operation of fuelling stations without a

business license or in divergence from a permit. In the Company's assessment, based on the best knowledge of Granite's management, the Company's exposure with respect to the aforesaid is immaterial.

11.17.23. Antitrust

A. The Restrictive Trade Practices Law (Amendment no. 12), 5771-2011 – the said amendment came into force in July 2011. Pursuant to the amendment, the General Director may define a concentration group and instruct all or some of its members to take certain measures to avoid damage or a concern of substantial damage to the public or to competition or measures to enhance competition or create the conditions for the significant enhancement of competition.

B. Internal compliance program – Since 1999, Sonol has participated in an internal compliance program on behalf of the Israel Antitrust Authority (in this Section: the "**Authority**"). At present, Sonol is working on the preparation of an updated compliance program.

C. Exclusivity arrangements for the supply or purchase of fuels at fuelling stations – In 1993 the Commissioner of Israel Antitrust Authority (the "**Commissioner**") published a decision according to the Restrictive Trade Practices Law, 5748-1988 (in this Section: the "**Law**"), on the matter of a set of agreements between the fuel companies and the operators of the fuelling stations of Paz, Delek and Sonol. In this decision it was determined that these agreements, which comprise an undertaking of the station operators to purchase products exclusively from the fuel companies or an undertaking for the exclusive supply of such products, constitute a Restrictive Arrangement as defined in the Law.

In 1995 the Commissioner reached an agreed upon arrangement with Sonol and Paz pertaining to new rules of conduct of the companies. According to the arrangement, the application of the Commissioner's original decision was limited so that it would apply solely to fuelling stations with which the fuel companies have no "customary lease agreement" (i.e., a lease agreement where the lease fees paid or other consideration given according thereto are real. Real lease fees are deemed as lease fees that are similar to the lease fees which the Israel Lands Administration collects in respect of a fuelling station with a similar extent of sales). Paz and Sonol undertook on their parts that they would release the stations that are not connected with

them in a standard lease agreement from the duty of exclusivity. To the best understanding of the Company, based on the position of the management of the Granite company, Sonol has fulfilled its undertaking, as aforesaid.

As part of the arrangement, conditions were determined, *inter alia*, for the future engagement of the Paz and Sonol companies with fuelling stations in exclusivity agreements. These conditions include, *inter alia*, the duty of the companies to submit an application for authorization of such agreements to the Antitrust Tribunal. It was further determined in the arrangement that the Commissioner will recommend the approval of the agreements for the following periods: in a fuelling station set up by Sonol, the period of agreement will be up to14 years; in a fuelling station wherein Sonol performed a complete renovation, in the amount of approx. 60% of the establishment of the station, the period of the agreement will be up to 7 years; for an agreement to supply an existing fuelling station, the period of the agreement will be up to 3 years. It was further determined that the companies can also request individual authorization for longer periods from the Tribunal. According to the arrangement, the companies were restricted so that a company may enter into an exclusivity agreement with a fuelling station that was released from such agreement with it within the context of the arrangement for a period solely of one year. The arrangement was authorized by the Antitrust Tribunal. According to a public notice of the Commissioner, at a later stage Delek reached an arrangement similar to the arrangement of Paz and Sonol, save for certain differences that are irrelevant to the Granite Group.

It should be noted that at a later stage the Antitrust Tribunal determined, concerning the matter that Delek raised before the court, that the longer periods mentioned above, of 14 years and 7 years, should be curtailed to solely 6 years.

As a result of the publication of the arrangement, several proceedings were initiated in a variety of courts pertaining to the set of agreements between the fuel companies and operators of fuelling stations, including against Sonol, with several operators contending that they ought to be released from the exclusivity agreements. To date, a principle decision has yet to be given by the Supreme Court pertaining to these

proceedings. On this matter see Note 36 of the Financial Statements of the Company in Chapter C of this Report.

D. Agreements for lease of stations – In June 2001, the Commissioner contacted the fuel companies, Paz, Sonol and Delek and informed them that he is examining the possibility that the lease agreements between the fuel companies and the fuelling stations constitute "a merger" as defined in the Law. As aforesaid, as regards the Commissioner's approach, the rationale that stood at the base of his examination is that the lease or operating agreements between the fuel companies and the fuelling stations grant the fuel companies rights to the effect that their activities at the fuelling stations are subject to the decision-making system of the fuel company, which, according to the Commissioner's approach, amounts to a merger. Accordingly, the Commissioner advised the fuel companies to agree with him on a text for an agreed order to the effect that any rental agreement of a fuelling station, for a period that exceeds 7 years, shall be deemed a merger that requires the authorization of the Commissioner. Sonol was of the opinion that each rental agreement ought to be examined in substance and if it comprises a type of merger, in Sonol's opinion, then Sonol will act in accordance with the provisions of the Law as regards a merger. Delek accepted the Commissioner's proposal and agreed with him on a text of an agreed order, as aforesaid, that entered into effect in November 2003. We would clarify that the aforesaid accords do not apply to Sonol.

11.17.24. An exemption from a restrictive arrangement

On December 20, 2011 an exemption from approval of a restrictive arrangement under Clause 14 of the Restrictive Trade Practices Law was granted by the Antitrust Commissioner to the arrangement between Dor Alon and Sonol. For details see Section 11.13.1 above.

11.17.25. Approved supplier of the Ministry of Defense

In order to supply Sonol's products to the Ministry of Defense, Sonol is required to meet certain criteria, including security conditions, so that following confirmation of the fulfillment thereof, Sonol received authorization that it is a recognized supplier of the Ministry of Defense. In accordance with such authorization, Sonol may supply its products to the Ministry of Defense. It should be noted that authorization, as aforesaid, is limited in time and must be renewed as required.

11.17.26. Standards and quality control

Sonol markets its products in accordance with a variety of standards relevant to the Oil Distillates operating segments that are published from time to time by virtue of the Standards Law, 5713-1953. The standards specify technical requirements that apply to products, including as regards product specifications, manners of production, storage, supply, operation, packaging, etc.

11.17.27. Safety and security provisions

Sonol acts in accordance with strict safety rules pursuant to directives of the Ministry of Labor, since due to the involvement in activities requiring hazardous substances, a great deal attention and precision with respect to safety is necessary. Granite's internal certified safety superior maintains contact with external entities, such as the armed and the rescue forces, and safety drills are occasionally take place. Sonol's internal safety trustees are responsible for the enforcement of safety procedures in its facilities.

Furthermore, due to dealing with hazardous substances, Sonol is required to comply with strict security rules and is considered to be a body "directed by the Police and the General Security Services." Sonol maintains a safety committee as per the requirements of the Safety at Work Law.

11.17.28. Environmental Protection

Regarding standardization on the subject of environmental protection, see section 11.16.1 above.

Subject to the aforesaid, to the best of the Company's knowledge, based on the best of Granite's management's knowledge, the Company satisfies the requirements of the laws and regulations described above.

11.18. **Material agreements**

11.18.1. The agreements of Sonol in these operating segments are madein the ordinary course of business and on market conditions. Among these agreements the agreement with BAZAN for the supply of oil products (fuels), as specified in section 11.13.3 above can be listed as well as the agreements pertaining to the lease, operation and supply of fuels in the various Sonol fuelling stations, as specified in Section 11.9.5 above.

11.18.2. In August 1990, an agreement was signed, which was

amended in 2005, between Sonol and Delek of the first part, Orpak Systems Limited and Rapak Electronics Ltd. ("**Rapak**") of the second part, and an additional party. According to the agreement, as aforesaid, Delek and Sonol purchased jointly and in equal parts the rights of production, development, marketing, maintenance and service of the computerized automated fueling system known as Dalkan 2000, which comprises software and equipment designated to streamline the sale of fuels particularly to customers with fleets of vehicles.

According to the agreement mentioned above, Orpak Systems Ltd. and Rapak (hereinafter jointly: "**Orpak**") were granted the exclusive right to provide supply services of units of the Dalkan system, of various types, spare parts for the system as well as maintenance services, consultation and development of the Dalkan system. Orpak undertook to manufacture the systems and equipment as aforesaid and provide the services as aforesaid to Delek and Sonol exclusively in Israel as well as to service stations and sites, as Delek and Sonol shall instruct. On August 21, 2011, within an agreement with respect to a change in commercial terms, the Company and Orpak agreed to extend the agreement's term until January 1, 2016. Sonol pays Orpak a monthly sum for maintenance of the system and an additional sum in respect of each Dalkan system that Orpak installs.

In respect of the aforementioned system, Delek and Sonol have registered patents. On this matter, see Section 11.75.1 below.

11.18.3. Agreement for cooperation in the import of Distillates – on November 1, 2007, an MOU was signed between Sonol and Dor Alon, whereby, subject to the approval of the Antitrust Commissioner, the parties agree to cooperate in the purchase and import of Distillates in the following areas: negotiating with suppliers and carriers in Israel and abroad and signing joint purchase agreements. The parties agreed that only information which is necessary for the aforesaid cooperation will be passed between them. On December 20, 2011, the Antitrust Commissioner decided to grant the said agreement an exemption from approval as a restrictive arrangement, which shall be in force for two years.

The Supergas Segment

11.19 General

11.19.1 Supergas is a subsidiary of Granite (until December 2010, Supergas was held in equal shares by Sonol and Granite, as of December 2010, Supergas is wholly owned (100%) by Granite).

11.19.2 The main business of Supergas is in the segment of marketing and supply of LPG. In the context of this operating segment, Supergas performs local purchase, import, storage, marketing and distribution of LPD to various customers.

11.19.3 Marketing and supply of LPG by Supergas is made to both domestic customers and institutional, governmental, commercial and business customers, for industry and agriculture. The supply of LPG is made through mobile and stationary containers.

11.19.4 The sale of LPG is made to the domestic, business and institutional customers directly through Supergas, through agencies controlled by Supergas as well as through independent distributors and agents owned by third parties.

11.19.5 Some of the commercial and institutional customers of Supergas may in the future have potential substitutes to LPG, such as natural gas. However, as of the date of the Report, natural gas is still not available for them. Nevertheless, to the best knowledge of Supergas, the Israeli economy starts to prepare for the marketing of natural gas. On this matter and on the matter of Supergas's preparation for the marketing of natural gas, see also Section 1.5 below.

11.19.6 The main success factors in the marketing and supply of LPG market are professional knowledge, reliability of the supply, the safety level, service quality and price.

11.19.7 In the year of the Report, Supergas purchased the majority of the LPG for marketing and distribution of LPG from BAZAN and BAZA in similar scopes. On this matter, see also Section 11.30.2 below. And see Section 11.35.7.1 below on the matter of the price increase following the decontrolling of the refineries.

11.19.8 The purchase price of the LPG from the refineries as of December 31, 2011 is 1.2% higher than the purchase price of LPG on December 31, 2010. The purchase price of the LPG from the refineries as of December 31, 2010 was 22% higher than the purchase price of LPG on December 31, 2009. The increase in the LPG prices, as aforesaid, which is affected, inter alia, from the

increase of the petroleum prices worldwide, affected the value of the stocks and increased the liabilities of Supergas's customers.

11.19.9 Supergas, through subsidiaries, is preparing to expand its business to the natural gas segment and to the segment of production of solar electricity in a photo-volt technology. In the natural gas segment Supergas is preparing to act in two main sub-segments: construction and operation of regional natural gas distribution networks under appropriate licenses and marketing of natural gas.

11.19.10 In the segment of the construction and operation of a natural gas distribution network, Supergas acts through Super N.G. Natural Gas Distribution Company Ltd. ("Super NG") which is held through a subsidiary of Supergas (Supergas Natural Holdings Ltd.) and by Shapir Civil and Marine Engineering Ltd. ("Shapir") in equal proportions (50/50). Super NG won a tender to construct and operate a natural gas distribution network in the Central Region and was granted the appropriate license.

11.19.11 Supergas intends to continue developing this operating segment, *inter alia*, through participation in tenders published by the Natural Gas Authority for granting licenses for the construction and operation of a natural gas distribution network in additional areas.

11.19.12 In the segment of the marketing of natural gas, Supergas acts through a wholly owned subsidiary thereof (Supergas Natural Ltd.), which acts to market natural gas among potential industrial and institutional customers in various areas within the State of Israel to which the natural gas distribution network is designed to reach.

11.19.13 In addition, Supergas acts to develop and expand its activity in the production of solar electricity segment. Supergas intends to engage in this segment of solar energy by initiating projects for the construction of photo-volt facilities for producing electricity, constructing photo-volt facilities and producing electricity therethrough, in accordance with the regularizations published by the Public Services Authority - Electricity.

11.19.14 It should be stressed that the information regarding Supergas's activity in the natural gas and production of solar electricity segments is forward-looking information, as defined in the Securities Law, which is based on information known to the Company based on the management of Granite and on the management of Supergas on December 31, 2011, on subjective estimates and assessments of the Company based on estimates of the management of Granite and the management of Supergas, considering the past experience thereof and on the intentions and plans thereof on the date of the Report. These may not materialize in case changes occur in the plans and intentions of Granite and

Supergas as aforesaid, for any reason, including - the structure of the markets, the regulatory and statutory regularizations in the segment, the availability of natural gas and the price thereof, competition, Supergas's estimates regarding the business profitability or due to the realization of any of the risk factors specified in Section 11.80 below.

11.19.15 Supergas's activity in the operating segments thereof is subject to various legislative and standardization restrictions. On this matter, see also Section 1.16 below.

11.19.16 Various regulatory requirements, including those which compel meeting strict safety requirements for the supply of LPG, impose on Supergas an obligation to perform substantial monetary investments in order to meet them. On this matter, see also Section 11.35.16 below.

11.19.17 The LPG market is characterized by the existence of competition with regard to both marketing and distribution to commercial and institutional customers and marketing and distribution to domestic customers. On this matter, see also Section 11.26 below.

11.19.18 The activity of marketing and distribution of natural gas to industrial and institutional customers is also characterized by the existence of competition.

11.19.19 There is competition also in the context of tenders published by the Natural Gas Authority for granting licenses for the construction and operation of natural gas distribution networks.

11.19.20 The production of solar electricity operating segment is characterized by extensive competition as well, where to the best knowledge of Supergas, hundreds of applications for granting licenses to produce electricity are submitted to the Public Services Authority - Electricity.

11.20 **Principal Products**

The main product that Supergas markets and supplies is LPG. The LPG is a gas that is released in the distilling process of the crude petroleum. The main use of LPG is energy for operating burners in industry, bakeries and restaurants, for heating institutions, for heating henhouses in agriculture as well as for cooking and heating in households. This product is directly marketed and supplied by Supergas to the various customers thereof.

11.21 **Material Changes Expected in the Corporation's Share and in the Mix**

In the Company's estimate, based on the best knowledge of the managements of Granite and Supergas, no material change is expected in Supergas's share in

the markets of marketing and supply of LPG to domestic customers and to commercial and institutional customers.

As specified, Supergas intends to expand the activity segments thereof and develop activity in the natural gas segment. Future entry of natural gas to the Israeli market will also serve consumers that Supergas provides them with LPG and the concern is that such customers will stop being customers of Supergas in the marketing and distribution of LPG segment. Therefore, Supergas estimates that future entry of natural gas to the Israeli market might affect the LPG quantities marketed by Supergas. However, Supergas wishes to compensate the loss of the LPG customers and the expected decrease in the quantities of LPG sales as aforesaid by marketing of natural gas.

The information in this section is forward-looking information, as defined in the Securities Law, which is based on information known to the Company based on the estimations of the management of Granite and on the estimations of the management of Supergas on December 31, 2011, on subjective estimates and assessments of the Company based on estimates of the management of Granite and the management of Supergas, considering the past experience thereof and on the intentions and plans thereof on the date of the Report. These may not materialize insofar as changes occur in the plans and intentions of Granite and Supergas as aforesaid, for any reason, including - the structure of the markets, the regulatory and statutory regularizations in the segment, the availability of natural gas and the price thereof, competition, Granite's and/or Supergas's estimates regarding the business profitability or due to the realization of any of the risk factors specified in Section 11.80 below.

11.22 **Revenue Segmentation**

Supergas's revenues from the business of marketing and supplying LPG do not exceed 10% of the total revenues of the Company.

11.23 **New Products and Services**

11.23.1 Natural Gas Distribution

Following the winning of Super NG in the tender for the construction and operation of a natural gas distribution network in the Central Region, in November 2009 Super NG was granted a license for the construction of a natural gas distribution network in the Central Region and the operation thereof for 25 years. Pursuant to the terms of the license, Super NG shall receive the revenue thereof from a one-time connection fee and from the distribution fee tariff by the size of the customer (the extent of natural gas consumption) as specified in the license.

In November 2010, Super NG signed an agreement with the government company Israel Natural Gas Lines Ltd. ("INGL"), for the

ordering of four pressure-reduction stations ("PRMS") for connection of the transmission system to the distribution system. The construction of the PRMS will be performed in the coming years by INGL, or another on its behalf, and it shall also operate them. As of the date of the report, Super NG is performing planning and construction activities.

According to the provisions of the license granted to Super NG, it is required to invest in the construction of the distribution network a sum of approximately NIS 160 million, spread over 8 years, in accordance with the milestone prescribed in the license. According to the proposal, in the first milestone, Super NG is supposed to invest 40% of the sum of the investment in the first two years from the date of the license and according to the terms thereof. For the activity of Super NG, the shareholders thereof provided a guarantee, according to the holdings thereof, in favor of the Natural Gas Authority in accordance with the terms of the tender and the license.

In October 2009, the Ministry of National Infrastructures published a tender for the construction and operation of a natural gas distribution network in the Southern Region. On April 18, 2010, Super N.G. South - Natural Gas Distribution Company Ltd. ("**Super NG South**"), a company jointly owned, in equal shares, by Supergas and Shapir, submitted a bid in the tender. Its bid was disqualified and the bid of Natural Gas South Ltd. was declared as the winner. Supper NG South filed an administrative petition with the court. On December 27, 2011, the petition was denied by the court.

11.23.2 Marketing of Natural Gas

Supergas intends to act for the marketing and supply of natural gas (a mixture of gases that the main component therein is Methane CH4 which is extracted from wells and conducted directly to the consumer through piping) to industrial and institutional customers which are intended to connect to the distribution network. For this purpose, Supergas started to perform the preparations required for the performance of this activity, including - locating potential customers and engaging therewith in appropriate agreements. As of the date of release of the Report, Supergas engaged with a number of customers in contracts for the supply of natural gas.

11.23.3 Production of Solar Electricity in a Photo-Volt Technology

Supergas acts, through corporations controlled thereby, for the initiation and construction of facilities for the production of solar electricity through photo-volt facilities. Supergas intends to perform the construction and operation through subcontractors.

Medium facilities - in January 2010, the Public Services Authority - Electricity published a regularization regarding facilities for the

production of energy in a photo-volt method with output of over 50KW and up to 12MW which are connected to the electricity network, in an overall scope of 300MW. Supergas, through subsidiaries and partnership controlled thereby, filed several applications for conditional licenses as defined in the regularization, some of which have been approved, and it progresses in the course of the additional approvals required for the construction of the systems. Supergas obtained, through subsidiaries and partnership controlled thereby, conditional licenses for the construction of solar electricity production facilities which are connected to the distribution network in an overall scope of approximately 20.979MW, conditional tariff approvals for the production of electricity in a scope of approximately 11.132MW and a fixed tariff approval in a scope of 0.45MW.

In the next two years Supergas intends to invest in the construction of such facilities investments in sums that may be material. However, the date of realization and scope thereof is unknown since it is contingent on the receipt of various statutory approvals and licenses.

On December 14, 2011, the Electricity Authority announced a reduction of the tariffs paid for the electricity produced through medium photo-volt systems, so that the base rate will be NIS 1.09 per each kWh produced (according to a linkage mechanism) (instead of NIS 1.44 and NIS 1.37 originally) and be reduced in accordance with the reduction rates prescribed by the Authority over the years. The outline of the tariff reduction will not apply to the projects with met the required conditions by the date of the hearing and submitted by December 31, 2011.

Small facilities - until the date of the Report, Supergas constructed small facilities (output of under 50KW) in a scope of 375KW for the production of energy in a photo-volt method.

Land tenders - In October 2011 the Israel Land Administration published three land tenders for the lease of lots in the Southern Region for a period of 24 years and 11 months for the construction of photo-volt systems. The Electricity Authority allocated a designated quota in a scope of installed 60MW, which will join the quota of the medium facilities published in January 2010, see this section above. Supergas, through subsidiaries controlled thereby, submitted bids for 2 of the lots and won both of them. One lot is in Mizpe-Ramon, the area thereof is approximately 105 dunams and the sum proposed therefor was NIS 14 million for the construction of a system with an output of approximately 4MW. The other lot is in Ein Evrona whose area is approximately 69 dunams in consideration of approximately NIS 18.7 million for the construction of a system with an installed output of 5MW. The tariff which will be paid for the electricity produced is NIS 1.025 per each kWh conducted to the network. The tariff will be reduced by 10% on December 31, 2012, insofar as a tariff approval will not be given until then. After the date of the Report, in January

2012, two administrative petitions were submitted against the winning of Supergas. On February 8, 2012, the court ordered the deletion of the petitions and the cancelation of the interim orders granted in the proceeding and left the winning of Supergas intact.

It is hereby clarified and stressed that the information regarding Supergas's activity in the natural gas segment and in the production of solar electricity segment is forward-looking information, as defined in the Securities Law, which is based on information known to the Company based on the management of Granite and on the management of Supergas on December 31, 2011, on subjective estimates and assessments of the Company based on the management of Granite and the management of Supergas, considering the past experience thereof and on the intentions and plans thereof on the date of the Report. These may not materialize in case changes occur in the plans and intentions of Granite and Supergas as aforesaid, for any reason, including - the structure of the markets, the regulatory and statutory regularizations in the segment, the availability of natural gas and the price thereof, competition, Granite's and Supergas's estimates regarding the business profitability or due to the realization of any of the risk factors specified in Section 11.80 below.

11.24 **Activity Segment Customers**

In the segment of marketing and supply of LPG, Supergas supplies LPG to a vast array of varied domestic (private household), commercial and institutional customers, including - customers in the agriculture, industry and trade segments. The LPG is acquired by the customers for cooking, heating, operation of ovens and different burners.

Supergas is not dependent on a single customer or a small number of customers, whose loss will significantly affect this operating segment. Moreover, Supergas does not have a single customer that the revenue therefrom constitutes 10% or more of the total revenue of Granite as of December 31, 2011. However, it should be noted that Supergas sells LPG in large scopes to institutional customers, such as governmental bodies, and to large industrial companies. Usually, insofar as the acquisition scopes of the customer are larger, the profitability rates from the sales thereto are smaller.

Distribution of Supergas's Sales according to Customer Types

The following is a table describing the distribution of Supergas's sales in 2011 and 2010, distributed according to customer types as well as their percentage out of the total revenues from this segment in this period:

Customer type	2011		2010	
	Sales (NIS in thousands	Percentage of total revenues in activity segment	Sales (NIS in thousands)	Percentage of total revenues in activity segment

Institutional, governmental, commercial and business customers	264,079	51%	211,951	50%
Domestic customers	250,622	49%	215,629	50%
Total	514,701	100%	427,580	100%

11.25 **Marketing and distribution**

11.25.1 Storage, Filling and Issuance of LPG

Supergas operates two main logistic facilities for storage and issuance of LPG in Kiryat Ata and Ramle. In addition, Supergas leases storage volume of hundreds of tons in the facilities of EAPC in Ashkelon, which allows it to accumulate stock of LPG and thereby reduce imports of LPG in the winter season. In addition, Supergas stores LPG in bulk tanks installed at the customers' premises.

11.25.2 Supply of LPG to Customers

The supply of LPG to customers is made nation-wide in a number of ways: through Supergas branches, through agencies controlled by Supergas or through independent distributors and agents.
LPG sales to the domestic customers are performed also through a call center located at the main office of Supergas and through service representatives in the relevant branches and agencies, both by telephone communication devices and in the points of sale themselves.
The supply of gas to the customers is performed through transportation of mobile gas containers (with capacities of 12 kg and 48 kg) and supply and filling of gas in stationary bulk tanks located at the customers' premises. The transportation is mainly performed by subcontractors of Supergas.

11.25.3 Marketing of LPG

With regard to the marketing of the LPG, Supergas performs marketing actions through marketing personnel, agencies controlled by Supergas and independent agents and distributors acting to locate customers and engage therewith.
Supergas has 16 branches providing service in various areas in Israel as well as two agencies which are subsidiaries controlled thereby (jointly owned with third parties). Moreover, Supergas has 15 independent agents and distributors.
The marketing of the LPG to the domestic customers is conducted through a customer center, marketing personnel of Supergas, agencies controlled by Supergas, independent agents and distributors.

The marketing and sale to large institutional customers, which the engagement therewith is usually done according to a national tender, is performed by the marketing personnel of Supergas.
The activity of Supergas is not dependent on any single marketing factor and Supergas is not substantially dependent on the marketing and distribution channels that are not fully controlled thereby as specified above.

11.26 **Competition**

According to the data of the Ministry of Energy and Water Resources, on the date of the Report, 36 companies are listed as "gas suppliers" in the supply of LPG segment, out of which, 27 companies engage in the marketing of LPG. Part of the aforesaid companies only competes for sales to customers of a certain type whereas the other part competes for sales to all customer types, private, commercial and institutional.

In the marketing of LPG segment, there are four large gas companies. In the Company's estimate, based on the estimates of the management of Granite and the management of Supergas as of the date of the Report, the market share thereof in such operating segment is approximately 18%. Such estimates are based only on internal estimates and there is no certainty that Supergas's estimates are correct and accurate.

The marketing and supply of LPG segment is characterized in that the activity therein involves substantial monetary investments, *inter alia*, due to many regulatory requirements, including of the Ministry of Environmental Protection, and due to the need to meet high safety requirements.

On the matter of the law to promote competition in the gas market, see Section 1.16.5 below.

In the Company's estimate, based on the estimates of the management of Granite and the management of Supergas, the main competitors of Supergas are: Pazgas 1993 Ltd., the American Israeli Gas Corporation Ltd. (known as Amisragas), the New Dorgas Ltd., S.A.M. Merkaz Hagaz Ltd., and Gaz Yagel Gaz Marketing & Distribution (1996) Ltd.

Supergas deals with the competition by giving discounts to the customers thereof because since the product marketed thereby and by all the competitors in the market is homogenous ("commodity", i.e. a product identical to the product provided by the competitor and that does not entitle it added value), the main parameters considered by the customer when choosing the supplier are: professional knowledge, reliability of supply, service safety and the product price. Supergas invests efforts to improve the service to its customers, *inter alia*, through improving the availability, the safety and the reliability. Moreover, Supergas continuously acts to deepen the professional knowledge of all of the employees thereof and of the employees of the agencies and distributors thereof.

11.27 **Seasonality**

The consumption of LPG during the year is affected by seasonality since it is used, *inter alia*, for heating (including water heating). Therefore, the sales of LPG are higher in the first and fourth quarter than in the second and third quarter due to the effects of the winter.

11.28 **Fixed assets, Pproperties and Facilities**

11.28.1 Issuance and Storage Facilities

Supergas has two main logistic facilities which are used for the activity of marketing and supply of LPG: (1) storage, filling and distribution facility in Kiryat Ata in an overall area of approximately 15 dunams. This area is leased by Supergas from the Israel Land Administration. The facility includes LPG warehouses with an overall storage capacity of approximately 780 tons in bulk tanks and 250 tons in containers. Following agreements with the Ministry of Environmental Protection, recently Supergas have been actually using approximately 20% of the facility's storage capacity; (2) a central logistical center located in the Ramle industrial zone in an overall area of approximately 4.4 dunams. This area is leased by Supergas from the Israel Land Administration. The facility includes two warehouses for the storage of LPG cylinders with an overall storage capacity of 100 tons, equipment warehouses, a heating department, a workshop, a laboratory and a machining shop.

11.28.2 Real Estate Properties

The management of Supergas and the customer service center thereof operate in rented offices located in an office building in Netanya ("the Supergas Offices"). The overall area of the Supergas Offices is approximately 3,000 square meters including related areas which are used for parking and warehouses. In the office Supergas holds, *inter alia*, additional fixed assets, including computers, furniture and office equipment.

Moreover, Supergas rents lots and stores across the country which are used thereby for the needs of the branch offices thereof and authorized gas warehouses. In addition, Supergas has real estate properties, some of which are leased, some of which are rented and some of which are owned thereby and rented to third parties. Additionally, as aforesaid in Section 11.23.3 above, Supergas won land tenders and accordingly signed authorization agreements and intends, insofar as it will act in accordance with the terms of the tenders, to lease the lands.

11.28.3 Equipment at the LPG's Customers

Supergas usually lends the LPG's customers equipment which is used for the supply of LPG to the customers, such as: mobile or stationary

gas containers, meters, regulators and additional gas equipment which are installed at Supergas's customers (both the domestic customers and the commercial and institutional customers). In most cases, at the end of the engagement, the customer is required to return to Supergas the equipment lent thereto.

11.28.4 Vehicles

Supergas uses, on a current basis, a fleet of trucks for distribution of containers, integral tanker trucks for distribution of gas to stationary containers, as well as a fleet of vehicles in order to provide ongoing service to all of the customers thereof across the country.

11.28.5 Computing Systems

In managing the activity thereof in the activity segment, Supergas is assisted by an ERP system which is used for managing the Company's book, registration of the sales, follow up with customers, clearing house, tracking stocks and fixed assets, treasury and banks system, etc.

11.28.6 Gas Containers

Supergas owns approximately 500 thousand mobile gas containers and 12,000 stationary gas containers which are used thereby for the supply and sale of LPG to the costumers thereof.

11.29 **Licenses**

Supergas has a gas supplier's license from the Ministry of Energy and Water Resources, for the purchase of LPG and its marketing of LPG in movable and immovable tanks, LPG storage in movable tanks, LPG transport, LPG refilling in movable tanks and LPG storage in bulk, the purchase of LPG and marketing thereof in non-refillable tanks and the purchase of LPG and marketing thereof for gas-powered vehicles at fuellign stations. Additionally, Supergas for the Home LTD., which is a wholly-owned subsidiary of Supergas, has a gas supplier's license for the purchase of LPG and marketing thereof in movable and immovable tanks.

Supergas has permits for the construction and operation of LPG repositories across the country, including Supergas's logistic center at Ramla and Supergas's refilling, storage and distribution facility at Kiryat Atta. For the past several years, the facility at Kiryat Atta has not had a business license due to the municipality's refusal to grant a business license, as stated In this context it should be noted that on October 26, 2011, the Kiryat Atta municipality filed two proceedings against Supergas at the Court of Local Matters in the Krayot – an indictment pursuant to the Business Licensing Law against Supergas and the directors thereof for operating the gas farm absent a business license and a motion for an order for cessation of a business operation, whereby it is requested that an order be granted against Supergas, ordering it to immediately cease the gas farm operation due to the absence of a

business license. In the first proceeding, a hearing is scheduled for July 2012. In the second proceeding, after the date of the Report, on January 29, 2012, the court dismissed the municipality's motion. As to additional legal proceedings pertaining to the gas farm and the conditions required for the continuance of its operation, see Note 36 of the financial statements in Chapter C of this Report.

Each of the aforementioned licenses is for a limited period, which is stipulated in the license, and may be renewed at the end thereof. Supergas is acting both for compliance with the licenses' conditions and for their renewal upon the end of their term of validity.

In addition to such, Supergas hold vital plant certifications see Section 11.35.13 hereunder.

Super NG has been granted a license for the construction and operation of a natural gas distribution network in the central region, as defined in the license. For this matter see Sections 11.19.10 and 11.23.1 above.

Super Solar Projects Ltd., a wholly-owned (100%) subsidiary of Supergas, holds, through subsidiaries thereof and partnerships under joint control thereof, contingent licenses for the construction of solar electricity production facilities, which join the distribution network at a total scope of 20.979 MW, contingent tariff approvals for electricity production at a scope of 11.132 MW and a permanent tariff approval at a scope of 0.45 MW. All from the Public Utilities Authority – Electicity. For this matter see Section 11.23.3 above.

The contingent licenses and contingent tariff approvals are some of the stepping stones lined by the Public Utilities Authority – Electricity, toward the receipt of a permanent license for electricity production.

11.30 **Raw Materials and Suppliers**

11.30.1 Main Raw Materials Used in the LPG Segment

The main raw material in the LPG segment is the LPG. The LPG is a gas which is created during the distilling process of the crude petroleum. Supergas purchases the LPG as a finished product. After the splitting up of the refineries, the sale of BAZA to Paz and the privatization of BAZAN, Supergas purchases LPG from both refineries.

As of 2007, when both refineries started to operate separately, the control over the LPG prices was removed and in its stead control occurs by way of reporting of prices, quantities and profitability. On this matter, see also Section 1.16.7 below.

Because of the increase in the LPG consumption during the winter months and the inability of the refineries in Israel to provide such quantities, a shortage in LPG is created in the winter months. Therefore, Supergas imports LPG. The price of the imported LPG is usually higher than the purchase price thereof from the refineries in

Israel. The average import of LPG is 25% of the overall purchases of LPG by Supergas.
The Gas Regulations (Safety and Licensing) (Application of Standard 1134), 5761-2001, prohibits the production and import of LPG which does not meet the Israeli Standard 1134 (the "Gas Standard"), which is concerned, inter alia, with the composition of the LPG and prescribes the maximum permissible quantity of olefins. According to the current standard, the permissible quantity of olefins dropped and consequently, the quantity of LPG that the refineries in Israel can produce decreased.

11.30.2 Percentage of Supergas's Purchases from Main Suppliers

In 2011, 2010 and 2009, Supergas purchased from BAZAN approximately 42%, 31% and 26% of the overall LPG purchased thereby, respectively. In these years, it purchased from BAZA approximately 30% and 35% of the overall LPG purchased thereby, respectively. The balance of the LPG purchased by Supergas in these years was purchased mainly from import.

11.30.3 Manner of Engagement with Main Suppliers

Every month Supergas orders LPG from BAZAN and BAZA through an order letter. Insofar as Supergas wishes to purchase additional quantities, according to past experience, BAZAN and BAZA will agree to sell thereto insofar as they have production surpluses, in accordance with and subject to the requirements of other gas suppliers, and subject also to the provisions of the State Economy Arrangement Regulations (Legislative Amendments) (Sale of Gas by Refineries and Gas Suppliers), 5770-2009. However, sometimes, especially in the winter months, BAZAN and BAZA do not have production surpluses. Therefore, Supergas performs import of LPG independently.
The payment terms of Supergas to BAZAN and BAZA for the purchase of LPG are end of month plus 15 days. As a security for payment, Supergas pays an advance for which it is entitled to interest.

11.30.4 Dependence on Supplies and the Products for which Dependence on Suppliers exists

Supergas, like other gas companies in Israel, is dependent on BAZAN and BAZA as the major and central suppliers of LPG.

In case BAZAN and BAZA will not provide Supergas with the quantity of LPG it wishes to purchase therefrom and Supergas will be required to increase the quantity of LPG directly imported thereby, a preparation period will be required and additional costs may be involved. Such import will be subject to and contingent on finding a solution to an existing problem of lack of sufficient storage spaces for the imported LPG and possibility of the discharge thereof. However, it should be noted that BAZAN and BAZA are obligated by law to avoid discrimination in the supply of LPG to the customers thereof.

Moreover, the State Economy Arrangement Regulations (Legislative Amendments) (Sale of Gas by Refineries and Gas Suppliers), 5770-2009, prescribe the quotas which will be provided by the refineries to the gas marketing companies in months of shortage. On this matter, see Section 11.35.4 below.

11.31 **Working Capital**

11.31.1 Policy on Holding Stock of Finished Products

Due to the production limitations of LPG by the refineries in Israel which, as specified in Section 11.30.1 above, create seasonal shortage in LPG in the winter months, towards the winter months Supergas accumulates LPG stock to the extent possible. Moreover, due to the volatility of the LPG prices Supergas operates, yearlong, to manage the LPG stock thereof in an optimal manner.

11.31.2 Credit Policy

a. Customer Credit

In the segment of marketing of LPG to domestic customers, in accordance with the provisions of the law on this matter, Supergas gives the customers thereof credit for a period of end of month plus 15 days.

In the segment of marketing of LPG to commercial and institutional customers, Supergas gives the customers thereof credit for an average period of end of month plus 90 days, inter alia, in accordance with the customer's characteristics, the scope of the purchase, the state of the securities and the type of engagement therewith.

b. Supplier Credit

The major suppliers of Supergas in the activity segment are BAZAN and BAZA. These refineries give credit for a period of end of month plus 15 days.

The average of the stock days in 2011, 2010 and 2009 is approximately 46 days, 46 days and 43 days, respectively.

11.31.3 Supergas's Policy and Plans for Handling Working Capital

As of December 31, 2011, Supergas has working capital in a sum of approximately NIS 99,965 thousand comprising of current assets in the sum of NIS 375,339 thousand net of current liabilities in the sum of NIS 275,374. As of December 31, 2010, the working capital totaled in the sum of NIS 131,002 thousand comprising of current assets in the sum of NIS 345,049 thousand net of current liabilities in the sum of

NIS 214,047. The change in the working capital derived from an increase in the customers' balance due to the increase in the quantities sold and the rise in the retail price in the last quarter of 2011 net of the increase in deposits from customers, suppliers' balance and credit from bank corporations.

11.32 **Investments**

With regard to the expected investments in the facility in Kiryat Ata, see Section 11.34.4 below.

With regard to the expected investments in the construction of the distribution system of Super NG in the Central Region, see Section 11.23.1 above.

With regard to the expected investments in the construction of solar electricity facilities, see Section 11.23.3 above.

11.33 **Taxation**

In October 2009, Supergas received assessments for 2005 until 2007. In July 2011, Supergas received assessments for 2008 until 2009. On this matter, see Note 33 to the financial statements in Chapter C of this Report.

11.34 **Environmental Risks and Ways of Management thereof**

11.34.1 Material Implications of the Provisions of the Law and the Regulation regarding Environmental Protection for Supergas's Activity

The engagement in the operation segment entails many risks due to LPG being a hazardous substance both to those handling it and to the environment. Improper use or activity may cause an explosion, flare-up or poisoning on account thereof. The activity in the segment is subject to extensive regularization and control, both in primary legislation and in various regulatory provisions, whose purpose is to prevent harming the environment and to protect the public safety and the safety to employees. Such provisions of the law obligate Supergas to allocate monetary resources to handle these matters.

Following are the provisions of the law applicable to Supergas which have material implications for the activity thereof -

The Gas Law (Safety and Licensing), 5749 - 1989 - is concerned with the manner of treating LPG and LPG facilities, including imposing a licensing obligation on LPG suppliers and LPG works as well as an obligation to obtain a permit for installing LPG facilities. As aforesaid, in accordance with the provisions of this law, Supergas was granted a gas supplier license. It should be noted that this law provides the

Minister of Energy and Water Resources and the Director of Gas Safety Matters (as defined in the law) with extensive regulative, supervision and control powers. Failure to comply with the provisions of the law might constitute a criminal offense.

Hazardous Substances Law, 5753-1993 – LPG constitutes a toxin pursuant to this law. Hence, the handling of and dealing with LPG (including the storage and transportation thereof), are subject to regulation and supervision pursuant to this law. As aforesaid, pursuant to the provisions of this law, Supergas is required, inter alia, to hold a toxic materials permit in accordance with Section 3 of the law.

In this context it shall be stated that pursuant to the provisions of this law and in accordance with the requirements of the Ministry of Environmental Protection, Supergas is obligated to hold 3 different toxic materials permits –

A general toxic materials permit for Supergas and Supergas for Home Ltd., a subsidiary which is entirely owned by Supergas – for LPG trade.

A toxic materials permit for the Supergas warehouse in Ramla – for transportation, storage, trade, issuance and marketing of LPG.

A toxic materials permit for a storage and filling facility in Kiryat Ata - for storage, transportation and issuance LPG. With regard to the legal proceedings regarding this facility, see Section 11.34.2 below.

For details on the permits held by Supergas, see Section 11.35.9 below.

The Gas Order (Safety and Licensing) (Safety of Storage of Tanks and Camping Tanks in the LPG warehouse and in an Auxiliary Warehouse), 5752-1992 – imposes restrictions on Supergas pertaining to LPG storage.

National Zoning Plan 32C – This national zoning plan applies to the Kiryat Ata facility. Pursuant to such plan, the company shall perform above-ground burial of the gas containers which exist in the facility in Kiryat Ata, in accordance with the instructions, conditions and timetables determined in the plan. The expected costs for Supergas due to the performance of the instructions of the plan are estimated to be in the amount between NIS 25,000 thousand and NIS 35,000 thousand. Additionally to the aforesaid, as a condition to the receipt of a building permit for the above-ground burial of the gas tanks on the Kiryat Ata site, by virtue of N.Z.P. 32C, the local committee and the city of Kiryat Ata sent payment demands due to betterment levies in the amount of approx. NIS 59 million, fees and development levies and usage fees in the total amount of NIS 8.5 million. Supergas disagrees with the aforesaid payment demands and instituted the appropriate legal proceedings. With regard to the assessment of the chances of Supergas

with respect to such demands see Note 36 of the consolidated financial statements in Chapter C of this Report. In any event, the payment demands in respect of the betterment levies, fees and development levies are not forced on Supergas in the sense that insofar as Supergas will decide to withdraw the building permit application, no financial liability will apply thereto by virtue of the demands. However, in such a case, there is a real risk that Supergas will not be able to continue to use the facility in Kiryat Ata. For the ramifications of such an event on Supergas, see Section 11.34.4 below.
Fire department approvals – For the purpose of receipt of toxic material permits and/or licenses and permits from the Ministry of Energy and Water Resources and/or business licenses which are required for the operations of Supergas as aforesaid, Supergas is required to obtain permits from the fire departments for the various operations thereof. Supergas has a fire department approval for the Kiryat Ata facility, effective until April 30, 2012, in the context of which the facility will operate in a reduced scope as a filling and distribution facility, while reducing the quantities of LPG held, in accordance with the restrictions of the approval. It shall be clarified that the use of the facility is also subject to the obtainig of additional licenses or approvals. See also Section 11.34.2 below.

Israeli Standard 158 – The binding standard with respect to dealing with LPG facilities, including - LPG reservoirs, installing pipes and accessories, installing LPG-consuming instruments and inspections of proper working order.

11.34.2 Legal and administrative proceedings

Other than the legal proceedings pertaining to the facility in Kiryat Ata, there are no environmental claims pending against Supergas and the company is not a party to such proceedings.

Legal proceedings pertaining to the Kiryat Ata facility (HCJ 4887/10 Supergas et al. v. The Supervisor under the Hazardous Substances Law and the Ministry of Environmental Protection) – until the end of June 2010, Supergas had the toxic materials permit which is required for the operation of the facility in Kiryat Ata. In June 2010, the supervisor under the Hazardous Substances Law and director of the Haifa district at the Ministry of Environmental Protection notified that he decided not to renew the toxic materials permit for the gas farm of Supergas in Kiryat Ata, primarily because Supergas had not yet commenced the actual performance of the burial of the gas containers at the facility according to the instructions of N.Z.P. 32C.

Pursuant to such decision, in June 2010, Supergas filed a petition with the Supreme Court against the aforesaid decision. In the context of the petition it was argued that the supervisor's decision was tainted by severe administrative flaws, and that the decision was unreasonable and issued without authority, since it contradicts the national zoning

plan which has the status of secondary legislation. The High Court of Justice was moved to issue an interim injunction and an order nisi ordering the cancellation of the decision pertaining to the non-renewal of the toxic materials permit of Supergas at the gas farm in Kiryat Ata, and ordering on the renewal of the toxic materials permit.

The Supreme Court issued a temporary interim injunction which stays the effect of the supervisor's decision not to renew the toxic materials permit of Supergas, and left the current toxic materials permit in effect. Recently, the National Roads Company of Israel was added, at its request, to the proceeding. On January 30, 2012, a judgment was issued which rejected the petition of Supergas and hence the toxic materials permit of Supergas for the gas farm in Kiryat Ata was cancelled. In the absence of such a permit, Supergas shall not be able to continue to operate the gas farm in the regular format. The aforesaid notwithstanding, pursuant to the conduct of Supergas vis-à-vis the Ministry of Environmental Protection, the Ministry's approval was obtained for the continued operation of the gas farm in a reduced format in the outline which was specified in the approval. On March 1, 2012, the gas farm was issued a toxic materials permit effective until May 1, 2012, which permits Supergas to use the facility subject to conditions which were specified in the permit. In addition, Supergas believes that both in the short term and in the long term, solutions will be found for LPG storage and filling, and it is preparing to find temporary and long-term alternative solutions, subject to the provisions of the law, which will enable it to continue to provide services to its customers.

The aforesaid is forward looking information, based on the company's assessments based on the assessments of the managements of Granite and Supergas. There is no guarantee that a long-term alternative solution will be found, or that the cost thereof shall be worthwhile to the company.

In addition, it shall be stated that it has been several years since the facility in Kiryat Ata had a business license, due to the refusal of the local authority to issue such a business license, see also Section 11.29 above.

11.34.3 <u>The policy of Supergas in the management of environmental risks</u>

Supergas takes many steps and invests many resources for the purpose of preventing damage to the environment and preventing environmental risks. In such context, Supergas acts, in a current manner, to maintain a quality system for the enhancement of safety among its employees, customers, suppliers and third parties, and to prevent LPG events and accidents, and – for fast, efficient and damage-mitigating actions in the event of LPG events, accidents and problems.

For such purpose, inter alia, Supergas has International Standard OHSAS 18001and Israeli Standard ISO 9001.

Supergas operates in a current manner to implement and fulfil the provisions of the law and the regulation which are applicable thereto, including – the instructions and guidelines of the Ministry of Energy and Water Resources and the Ministry for Environmental Protection. Supergas also maintains continuous contact with the local authorities that are relevant to its operations, the fire department and any other relevant authority, all, in order to prevent damage to the environment and reduce potential environmental risks.

11.34.4 Environmental costs

Supergas invests resources in order to comply with the provisions of the law which apply thereto on the issues of environmental protection, licensing and safety at work.

The investments of Supergas in such areas which are performed for the purpose of the prevention or reduction of damage to the environment, are performed in a current manner, as an integral part of the operations thereof.

Below shall be specified the investments in such areas in the period of the Report (which may be isolated):

(1) Costs of inspections of proper working order of the LPG systems at customers of Supergas – approx. NIS 2,500 thousand; (2) Costs of pulling out, inspection, repair and replacement of old containers – the amount of approx. NIS 12,000 thousand; (3) Costs of compliance with the instructions and requirements of the fire departments - the amount of approx. NIS 500 thousand.

Below shall be specified the main investments in such areas, which are expected in the year 2012 and in subsequent years:

(1) Costs of inspections of proper working order of the LPG systems at customers of Supergas – the amount of approx. NIS 2,500 thousand (in each one of the years); (2) Costs of pulling out, inspection, repair and replacement of old containers – the amount of approx. NIS 12,000 thousand (in each one of the years); (3) Costs of compliance with the instructions and requirements of the fire departments - the amount of approx. NIS 500 thousand (in each one of the years).

Costs of performance of above-ground burial of the gas containers at the facility in Kiryat Ata – in 2012: approx. NIS 15,000 thousand, in 2013: approx. NIS 10,000 thousand up to NIS 20,000 thousand.

Risk of termination of the operation of the gas facility of Supergas in Kiryat Ata for any reason – The company is preparing for a situation

which may be created in which the operation of the facility in Kiryat Ata, which is essential for the operation of Supergas, will be terminated. As aforesaid, pursuant to the conduct of Supergas vis-à-vis the Ministry of Environmental Protection, the Ministry's approval was obtained for the continued operation of the gas facility of Supergas in Kiryat Ata in a reduced format in the outline which was specified in the approval. Nevertheless, Supergas estimates that an event of termination of the operation of the facility as aforesaid, may lead to amortization of fixed property in the books in the amount which shall not exceed NIS 2 million. In addition, such an event may cause significant operational difficulties which may lead to an increase in the company's operational expenses, however, the examination of the scope of the expenses has not yet been completed and at this stage, the cost thereof cannot be estimated. Nevertheless and as stated above, Supergas believes that both in the short term and in the long term solutions will be found for LPG storage and filling, and it is preparing to find temporary and long-term alternative solutions, subject to the provisions of the law, which will enable it to continue to provide services to its customers.

The information contained in this Section 1.32 is forward looking information, as defined in the Securities Law, which is based on information which is known to the company based on information which is known to the managements of Granite and Supergas on the date of the Report, on the company's assessments based on subjective evaluations and assessments of Granite and Supergas considering the past experience thereof and their intentions and plans on the date of the Report which may not materialize in the event that changes will occur in the markets in which Supergas operates and/or in the plans and intentions of Supergas as aforesaid, for any reason, including – the market structure, statutory and regulatory arrangements in the field, competition, assessments of Supergas in respect of the business merit or due to the materialization of any of the risk factors which are specified in Section 11.80 below.

11.35 **Restrictions on Supergas'soperations and supervision thereof**

The operation of Supergas in the LPG field is subject to laws, regulations and orders which pertain, inter alia, to the determination of specific instructions pertaining to marketing and supply of LPG to domestic customers, to the determination of standards of quality, safety, security, storage, marking and identification of products, transportation, proper business management, consumer protection, environmental issues and price supervision, the essence of which is reviewed below.

11.35.1. Gas Law (Safety and Licensing), 5749-1989

The aim of the law is to regulate the issue of gas supplier licensing and the issue of safety in dealing with gas.

The law sets forth a duty to obtain a permit to install gas facilities (in other words: for each facility which does not serve for self consumption or a self consumption facility whose capacity exceeds 10 tonnes for a residential area and 20 tonnes for an industrial or agricultural area). In addition, the law mandates performance of an inspection of the proper working order of a consumer's gas facility prior to the commencement of the gas supply to the consumer. In addition, the law determines an obligation of the gas supplier to obtain a gas supplier license, and an obligation of anyone who engages in gas work to obtain a gas work license.

The law mandates an obligation to perform a periodic inspection of the proper working order for each gas consumer once every 5 years, and to take out a liability insurance which grants coverage in the amount of at least $5 million.

11.35.2. Arrangements in the State's Economy Law (Legislative Amendments), 5749-1989

The law created the first reform in the gas market, in the context of which the gas market was opened to competition.

The law determines that a gas consumer is entitled to disconnect, at all times, from his gas supplier, and move to a different gas supplier (also if the contract between them includes a long term engagement). According to the case law, this section enabled a one-time disconnection of all types of consumers from their gas suppliers at the time of its enactment. Thereafter, the provisions of the sections were set forth as a fixed arrangement with regard to domestic consumers, however, it does not apply with regard to commercial consumers.

This law was amended once more in the context of the second reform in the beginning of 2008 and currently includes also the provisions of that reform. In this regard see Section 1.33.5 below.

11.35.3. The Land Law, 5729-1969 and the Land Law (Replacement of a Gas Supplier in a Condominium), 5751-1991

The law determines the manner of replacement of a gas supplier in central gas systems. The law determines, inter alia, that a replacement of a gas supplier for a central gas system in a condominium may be performed at all times with a majority of 51% of apartment owners, that the outgoing gas supplier is obligated to dismantle the gas facilities thereof within 15 days from the date of receipt of the notice, and that the outgoing gas supplier is obligated to return the deposit which the consumers deposited within 30 days from the date of receipt of the notice.

This law was amended once more in the context of the second reform in the beginning of 2008, and currently also includes the provisions of that reform. In this regard see Section 1.33.5 below

11.35.4. Arrangements in the State's Economy Regulations (Legislative Amendments) (Gas Economy – Replacement of Gas Supplier), 5751-1991

The regulations determine the manner of replacement of a gas supplier at private customers, including ones who are not connected to a central gas system.

The regulations determine, inter alia, that a domestic gas consumer can inform his gas supplier, at all times, of his wish to disconnect therefrom, and that upon receipt of the notice, the outgoing gas supplier is obligated to dismantle the borrowed equipment thereof within 10 days. If it shall have failed to do so, the consumer may (including through the incoming supplier) do so himself. In addition, the regulations include a prohibition on the collection of a payment/fine by the outgoing supplier due to the consumers' disconnection.

11.35.5. Gas Economy Law (Promotion of Competition in Gas for Domestic Consumption) (Legislative Amendments), 5768-2008

In the context of this law, a reform, the purpose of which is to promote competition, which included a modification of several laws and regulations, was approved in the gas market. The main points of the reform are: (1) A prohibition on engagement and offering benefits to a consumer who delivered, to the outgoing gas supplier, a notice on his decision to replace a gas supplier. Such prohibition shall be in effect for six months from the moment of receipt of the notice on the replacement of a gas supplier as aforesaid; (2) The granting of an option, to an incoming gas supplier, to purchase the gas containers from the outgoing gas supplier at a price which shall have been determined by a price committee; (3) Requiring a nation-wide gas supplier to supply gas to a domestic consumer in the area where it supplies gas under similar conditions to the conditions under which it supplies gas to a similar consumer; (4) Cancellation of the exclusivity which was conferred on a gas supplier pursuant to the legal situation which prevailed prior to the enactment of this law, to supply gas in the first year once a gas system was activated; and (5) A prohibition on the inclusion of conditions in a gas purchasing contract which hamper the consumer's ability to replace the gas supplier.

11.35.6. Supervision of Product and Service Prices Law, 5756-1996, and the regulations thereunder

The Supervision of Product and Service Prices Law, 5756-1996 (the "Price Supervision Law") enables the minister in charge, inter alia, to apply the provisions of this law, in an order, to a specific service or product which fulfils the grounds which were determined in the law as justifying price supervision. Among such grounds are the grounds whereby the product or service is essential and there is a need to supervise its price due to public interest considerations.

There are many orders which were issued by virtue of the Price Supervision Law with regard to the dealing with LPG. Such orders include various instructions pertaining to the safety and quality of the service to the customer (such as: the obligation of an identifying mark of the company on the gas tank, prohibition to supply gas to an unsafe location, length of time of arrival to the customer after a call, dates of customer payments, instructions pertaining to the amount of the deposit which a gas supplier is entitled to collect, rates of increasing the same, and instructions regarding the return of the deposit to the customer etc.).

In the context of the legislation in this area, the Stability in Products and Services Order (Temporary Provision) (Maximum Prices for Petroleum Products), 5756-1996, was also enacted, which determines, inter alia, that the price which the gas supplier collects for the LPG also includes various related services which are specified in the section, and no additional payments shall be collected thereon (such as: a call to treat a gas leakage; transportation of gas tanks to the customer's house; replacement of a gas pipe; periodic inspection of proper working order; services related to collection of gas invoices including bank fees; insurance).

11.35.7. Supervision of Oil refinery prices

11.35.7.1. Supervision of Products and Services Order (Maximum LPG price ex-ORL) (Amendment), 5766-2006

Pursuant to the order (the "New LPG Order") which was amended for the second time in 2008, in the Supervision of Product and Service Prices Order (Maximum LPG price ex-ORL) (Amendment), 5768-2008, subject to the conditions determined therein , in 2007, the supervision through the determination of a maximum price for LPG, of the oil refineries, was removed, and instead, supervision exists through reporting profitability, prices and quantities, under the assumption that at least two oil refineries will operate in the country, each owned by a different body, and without there being any cooperation between them in the sale system. In the event that the oil refineries will fail to fulfil the reporting duties which apply to them in respect of the quantities of petroleum products and prices thereof, or if it will transpire that the oil refinery sold LPG at a price which exceeds the import price in the month before the month in which the sale was performed, or that the oil refinery supplied LPG to different consumers, at a different price, on the same date, the supervision of the Maximum LPG price ex-ORL shall apply again.

Supervision of prices of services which are received by Supergas – Pursuant to the Notice on Supervision of Product and Service Prices (LPG Issuance Prices), 5768-2008, there

is a tariff for the price of the services of issuance of LPG by the oil refineries.

11.35.7.2. Supervision of Product and Service Prices Order (Application of the Law to LPG), 5770-2010

On April 18, 2010, this order was published, which determined that the level of supervision of LPG shall be reporting on profitability and prices pursuant to Chapter G of the Price Supervision Law. In accordance with the aforesaid order, in May 2010, the manner of reporting on LPG profitability was published, while in accordance with the provisions thereof, the gas marketing companies, including Supergas, shall provide data to the supervisor of prices, each year, as provided in the manner of reporting on the profitability.

In this context, of supervision of the LPG prices, the report of the committee for social economic change (the "Trajtenberg Committee") was published, in the context of which the Trajtenberg Committee proposed, in the short term, to impose supervision on the LPG prices ex-refinery and to the consumer, which would lead to a reduction in its price. At the same time, the Trajtenberg Committee proposed to put together a government team which would propose an additional reform in the LPG sector, based on assurance of free access to containers, to increase competition – the aforesaid, as argued by the Trajtenberg Committee, in view of the limited success of the last reform in the industry.

On December 18, 2011, the government deliberated, inter alia, the promotion of competition in the LPG market. In the context of this deliberation the government decided, pursuant to the Trajtenberg report, as follows: (1) To instruct the price committee, which operates pursuant to the Price Supervision Law, to examine the required level of supervision over the LPG sale price ex- refinery, including the maximum supervised price. It was further decided that in the context of the examination of the need to impose supervision on the LPG marketing margin, the various marketing segments should be addressed, including marketing gas to the institutional market, marketing domestic gas in containers, and marketing domestic gas in mobile tanks. (2) To instruct the Minister of Finance and Minister of Energy and Water Resources, based on a recommendation of the price committee, if any, to determine in an order under the Price Supervision Law that the LPG marketing margin shall be supervised. The ministers shall make a decision in connection with the recommendations of the price committee. (3) To put together an inter-office team headed by the Fuel Administration and with the participation of representatives of the Ministry of Finance, Industry, Trade and Labor, Justice and the Antitrust Authority, in order to formulate arrangements to increase the competition in LPG marketing, while instructing the team with regard to arrangements which should be examined.

As of the date of release of the Report, it has not been decided whether such supervision will be imposed. Insofar as supervision will be imposed it is unclear how it will be imposed and what its ramifications will be. Hence, the Company cannot anticipate what the effect of the supervision will be on the Company, if and insofar as it will be imposed.

11.35.8. Arrangements in the State's Economy Regulations (Legislative Amendments) (Sale of Gas by Oil Refineries and Gas Suppliers), 5770-2009

The aforesaid regulations regulate the issue of LPG sale by the oil refineries. Pursuant to the aforesaid regulations, the oil refinery is entitled to sell gas only to a gas supplier who has a gas supplier license. In addition, the refinery shall notify in advance, according to the provisions of the regulations, what is its supply capacity forecast and the manner of ordering gas by the gas suppliers.

The regulations define who are new, small, and large gas suppliers and accordingly, what are the gas allocations for such suppliers in months of shortage, in other words, during months when the oil refinery is unable to supply the full gas demand therefrom.

The regulations further determine reporting duties of the oil refineries and the gas suppliers to the person appointed by the Minister of Infrastructures as the director for gas safety issues.

11.35.9. Hazardous Substances Law, 5753-1993

Supergas has a general toxic materials permit for the operations thereof and for its facilities which need a toxic materials permit as required by this law. In this regard see also Sections 11.34.1 and 11.34.2 above.

11.35.10. The Weights and Measurements Ordinance

The Weights and Measurements Ordinance, 1947, determines different standards for weights and measurements. By virtue of this ordinance regulations were promulgated which determine, inter alia, various instructions regarding LPG measuring instruments which are affixed to tankers and the installing of a calibration stamp on such instruments. It is prohibited to use such instruments unless they are calibrated and stamped in accordance with the regulations.

11.35.11. Miscellaneous bills

As of the date of release of the Report, there are several bills pending which, if the same will be passed, each one may have an effect on the field of operations. And they are: (1) The Gas Bill – The Gas Law (Safety and Licensing) (Amendment), 5771-2011; (2) The Fuel Market Bill, 5771-2011; Fuel Market Bill for the regulation of the fuel market in Israel; (3)

Arrangements in the State's Economy Regulations (Legislative Amendments) (Delivery of Information Pertaining to Gas Supply), 5772-2011; and (4) Arrangements in the State's Economy Regulations (Legislative Amendments) (Similar Conditions Regarding Unreasonable Refusal), 5772-2011.

11.35.12. Transportation licenses

In its operations in the LPG field, Supergas, both itself and through subcontractors, transports LPG which, as aforesaid, is deemed a hazardous substance. For purposes of this activity, Supergas holds a suitable transportation license and a license to transport hazardous substances in accordance with the Traffic Regulations.

11.35.13. Essential enterprise

Supergas holds an essential enterprise approval. According to such approval, in times of emergency, the automobile fleet and issuance and filling facilities thereof are recruited for the benefit of the Market in an Emergency, in order to enable regular LPG supply.

11.35.14. Antitrust

Internal enforcement plan – Since 1999, Supergas participates in the internal enforcement plan on behalf of the antitrust authority (in this section, the "**Antitrust Authority**"). In 2009, Supergas updated the internal enforcement plan and it operates in accordance with an outline which was defined in the context thereof for effective and efficient internal enforcement of the provisions of the Antitrust Law, 5748-1988, regulations and orders which were issued thereunder. On August 10, 2010, a team of the Antitrust Authority arrived at the offices of Supergas to perform a search regarding Afikei Gas Ltd., 50% of which is held by Supergas. Supergas cooperates, insofar as required. In addition, several officers were investigated on the issue. On March 19, 2012, Supergas's counsel received notice (the "**Notice**") that the Antitrust Authority had decided to file an indictment against Supergas and three officers thereof, claiming non-delivery of information, documents, ledgers or certificates that were required by the entity authorized by the Antitrust Authority. It shall be clarified that Supergas intends to voice its claims in writing against the filing of the indictment in accordance with the right granted thereto in the Notice, and that it believes that it has good claims. It shall be clarified that it is not at all certain that the Antitrust Authority will accept Supergas's objections, in whole or in part, and that an indictment will indeed not be filed against Supergas and three officers thereof or what the outcome of the proceeding will be. For further

details, see Note 44 to the financial statements.

11.35.15. Supplier which is recognized by the Ministry of Defence

For purposes of supplying Supergas products to the Ministry of Defence, Supergas was required to fulfil specific criteria, including of security, which, after the examination of its fulfilment thereof, Supergas received an approval that it is a supplier which is recognized by the Ministry of Defence. Pursuant to such approval, Supergas is entitled to supply its products to the Ministry of Defence. It shall be stated that such an approval is limited in time, and ought to be renewed as required.

11.35.16. Standardization and quality control

Supergas markets its products according to various standards which are relevant to the marketing and supply of LPG which are published from time to time by virtue of the Standards Law, 5713-1953. The standards specify technical requirements which apply to products, including with regard to product specification, methods of production, storage, issuance, operation, etc.

In addition, Supergas holds certification for Quality Standard ISO 9001-2000 and Safety Standard OHSAS 18001

11.36 **Environmental protection**

11.36.1 Regarding the legislation and standardization on the issue of environmental protection, see Section 11.34.1 above.

11.36.2 Subject to the aforesaid, to the company's best knowledge based on information which was delivered thereto by the managements of Granite and Supergas, as of the date of the Report, Supergas complies with the requirements of the described laws and regulations.

The Tambour Segment

11.37. General information

The Granite Group operates in the paint and building finishing industry through Tambour Ltd. and its consolidated companies (the "**Tambour Group**" or "**Tambour**"). The Tambour Group operates in the manufacture, import and marketing of a broad range of paints and auxiliary materials, as listed below and is Israel's leading group in the field of paints and coatings. Tambour is also one of Israel's leading companies in the field of advanced construction materials.

As of the Date of this Report, Tambour is a public company whose shares are traded in the Yeter Index on the TASE

Within this segment, the Tambour Group operates in the five sub-segments described below:

(1) The domestic paint segment – This is the principal business of this operating segment (some two thirds of Tambour's businesses). (2) Domestic supplementary products segment – These business include cement based building products, various types of sealing products, additives, grout, paint emulsions, adhesives, adhesive compounds for the paint, textile and paper industries, decorative tiles, etc. (3) Printing inks segment local – As part of this business, the Tambour Group manufactures and imports various types of printing inks used mainly by the printing house industry. (4) Plaster and dry construction segment – local - in this framework Tambour manufactures and markets, through the Gypsum Gesher Company, building finishing products based mainly on gypsum and manufactured by the plant at Kibbutz Gesher in the Jordan Valley. During 2008, Tambour began establishing a plant manufacturing gypsum boards and blocks - on a site in the south of Akko and in March 2010, construction was completed and the plant began its activity. Furthermore, in 2009 Tambour began importing and marketing acoustic ceilings, insulation products and complementary products for the gypsum segment. (5) International marketing segment – This segment includes the international marketing activity of the sub-segments of the activity as described above, vis-à-vis local customers who purchase the products in order to export the same.

In the year of the Report, the following changes occurred in the context of the business of the Granite Group in this operating segment: Income from outside parties from paint products – local - rose by approx. 6% and the profitability decreased by 9.5%. The income from outside parties from the supplementary products - local - rose by approx. 58% and the profitability increased by 7%. The income from outside parties from printing inks products decreased by approx. 18% compared with the scope of revenues in the previous year and the profitability increased by approx. 6%. The income from gypsum and dry construction products rose significantly by 52% due to the

commencement of the activity of the gypsum plant in March 2010. Operational profitability significantly improved. Revenues from international marketing rose by approx. 2% and the profitability rate remained significantly similar to the previous year.

The critical success factors in this operating segment are: improvements in the security and economic situations, Tambour's branding as a leader, the high quality of Tambour products, Tambour's entry into the dry construction industry and the successful introduction of new gypsum products, innovation, service levels, new growth engines and synergy between the sub-segments in the area of activities.

To the best of the Company's knowledge, based on the best of Tambour management's knowledge, in the external coatings segment, there are alternatives to the products, such as stone, aluminum, glass, etc. In the wall paints segment, the alternative is wallpaper. However, such are not alternatives, which when purchased by consumers, will have a material effect on this operating segment.

As pertains to the structure of the competition in this segment, see Section 11.23 below.

As pertains to regulatory restrictions applicable to this segment, see Section 11.31 below.

11.38. **The Products**

11.38.1. Below are Granite Group's principal products in this operating segment:

Paints – Paint is described as a mixture of materials that are intended for smearing or spraying on various surfaces in order to coat them. After the paint dries on the surface, the paint serves as protection against the hazards of time and nature and to provide an esthetic appearance. Paints are categorized by their usages, which are *inter alia*, as follows: Wall paints, metal paints, powder paints, paint for the wood industry, wood paints and oils for domestic use, road marking paint, vehicle paints, thinning products for wood and metal paints, filler products and supplementary paint accessories.

Supplementary products - This range of products includes: (1) Sealing materials – coatings to seal roofs, verandas, etc. (2) Adhesives for construction, adhesives for industry, contact glues for wood and carpets, PVA adhesives for the paper, cardboard and wood industries, plastic adhesives and contact adhesives for home and office uses. In addition, Tambour markets cement adhesives for the building industry. (3) Liquid additives used in plaster mixes and the import of powdered additives for the building industry. (4) Adhesive

compounds for the paper, glue and textile industries. (5) Decorative and sealing tiles for internal and external use. (6) Polymer emulsions, which are used as binders and as bases in the manufacture of paint for construction, for coatings and textile (7) cement-based and acrylic-based construction materials – cement-based products for the construction sector, such as powdered glues for tiles, rapidly-drying concrete products, products for concrete infrastructure fortification and acrylic-based construction materials.

Printing inks – These products include various types of printing inks used by the different processes used to print on different surfaces as used by the cardboard, paper, packaging and plastics industries and printing shops. In addition, Tambour manufactures thinners, a range of cleaning products and additional supplementary products for the printing industry.

Gypsum and dry construction – Finishing products for the construction industry based mainly on natural gypsum, such as: gypsum boards, gypsum blocks, insulation products, acoustic ceilings, cement boards, gypsum plaster, white gypsum, powdered fillers, adhesives etc., as well as supplementary products to the dry construction segment that are marketed in the local market.

11.38.2. Expected material changes to Tambour's share and mix

In the year of the Report, there were no material changes in the market or characteristics of the customers of the operating segments. The Granite Group management does not expect any significant changes in market demand or the product mix in this segment.

The information in this Section includes forward-looking information as defined in the Securities Law. Forward looking information is uncertain information about the future, based on the information extant at the Company on the Date of this Report and including estimates of the Company, based on the best knowledge of Granite management on the Date of this Report and *inter alia*, on past experience and accumulated knowledge of the subject matter. Actual results might differ materially from the results as forecasted or as inferred from that information. Furthermore, the Company's estimates, based on the best knowledge of Granite management which served as the basis for the presentation of the information as aforementioned might prove to be incorrect and/or materially different from those considered.

11.39. **New Products**

In 2011, the marketing of a number of new products began in this operating segment, the most important of which are: Terrano Acrylic Coating – colored acrylic coating for external and internal use, mineral-like, Negbah – sand-textured coating paint, Hofit – delicate-textured acrylic coating, Cashmere – velvet-like prestigious metallic effect, Glittering Safari –glittery sand paint, paint for parking spaces, linen oil – used for wood articles in the garden, , glittery metal Hammertone - metal paint in various shades for direct painting over metal, various lacquer paints, concrete additives, insulation and filling foam, various glues and various emulsions for industrial use, external plasterboard, high evaporation plasterboard, thick board and more.

11.40. **Customers**

In this segment, Tambour is not dependent upon a single customer or a small number of customers, the loss of which could have a material effect on this industry.

11.40.1. Segmentation of sales per customer type

The following table gives the segmentation of sales and their relative part in total sales in this operating segment, according to customer type and distribution by type of products in this operating segment:

In 2011

Total		International Marketing Sales		Domestic Sales of Printing Ink		Domestic Sales of Gypsum and Dry Construction		Domestic Sales of Supplementary Products		Domestic Paint Sales		Type of Customer
%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	
56%	435,371	-	-	-	-	83%	127,694	39%	37,371	58%	270,306	DIY chains, building material stores (color mixing systems) and contractors
34%	261,015	6%	1,583	-	-	17%	25,358	60%	57,771	38%	176,303	Wholesalers, institutional and industrial customers
4%	27,896	94%	27,896	-	-	-	-	-	-	-	-	Export
3%	24,415	-	--	100%	24,415	-	-	-	-	-	-	Print Shops
3%	22,108	-	-	-	-	-	-	1%	422	4%	21,686	Miscellaneous customers
100%	770,805	100%	29,479	100%	24,415	100%	153,052	100%	95,564	100%	468,295	|**Total:**

In 2010

Total		International Marketing Sales		Domestic Sales of Printing Ink		Domestic Sales of Gypsum and Dry Construction		Domestic Sales of Supplementary Products		Domestic Paint Sales		Type of Customer
%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	
53%	359,504	-	-	-	-	81%	81,942	38%	31,489	56%	246,073	DIY chains, building material stores (color mixing systems) and contractors
34%	235,330	2%	630	-	-	19%	18,982	61%	50,680	37%	165,038	Wholesalers, institutional and industrial customers
4%	28,306	98%	28,306	-	-	-	-	-	-	-	-	Export
4%	29,840	-	--	100%	29,840	-	-	-	-	-	-	Print Shops
5%	31,218	-	-	-	-	-	-	1%	1,044	7%	30,174	Miscellaneous customers
100%	684,198	100%	28,936	100%	29,840	100%	100,924	100%	83,213	100%	441,285	**Total:**

In 2009

Total		International Marketing Sales		Domestic Sales of Printing Ink		Domestic Sales of Gypsum and Dry Construction		Domestic Sales of Supplementary Products		Domestic Paint Sales		Type of Customer
%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	%	NIS in thousands	
50%	287,227	-	-	-	-	100%	39,255	34%	24,902	57%	223,069	DIY chains, building material stores (color mixing systems) and contractors
35%	201,629	7%	2,211	-	-	-	-	66%	49,235	38%	150,183	Wholesalers, institutional and industrial customers
5%	28,821	93%	28,821	-	-		-	-	-	-	-	Export
6%	33,802	-	-	100%	33,802		-	-	-	-	-	Print Shops
4%	20,882	-	-	-	-	-	-	-	33	5%	20,850	Miscellaneous customers
100%	572,361	100%	31,032	100%	33,802	100%	39,255	100%	74,170	100%	394,102	|**Total:**

Granite has no revenues from a principal customer in this operating segment, the revenues from which constituted 10% or more of the Granite's total sales.

11.41. **Marketing and distribution**

The Tambour Group invests in a variety of marketing activities, including *inter alia*, Beit Tambour – Located in Bnei Brak, which is Israel's largest color design center; advertising and public relations; the presence of paint consultants at DIY chain stores and advertising at sales points; demonstrations and guidance, activities aimed at building and refurbishing industry professionals, operation of a telemarketing array, management and maintenance of an internet information service website, in the gypsum segment Tambour has a sales and service team which operates in stores and vis-à-vis professional audience, and more.

This segment also includes product export activities, mainly under the Tambour brand name. In specific markets, some Tambour products are sold under customers' private brand names. Tambour markets to more than 20 countries, in which it mainly operates purchasing bodies (such as local paint companies), distributors and local sales agents, some of which have signed agreements with Tambour. Local distributors and sales agents are responsible for promotion, marketing and sales of products. Sometimes, agreements grant distributors and sales agents exclusivity rights for the distribution and selling of certain products within the territory of the relevant country.

In general, agreements with the distributors and agents are drawn up based on orders and in accordance with the payment conditions as agreed by the parties and. As pertains to distributors, contacts with customers are solely made through the foreign distributor. Payments for goods are not conditional upon the sale of the products by the distributor and the distributor constitutes the final customer from the Tambour Group's point of view. Occasionally, such agreements include the payment of a fixed sum for sales promotions.

11.42. **Competition**

To the Company's belief, based on the best knowledge available to and estimates of Granite Group's management, Tambour is a significant factor in the paint and building-finishing segment, which is exposed to fierce, vibrant competition from a number of local manufacturers and importers competing against Tambour principally within the borders of the Israel and the Palestinian Authority. In the opinion of the Company's management based on the best knowledge available to the Granite Group's management, there are no barriers to entry to those segments in which Tambour is involved in Israel, with the exception of the paint products market, which is mostly branded and requires considerable investment in the establishment of brand identity and considerable investment in advertising and color mixing machines and,

in the gypsum board and block sub-segment, requiring investment in the establishment of a manufacturing plant.

In the paint sub-segment, Tambour's main competitors are: Nirlat Ltd, Jacoby Jack and Sons Ltd.; B.G. (Israel) Technologies Ltd.; Delek Oil – Delokol Ltd., Epolac (Eng.Y. Zamlar) Ltd.; Bahak A. Shoshani Ltd.; Denber Paints and Cotatings Israel Ltd.; Decoline Decorative Coatings Ltd. and Nadir Paint Industries Ltd..

In the supplementary products sub-segment, Tambour's main competitors are: Carmel Resins Ltd.; Carmit Construction Improvement Products (1982) Ltd.; B.G. Polymers Ltd.; Termorkir Industries (1980) Ltd.; Sika Plast Industries Ltd., Polystick Ltd.; A.Z. Insulation and Coating Materials Marketing Ltd.; Pazkar Ltd.; Bitum Petrochemical Industries Ltd., Yehezkel Aharon Ltd. and more.

In the printing inks sub-segment, Tambour's main competitors are: Chemiprint Ltd.; Niri Raw Materials and Equipment Agencies Ltd.; Paintone Ltd.; Bloyar Inks Ltd. and Blucolor Ltd.

In the gypsum sub-segment, Tambour's main competitors are: Orbond Gypsum & Gypsum Products Industries Ltd, Carmit in the Ytong Industries Group; Termokir (1980) Ltd. and Irland Peles Ltd., S. Cohen Metal Works Ltd. and Judea International Export Import (1971) Ltd..

Utilizing the best of Tambour management's knowledge, the Company cannot estimate its market share for the aforementioned products.

Tambour implements a number of different measures in order to deal with competition, including brand reinforcement, expanding and safeguarding knowledge, maintenance of high product quality and investment in constant improvement of the Company's products and the expertise of Tambour's sales force and its customer service array.

11.43. **Production capacity**

Tambour's production arrays are concentrated at six sites: In the Akko area (South Akko and Askar), in the Ashkelon area, the Jordan Valley, at Migdal Ha'Emek as well as a production plant in Nizanei Oz.

11.43.1. The paint segment

The south Akko facility has a potential production capacity of 50,000 thousand liters of paint annually working two shifts and 65,000 thousand liters of paint annually working three shifts. In practice, in the years 2011, 2010 and 2009, Tambour manufactured at this site approx. 39,000 thousand liters, approx. 37,000 thousand liters and approx. 32,900 thousand liters of paint, respectively.

The Askar facility has a potential production capacity of some 7,000 thousand liters of paint and 600 thousand kg of

powders annually working two shifts or 10,000 thousand liters of paint and 900 thousand kg of powders annually working three shifts, depending on the composition of the product range. In practice, in the years 2011, 2010 and 2009, Tambour manufactured at this site approx. 8,400 thousand liters, approx. 7,700 thousand liters and approx. 6,800 thousand liters of paint, respectively. In addition, approx. 400 thousand kg, approx. 400 thousand kg, and approx. 300 thousand kg of powders, respectively.

The David Powders facility at Migdal Haemek has a potential production capacity of approx. 1,400 thousand kg of powders annually. In practice, in the years 2011, 2010 and 2009 Tambour manufactured at this site approx. 1,200 thousand kg. of paint, approx. 1,100 thousand kg of paint and approx. 1,000 thousand kg of paint respectively.

11.43.2. The supplementary products segment

The facility at the Serafon site has a potential production capacity of 20,000 thousand kg annually working two shifts and 30,000 thousand liters annually working three shifts. In practice, in the years 2011, 2010 and 2009, Tambour manufactured at this site about 15,000 kg, about 16,000 thousand kg and about 16,000 thousand kg, respectively.

In addition, Tambour has a facility in Nizanei Oz for the manufacture of construction powders (Tambour Building Keshet). This facility began to operate in 2010. The potential production capacity is 1200 thousand kg and in practice Tambour manufactured approx. 600 thousand kg in 2011.

11.43.3. The printing inks segment

The Tzah facility operated at Be'er Tuvia until June 2010, and as of same month was transferred to a site in Ashkelon. The facility specializes in the manufacturing of ink prints of various types and is mostly operated on a one-shift basis. Its potential production capacity is 3,700 thousand kg of inks annually working three shifts. In practice, in the years 2011, 2010 and 2009, Tambour manufactured at this site approx. 1,200 kg, approx. 1,300 thousand kg and approx. 1,400 thousand kg, respectively.

11.43.4. The gypsum and dry construction segment

The facility's production capacity is some 45,000 thousands kg working three shifts. In the years 2011, 2010 and 2009, the plant manufactured approx. 39,300 thousand kg, approx. 35,600 thousand kg and approx. 35,000 thousand kg, respectively. The Tambord plant is situated in the south

Akko siteand manufactures gypsum boards and blocks. The plant began production in March 2010, and it is still in development and optimization stages. During 2011, the plant manufactured, *inter alia*, white, green, pink and blue gypsum boards, which are fit for various uses, as well as gypsum boards for external use. The maximum production capacity of the plant depends on the products manufactured at that time. Calculated on average, the potential production capacity is approx. 150,000 tons of gypsum boards and blocks. In 2011, approx. 101,000 tons of gypsum products were produced by the plant.

11.44. **Fixed assets and facilities**

Tambour's property is used entirely for the manufacturing and distribution systems.

11.44.1. The paints segment

The main manufacturing site for this segment is at south Akko and it is on land owned by Tambour with an overall area of some 108,000 sqm, of which some 78,000 sqm, serves the purposes of the paint segment. The site includes a number of buildings with an overall constructed area of about 37,360 sqm. The land is mortgaged to the banks on a first and equal charge.

The Tambour Group has additional manufacturing sites, including the Askar site in south Akko which is situated on land located south of Akko of a total area of approx. 53,200 sqm, upon which are built various buildings with a total constructed area of about 19,500 sqm. Tambour has non-capitalized leasing rights from the Israel Lands Administration, which will end in 2039.

11.44.2. The supplementary products segment and the printing inks segment

These segments use an area of 32,000 sqm out of which approx. 12,000 sqm are built-up in the manufacturing site at the Ashkelon industrial area. The site is on an area with a total size of 47,000 sqm, of which some 15,000 sqm is constructed buildings. Tambour owns 80.5% of the rights in the perpetual lease of the land at this site. Tambour has been granted the option to purchase the rights to the rest of the land (19.5%) at its fair value on the date on which the right shall be exercised. Under specific conditions, Tambour has the right to extend the leasing period for another 49 years. The remaining leasing period, including the option, comes to a total of approx. 62 years.

An area of approx. 15,000 sqm of the above-described Serafon manufacturing site in which the Granite Group owns the capitalized lease rights from the Israel Land Administration, which ends in 2043, is used as storage space for the gypsum and construction segment.

11.44.3. The gypsum and dry construction segment

The Gesher Gypsum manufacturing site located at Kibbutz Gesher, which has an overall area of some 29,000 sqm, is used for Gesher Gypsum activities and is leased to Tambour for the purposes of its activities. An area of some 30,000 sqm at the south Akko site is used by the gypsum boards and blocks plant, of which app. 11,000 sqm are built-up area. In addition, a built-up area of 3,000 sqm is used for storage of the gypsum and dry construction products at the site in Ashkelon and a leased area of approx. 2,400 sqm at the South Akko site, adjoined to the Tambour site .

11.44.4. Machinery and equipment

These assets include principally, the machinery and equipment used to manufacture the paints, supplementary products, printing inks and gypsum and dry construction products at the various sites, and the computerized color mixing machines placed with Tambour customers.

11.44.5. Improvements to the leasehold

In 2001, Tambour entered into a leasing agreement with a third party for the leasing of an office area of approx. 1,718 sqm in Netanya and from 2010, an additional area of approx. 470 sqm. Such offices house the Tambour Group's management and marketing employees. The lease period is effective until December 2015.

Beginning in 2006, a subsidiary company entered into a leasing agreement with Kibbutz Gesher, for the leasing of an area of some 28,785 sqm for a period of seven years, for the purposes of manufacturing and storing the subsidiary company's products. The subsidiary company has an option to extend the lease for another three periods, each for five years.

In 2007, Tambour entered into a leasing agreement with a third party for the lease of an area of some 650 sqm in the Gush Dan area, for a period of 10 years, which is used by Beit Tambour. The leasing period will be extended by additional five year periods, unless Tambour will notify on the cancellation thereof by no later than 6 months before the expiry of the period.

Tambour's subsidiary, Tzah Serafon, is engaged in a lease agreement with a third party with regard to part of the site which is not owned by Tambour (19.5%). The lease agreement is effective until January 2013. In addition, it has the option to extend the lease.

In this segment, Tambour and its subsidiary companies have entered into additional leasing agreements on a non material scale and, primarily, those areas are used by Tambour subsidiary companies.

11.44.6. Other

Tambour has additional fixed assets comprising computing systems, office equipment and vehicles.

In January 2010, Tambour executed an agreement for the sale of the land, building and equipment which were used by the printing inks plant, which is owned thereby on the Be'er Tuvia site in consideration for the amount of approx. NIS 9.2 million.

11.45. **Research and development**

Tambour has a research and development department which acts, *inter alia*, to maintain quality and improve products, develop new products, to support manufacturing array by providing solutions for technological problems, to determine rules for the adaptation of Tambour activities to standards and regulations pertaining to safety and environmental quality. Tambour's investments in product development in this segment reach immaterial sums.

11.46. **Raw materials and suppliers**

The principal raw materials used by Tambour are titanium dioxide – a white pigment for paint (T102) and VAM (Vinyl Acetate Monomer), which is used as the raw material in the manufacture of emulsions for water colors, emulsions (binding materials), plastic packaging and raw gypsum. The purchased raw materials are tested by quality control laboratories and the quality assurance department. Most of the raw materials needed in the production processes of the products in this business segment are imported and purchased from manufacturers in Europe and the Far East. In the years 2009 to 2011, imported raw materials constituted two thirds of all the raw materials used by the Tambour Group to manufacture its products.

In the years 2011, 2010 and 2009, there was no single supplier, from which purchases reached more than 5% of the total purchases of raw materials for this segment.

Customarily, Tambour does not enter into long-term contractual agreements with any supplier for the supply of raw materials. The raw materials for the paint industry are readily available and the Tambour group has no dependency on any supplier whatsoever.

The information in this section includes forward-looking information, which is based on information which exists in the Company on the Date of the Report, and includes the Company's estimations as of the Date of the Report, based on Tambour's management, *inter alia*, based on the past experience and knowledge accumulated by Tambour. The actual results may be materially different from what is implied by this information. In addition, the Company's estimations may prove to be incorrect or materially different than those which were taken into consideration.

11.47. **Working Capital**

11.47.1. Inventory policy for raw materials

As part of this segment, Tambour usually holds an inventory of raw materials in accordance with the anticipated level of orders, its past experience and its own assessments. Tambour generally holds in its inventory an amount of imported raw materials sufficient to cover production for a period of two to three months, and an amount of raw materials purchased on the local market sufficient to cover production for a period of three to four weeks. Sometimes, Tambour advances the purchase of raw materials as a result of the expectation of an increase in prices and future shortages of raw materials. The average number of days of raw materials inventory is 65 days.

11.47.2. Inventory policy for finished goods

The policy in the segment is primarily affected by the seasonal nature of sales in this segment, in that around holiday periods and in the summer, procurement is increased. Tambour is accustomed to holding an inventory of finished goods of about a month on the shelf, and an inventory of purchased products, which have a shelf life of about two months. The average number of days of inventory of finished goods is around 60. The average number of days of inventory of Tambour products is approx. 125.

11.47.3. Policy for return of goods

The products in this segment are returnable with the approval of Tambour's Vice President, Sales or someone authorised to act on his behalf.

11.47.4. Policy for product warranty

Tambour grants warranty to its customers with regard to the quality of acrylic paints for internal walls for a period of 7 years in relation to yellowing, crumbling, and certain types of peeling. In addition, in certain projects, warranty is granted in respect of the "Multiflex" (Rav Gamish) brand for a period of 5 years relating to the covering and bridging the fine non-structural cracks. In any event, the liability is restricted to the amount paid by the consumer for the actual purchase of the product, with the warranty refund possibly being made in kind with paint or in the monetary value of the product. Tambour is not responsible for payment in respect of painting work or any other alleged financial loss. In addition, Tambour's warranty for its various products varies in periods of time up to a maximum of 10 years. The expenses of the Granite Group arising from the grant of warranty for products as outlined above are not material.

11.47.5. Credit policy

Customer credit – The payment terms for customers of this segment ranges from payment in cash to credit of end-of-month + 120 days. Most of the customers deposit personal guarantees with Tambour, some with collateral, such as various types of liens and bank guarantees. In addition, Tambour has insured most of its customers' debts with external credit insurance.

Supplier credit – Credit received by Tambour from its suppliers as aforesaid is for periods of end-of-month plus 60 -120 days, with most being for periods of end-of-month plus 90 to 120 days.

Data with regard to the average levels of supplier credit and customer credit in this segment are as follows:

	2011		2010	
	Average days of credit	Average credit level in NIS	Average days of credit	Average credit level in NIS
Customers	130	315,000	120	270,000
Suppliers	100	150,000	100	130,000

11.48. **Investments**

Tambour has not made substantial investments in the year of the Report.

11.49. **Environment**

11.49.1. General

Tambour treats environmental protection as an integral part of the corporation's policy, which policy is published on its website.

Tambour and its employees take the required steps to prevent environmental hazards, to minimize the environmental effects resulting from the processes in the plant and the products supplied by it, and work, *inter alia*, to reduce hothouse gas emissions by lessening the use of electricity and water. Tambour is obligated to all laws pursuant to the legislative demands in the quality of the environment field relevant to the plant's activity. When it receives building permits and business licenses for its new plants, Tambour is required to meet the various demands of protecting the quality of the environment, the guidelines of the Ministry of Environmental Protection, the Ministry of Health and more, as well as the various legislative demands e.g. the Business Licensing Law.

Tambour invests in ensuring compliance with the environmental law guidelines to which it is subject, in fixed and ongoing expenses, and acts to prevent or minimize the environmental risks that are likely to occur during its operation. Tambour acts to assimilate and include its employees in the processes related to the quality of the environment.

It should be noted that Tambour is developing green solutions by development and manufacture of unleaded and chromatized paints and insulation and sealing materials (saving energy, blocking radiation etc.) with green tags approved by the Ministry of Environmental Protection and the Standards Institution of Israel. In 2011, Tambour participated in Maala's corporate responsibility index and received the platinum grade. As of the date of this Report's publication, Tambour is in the process of building environmental management systems, within which its sites will be ISO 14001 certified. In addition, in the last quarter of 2011, a process of energetic surveys and energetic efficiency has been implemented in the various Tambour sites.

11.49.2. Environmental regulation

Tambour is subject, *inter alia*, to the provisions of the following environmental laws: the Prevention of Hazards Law, 5721-1961, the Hazardous Substances Law, 5753-1993 (the "**Hazardous Substances Law**"), the Business Licensing

Law, 5728-1968, the Water Law, 5719-1959, the Freedom of Information Law, 5758-1998, the Clean Air for Israel Law, 5768-2008 and the regulations issued pursuant thereto, and the Regulation of the Handling of Packaging Law, 5771-2011.

11.49.3. The environmental risks having or expected to have a material effect

Most of Tambour's operating segments are based on use of chemicals, including use of hazardous substances. Accordingly, Tambour's potential environmental damage is air pollution, soil, water and hazardous substances contamination. In view of the aforesaid, Tambour is under the supervision of Ministry of Environmental Protection and the municipal authorities and is obliged to maintain environmental quality and to work in accordance with environmental laws, planning and construction laws, quality standards, directives of the Ministry of Environmental Protection and the relevant associations of municipal authorities and relevant city unions and municipal by-laws. Tambour's plants that are dealing with hazardous substances have toxic materials permits (by virtue of the provisions of Section 3 of the Hazardous Substances Law) that are renewed every year, and it acts according thereto.

Tambour constantly acts to prevent environmental risks, such as air pollution, soil and water contamination, including through external consultants specializing in environmental issues, and does not know of such risk having or expected to have a material effect. Such Company assessments, based on Tambour's management, are forward-looking information as defined in the Securities Law, 5728-1968. They may actually change due to events which are not under the control thereof.

11.49.4. Material implications of the provisions of the law

Tambour implements a variety of measures to prevent air pollution, soil and water contamination through ongoing treatment of the Company's wastewater, emissions and hazardous wastes. In some of Tambour's manufacturing sites there are wastewater treatment plants. All of the wastewater produced by these sites undergoes treatment at a plant and flow to the municipal system. As of the date of this Report, any deviation found, if found, in wastewater and particularly in joint sampling points with GES, was treated to the authorities' satisfaction. Tambour transports surplus hazardous wastes pursuant to the Hazardous Substances Law and the regulations promulgated thereunder and pursuant to the Company's toxic materials permit, subject to Transport Services to Hazardous Substances Regulations, 5761-2001.

Tambour transports the surplus paint mainly to the Ramat Hovav hazardous waste disposal site and other authorized waste disposal sites, all in coordination with the Ministry of Environmental Protection.

In view of the fact that Tambour has submitted requests for building permits in the South Akko paint complex, Tambour was conducting comprehensive soil testing, in accordance with a plan that has been approved by the Ministry of Environmental Protection, and an environmental impact report on the South Akko site has been submitted on Tambour's behalf in accordance with the guidelines of the Association of Municipal Authorities for Environmental Quality and Ministry of Environmental Protection. After completing all of the authorities' requirements to their satisfaction, approval has been granted for the continuation of work. Tambour is continuing testing in other parts in accordance with binding statutory requirements.

Tambour's investments in and expenses on environmental issues in 2011 for complying with laws and regulations and for prevention of environmental risks only, amounted to approx. NIS 2 million. Tambour's investments have no material effect on its profit or competitive status. Tambour's investments in fire extinguishing and environmental quality in the recent three years were in the sum of approx. NIS 7.8 million. Tambour's expenses on environmental quality in the recent three years were in the sum of approx. NIS 3 million. All of the amounts have been used for prevention only. In the recent 3three years Tambour's investments and expenses were used for prevention only, and an immaterial amount has been incurred in 2009 for repair (as part of the environmental authorities' conditions prior to the construction of the gypsum plant).

11.49.5. Projected material environmental costs and investments

In view of the fact that Tambour invests on an ongoing basis in environmental issues (prevention of environmental risks and complying with the requirements of every law), fire extinguishing, licensing, workplace safety and health and in view of its past investments, the Company, based on Tambour management, does not project a material change in the scope of its investments in the near future.

Such assessments of the Company, based on Tambour management, are forward looking information, as defined in the Securities Law, 5728-1968. They may actually change due to events which are not under the control thereof.

To the Company's best knowledge, based on Tambour management, no event or matter occurred therein, which have caused or may cause damage to the environment and has a material effect thereon. Such assessments of the Company, based on Tambour management, are forward looking information, as defined in the Securities Law, 5728-1968. They may actually change due to events which are not under the control thereof.

Tambour has no legal or administrative proceedings that are related to the environmental quality.

11.49.6. Tambour's policy in environmental risk management

In each of Tambour's sites, a manager responsible for the quality of the environment, and a manager responsible for all of Tambour are appointed, while each year Tambour performs company-wide projects in the quality of the environment field. In addition, Tambour takes various actions to increase the awareness amongst its employees, *inter alia*, by lectures on the subject.

Tambour's manufacturing sites are checked both independently through external laboratories, and in a continuous manner, and in a random manner by samplers of the Ministry of Environmental Protection, and city organizations. To the best of Tambour's knowledge, it fulfills all of the laws, regulations, demands and standards for protecting the quality of the environment, and acts in a continuous manner in accordance with binding statutory obligations. Even when an insubstantial deviation is discovered (such as sodium in a sample of wastewater), the deviation is immediately dealt with to the satisfaction of the Ministry of Environmental Protection.

The plaster plant manufactures green and environmentally friendly materials, and was built according to these principles, including the principles of heat preservation, prevention of contamination and emissions. The only emission that occurs from the plant is solely of water vapor. Many of Tambour's products are environmentally friendly products with "green label" markings on behalf of the Standards Institution of Israel in conjunction with the Ministry of Environmental Protection. The permits are granted only to plants whose products are considered "green" and are conducted based on important criteria and standards of protecting the quality of the environment. Every year Tambour develops new green products. In addition, Tambour recycles paints, recovers solvents through recovery devices for re-use, recycles surfaces and plastic bags, and acts to reduce and minimize the amounts of waste for removal.

Tambour has received high grades of beauty stars in the Council for a Beautiful Israel's "Beautiful Industry" project for many years, as its activities on behalf of the quality of the environment contribute to its high ranking. Tambour acts continuously to implement safety and hygiene laws and regulations in the workplace, through its safety and hygiene department, which is responsible for implementing safety provisions in the workplace, and for performing training according to the law in general and particular subjects related to safety in the workplace. In addition, Tambour performs monitoring of workplaces as required by the regulations. In addition, its employees who come into contact with hazardous substances undergo periodic medical tests by an occupational physician. Furthermore, in 2007, Tambour was licensed by the Standards Institution of Israel for IS 18001 in safety and hygiene which guides its safety and hygiene policies, commitment to constant improvement, planning of safety management systems, control, evaluation and measuring of the safety and hygiene performance. Tambour is under continuous supervision by a work supervisor of the Ministry of Industry, Trade and Labor regarding the implementation of the safety and hygiene laws and regulations in the workplace. In addition, Tambour periodically performs work in conjunction with fire departments and planning companies in order to suit the extinguishment needs to the subject of paint storage in its warehouses, in accordance with the fire departments' demands. In 2011, many projects were performed whose purpose is reduction in use of electricity and water.

As Tambour invests, on an ongoing basis, in issues of environmental quality, fire extinguishing, licensing, safety and health in the workplace, and in view of its investments in previous years, the Company, based on an estimation of Tambour's management, does not expect a significant change in the scope of its investments in the near future. These estimations are forward-looking information, as defined in the Securities Law, 5728-1968. In practice, they may change due to events which are not under its control.

Except for continuous provisions, Tambour does not have any exceptional provisions for the aforesaid.

11.50. **Restrictions and regulation of the Tambour segment**

The general laws in Israel that apply to the seller of products and services and to an industrial manufacturing company, which employs employees, as well as to a monopoly, and the Restrictive Trade Practices law and the environmental protection law, to which the laws specified hereunder are added, apply to Tambour.

11.50.1. Price control

In the past most of the Tambour Group's products were under control pursuant to the Price Stability of Products and Services (Temporary Order), 5745-1985 (the "**Stability Law**"). In July 2010 the control on Tambour's products was removed.

11.50.2. Business licenses Tambour

Tambour incessantly acts for the renewal and/or issuance of business licenses for new sites, while as of the date of the Report, Tambour's gypsum plant is in the process of obtaining an license, two additional sites are in the process of license renewal, the Migdal HaEmek site holds a provisional license until March 31, 2012 and Tambour is in the process of obtaining a permanent license. In addition, Tambour is acting for the finalization of the obtainment of business licenses for two retail stores. The rest of the Company's plants hold permanent business licenses.

11.50.3. Antitrust

Tambour constitutes a monopolist in paint products, as defined in the Restrictive Trade Practices Law, 5748-1988, except with respect to wood paints for industrial use, paints for concrete and flooring, cured paints, vehicle paints, single comppnent metal paints for industrial use and the series of outdoor coatings, , in accordance with the decision of the Antitrust Commissioner. After the date of the Report, on February 29, 2012, Tambour filed an application with the Antitrust Commissioner, whereby it requests to revoke its definition as "monopolist". In addition, Tambour acts in accordance with an internal compliance program on behalf of the Antitrust Authority.

11.50.4. Export licenses

Tambour sells as an exporter authorized by the authorities. The export license is valid until January 2013.

11.50.5. Approved supplier to the Ministry of Defense

Tambour is an authorized supplier of the Ministry of Defense. Work with the Ministry of Defense is performed by way of tenders or requests for price proposals.

11.50.6. Standardization

The Standards Institution of Israel has granted Tambour factories a permit to mark various types of paints and additional products manufactured by Tambour with a

standards symbol. In the Company's estimate, based on the best knowledge of Tambour's management, the absence of permits on the part of the Standards Institution for other products in this industry does not constitute any restriction whatsoever of Tambour's activities. Tambour is taking steps to renew and extend the permits on an ongoing basis and to add permits for new products.

Tambour products comply with the Israel Standard (IS) 1343: paints and lacquers packing and marking, with respect to the product packing, amount and product marking and with the Israel Standard (IS) 2302 on dangerous substances and preparations: classification, packaging, labeling, transport and marking.

Tambour paint plants act in accordance with the Israeli ISO 9001:2008 standard. Tambour's authorization is in effect until February 2013.

The paint plants were authorized in 2007 by the Standards Institution of Israel for Israel standards 18001 for safety and health, and this guides Tambour's policy for safety and health, obligations for continuous improvement, planning systems for safety management, control, evaluation and review of the safety and health performances. Israel Standards testing 18001 is integrated with ISO 9001 testing and performed concurrently twice a year.

11.50.7. Quality control

The Tambour Group has seven laboratories for control of production processes of its products, which are adjacent to the production sites.

11.51. **Material agreements**

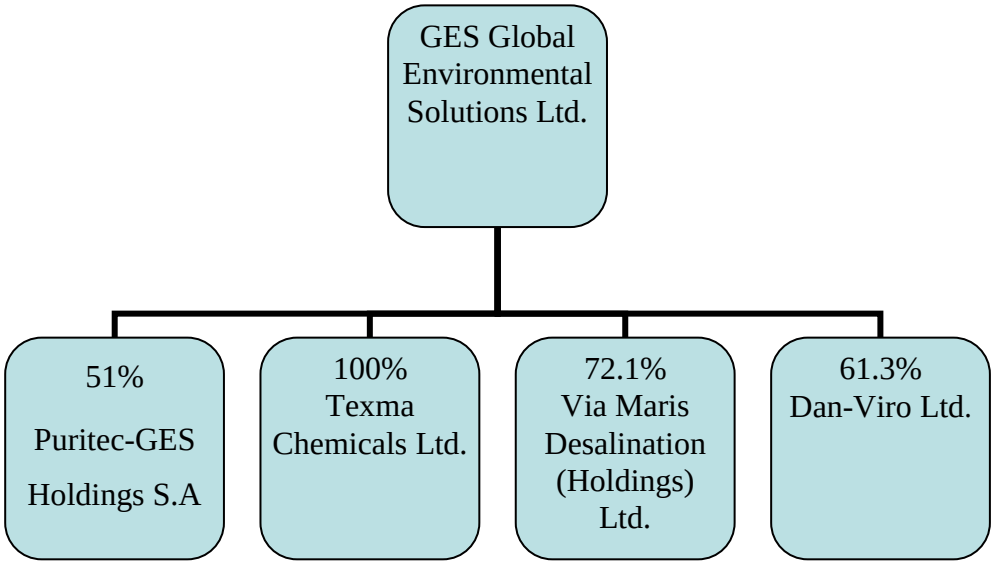
Concession, distribution and knowledge agreements – see Section 11.74 below.

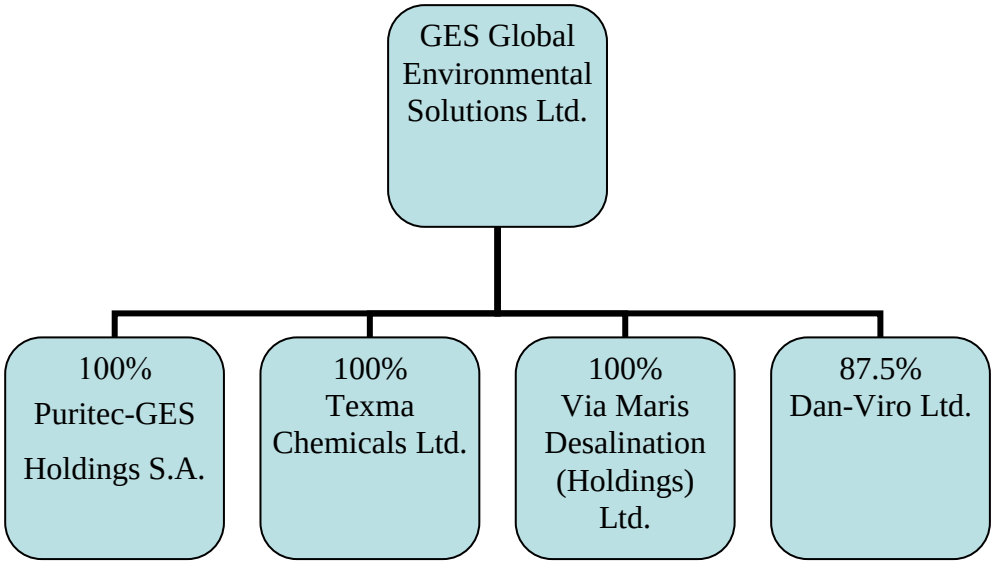
Activity in the GES Wastewater Segment - Water and Wastewater

11.52. **General information on the wastewateroperation in the GES segment**

In the water and wastewater segment, the Company operates through GES, and consolidated companies thereof. GES engages in engineering design, establishment and production, operation and maintenance of facilities for the improvement of water and water filtering, sea water desalination, pumping stations and water pools, treatment of well water and effluent water and treatment of sanitary, industrial, municipal and organic wastewater. In addition, GES by itself and thorough its subsidiaries engages in marketing and development of chemical products for the purpose of metal treatment and protection as well as importation and marketing of oils, adhesives and chemicals for industry.

Following is a diagram of the main holdings of GES*:





*As of the date of the Report, GES increased its holdings in Dan Viro Ltd. up to 87.5%.

GES and its consolidated companies act in this operating segment through two divisions:

11.52.1. The Water and wastewater division

The division engages in desalination of sea water and brackish water; wastewater treatment and return of effluent water; water improvement and wastewater treatment in the industrial segment; water and wastewater purification in the municipal segment; implementation of special chemicals for treatment of water, wastewater, desalination and chilling plants for the municipal and industrial segment; provision of system operation and maintenance services; planning and production of systems for wastewater and water treatment. To-date, GES operates approx. 70 plants all over Israel (approx. 40 plants for water treatment and approx. 30 plants for wastewater treatment), including sea water desalination plant in Plamachim using the BOO method (through Via Maris Desalination (Holdings) Ltd and subsidiaries thereof.; hereinafter: "**Via Maris**"). In addition, GES completed the construction work in the brackish water desalination plant at Lahat site for Mekorot Water Company Ltd. on turn-key basis.

11.52.2. Industrial chemicals division

The division engages in production, importation and marketing of chemicals and finishing processes for metals; Chemicals for preparing surfaces for painting and industrial paint stripping; Materials for electrochemical plating for high-tech and electronics industry; Industrial cleaning materials; Special adhesives and lubricants for industry.

11.53. **Changes in the scope of operations in the segment and the profit thereof**

11.53.1. Inbar committee regulations – On April 25, 2010 the Public Health Regulations (Effluent Quality Standards), 5770-2010 that took effect gradually since July 2010 (the "**Inbar Regulations**") were published in the Official Gazette. The Inbar Regulations impose strict obligations, *inter alia*, on wastewater purification plants, in connection with the wastewater treatment quality and the products of the wastewater purification plants. To the Company's assessment, based on Granite management, in order to meet the provisions of the regulations, considerable part of the Israeli wastewater purification plants will have to upgrade their systems and their wastewater treatment methods. To the Company's assessment, these changes may have significant implications on the scope of GES operations in the water and wastewater unit and its profitability in such unit.

11.53.2. Changes in the purchase of desalinated water – The year of the Report saw the commencement of construction of two large desalination facilities in Soreq and in Ashdod and the expansion of existing desalination facilities in Ashkeon and Hadera. In addition, in 2012, Via Maris began to expand the desalination facility in Palmachim and therefore, the quantity of desalinated water available to the State will increase. Following such increase, there is a future possibility of changes in the demand for desalinated water. However, as long as water shortage persists in Israel, the Company does not expect a decrease in purchasing the amounts of desalinated water.

The information as to the Company's assessment of the implications of the implementation of the Inbar Regulations and the changes in desalinated water purchase is forward-looking information, as defined in the Securities Law, based on the Company's subjective assessments, *inter alia*, on the basis of estimations by external factors and various publications, as well as the Company's management estimations with respect to the possible implications of compliance with the provisions of the Inbar Regulations and the implications of changes in the purchase of desalinated water. In actuality, the aforesaid Company's assessments may be different, and even materially different, than the assessments foreseen as stated, as a result, *inter alia*, of various factors, the principle ones thereof being the market condition, competition, a change of trend in this business segment of the Company as well as the effect of the risk factors characterizing the Company's operations as specified in Section 11.80 of this Report.

11.54. **Developments in the markets of the operating segment or changes in its customers' characteristics**

In recent years there is a developmental trend in the water and wastewater segment. The rise in the awareness for shortage of clean water in various areas over the world, including in Israel, along technological developments that caused reduced the water treatment costs, create a window of opportunities in the water desalination and treatment segment.

Following are several changes that the Company expects in the segment: (1) Rise in the global demand for water sources (wells, lakes and rivers) filtering and improvement systems and in systems desalinating sea water due to global water shortage and an increase in the awareness of such shortage. In addition, the Company intends to expand its operations in the water desalination and wastewater purification in international markets. The Company examines possibilities to enter new markets especially in countries in East Asia, Latin America and South America; (2) Increase in acquisitions/upgrades of wastewater treatment systems in Israel following the implementation of the Inbar Regulations; (3) Industrial wastewater regulation.

The information with respect to the trend development in the water segment includes forward-looking information as defined in the Securities Law. Forward looking information is an uncertain information about the future, which is based on information existing in the Company on the Date of the Report, and includes the Company's assessments, based on Granite management, as of such date, *inter alia*, based on past experience and know-how accumulated in Granite on this subject. Actual results may be materially different than the results that are estimated or implied from this information. In addition, the Company's assessments, which based thereon such information was presented, may emerge as materially untrue and/or different from those taken into account.

11.55. **The critical success factors in the operating segment and the changes occurring therein**: (1) Energetic increasing efficiency – the main factor affecting the production costs in the water and wastewater facilities operated by GES is the energy costs for operation of the facilities, accordingly, the reduction of energy costs is a critical factor in this business segment; (2) Winning the tenders; (3) Ability to sell water and wastewater treatment plants, mainly outside of Israel.

11.56. **Main entry and exit barriers of the business segment and changes occurring therein**

In the Company's operations of desalination of sea water, there are high entry barriers in view of the need to obtain concessions from the

State to sell desalinated water and also as a result of the high capital investments required for the foundation of desalination facilities, which necessitate financial soundness. The main exit barrier in this business segment is the existence of years-long obligations. With respect to the competition structure in this business segment and the changes occurring therein, see Section 11.62 below. As to the regulatory restrictions applicable to this business segment, see Section 11.70 below.

11.57. **Products and services**

11.57.1. The main products and services

The water and wastewater division

The main systems used by GES for treating water and wastewater are: membranal high-pressure systems for separation of salts, filtering and purification systems through chemicals, anaerobic and aerobic systems for treating industrial and municipal wastewater and systems for treating sludge. The systems include dosage, command and control units.

GES offers to its customers a wide range of systems and solutions for water and wastewater treatment, the main of them being: brackish water and sea water treatment systems; wastewater treatment systems; well improvement and upgrade plants; various water treatment methods based on various technologies; treatment with steam systems and energy centers; plants for desalination of effluent for unlimited watering level. In addition, GES offers to the customer project monitoring and management, including establishment, professional backup and support services.

The chemicals division

GES main products and services in the chemical division includes area treatment, adhesives and sealing materials, chemicals for electrolytic plating and printed circuits, special lubricants, products for maintenance in industry, recycling of industrial detergents, fuel additives.

11.58. **Material changes that are expected in GES' share and product mix**

The water and wastewater division

The Company, based on Granite management, expect an increase in the demands for construction of new plants and expansion of the existing plants for water desalination and wastewater purification on the part of the Israeli and global market, as aforesaid in Section 0. In addition, the acquisition of Nitron Chemtec Ltd. is expected to increase GES operations in the field of operations of the municipal and industrial wastewater plants.

The chemicals division

The industrial chemical division was strengthened in 2011 compared with 2010, especially in the fields of aviation, electronics and the metal and equipment products. GES acts for the improvement of its customer and product mix and continues improving efficiency. However, Lately, a slowdown trend in the sales of GES in the chemicals segment is

recognizable, and the Company estimates that the total sales in 2012 will be similar to that of 2011, with a strong influence of trends in the global economy.

The information as to the Company's assessment of demands for founding new facilities and expanding existing facilities for water desalination and water waste purification is forward-looking information, as defined in the Securities Law, which is based on the Company's estimations based on subjective assessments of the GES company's management, , *inter alia*, based on estimations of external entities and various publications. In actuality, the Company's aforesaid assessments may be different and even materially different than the assessments foreseen as stated, as a result, among other things, of different factors the principal ones of which are the situation of the market, competition, a change of trend in this business segment of the Company and the influence of risk factors which characterize the Company's business, as described in Section 11.80 of this Report.

11.59. **Segmentation of revenues and profitability from products and services** - the Company's revenues in the water and wastewater segment are immaterial to the Company's business.

11.60. **Customers** - the Company's business in the water and wastewater segment is not dependant on a single customer or a limited number of customers, which the loss thereof will materially affect this operating segment. Notwithstanding, it should be noted that the Company's operations in the desalination segment is influenced by government policy and is dependent upon, *inter alia*, the demand level for desalinated water and the scopes of anticipated State purchases.

11.61. **Marketing and distribution**

11.61.1. Marketing - GES markets through national sale agents, distributors, Internet information websites, exhibitions (in Israel and outside of Israel), professional conferences and tenders, etc.

11.61.2. The sales and distribution array outside of Israel - GES operates an export activity in all of its operations divisions. Most of GES products that are marketed outside of Israel, are marketed under the "GES" brand.

11.62. **Order backlog**

Term of Recognition of Projected Revenues	As of December 31, 2011 (NIS in millions)
First Quarter of 2012	68

Second Quarter of 2012	78
Third Quarter of 2012	117
Fourth Quarter of 2012	74
2013	212
2014	41
Total	590

The data with respect to the term of recognition of projected revenues as well as the projected revenues as specified above, constitute forward looking information based on the Company's estimations and assumptions, based on the Granite's company management, and thus there is no certainty as to their materialization, as a result, among other things, of the possible effect of the risk factors as detailed in Section 11.80 of this Report.

11.63. **Competition**

11.63.1. The competition terms in the operating segment

The market in which GES operates is a competitive market in which many entities operate. The competition exists both in the search and finding new customers segments and in providing qualitative services in all GES operating segments. The competition is on price, service quality, funding terms and technical specification.

The water and wastewater division

In the sea water desalination, GES holds control of the Palmachim facility with a manufacturing capacity of approx. 45 million cube water a year, which presently constitutes approx. 15% of the of the sea water desalination market share in Israel. The Palmachim facility is expected to increase its capacity by an addition of 45 million cube in 2013. On this matter, see Section 11.71.1 hereunder. According to the data of Israel's Water Authority, the remaining main facilities today for sea water desalination are a facility in Ashkelon which is owned by IDE Veolia and it manufactures approx. 120 million cubic meter per annum; and a sea water desalination facility in Hadera which is owned by Shikun

Vebinui and IDE, that manufactures approx. 127 million cubic meters per annum. In addition, there are national plans for the establishment of two additional facilities; a sea water desalination facility in Soreq in the scope of approx. 150 million cubic meter per annum that DIE won the tender for the establishment thereof in 2009, and a sea water desalination facility in Ashdod in the scope of 100 million cubic meter per annum that will probably be operated by Mekorot starting from 2014, and thence.

In the wastewater segment GES operates several municipal and industrial wastewater facilities, the scope of which is inconsequential in relation to the market scope in Israel. In addition, GES holds 87.5% of the Dan-Viro plant (SHAFDAN), which treats 36 thousand ton of sanitary sludge per annum, which constitute approx. 15% of the SHAFDAN sludge.

The Chemicals Division

The Company estimates that relatively to other companies, its scope of operations is immaterial to the Israeli market.

11.63.2. Names of the main competitors

The water and wastewater division

In the water segment, GES main competitors are: Tahal, IDE Technologies Ltd., Yamit Filtration and Water Treatment Ltd. Nirosoft Industries Ltd., Odis Filtering Ltd., Desalitech Advanced Desalination Technologies (ADT) Ltd.

In the wastewater segment (municipal and industrial) there are several companies in the Israeli market that compete with GES in various sub-segments in the context of GES operations in this segment as follows: Kal Binyan Water Technologies Ltd.; Palgey Maim Ltd.; ALD Environmental Protection Ltd.; Mekorot; RGA Wastewater and Water Purification Ltd.; Arrow Ecology Ltd.; Zenon Israel; Triple-T Purification Ltd., Nirosoft Industries Ltd. and self-operated municipal water associations.

The Chemical Division

In the chemical division GES has several competitors in the various segments in this segment, as follows: Amza Ltd. (coating and metal preparation before painting); Paz Lubricants and Chemicals Ltd. (lubricants and metal preparation before painting); Rotal Adhesives and Chemicals Ltd. (adhesives segment); Pro Net Industries Ltd. in the adhesives and grease segment.

11.64. **Production capacity**

The production of GES is concentrated in two sites: Akko South and Askar (in Akko area). In the water and wastewater division, GES is capable to manufacture in parallel large number of plants. In the chemicals division, according to GES policy, the production site does not produce a fixed inventory, but in accordance with customer orders. GES exploits approx. 60% of the production potential of the production site, which is approx. 5,000 ton, assuming that production work is carried out in two shifts a day (as of today, the work is carried out in one shift).

11.65. **Fixed assets, property and facilities**

11.65.1. Property

Via Maris, which is a subsidiary of GES, is engaged, since 2002, in an engagement contract with third parties for the lease of areas in the proximity of Kibbutz Palmachim. Two addenda to the agreement were executed in February 2005. The leased property includes a main area of approx. 30 dunam, on which the desalination facility was established, an area of 22.3 dunam which is held for option holding fees for the purpose of future expansion, out of which were exercised, over the years, approx. 4,500 sqm, and an additional area of approx. 3.6 dunam on which the transformation station was established. The term of the lease of all of the areas is 24 years and 11 months, beginning from February 2005.

11.65.2. Machines and equipment

GES has several BOT and BOO type water treatment facilities with the private segment. The cost of establishment of the facilities is reduced throughout the period of the operation contract. GES has machines and equipment used to produce chemicals and an evaporation plant for industrial wastewater treatment located on the production site in Akko south. GES's subsidiary – Dan Viro Ltd. ("**Dan Viro**"), has a sanitary sludge treatment plant in the Dan Metropolitan wastewater plant (The Dan Region Wastewater Treatment Plant). As of November 2011, the plant is operated, as a commercial pilot by Dan Viro, for a period of at least 3 years after which it will be transferred to the ownership of the Dan Metropolitan conurbation (The Dan Region Wastewater Treatment Plant).

11.65.3. Improvements in the leasehold

Since 2004, GES is engaged in a lease contract with Tambour for the lease of areas of approx. 19,500 sqm in the Akko south industrial area, which is located in the municipal

area of the city of Akko and on the Askar site in the territory of the Mate Asher regional council. The leased property is used by GES as a site for chemical production, water plant production, storage of materials and the management's offices. Under the lease agreement, from January 1, 2009, the lease was automatically extended for 5 additional years until December 31, 2013, at the Akko south site, and for two additional years until December 31, 2012, at the Askar site. The lease contract is automatically extended for an additional period unless any party will notify of termination thereof.

A subsidiary of GES – Texma ("**Texma**") is engaged in an engagement contract with third parties for the lease of an industrial building in an area of approx. 300 sqm in Kiryat Arieh in Petach Tikva, which is used as offices and a distribution warehouses. The lease agreement will remain in effect until March 31, 2013, with an option to extend until March 31, 2019.

A subsidiary of GES, Puritec-GES is engaged in several engagement contracts for the lease of offices and warehouses in several states in Central America.

11.65.4. Other – GES has additional fixed assets which include computation, office equipment and vehicles.

11.66. **Research and development** - GES engages in developing processes for the improvement of sea water desalination processes and developing technology for water disinfection as a replacement for chlorination through electrolytes' processes.

11.67. **Raw materials and suppliers**

The water and wastewater unit

The main raw materials which GES uses are: finished equipment items including pumps, membranes, pressure chambers, containers and chemicals for operation of water and wastewater plants. Such raw materials and equipment items are purchased from the world's leading companies. Supply times of such equipment range from one month to over a year. The material raw materials are purchased mainly from the local suppliers, and parts are also imported.

The chemical unit

The unit uses many raw materials for its needs and its customers' needs, while the main ones are: 60%Nitric acid and hydrochloric acid (tech). Such raw materials are purchased from the domestic market. Their availability and supply time is immediate (from the domestic market) and approx. two months (import).

11.67.1. Rate of GES's purchases from the main suppliers and manner of engagement therewith

The water and wastewater unit

GES has several significant suppliers in the wastewater and water unit segment. The scope of purchases from such suppliers are not material to the Company.

The chemical unit

GES has several material suppliers in the chemicals segment. There is an alternative for each supplier and there is no dependency on any single supplier.

11.68. **Working capital**

11.68.1. Policy on keeping of raw materials inventory

The water and wastewater unit

GES generally keeps an inventory of raw materials according to the scope of the anticipated orders of its products and services, past experience and estimations of GES's management.

The chemical unit

GES mostly keeps the imported raw materials in the inventory in a sufficient scope for production during a period of two to three months and an inventory of raw materials which are purchased in the local market in a scope that is sufficient for production during a period of three to four weeks.

11.68.2. Policy on keeping of finished products inventory

The water and wastewater unit

GES's finished products in this unit are water and wastewater treatment facilities which are usually adjusted to the customers' needs and specific technical specifications and therefore, GES does not keep an inventory of finished products in the segment.

The chemical unit

GES generally keeps on the shelves an inventory of finished products for one month. Imported products get a shelf life of approx. 3-6 months. Finished products are in the inventory for an average of approx. 60 days.

11.68.3. Product warranty policy

The water and wastewater unit

GES provides technical advice and service to customers, through the operation and/or engineering department. With regard to most of the equipment, the warranty is given back-to-back with the manufacturer's conditions. Facilities usually have a one-year warranty.

The chemical unit

GES provides technical advice and service to customers, through the technical advice department. In addition, each finished product comes with product quality certificates which are a product certificate of compliance (COC) and a certificate of analysis (COA) which GES is obligated to attach under ISO standards (product quality standards).

11.68.4. Customer credit - ranges from payment in cash to credit of end-of-month plus 120 days.

11.68.5. Suppliers credit - end-of-month plus 60-120 days (usually end-of-month plus 90-120 days).

Below are figures with regard to the average amounts of the supplier credit and customer credit (without Via Maris):

2011		
	Average amount of credit In NIS thousands	Average days of credit
Customers	65,500	Approx. 140
Suppliers	26,800	Approx. 100

2010		
	Average amount of credit In NIS thousands	Average days of credit
Customers	54,654	Approx. 100
Suppliers	19,290	Approx. 120

11.69. **Investments**

For details regarding GES's investment in Via Maris Desalination Ltd., see Section 11.52.1 below.

11.70. **Environmental risks and manners of management thereof**

11.70.1. Environmental Risks of Material Effect

GES fully treats industrial wastewater, which are created in the production of chemicals at GES's production site South Akko, in accordance with the law's provisions and the requirements of the Ministry of Environmental Protection and the Urban Union for Environmental Protection. Additionally, GES handles poisonous and hazardous substances within its business operation of manufacturing products in the segment of chemicals for industry and water and within the maintenance of GES's water and wastewater treatment facilities. GES has a valid poison permit and a hazardous substances approval. The operation of the desalination of sea water at Palmachim is involved, among other things, with the use of hazardous substances. Accordingly, the facility operates as per a poison permit from the Ministry of Environmental Protection. At the sea water desalination facility at the Palmachim site, as part of the process of producing desalinated water, Via Maris discharges salts into the sea, in accordance with a discharge permit from the Ministry of Environmental Protection.

11.70.2. Material implications of the legal provisions on Granite

GES's business in the water and wastewater segment is subject to the environmental regulation which is relevant to the operating segment. The water and wastewater business is performed under the supervision of the Ministry of Health which performs routine tests to examine the quality of the water which is generated in the treatment facilities, and under the supervision of the Ministry of Environmental Protection and the Water Authority pertaining to the quality of the treatment of the wastewater in the treatment facilities and compliance with the generation permit. In addition, in the context of this activity, supervision is exercised also by government authorities such as the Water Commission and the Water Economy Administration.

On April 25, 2010, the Inbar Regulations were published in the Official Gazette. For details see Section 11.34.1 above.

On GES's chemical production site there is a wastewater treatment facility. The plant handles the production site's wastewater and customers' wastewater which is transported to the site with the approval and supervision of the Ministry of Environmental Protection.

At the beginning of 2010, pursuant to the need to comply with the Ministry of Environmental Protection's changes and

regulations, GES purchased an electric wastewater evaporator for the treatment of the industrial customers' wastewater as aforesaid, at the cost of approx. NIS 2.8 million, which joins the wastewater facility which exists on GES's site in Akko south. The evaporator began to operate during Q2 2010. The evaporator constitutes an additional stage in the treatment of wastewater (after the treatment in the wastewater treatment facility which is located on GES's chemical production site) and enables compliance with the requirements of the Business Licensing Regulations (Removal of Hazardous Wastes) with regard to salt concentrations in industrial wastewater, in addition to the other qualities which are required by law.

In addition, since a large slice of GES's activity is based on the use of chemicals, GES is supervised by the Ministry of Environmental Protection and by the municipal authorities and is committed to protection of the environment and working according to the environmental standards, laws and regulations of the Ministry of Environmental Protection and relevant conurbations. GES is certified for the Israeli Standard ISO 14001: environmental management system, since 2006.

GES's production site is checked and sampled on a regular and random basis by samplers of the Ministry of Environmental Protection and conurbations, through qualified labs. To the best of GES's knowledge, GES fulfills all of the laws, regulations, demands and standards for protection of the environment and currently institutes all of the measures in accordance with binding statutory requirements.

Over and above the acts and investments which are described above, the Company, based on Granite's management, does not anticipate additional material investments which are required from GES in order to fulfill the provisions of the law. The Company estimates, based on the management of the Granite company, that further investments in GES facilities will be required in 2012 at a scope of approx. NIS 200 thousand for the prevention of harm to the environment.

In addition, at this stage, it is impossible to estimate the expected cost of implementation of the Inbar Regulations, and the expected effect on Granite's profitability. It is also impossible to estimate the costs and income expected from upgrading the wastewater treatment facilities in treating the wastewater to the tertiary level.

11.70.3. Events which caused or are expected to cause damage to the environment

GES is involved in several legal and administrative proceedings pertaining to alleged damage to the environment which are described in Section 11.50.4 below and in Note 36 to the financial statements in Chapter C of this Report.

11.70.4. Material legal proceedings in connection with the environment

In March 2010, a hearing before institution of legal proceedings was held for GES, the Emek Hefer Partnership, and its managers, in the Ministry of Environmental Protection on a suspicion of polluting the Alexander Stream which was caused, according to the Ministry of Environmental Protection, by a leakage of filtrate into the stream, in December 2009. The proceeding has not yet ended and at this stage its results cannot be estimated. During 2010, Granite sold all of the holdings thereof in the Emek Hefer Partnership.

In June 2010, GES received a warning and invitation to a hearing from the Ministry of Environmental Protection due to the operation of an agricultural sludge treatment plant in Emek Hefer. In July 2010, GES applied to the Ministry of Environmental Protection through its legal advisors to remove the proceedings pursuant to GES's leaving the Emek Hefer Partnership at the beginning of the year.

In 2009, a claim was filed by Kibbutz Bahan which, for fee purposes, was set in the amount of NIS 10 million, against the Emek Hefer Partnership, GES, the partner in the Emek Hefer Partnership, and Afikei Emek Hefer Ltd., which supplies water within the territory of the Emek Hefer regional council. The remedy sought in the claim is a judgment to receive damages due to damage which was caused, according to them, to an avocado plantation, due to irrigation water which allegedly included filtrate which, according to the plaintiff, caused damage to the plantation. At this stage, the insurance company notified the partnership that the insurance coverage does not cover the event, the partnership's management is of the opinion that this notice is inconsistent with the insurance policy and hence, is in the process of examining the aforesaid notice. In April 2010 GES filed a statement of defense and various preliminary motions were filed. In October 2011, a ore-trial hearing took place, where the court suggested to the parties that an expert on behalf of the court be appointed in order to conduct an experiment testing whether it is possible to discharge "ballast" through the filters of the same type as those in the

avocado plantations' irrigation system. After receipt of the opinion, the hearing will be split so that firstly decided would be the issue of the various parties' liability later the issue of damages. The plaintiffs requested that the appointment of an expert be contingent upon the receipt of various documents and on the experiment being conducted in the existing system. A decision on this matter has yet to be given. In Granite's opinion, based on the relevant legal advisers, the claim's prospects are lower than 50%.

In April 2010, the Palmachim Desalination Plant Operation Company (the "**Operation Company**") received an invitation to a hearing in the Marine & Coastal Division of the Ministry of Environmental Protection, due to alleged deviations from the emission into the sea permit. In May 2010, the aforesaid hearing was held, following which the Operation Company acts, and continues to act intensively, to fulfill the requirements of the Ministry of Environmental Protection, as the same were clarified, *inter alia*, in the hearing summary of May 26, 2010, and in cooperation therewith.

In September 2010, the Operating Company received the Ministry of Environmental Protection's demand to receive details on the annual sales turnover of the Operation Company by virtue of Section 5C(b)(2) of the Prevention of Sea Pollution from Land Sources, 5748-1988 (the "**Law**"). According to the language of the notice, the Ministry of Environmental Protection requires this figure in order to determine the amount of the financial sanction which the ministry intends, according to the notice, to impose on the Operating Company. It shall be stated that under the Law and according to the Operating Company's annual sales turnover, the level of the financial sanction, insofar as will be imposed on the Operation Company, may be in the amount of NIS 600 thousand, subject to the ministry's ability to impose a higher amount when the alleged offenses are continuous or repeat offenses, while such amount cannot be estimated, and subject, in addition, to the ministry's discretion to lower the amount of the sanction, insofar as it will be decided to impose the same, pursuant to the franchisee company's and/or Operation Company's institution of acts to prevent a recurrence of the violation and mitigate the damage.

On December 27, 2011, the desalination facility obtained an updated marine discharge permit, which is in force until March 31, 2012, reflecting the current output of the facility, which amounts to 50 million cube per year.

In view of the aforesaid and considering the fact that the Operation Company currently acts intensively to regulate the

activities which were required by the ministry as provided in the hearing summary, and in view of the fact that some of these activities became known to the Ministry of Environmental Protection only after the dispatch of the letter dated September 16, 2010, and based on that this is a first hearing, and on the obtainment of a discharge permit as stated, according to the estimation of Via Maris's legal advisors, there are three main possible methods of action vis-à-vis the Operation Company: (1) enabling the Operation Company to complete regulation of the various activities, against the background that, as aforesaid, the Operation Company is acting intensively to fulfill all of the requirements of the Ministry of Environmental Protection; (2) imposition of a financial sanction on the Operation Company in accordance with Section 5C of the Law. As aforesaid, as of the Report Publication Date the Operation Company has not yet received an official notice pertaining to an intention to impose a financial sanction, and an argumentation proceeding has not yet been held, and no payment demand has been received; (3) filing an indictment against the Operation Company and institution of criminal proceedings according to Section 6 of the Law. In view of the time that has elapsed and in view of the fact that a demand for a financial sanction has not yet been received and it is unknown whether such a demand will even be received, no provision was included in the financial statements.

11.70.5. Environmental risk management policy

The Company's policy is to fully comply with all of the requirements of the provisions of the law pertaining to the environment. GES regularly implements the environmental standard ISO 14001 and is certified every year by the Standards Institute. GES performs occupational and environmental monitoring each year, in order to ensure that there are no deviations from the permitted level according to the standardization. GES performs once every three years an environmental risk survey at all of the Company's sites and performs the correction acts which are required according to the survey. In accordance with the guideline of the Marine & Coastal Division, GES performs continuous monitoring at the Palmachim desalination plant for the examination of the quality of the concentrated water and the raw water as specified in the emitting permit and reports, on a monthly basis, the figures which are required, according to reporting formats of the Marine & Coastal Division. According to the emitting permit, GES is obligated to perform a multi-year sea monitoring plan of the sea environment according to an approved plan and the guidelines of the Marine & Coastal Division. To the Company's best knowledge, the desalination

facility complies with the requirements of the sea monitoring plans.

In addition, GES employs a full time, safety and environmental protection manager, the responsibility of whom includes management, monthly supervision on the sites, training and establishment of emergency teams for an environmental event, event investigation and implementation of correction acts, in order to reduce the exposure to environmental risks. At Via Maris there is a part time safety manager. GES performs annual occupational health check-ups for employees under the provisions of the law by an occupational physician.

11.70.6. Amounts, environmental costs and provisions

The total costs borne by GES for the prevention or reduction of damage to the environment amount, in the year of the Report, to approx. NIS 300 thousand. Since in the context of the areas of its activity GES currently invests in issues of the environment, licensing, work safety and hygiene, the Company's management does not expect significant investments in the foreseeable future in these areas.

The desalination facility in Palmachim continuously invests in operations related to environmental protection issues and compliance with the provisions of the statutes and law applicable thereto. The costs of the actions for environmental protection are included within the current operating budget of the facility, while most of the amount is invested in reducing environmental risks and preventing damage to the environment. As s result of the facility's output's expansion to 90 million cube per year (see Section 11.71 below), the Company expects the environmental costs of the desalination facility's operation to increase in accordance with the expansion of the facility's operation.

Following are the material projected environmental costs until 2014 with respect to the desalination facility at Palmachim (in NIS in thousands):

Objective/Year	2012	2013	2014
For prevention	720	830	890
Damage repair	0	0	0

Furthermore, in accordance with the requirement of the Marine and Coastal Environmental Division at the Ministry of Environmental Protection, an extension of the desalination facility's marine desalination concentrate line from 800 meters to 2000 meters off shore is required, subject to the obtainment of an offshore construction permit. The execution of the extension of the desalination concentrate line is expected to commence by July 2012, subject to the obtainment of a construction permit. The projected cost of said execution is estimated by the Company at approx. €5.5 to 6 million.

The information as to environmental risks and manners of management thereof at GES, is forward looking information, as defined in the Securities Law, some or all of which may not materialize, or materialize differently than foreseen by the Company, as it is based, to a substantial degree, on expectations and assessments of the Company, considering past experience and its subjective estimations. From time to time, all or some of such assessments may change, due to, among other things, developments in GES's operation segments.

11.71. **Limitations and supervision of the activity**

11.71.1. Specific laws which apply to the activity

The water and wastewater unit

This activity in Israel is subject to the legal provisions which regulate the environmental protection issue, the main ones of which are the Water Law, 5719-1959, which sets forth a list of provisions pertaining to the preservation of the water sources and prevention of water pollution. Under of the Water Law, a list of regulations have been promulgated on the issue, including the Prohibition of Hard Detergents [the Water Regulations (Prohibition of Hard Detergents), 5734-1974], Prohibition of Emitting Brines into Water Sources [the Water Regulations (Prevention of Water Pollution)(Prohibition of Emitting Brines into Water Sources), 5758-1998] and pH Levels of Industrial Wastewater [the Water Regulations (Prevention of Water Pollution)(pH Levels of industrial Wastewater), 5764-2003]; the Water Regulations (Prevention of Water Pollution) (Use of Sludge and Removal thereof), 5764-2004), which deal with removal of the sludge which is created in the wastewater treatment facilities; the Water Regulations (Prevention of Water Pollution) (Metals and other Contaminators), 5761-2000, concern the protection of water sources from metals and other contaminators, by reducing the amounts of wastewater discharged from polluting factors and

restricting the concentration of contaminators therein; the Environmental Protection Law (the Polluter Pays) (Statutory Amendments), 5768-2008, aimed at protecting and maintaining appropriate environmental quality and improvement thereof, *inter alia*, through penalization; the Prevention of Contamination of the Sea by Overland Sources Law, 5748-1988 and the Prevention of Contamination of the Sea by Overland Sources Regulations, 5750-1990, concerning the prohibition of waste into the sea; the Municipal Authorities Law (Wastewater), 5722-1962 which deals with collection of wastewater and treatment thereof; the Nation's Health Ordinance, 1940, and the regulations promulgated thereunder including, the Nation's Health Regulations (the Sanitary Quality of Drinking Water), 5734-1974, which determine a general framework for all water types and handling thereof, including water generated via sea water desalination plants; the Business Licensing Law, 5728-1968, and the regulations promulgated thereunder, including the Business Licensing Regulations (Salt Concentrations in Industrial Wastewater), 5763-2003, which determine permitted levels of pollutant concentrations in wastewater discharged from a plant to a treatment facility; in addition, business licenses and toxic materials permits that are given to any plant may include instructions for treatment of wastewater. Furthermore, in the year of the Report, additional laws, which apply to this segment, have entered into effect, among which are: The Clean Air Law, 5768-2008, which provides definitions and requirements pertaining to the conduct of plants and facilities, emission permits, if required, their financial cost and execution timetable; the Clean Air Regulations (Air Quality Values) (Provisional Directive), 5771-2011, which provide target values, environmental values and cautionary values of substances listed in the addendum to the regulations.

In addition, on January 25, 2010, the Knesset's Committee of Internal Affairs and Environmental Protection approved regulations which will take effect gradually, from July 2010 until January 1, 2015. Inbar Regulations impose duties both on a wastewater producer and on operators of wastewater treatments facilities for treatment of the wastewater to the strict values that are set forth in the regulations. In addition, Inbar Regulations impose duties on a wastewater producer and on an operator to monitor and control the wastewater, sample the treated wastewater which comes out of the treatment facilities, and extensive duties to report and publish the information to the public. In addition, a special emphasis has been placed in them on transparency to the public, including a duty to report and publish results of the tests which were performed of the treated wastewater. In addition,

the Inbar Regulations also include, *inter alia*, transitional provisions with regard to wastewater treatment facilities which were established immediately before the publishing of the regulations, such that within 5 years (by January 1, 2015) all of the treatment facilities in Israel will produce water in the tertiary quality level (tertiary treatment is an additional treatment of treated wastewater which raises the quality of the treated wastewater such that the treated wastewater may be used for unlimited irrigation of agricultural growths for human consumption and/or irrigation above aquifers, without a concern for public health or aquifer pollution).

In addition, the water and wastewater unit is affected by the Water and Sewage Corporations Law, 5761-2001, which mainly targets ensuring a level of proper service, quality and credibility for consumers at reasonable prices, ensuring the designation of revenues to investments in the segment and regulating the business and professional management of the municipal sewage and water economy. The Water and Sewage Corporations Law was amended in 2004 imposing upon municipal authorities the duty to switch to management of the water economy, including treating sewage and wastewater, through public service water corporations to be incorporated by the authorities, while prohibiting the self-operation of water and sewage services.

Palmachim sea water desalination plant

As part of its operations, GES operates the desalination facility in Palmachim for sea water desalination, designated to supply water of drinking water quality to the pipes of the company of.

The sea water desalination process includes a series of chemical and physical processes whose purpose is to receive the sea water and prepare the same for membrane desalination through several stages of preliminary treatments.

The desalination facility's operation is subject to the provisions of various environmental laws, pertaining to, *inter alia*, the prevention of contamination of water sources, the assurance of the sanitary quality of drinking water and the matter of hazardous substances. Among the laws applicable to the facility's operation are: The Water Law, 5715-1955, which stipulates various provisions for the prevention of water sources' contamination, the People's Health Ordinance, 1940, the People's Health Regulations (the Sanitary Quality of Drinking Water), 5764-1974, the Business Licensing Law, 5728-1968 and the regulations thereunder, the Hazardous Substances Law, 5753-1993 and the regulations thereunder, the Overland Sources Law and the regulations thereunder,

the Protection of Coastal Environment Law, 5764-2004, the Clean Air Law, 5768-2008, the Freedom of Information Law, 5758-1998 and the regulations thereunder, and more. The Prevention of Sea Contamination from Overland Sources (Levy for Prevention of Sea Contamination), 5771-2011, which came into effect on October 1, 2011, provide that the holder of a marine discharge permit must pay a levy for preventing sea contamination, and report to the Ministry of Environmental Protection, quarterly, various data with respect to the wastewater discharged thereby. The regulations further provide that the permit holder may file an application for reduction of the levy's amount. Accordingly, as of the date of this Report, Via Maris is in the process of preparing a reduction application. The Company estimates, based on the Granite Group management, that costs relating to the levy are not expected to have material impact its operation.

Pursuant to the terms of the business license granted to the facility, it is provided that the facility is required to comply with a threshold level of water alkalescence. As of the date of this Report, the facility does not comply with the required level due to an inconsistency between the required levels and the original planning characteristics of the facility, and the Ministry of Health is aware of this issue. The Company expects that the issue will be resolved upon the enactment of the People's Health Regulations (the Sanitary Quality of Drinking Water), 5771-2011 all as described hereunder.

During the past year, several environmental bills have been published, which are in different stages of legislation and may affect the desalination facility's operation, as specified below: (1) the bill of People's Health Regulations (the Sanitary Quality of Drinking Water), 5771-2011 –On November 21, 2011, the Knesset's Internal Affairs and Environmental Protection Committee commenced discussions with respect to the aforesaid bill, which is meant to replace, insofar as it will be approved, the People's Health Regulations (the Sanitary Quality of Drinking Water), 5734-1974, which are currently in force and apply to the facility. Insofar as the People's Health Regulations' bill is approved, the Company may be required, among other things, to execute operational and other changes in the desalination facility. In the People's Health Regulations' bill, the facility is further required to comply with a threshold level of water alkalescence. As the facility is of the first generation of desalination facilities, which were not required to comply with alkalescence values at the outset (i.e., the tender documents included no reference to such parameter), the desalination facility was not planned and is not prepared, in terms of area and technology, to comply with the

alkalescence requirement currently included in the People's Health Regulations' bill. Granite is working vis-à-vis the Ministry of Health in order to reach an agreement which will facilitate granting the facility an extenuation with respect to the alkalescence parameter, in accordance with a clause in the draft regulations, which provides that the director may permit a different required level in this parameter, as long as the new permitted level brings the water to an equivalent stabilization level. The Company expects, based on Granite's management, that an approval of the People's Health Regulations' bill may have an effect on the manner of operation of the Palmachim desalination facility, which depends, *inter alia*, on an arrangement with the Ministry of Health as to the alkalescence levels whereto the facility will be subject. Therefore, as of the date of this Report, the Company is unable to assess the effect of the People's Health Regulations' bill on the operation of the desalination facility; (2) the bill of Environmental Protection (Information on Emissions and Discharges to the Environment), 5772-2012 – the bill's objective is to impose a duty to report contaminating factors with respect to emission and discharge of waste and contaminators to the environment and to create an emissions' register, to be made available for public perusal. As per an updated version of the bill, the bill will apply to a desalination facility of an output exceeding 30 million cubic meters as well. As of the date of this Report, the aforesaid bill has passed first reading in the Knesset's plenum and has been moved to preparation for second and third readings to the Internal Affairs and Environmental Protection Committee. The reporting and environmental information system is expected to be operating regularly sometime in 2013. As of the date of this Report, the Company, based on the management of the Granite company, does not expect the bill to have a significant effect on the desalination facility's operation, if the legislation process will have been finalized. (3) the bill of Prevention of Land Contamination and Contaminated Lands Rehabilitation, 5771-2011 – the bill prohibits, *inter alia*, the performance of actions causing or capable of causing land contamination, and also imposes the liability to bear the costs of damages and expenses caused as a result of the contamination upon the contaminating factor. The bill further imposes various active duties on the contamination factor, the owner or holder of a contaminated land, among which are, *inter alia*, a report of any concrete suspicion or concern of the land being contaminated, the immediate performance of various actions for the reduction of the contamination and the prevention thereof any time such suspicion is aroused as stated, the performance of various surveys with respect to the land, and the bill also provides financing mechanisms for the treatment

and rehabilitation of contaminated lands, a duty to register the land as contaminated at the Land Registry and more. As of the date of this Report, the Lands Rehabilitation bill passed first reading. The Company estimates, based on the management of the Granite company, that insofar as the bill matures to legislation, no significant effect on the costs of the desalination facility's operation is expected.

GES holds all of the licenses and permits which are required by law, as aforesaid.

It shall be stated that the desalination plant's infrastructures were constructed in the manner that would prevent leakage and spillage, while instituting measures to monitor leakage of chemicals and water concentrate.

Chemical Segment

This activity is subject to legal provisions which regulate the environmental protection issue, the main ones of which are the Hazardous Substances Law, 5753-1993, which determines that a person shall not engage in toxic materials unless he has a toxic materials permit from the relevant supervisor at the Ministry of Environmental Protection. Hence, GES holds toxic materials permits and keeps a "toxic materials register" for the chemicals activity on all of the Company's sites. Furthermore, the activity of the chemicals unit in all that pertains to the removal of hazardous wastes is subject to the Business Licensing Regulations (Removal of Hazardous Wastes), 5751-1990 and the Hazardous Substances Regulations (Import and Export of Hazardous Wastes) Amendment, 5768-1998, which set forth that the import and export of hazardous wastes to and from Israel will be performed only in the context of a permit which be issued by the relevant supervisor at the Ministry of Environmental Protection. The production and storage site of hazardous substances of the chemicals unit of the Company is a "dangerous plant", as defined in the Business Licensing Regulations (Dangerous Plants), 5753-1993, the plant must fulfill the requirements determined in the regulations such as: keeping a plant file and reporting to the licensing authority on the inventory of the hazardous substances.

Since part of GES's activity is performed outside of Israel, GES is required to fulfill the requirements of any law including the local environmental requirements which exist in the relevant countries.

11.71.2. Safety

In GES there operates a safety department which regularly and strictly acts for the implementation of all of the work safety and hygiene regulations and laws. The department is responsible for the implementation of the work safety instructions through various means including the maintenance of a system of training sessions on safety (as required by law and in accordance with Organization and Supervision of Work Law, 5714-1954 and its regulations and the Work Safety Ordinance, 5730-1970 and its regulations), designated training sessions for the various work departments, according to the various risks, drills for the emergency teams and various qualifications for employees.

The chemicals unit ensures compliance with the provisions of the work safety rules. The activity of the chemicals unit is subject to the rules of the Work Safety Ordinance [New Version], 5730-1970 and to the work safety regulations which are relevant to its activity such as the Work Safety Regulations (Prohibition of Work with Specific Carcinogenic Substances), 5745-1984 and the Work Safety Regulations (First Aid at Work Places), 5745-1988.

In February 2010, GES was certified for the International Work Association Standard: ILO-OSH 2001, which guides GES's policy in safety and hygiene, commitment to constant improvement, planning of the safety management system, control, decision and measurement of the safety and hygiene performances. GES is under regular supervision of the supervisor of work at the Ministry of Industry, Trade & Labor, who examines and monitors its compliance with the laws and work hygiene and safety regulations. GES holds, as needed, activity vis-à-vis the fire fighting services and specialty planning companies, in order to fulfill the requirements of the fire fighting services for prevention of fires and treatment of fire events.

The operation of a production site requires the obtainment of a business license as provided in the Business Licensing Order (License Requiring Businesses), 5755-1995. The GES production site at the Askar sit in Akko had a valid business license until December 31, 2011 and GES is working to extend it in coordination with the authorities. The remaining GES sites, including the desalination facility in Palmachim, operate in accordance with a valid business license.

GES is recognized as a certified importer and exporter by the authorities.

GES is a licensed supplier of the Ministry of Defense, the Israel Aerospace Industries and the Israel Electric Corporation Ltd. Work vis-à-vis the customers is performed through tenders or RSPs.

11.71.3. Standardization and quality control

In February 2010, GES joined the club of organizations who implement systems for the management of employment health and safety, and was certified for the International Work Association Standard: ILO-OSH 2001, which guides GES's policy in safety and hygiene, commitment to constant improvement, planning of the safety management system, control, decision and measurement of the safety and hygiene performances. As aforesaid, GES is certified for Israeli standard ISO 14001. GES performs environmental monitoring to test the levels of exposure to chemicals and noise at the various work stations, as required by the regulations. In addition, GES's employees who come into contact with risk factors (chemicals and noise) undergo annual occupational check-ups by an authorized medical body.

11.72. **Material agreements**

11.72.1. Via Maris Desalination Holdings Ltd.

GES holds 100% of the share capital of Via Maris Desalination Holdings Ltd. ("**Via Maris**"). This is subsequently to GES's engagement, on October 3, 2011, in an agreement to purchase the holdings of TAHAL Consulting Engineers Ltd. (27.9%), including the right for repayment of shareholder's loan, which TAHAL provided to Via Maris in consideration of approx. NIS 62 million (the transactions was finalized on November 24, 2011).

In October 2002, the concessionaire company signed an agreement with the State of Israel (the "**Concession Agreement**") for the planning, financing, establishment, operation and maintenance of a sea water desalination plant with an annual capacity of 30 million cubic meters using the BOO (Build, Own and Operate) method (the "**Desalination Plant**").

The concession period of approx. 25 years will end in 2029. In accordance with the concession, Via Maris is obliged to establish a desalination facility with an annual production capacity of 30 million cubic meters and to supply the State the quantity of desalinated water to be determined by the State, with the minimum quality determined in the Concession Agreement. In return for the establishment of the

desalination facility and its operation, Via Maris is entitled to receive a fixed payment for the availability of the desalination capability and a varying payment for the quantities of desalinated water which will be supplied. In accordance with the provisions of the Concession Agreement, failure to supply water in a timely manner, in the quantities determined by the State, or the supply of water at a quality level lower than the minimum quality determined in the Concession Agreement, shall incur the payment of liquidated damages to the State and the adjustment of the price of the water.

As of May 2007, Via Maris has been supplying water to the national water network at the required level of quality. On August 30, 2007, Via Maris received final approval for operations (PTO).

GES provided Via Maris with operating and maintenance services for the desalination facility in accordance with agreements between GES and Via Maris which were valid until completion of the expansion of the plant in June 2010. After that date, the facility is operated by Via Maris Operations Ltd., while GES provides Via Maris with manpower services for the operation of the facility as per an agreement of December 30, 2010..

In June 2008, the Inter-ministry Tender Committee for Desalination Matters contacted the three operators of existing desalination facilities, asking them to propose expansions of the quantities of water desalinated at stated prices and stipulate the time periods required for the preparations necessary for the supply of those quantities. in March 2009, an agreement was executed with the State for the supply of the additional quantities of an additional five million cubic meters per annum on an immediate basis (Stage A) and of an additional ten million cubic meters per annum after 14 months (Stage B) (the "**Expansion Agreement**"). On April 28, 2009, Via Maris began the immediate supply of an additional five million cubic meters per annum and in April 2010 it completed the expansion of the facility for the supply of the additional ten million cubic meters per annum. The permanent operation approval was received on July 4, 2010. It shall be stated that the expansion of the facility has no effect on the concession period. It should be noted that according to the concession conditions, Via Maris may only sell water to third parties with specific approval from the State of Israel.

On August 13, 2009, Via Maris signed a financing agreement with the bank, in reference to several credit frameworks extended to Via Maris, which shall be used to finance

approx. 90% of the costs of the expansion, which are in the amount of approx. $20 million. In addition, further credit in the amount of approx. NIS 85 million was extended to Via Maris for the financing of the repayment of the shareholder loans.

Supply of Additional Quantities and an Additional Expansion of the Desalination Facility

In May 2011, Via Maris signed an agreement with the State, to supply additional quantities of desalinated water from the excess ability of the desalination facility, beyond the existing engagement. The agreement is for a term ending at the end of 2013. Furthermore, following the government's decision to increase to desalinated water quantities in the existing facilities, in July 2011, the State invited Via Maris to submit an offer for further expansion of the facility to a total annual production of approx. 90 million cubic meters (double the output). Such offer was submitted by Via Maris in September 2011. On October 30, 2011, an agreement was signed between the concessionaire company and the State ("Amendment no. 6 of the Concession Agreement") to double to desalination facility's output ("the additional expansion"). Pursuant to the agreement, the output's doubling will be done in two stages: by the end of 2012, approx. half of the additional output will be added and the balance will be completed by July 13, 2013. The overall scope of investment in the project is estimated at approx. $100 million. Via Maris's annual revenues for the addition of desalinated water will exceed the full increased amount by approx. NIS 95 million, as described above. Insofar as Via Maris will have not meet the timetables set in the agreement, penalties will be imposed thereon for the lag as provided in the agreement. On December 25, 2011, GES engaged in an agreement with the Construction Partnership, whereby GES will provide planning services to the project of additional expansion of the desalination facility as aforesaid, including services of superior supervision of its construction. For details with respect to the financing agreement in connection with the additional expansion, see Section 11.74.1 above.

The Acquisition of Middle East Tube Company Ltd. ("**Tubes**")

On February 15, 2010, the Company signed an agreement with Tubes, whereby it purchased its holdings (22.1%) in Via Maris, the rights deriving thereto from the expansion, and its rights in the shareholders' loans it provided to Via Maris in consideration for NIS 50.7 million, after an adjustment due to the partial repayment of shareholders' loans which was performed immediately before the time of closing of the

transaction. In addition, Granite provided additional guarantees to Via Maris in the amount of approx. NIS 30 million instead of Tubes. The transaction was closed on April 28, 2010.

On December 30, 2010, in the context of the restructuring of the holdings in the Via Maris group, the holdings of the owners of Via Maris Desalination Ltd., Via Maris Operation Ltd., and Via Maris- Partnership under organization (the "**Transferred Companies**") were transferred to Via Maris Desalination (Holdings) Ltd., against the issuance of share capital. The transfer was performed in accordance with the provisions of Section 104 B of the Income Tax Ordinance. At such time and immediately before the aforesaid restructuring, Granite's holding in Via Maris Desalination Ltd. was transferred to GES. The aforesaid transfer did not derogate from Granite's financial and legal responsibility in all that pertains to Via Maris.

Other Business and Information on the Granite Group in its Entirety

11.73. **General information**

The Granite Group has several different businesses which are not included in the operating segments described above, and from which revenues is immaterial to Granite Group. Below is a description of the main businesses:

Tourism activities – the Mini Israel site

The Granite Group holds a 50% stake as a limited partner in the limited partnership, which built and operates the unique tourist site known as “Mini Israel”, where miniature models of well known sites in Israel are on display.

Until December 31, 2011, the Granite Group has invested in a capital note and shareholders loans for Mini Israel, approx. NIS 110 million. The Granite Group has extended a limited guarantee in the amount of NIS 12 million to guarantee the partnership’s compliance with the conditions of the government grant awarded by the Investments Center.

Communications infrastructure activities

Granite holds 60% of the rights in Green Anchors Ltd. ("**Green Anchors**"), which leases real estate assets and sub-leases them to as many wireless communications parties as possible, primarily, mobile phone companies ("**Telecommunications Operators**") and provides Telecommunications Operators with civil engineering services. As of December 31, 2011, Green Anchors leases 52 sites, with an average occupancy rate of 2.2 operators per site and holds a construction permit

for a new site, which is expected to be built during the first quarter of 2012. Green Anchors is also in the process of receiving building permits for approx. 5 more sites and is actively seeking additional sites.

11.74. **Human capital**

11.74.1. Breakdown of employees by operating segments

The following is the breakdown of employees in Granite's operating segments – Sonol direct marketing and fuelling and commerce complexes, Supergas, Tambour, GES and others as of December 31, 2011:

Segment	**No. of employees December 31, 2011**
Sonol direct marketing and fuelling and commerce complexes segment	1,860
Supergas segment	300
Tambour segment	686
GES segment	**279**
Total employees	**3,125**

Between 2010 and 2011, there was an insignificant decrease in the number of employees in the Granite Group.

Furthermore, Granite's CEO is at the head of Granite's management. Subject to Granite's CEO are the CFO, the Chief Strategy & Investments Officer, a legal counsellor and a secretary of the company. The Company's CEO also serves as the Chairperson of the Board of Directors in major subsidiaries in the Group.

11.74.2. Investments by the Company in training and instruction

The Granite Group conducts professional training and instruction for its employees in accordance with the employee's position, the requirements of the law and the needs of the Granite Group. Employees of the Granite Group take part, *inter alia*, in exhibitions, seminars and training on various topics relating to the Group.

11.74.3. Benefits and nature of the employments agreements

The Sonol direct marketing and fuelling complex segment

About 273 employees of the Sonol operating segments (excluding the employees of fuelling complexes) are employed pursuant to the provisions of Collective Agreements. Sonol has an agreement regarding a change and extension of the Collective Employment Agreements with

representatives of the *Histadrut* national workers union and the Workers' Union. The agreement relates to efficiency measures, including, *inter alia*, waivers of various salary benefits due to the employees. The validity of this Collective Agreement was extended to 2018.

In addition, during 2010 Sprint Transportation's employees started being employed according to unique schedule to the collective agreement of Sonol. In addition, in November 2010 Sonol engaged in an agreement with the *Histadrut* and representatives of the Workers' Union in Sprint Motors that settles the employment terms of approx. 460 employees of the fuelling complexes' employees. The Agreement applies to employees with tenure of two years and more and the managers of fuelling complexes. The agreement is in effect for a period of 5 years.

There are general collective agreements, applicable to all of the employees in the companies in the Oil Distillates operating segments by virtue of their companies' membership in the Israel Industrialists' Association, relating, *inter alia*, to salary terms, to a transition to a 45-hour week of 5 work days, to payment of convalescence allowance, sick leave days, vacation days and the reimbursement of expenses for travel to and from work. In addition, the abovementioned employees are subject to special collective agreements. These agreements are revised from time to time through negotiations between the workers' union committee, representatives of the *Histadrut* and the management.

Some of the employees of these operating segments who are subject to the collective agreements and who are not employed under personal employment contracts are permanent employees. Some of them are in an interim period, in the end of which it will be decided whether they would be transferred to the status of permanent employees and a minority of the said employees have temporary status and their salary is determined according to actual hours of work. By virtue of Sonol's membership in the agreement with the Industrialists Association, all of the employees in these operating segments are insured with comprehensive pension insurance.

Approx. 1,390 employees are employed by the public fuelling stations operated by the Granite Group. In addition thereto, 94 headquarter employees and station managers are employed. As stated above, approx. one third of these employees are subject to a collective agreement signed on November 18, 2010 for a period of 5 years, regulating their terms of employment. The terms of employment of the rest are based mainly on the provisions of the Labor Laws.

According to the Group's past experience, most of the aforementioned employees are employed for short periods. The costs of employing some of these employees are affected by, *inter alia*, the rate of the minimum wages provided by Israeli law.

The employment terms of the rest of the employees (approx. 100 employees), including the officers and senior management in these operating segments, are organized through personal employment contracts, and include pension coverage or managers' insurance in various tracks, advance training funds, vacation entitlement, convalescence pay and sick leave, corporate participation in mobile telephone bills, reimbursement of sustenance expenses, prior notice period for resignation and dismissals, maintenance of confidentiality and non-competition. The salary of these employees is generally not linked to actual hours worked (no overtime pay) and some of these employees are entitled to a company vehicle.

Supergas segment

The 124 employees of Supergas are employed in accordance with the provisions of collective bargaining agreements. Supergas's plant collective bargaining agreement was extended after the date of the Report, in January 2012, and it is in force until September 2012.

There are general collective bargaining agreements, which apply to all of the Company's employees, who are not employed through personal employment agreements, by virtue of its membership in the Industrialists Association of Israel, pertaining, *inter alia*, to salary terms, transitioning to a 45-hours in 5-working days week, payment of a convalescence allowance, sick days, leave days and reimbursement of commuting expenses to and from work. Additionally, as stated, specific collective agreements apply to the employees as well. Such agreements are revised, from time to time, in negotiations between the workers' committee, representatives of the General Federation (*Histadrut*) and the management.

Some of the employees in this business segment, who the collective bargaining agreements apply to and who are not employed through personal employment agreements, are permanent employees. Some of them are employed for an interim period of 5 years, at the end of which it will be determined whether their status will change to permanent employees. A minority of the employees have a temporary employee status and their wages are determined according to actual working hours. By virtue of Supergas's membership in

the Industrialists' Association agreement, all of its employees are insured with comprehensive pension insurance.

The employees who are subject to the specific collective agreement are divided into Generation A employees (34 employees), who are entitled to special benefits, and Generation B employees (approx. 90 employees), whose employment terms are slightly improved compared with the provisions of the law. An employee who was instated at a Generation B status, will be classified as a trial-employee for a period of five years, at the end of which he will be classified as a permanent employee.

Salary discussions are held once a year with respect to the aforesaid employees and employees who are entitled to promotion receive salary premiums.

The employment terms of the rest of the employees, including the officers and senior management employees in the business segment, are set through personal employment contracts, which include pension coverage or directors insurance of various routes, an advanced training fund, leave entitlement, convalescence pay and sick days, contributions to cellular phone expenses, reimbursement of board and lodging expenses, a period of advanced notice of resignation and discharge, confidentiality and non-competition. Some of such employees are entitled to a vehicle.

Tambour segment

This business segment includes permanent employees, who are subject to specific collective agreements, employees working under personal contracts of employment, temporary workers employed under the principles of the special collective agreement and general labor laws, and seasonal workers, employed in accordance with agreements with manpower companies and the provisions of the law. On July 14, 2010, the validity of the specific collective agreements and the customs that apply to the Company, has been extended until December 31, 2012.

Permanent employees – In December 2003, a collective agreement was signed for 2004 and 2005, according to which the permanent employees were classified in three groups, a classification also relevant to the Date of the Report.

Veteran permanent employees – As of the date of the Report, this group consists of about 69 employees, whose employment terms are stipulated in a collective agreement from 1979, which has been amended many times during 1979-2010 and remains in force until the present date.

New permanent A employees – As of the date of the Report, this group consists of 19 employees. Their salary terms are as they were prior to receiving permanent status, with the addition of advance training fund. Pursuant to the collective agreement, the process of terminating the employment relationship of these employees is identical to that of the permanent veteran employees. If the number of permanent veteran employees falls below 88, the quota is completed by the transfer of any employees to the status of new permanent A employees.

New permanent B employees – Pursuant to the collective agreement, this group of employees numbers of at least 22; the employment terms of these employees are mostly based on the provisions of the labor laws, with the addition of advance training fund. The termination of their work is pursuant to a management decision, in accordance with the criteria stipulated in the Collective Agreement and on payment of a retirement grant at a rate of up to 40% of the last salary determining severance pay.

Employees under personal contracts – The other employees of the Tambour Group, including officers, senior management and sales personnel, are subject to personal employment contracts, including salary, social benefits and related conditions in accordance with the type of work and seniority of the employee, prior notice for resignation and dismissal and maintenance of confidentiality and non-competition. Most of the personal contracts include an explicit provision regarding the application of Clause 14 of the Severance Pay Law, 5723-1963 ("**Clause 14**"), with the balance covered by full allocations for severance pay. Personal contracts, which were signed with approx. 35 of the employees of the subsidiary Tzah Serafon, indeed do not contain such express provision as to the application of Clause 14, however, the arrangement pursuant to Clause 14 applies to such employees, , pursuant to the provision of a general collective agreement with respect to a framework for comprehensive pension insurance in the industry, which was signed between the Industrialists Association and the General Federation of Workers (*Histadrut*), and applies to Tzah Serafon, which is a member of the Industrialists Association.

Temporary workers – The temporary workers are employed in the paint plants in Akko pursuant to the principles of the Collective Agreement, which mainly grants the temporary workers rights anchored in the labor laws and their relevant expansion orders. Upon the end of the temporary work term, the employee's employment is ended or the employee is transferred to the group of employees under personal

contracts, or to a status of a new permanent employee, all according to a decision of the Tambour Group management.

Seasonal workers/employees of manpower companies – These workers are employed through manpower companies for periods of up to three months, as necessary.

The GES segment

In this operating segment are employed permanent employees, to whom special collective bargaining agreements apply, employees who are employed according to personal employment agreements, temporary employees who are employed according to the rules of the special collective bargaining agreement and general employment laws, and seasonal workers who are employed in accordance with agreements with the placement agencies.

Permanent employees – are divided into two groups as follows:

Permanent employees who are employed according to a collective bargaining agreement – As of the Date of the Report, this group consists of 54 employees (generation A and generation B). The terms of their employment are determined in the collective bargaining agreement of 1988 which is valid until today. GES workers who are employed in the manufacturing department, workshop and junior clerks [according to an agreed (defined) list of professions] are subject to the terms and conditions of the collective bargaining agreement as aforesaid.

Permanent employees according to personal agreements – As of the Date of the Report, this group comprises 167 employees. There are standard employment agreements between GES and these employees which determine, in most cases, the employee's salary, the working hours, social benefits such as managers' insurance and/or provident funds and/or pension fund, advanced training fund, entitlement to leave, recuperation pay and sick days, participation in mobile phone expenses, reimbursement of *per diems*, prior notice period for resignation and dismissal, confidentiality and non-competition. Most of the employees are employed on the basis of a global salary. Approx. one half of the employees receive a company car for their use for the purpose of carrying out their duties. Sales persons have quarterly incentives. All of the personal contracts include an explicit clause regarding the application of Section 14 of the Severance Pay Law, 5723-1963 and the balance is covered by full severance pay provisions.

Monthly employees – employed according to special personal part-time agreements and receive hourly wages. Most of the monthly employees are students who work in the framework of GES as part of performance of a thesis and/or internship. At the end of the period they either leave or are absorbed into the system as regular employees.

Temporary employees – GES has agreements with several placement agencies for the employment of temporary professional workers. The temporary workers are usually employed for specific needs and for predefined periods.

11.74.4. Liabilities due to termination of the employee-employer relationship

The liabilities of the Granite Group in relation to the termination of the employee-employer relationship of employees of theses operating segments are covered by regular payments to insurance companies in respect of managers insurance policies, pension funds and mutual trust funds, and through a provision in the financial statements of the Granite Group which reflect the Company's obligations not covered as aforesaid.

11.74.5. Employee remuneration plan

In relation to employees working under personal contracts, the Granite Group provides these employees with incentives, *inter alia*, based on the achievement of targets in accordance with the employee's position and rank (employees of the fuelling complexes are rewarded with sale commissions based on performance). The targets are derived from the Granite Group's work plan. The remuneration plans are not stipulated in personal employment contracts and vary from year to year, except with respect to Granite's CEO and CEOs of subsidiaries in respect of whom an annual grant shall have been determined which is computed as a percentage of targets defined in such agreements.

On March 17, 2010, the Audit Committee and the Board of Directors of Granite approved the grant of 2,238,677 phantom units to the CEO of Granite, entitling him to monetary remuneration derived from an increase in the value of the shares of Granite, on the basis of a mechanism set forth in the plan. The number of phantom units, if they were options exercisable into shares of the Company after their allocation, constitute 1.5% of the Company's issued and paid-in capital on a fully diluted basis, as of the date of their grant. The right to exercise the phantom units will be conferred in equal parts on three dates: September 1, 2010, September 1, 2011 and September 1, 2012. For further

details, see Note 25B to the financial statements in Chapter C of this report.

Tambour has approved an option plan for the purchase of shares in Tambour to be offered to employees, directors, consultants and other service providers of Tambour and its subsidiaries, related companies or its parent company. During the month of March 2010 senior employees at Tambour, including Tambour's CEO, exercised 410,000 options for the acquisition of shares of par value NIS 1 of the Company in the framework of the plan as aforesaid. After exercises, 60,000 exercisable options remained which are allocated to Tambour's CEO. The options will expire in December 2014.

On March 27 2010, the audit committee and the board of directors of Tambour approved the granting of 810,528 phantom units to Tambour's CEO (through a company owned by him), which entitle him to financial compensation deriving from the appreciation of Tambour's stock, based on the mechanism specified in the plan. For details see Note 25E to the Financial Statements in Chapter C of this Report. According to an agreement between Tambour and the CEO of its subsidiary Tambord, in addition to the 5% of Tambord shares held in trust therefor, the CEO was granted a share-based payment, in the framework of which, upon fulfillment of the service conditions and meeting the performance targets defined in the agreement, he will be entitled to 2%-4.5% of Tambord's share capital.

11.74.6. Loans to employees

The Granite Group extends loans to employees in accordance with its internal procedures; including taking into account the employee's salary. The loans are linked to the consumer price index and bear interest at rates stipulated in the Income Tax Ordinance. In addition, the employees pay VAT on the interest income. The balance of the loans to the employees as of the Date of the Report was in an immaterial amount.

11.74.7. The officers and senior management employees

11.74.8. In August 2010, Mr. Tamir Poliker gave notice of his resignation from the position of Sonol's CEO. In October 2010, Mr. Nir Galili was appointed as his replacement.

11.74.9. Exemption and Indemnification of Officers

Officers of Sonol, Tambour and GES receive letters of exemption and indemnification as approved by the organs of the aforesaid companies and in accordance with the law.

For details with respect to exemption and indemnification letters that Granite provides to officers thereof, see Section 11.76.1 below.

11.75. **Intangible assets**

11.75.1. The Granite Group is the owner of two patents registered in Israel relating to an automatic fuelling system in vehicles. In respect of this system, a patent was also registered in the United States. In addition, three patents have been registered in GES's name in Israel, two of which were also registered in the U.S., with respect to wastewater treatment, control of bacterial contamination in water and water treatment.

11.75.2. In addition, the Granite Group has a number of registered trademarks, including, in the Sonol segment (both parts thereof) the name: Sonol Israel Ltd. and the Sonol logo and the name "Sogood" of the fuelling stations' convenience stores, in he Supergas segment, the name: Supergas Israel Gas Distribution Company Ltd. and the Supergas logo, the name: "Natural Supergas" and the name: "Natural Supergas of the Azrieli Group" including the logo of Natural Supergas Ltd.. In the Tambour segment, *inter alia*, "Tambour", "Serafon", "Tambord", "Superacryl", "Polysid", "Vernit", "PolyOr", "Superlak", "Bondroll Super", "Classimo", "Poligag", "Tamglass", etc. In addition, Tambour has registered trademarks outside of Israel in accordance with the scope of sales of the products sold, such as registration of

the brand "TAMBOUR" in the European Union. In the GES segment, GES registered a trademark on goods and services which are provided thereby.

The registered trademarks are very important, because, through them the customers identify the companies of the Granite Group. According to the management's estimate, based on the best of the Granite management's knowledge, the life of the said trademarks is extensive because of the many years of use of these trademarks and their dominant status in the market.

The costs invested in recent years in the registration of the trademarks and the development of the patents are immaterial for the Granite Group.

11.75.3. In the Sonol operating segment, the Group has intangible assets, mainly including distribution rights, supply rights and station operation rights. In this respect, see also Note 16 to the Company's Financial Statements in Chapter C of this Report.

11.75.4. In December 2002, Tambour signed a licence agreement with Henkel KGaA ("**Henkel**"), a German company which manufactures various products, including building additives (in this Section: the "**Products**"). The agreement was valid until December 31, 2010.

In accordance with the agreement, Tambour commenced, in 2003, to market products under the joint brand of Henkel Tambour. Pursuant to the agreement, the Products shall bear the Henkel trademark. As of the Date of the Report, the parties are conducting negotiations with respect to extension of the agreement and modifications thereto.

11.75.5. The Tambour Group has a number of franchise agreements with the BASF corporation to market the products of Tambour on an exclusive basis, and to manufacture certain Glazurit-type products exclusively by Tambour and to import and manufacture, sell and market some of BASF's products in the field of chemicals for construction in Israel and the areas of the Palestinian Authority.

11.75.6. From time to time, and in the ordinary course of business, Tambour enters into franchise agreements with multinational corporations to receive production know-how or a distribution franchise for various unique products, in various operating segments.

11.75.7. In 2007 a license agreement was signed between Dan Viro, 87.5% of whose share capital is held by GES on the date of the Report, and N-VIRO International Corporation ("**N-VIRO**"). According to the license agreement, N-VIRO granted Dan Viro a license to use N-VIRO's technology for the purpose of the construction and operation of a land treatment facility for "Dan Area Water" – Agricultural Cooperative Water Society Ltd. (Shafdan).

11.75.8. GES is the official representative of several companies in the field of the marketing, manufacturing and import of such companies in Israel. Among the companies are Henkel (field treatment products in Israel), Fuchs Lubricants (emulsion oils, protective oils and special purpose oils), 3M (products in the field of gas and liquid filtration), Atotech (electrolyte coatings) and Molykote (lubrication materials).

11.76. **Financing**

11.76.1. Sources of financing

Granite group finances its activity by long-term bank loans and monies received from the issuance of non-negotiable shares and bonds to institutional investors.

In addition, Supergas provided Granite with a loan originating from the issuance of bonds of Supergas, the balance of which, as of the date of the Report, is approx. NIS 222 million. An amount of approx. NIS 200 million was provided as a loan to Sonol. The balance of Sonol's debt to Granite as of the Date of the Report is approx. NIS 56 million. Pursuant to a resolution by the Board of Directors, Granite invested cash surpluses which amount, as of the date of the Report, to the sum of approx. NIS 68 million in marketable securities and in managed portfolios in accordance with the instructions of the board of directors, as follows: Government bonds and corporate bonds rated A and higher with an average duration not exceeding 6 years, at a rate not exceeding 50% of the portfolio's value; up to 20% of the amount may be invested in shares, while up to 5% may be invested in exchange-traded notes that follow foreign stock indexes and the balance in TA-100 Index shares with dispersion restrictions that were determined.

Financing of Via Maris

Following are details of the average interest rate on long-term and short-term bank loans, for the financing of Via Maris Desalination as of December 31, 2011 and December 31, 2010:

	2011		**2010**	
	Value in books in NIS in thousands	**Average interest rate**	**Value in books in NIS in thousands**	**Average interest rate**
Bank sources, long-term, in NIS, index-linked , fixed interest	325,541	5%	311,628	5.2%
Bank sources, long-term, in NIS, variable interest	113,690	4.2%	116,003	4.2%
Total of loans from banking corporations	439,231		427,631	

In 2005, Via Maris Desalination Ltd. (the "**Concessionaire Company**") signed an agreement with HaPoalim Bank (the "**Bank**") for the provision of the senior financing required for the foundation of the desalination facility, at an overall scope of approx. NIS 315 million (also including financing for the construction of a power station adjacent to the area of the desalination facility, insofar as it is decided to erect such), but no more than a sum equal to 78% of the total amount of investment in the facility (the "**Original Financing Agreement**").

In August 2009, in the framework of the execution of the facility's expansion plan (see Note 13.a to the financial statements in Chapter C of this Report), Via Maris signed a new financing agreement with the Bank, incorporating the provisions of the Original Financing Agreement as well. Accordingly, the Bank provided financing facilities, in NIS and foreign currency, for the financing of up to 90% of the costs of the first expansion, which was completed. The balance of the financing was provided by the shareholders of Via Maris, principally by way of providing inferior shareholders' loans.

The financing agreement stipulates various provisions, representations and undertakings, including compliance with minimal financial ratios as follows:

Required ratio	**Ratio as of December 31, 2011**
Debt coverage ratio – 1.10:1	1.23:1
Fixed payment to fixed expense ratio – 1:1	1.16:1
Loan term coverage ratio – 1.15:1	1.22:1

Repayment of the senior debt during the operation period will be made according to a pre-fixed payment schedule, in semiannual payments until 2028.

After the date of the Report, on January 30, 2012, an additional financing agreement was signed between the parties, for the purpose of the additional expansion of the desalination facility's project as described in Section 11.71.1 hereunder, which incorporates the provisions of the Original Financing Agreement, as amended on August 13, 2009 and December 30, 2010 (the "**Consolidated Financing Agreement**"). It should be noted that the Consolidated Financing Agreement is a credit agreement which is material to the Company, as defined in Legal Position no. 104-15 of October 2011 of the Securities Authority.

The principal provisions of the agreement are as follows:

The facility's expansion will be financed through construction loans and through shareholders loans from the shareholders of Via Maris (GES) at a ratio of 20:80 during the construction period.

The Consolidated Financing Agreement includes senior debt facilities from the Bank for two terms of financing for the Concessionaire Company:

In the construction period – short loans of variable interest in three courses: NIS, Euro and U.S. dollar (based on the Bank of Israel interest, Euro LIBOR and US. Dollar LIBOR, respectively).

	Amount of Loans Facility	**Withdrawals Frequency**	**Currency**	**Linkage**	**Interest**
Construction loan in NIS	225 million NIS	Monthly, as per the construction plan	NIS	unlinked	Prime + 0.65%
Construction loan in dollars	Approx. $16 million	Monthly, as per the construction plan	USD	unlinked	U.S. dollar LIBOR + 4.40%
Construction loan in Euros	Approx. €25 million	Monthly, as per the construction plan	EURO	unlinked	Euro LIBOR + 4.40%

The operation term – 24 months of the date of receipt of the full operation permit for the additional expansion (PTO Phase C) the short-term loans will be converted to a long-term NIS loan in the amount of NIS 400 million at a fixed interest linked to the index (the last index known on the conversion date), the price of which, as of the date of the Report, is 4.35% (the "**Conversion Date**").

Repayment of the senior debt in the operation term will be according to a pre-determined payment schedule, in bimonthly payments until 2028.

On the Conversion Date, the required financing's reduction will be performed (Take-Out) from the shareholder at a rate of 5% of the amount invested in the construction against an increase in senior debt's scope, so that the leverage ratio due to the new expansion will be 85:15 and the leverage ratio due to the entire facility will be 80:20. The said capital reduction will be performed subject to conditions stipulated in the agreement, mainly the provision of a guarantee and compliance with a minimal coverage ratio.

On March 1, 2012, concurrent with the finalization of the Consolidated Financing Agreement as specified hereunder, Granite's signatures on, the following documents, guarantees and undertakings, among others, entered into effect: (1)

Granite's guarantee for the performance of GES's undertakings by virtue of a direct undertaking provided by GES and Via Maris Desalination (Holdings) Ltd. (the "**Holding Company**") vis-à-vis the Bank, which includes, *inter alia*, the following issues: (a) various representations and undertakings of GES and the Holding Company with respect to provision of information, the Concessionaire Company's financial model, transactions with interested parties and so forth; (b) an undertaking of GES and the Holding Company to provide the equity required for the additional expansion (and a guarantee to ensure the provision of equity as stated); and (c) and undertaking of GES and the Holding Company to cover a deviation in the construction costs of the additional expansion; (2) Granite's undertaking no to transfer any GES shares held thereby, without the Bank's approval; (3) Granite's undertaking to back the guarantee provided by GES for the performance of the undertakings of Via Maris Desalination – Construction Partnership (the "**Construction Partnership**") vis-à-vis the Concessionaire Company, according to a planning and construction agreement signed between the Construction Partnership and the Concessionaire Company (the "**Planning and Construction Agreement**"). Within the Planning and Construction Agreement, it was provided, *inter alia*, that the Construction Partnership would perform all of the planning, acquisition and construction work in the additional expansion, and would, as a rule, tale it upon itself, on a "back to back" basis, to perform all of the undertakings of the Concessionaire Company vis-à-vis the State under Amendment no. 6 of the Concession Agreement. The Construction Partnership's liability pursuant to the Planning and Construction Agreement is limited to the amount of consideration according to such agreement, subject to exceptions; (4) a guarantee of Granite backing the guarantee provided by GES for the performance of the undertakings of the Construction Partnership vis-à-vis the Bank, in accordance with a direct planning and construction agreement signed between the Construction Partnership and the Bank. Such agreement was mainly designated to stipulate the Bank's rights in events of breach of the financing agreements by the Concessionaire Company against it, including with respect to the appointment of an alternate entity (5) a guarantee of Granite backing the guarantee provided by GES for the performance of the undertakings of Via Maris Operation Ltd. (the "**Operation Company**") vis-à-vis the Concessionaire Company pursuant to an amendment of the operation and maintenance agreement signed between Via Maris Operation and the Concessionaire Company (the "**Operation and Maintenance Agreement**"). Within the amendment of the Operation and Maintenance

Agreement, it was provided, *inter alia*, that the Operation Company will perform all of the operation and maintenance work of the entire desalination facility (i.e., the facility together with the first expansion and the current expansion), and, as a rule, will take upon itself the risks of operation and maintenance with respect to the Concessionaire Company's undertakings vis-à-vis the State under the Concession Agreement; (6) A guarantee of Granite backing the guarantee provided by GES for the performance of the Operation Company's undertakings toward the Bank as per a direct operation and maintenance agreement signed between the Operation Company and the Bank. Such agreement was mainly designated to stipulate the Bank's rights in events of breach of the financing agreements by the Concessionaire Company against it, including with respect to the appointment of an alternate entity.

After the date of the Report, on March 1, 2012, the Consolidated Financing Agreement was finalized as stated. GES provided another shareholder's loan, so that the equity for the purposes of the expansion amounted to approx. NIS 41 million. Furthermore, Granite provided the bank with the following bank guarantees: (1) a performance guarantee – a bank guarantee of NIS 20 million and an addition lf $1.4 million and €2.7 million – a scope of 10% of the consideration amount pursuant to the Planning and Construction Agreement ,ensuring the undertakings of the Construction Partnership as per such agreement (2) additionally, a guarantee for the provision of equity was provided, in the amount of NIS 40 million, in force until December 31, 2012.

As per the Consolidated Financing Agreement, all of Via Maris's property, assets, shares, rights, in connection with the bank accounts, its intellectual property assets and the concession agreements and insurance policies, are pledged to the Bank.

For further details with respect to Via Maris's financing agreements, see Note 22 to the financial statements in Chapter C of this Report.

Details of the average interest rate and the effective interest rate on long-term and short-term loans, from bank sources and non-bank sources, in the Granite Group, including Via Maris, as of December 31, 2011 and December 31, 2010, are as follows:

As of December 31, 2011:

	Long-term			Short-term		
	Amount (NIS in thousands)	**Average interest rate**	**Effective interest rate**	**Amount (NIS in thousands)**	**Average interest rate**	**Effective interest rate**
Non-bank sources - unlinked	10,000	4.75				
Non-bank sources – linked to the index	730,076(1)	4.2-6.3	4.2-6.3	1,400	4	**4**
Bank Sources – Linked to the Index	454,477	1.07-6				
Bank sources – Linked to the dollar	314	8-15		840,112	2.4-5.3	
Bank sources - NIS	585,649	4.25-7.6		1,029,432	3.65-5.3	
Total financial liabilities from bank sources	**1,788,298**			**1,143,672**		

(1) Net of issue costs.

As of December 31, 2010:

	Long-term			Short-term		
	Amount (NIS in thousands)	**Average interest rate**	**Effective interest rate**	**Amount (NIS in thousands)**	**Average interest rate**	**Effective interest rate**
Non-bank sources – linked to the index	847,626(1)	4.2-8.0	4.2-9.46	2,529	3.4-5.5	**3.4-5.5**
Bank Sources – Linked to the Index	432,849	0.32-6.7				
Bank sources – Linked to the dollar	74,724	2-2.1		78,777	1.875-2.5	
Bank sources - NIS	493,630	3.7-7.6		566,817	2.9-4.5	
Total financial liabilities from bank sources	**1,856,681**			**648,123**		

(1) Net of issue expenses.

11.76.2. Credit facilities

In December 2011, Granite took short-term bank credit from two banks in the amount of NIS 60 million and NIS 65 million. After the date of the Report, On February 13, 2012, Granite tool bank credit in the amount of NIS 35 million, to be repaid in one lump sum in August 2013. Interest at a rate of Prime +1.25% will be paid each quarter. The aforesaid credit is used for needs of the Company and its subsidiaries.

Sonol has agreed short-term credit facilities with the banks in the amount of NIS 1,220 thousand. The balances of credit used as of the date of the Report amount to NIS 713 million. The average interest rate applicable to said facilities is Prime+0.16%. Due to the high financial costs of receipt of letters with respect to existing credit facilities, Sonol, Supergas and GES have decided not to request facilities' confirmation letters. Nonetheless, the Company, based on the management of the Granite company, believes that when necessary, the banks will grant Sonol, Supergas and GES the credits required thereby for their operations. This information is prospective and based on Granite's assessments in accordance with its many years of experience in working with the banks. However, for reasons of a change in policy, change in the economic situation, etc. there is no certainty that, when needed, the banks will grant Granite, including all of the companies in the Granite Group, all of the requested credit, due to reasons of a change in policy, a change in the economic situation and so forth. It should be noted that short-term credit from banks generally bears unlinked shekel interest, at variable interest which is a function of the Prime interest rate. The Prime interest rate varies monthly according to determination of the Bank of Israel.

11.76.3. Liabilities and restrictions of Granite vis-à-vis the banks.

In 2004, Granite endorsed credit in the sum of NIS 150 million (the "**Endorsed Credit**") to Tambour out of credit which was taken by Granite for the purpose of acquiring Tambour in 2001. As of the Date of the Report, the balance of Granite's bank credit (the "**Remaining Credit**") is in the sum of approx. NIS 45 million and the balance of the Endorsed Credit in Tambour is in the sum of approx. NIS 12 million.

In 2004 agreements were signed between Granite, Tambour and two banks which provided it with credit in 2001 for the purposes of acquiring Tambour (hereinafter in this Section, the "**Banks**"), which regulate the act of endorsement of part of the credit to Tambour and the terms of the Remaining Credit and the Endorsed Credit (the "**Endorsement Agreements**").

Pursuant to the Endorsement Agreements, as amended on August 27, 2009, and to secure the Remaining Credit, Granite has pledged for the benefit of the bank all of its holdings in Tambour, all of its holdings in GES, including the right to receive a dividend in respect thereof.

For the purpose of securing said lien, Granite's shares in Tambour was transferred to the name of the bank's trust company (the "**Trust Company**"), which held the Tambour shares in trust for the benefit of the bank as a lien-holder and for the benefit of Granite as a shareholder. As of the Report Publication Date and in accordance with agreements reached with the bank, part of the shares that Granite holds in Tambour will be released from the lien, such that 51% of Granite's holdings in Tambour will remain pledged to the bank.

Additionally, so long as the Remaining Credit shall not have been repaid in full, Granite has undertaken, *inter alia*, to meet criteria, to be examined on the basis of Granite's and its subsidiaries' consolidated financial statements, whilst during the Report Period, as of the Date of the Report and as of Report Publication Date, Granite fulfills these obligations: (1) The amount of equity of Granite together with its liabilities for customer deposits will not be less, at any time, than NIS 450 million linked to the consumer price index, with effect from the index published in January 1999. (2) The portion of the equity together with deposits, from the total consolidated balance sheet of Granite, less the balance of the Fuel Administration (the security inventory), will not be less, at any time, than 15%, provided that in any decrease below a level of 17%, an opinion will be given by the auditor of Granite, indicating a quantification of the extent of the impact of an increase in fuel prices on the inventory and receivables items, and that the ratio in cancelling this impact is equal to or higher than 17%. In addition, Granite undertook that as of July 1, 2010, and until the full repayment of the Remaining Credit, the ratio of the value of the Company's holdings in the shares of Tambour to the balance of the remaining credit is not less than 3 ON December 29, 2011, the supplement to the management terms was once again amended, so that in calculating the second criterion described above, the balance of receivables due to a concession arrangement (including current maturities) will also be deducted from the total of the consolidated balance sheet. During the report year and as of the Date of the Report, Granite met the required criteria. As of the date of the Report, Granite's equity, together with deposits, amounted to NIS 870 million, compared with NIS 585 million, as per the required calculation. The equity ratio

together with deposits divided by the consolidated balance sheet minus the Fuel Administration balance and minus receivables due to a concession arrangement is 19.35%, compared with the required 17%.

The ration of Tambour's market value to the Remaining Credit as of December 31, 2011 is 5.57.

Undertakings and restrictions of Sonol vis-à-vis the banks, including with respect to meeting financial criteria

As of the date of the Report, an undertaking to meet financial criteria of net financial debt to EBITDA ratio, with certain adjustments as defined in the agreement that will not exceed 12 and a net financial debt to CAP ratio that will not exceed 0.9, applies to long-term loans that Sonol received from banks, the balance of which, as of the date of the Report, is approx. NIS 140 million (excluding current maturities). As of the date of the Report, Sonol received a waiver from the Bank with respect to the first criterion and meets the second criterion (0.74).

On March 12, 2012, the Bank informed Sonol that the authorized organ of the Bank had approved an amendment to the criteria. Accordingly, the Company's management estimates, based on Granite's management and Sonol's management, that Sonol will meet the criteria in the course of 2012.

Liability note of Tambour to the banks

Tambour has signed liability notes vis-à-vis the banks, which arrange a number of liabilities Tambour has assumed against the receipt of credit, including fulfilling financial criteria. In addition, Tambour has undertaken in the liability notes to comply with various financial covenants, as described in Note 22.g to the Company’s financial statements in Chapter C of this Report.

Undertakings and restrictions of GES vis-à-vis the banks, including in relation to meeting financial criteria

To secure GES’s undertaking to banking corporations, GES undertook to meet financial criteria as specified below: (1) minimum equity of NIS 116 million; (2) minimum ratio of equity to total assets, which shall be no less than 30%, the combined total assets of Via Maris being discounted from the total assets, and inferior shareholder loans, which shall be no less than NIS 90 million, being added to the equity. As of the Date of the Report, GES's equity, together with the inferior

shareholder loans, amounts to approx. NIS 158 million and the aforesaid ration is 37.6%.

Additional liabilities of Granite vis-a-vis banks

Granite gave a guarantee unlimited in amount vis-à-vis the Banks to secure the assigned credit, whose balance, as of the date of the Report, is approx. NIS 12 million (on this matter, see this section above). For the purpose of securing the credit which the banks provided to GES, Granite provided a guarantee in favour thereof. In addition, Granite undertook that the shareholder loans that it had provided to GES would not fall below the sum of NIS 90 million and would be inferior relative to a loan from the banks. As of the Date of the Report, the balance of the credit guaranteed by Granite amounts to approx. NIS 52 million. Additionally, Granite undertook that the criteria described in this section above will also apply to short-term credit received by Granite from other banks in December 2011. Granite further undertook that Granite's total standalone financial credit will not exceed NIS 400 million and that Granite's equity will be no less than NIS 650 million and that the ratio of equity to the total standalone balance sheet will be no less than 50%. As of the date of the Report, Granite's equity amounts to approx. NIS 760 million, the financial credit amounts to approx. NIS 255 million and the ratio of equity to standalone balance sheet is 57.5%. Also, Granite undertook that, except the guarantees and securities provided thereby as of December 2011, it will not provide securities to a banking corporation or another credit provider and will not guarantee for others, without receiving the banks' approval. The aforesaid undertaking will not apply to guarantees for Via Maris and the solar projects executed by Supergas.

Granite further undertook that its liabilities vis-à-vis held companies will at no time be less than NIS 120 million. As of the date of the Report, Granite's liabilities to held companies (including Supergas) amount to approx. NIS 295 million and its liabilities to Supergas amount to approx. NIS 222 million.

11.76.4. Bonds issued by the Granite Group

In July 2007, a subsidiary of Supergas, to which were transferred the domestic gas activity and some of the commercial gas activity for marketing gas in portable gas containers, issued to institutional investors by way of private placements, NIS 600 million of bonds. The bonds are rated Aa1 by Midroog Ltd. The bonds are for a period of 18 years and are paid in quarterly principal instalments since 2010. The bonds are linked to the consumer price index for May

2007 and bear interest at 4.9% per annum, which is paid once every calendar quarter. On the occurrence of certain events, e.g., a change in control as a result of which the rating falls by two degrees, interest will be 5.2%.

The subsidiary of Supergas undertook to meet financial covenants. Non-compliance with the said covenants will enable the holders of the bonds to demand an acceleration of the repayment or early repayment as outlined below.

Instances in which acceleration may be claimed:

a. If the ratio of the average quarterly available cash flow of domestic gas activity in the last year (the cash flow of receipts from the domestic gas activity less the actual purchases of gas and the expenses in respect of the service agreement for the domestic gas activity) and the quarterly payment (principal and interest) that is expected to be repaid to the holder of the bonds at the expected date of the first principal instalment ("**debt cover ratio**") falls below 111%.

b. If rate of the margin of the commercial gas activity in containers falls below 12%.

Instances in which acceleration and realization of securities are possible, *inter alia*:

a. if the debt cover ratio falls below 103%;

b. in the event of insolvency;

c. if Supergas loses its gas supplier licence;

d. a change in control such that the Company will cease to control Supergas (which is not as a result of a re-organization in the Canit Hashalom Group);

e. a demotion in rating below Baa1;

f. failure to monitor rating.

In addition, there are grounds for the replacement of the subsidiary of Supergas as the gas server of the Company, including primarily: a debt cover ratio of less than 106%; events of insolvency of Supergas; and the loss of Supergas' gas supplier licence. In addition, Supergas has created in favour of the trustee for the bond-holders, a fixed charge first in rank unlimited in amount on the shares of its subsidiary, a floating charge on all of the assets of the subsidiary, a fixed charge on all of the subsidiary's rights in certain bank accounts, a fixed charge on all the rights of the subsidiary

vis-à-vis the insurance company insuring its assets with property insurance and a fixed charge on indemnification rights granted to the subsidiary vis-à-vis Supergas pursuant to an assets purchase agreement between them and on the rights pursuant to a services agreement.

In addition, Supergas' subsidiary undertook that for so long as the bonds had not been repaid in full, the subsidiary would operate only with regards to the domestic gas activity and additional activities as defined in the trust note, as well as any activity attendant thereto, including raising of additional financing in accordance with the provisions of the trust note.

During 2010 and up to the Date of this Report, Supergas had met the required covenants.

The money raised by Supergas was primarily used for the repayment of the short-term bank credit of companies in the Oil Distillates operating segment and for the repayment of a loan made available by the Company to Supergas.

11.76.5. Series 3 Bonds

In June 2004, the Company issued Series 3 Bonds in a total sum of NIS 200 million in a private placement, to institutional factors and they are traded only in the Institutional Sequence System. The bonds are linked to the consumer price index of May 2004, bear interest at 5.7% per annum. The principal of the bonds, together with linkage differences, is repaid in seven equal annual instalments, commencing in June 2007 and ending in June 2013. The interest is paid every six months. The balance of the bonds, as of the date of the Report, is approx. NIS 54 million.

The bonds in this series are rated by S&P Maalot ("**Maalot**").

On August 2, 2011, Maalot announced that it was entering Granite's bonds' rating, as well as of other companies engaging in the marketing of fuels, into CreditWatch with negative implications, in view of the announcement by the Ministry of Energy and Water Resources of its intention of reducing the marketing margin of gasoline by 20 Agorot per litre, as of the end of August 2011, subject to a hearing held for the companies. On December 14, 2011, Maalot announced the downgrading of the bonds (Series 3) to il A with a stable outlook. This was done in view of the Government's decision to considerably decrease the marketing margins for gasoline as of September 2011, which is expected to lead to the continuation of weak results in the fuel marketing segment. Furthermore, Granite's signing an

agreement with the State to increase the capacity of the desalination facility in Palmachim, in addition to other investments by Granite in the solar sector and natural gas distribution, which are expected to exceed, in Maalot's opinion, NIS 0.5 billion in the years 2012 and 2013, are expected to increase Granite's leverage. The stable ranking outlook reflects Maalot's assessment that Granite will succeed in implementing a plan to restore the loss due to the marketing margin reduction step and creating cash flow from ongoing operation to support the recycling of the majority of debt maturities in 2012. .

The bonds may be placed for immediate repayment in the events described in the trust deed, including if Maalot announces a demotion in the bonds' rating due to actions taken by the Company, which actions constitute a material breach of the terms of the bonds or the trust deed, or if Maalot announces a demotion in the rating of the bonds to a rating of BBB+ or lower.

As of the Date of th3e Report, to secure repayment of the abovementioned bonds, liens were placed on six fuelling stations, an office building in Netanya and a plot which is adjacent to a fuelling station.

11.76.6. Series 4 Bonds

In 2004 and 2005, the Company issued Series 4 Bonds in a total sum of NIS 100 million in a private placement to institutional investors.

The bonds are non-negotiable, linked to the consumer price index of July 2004, published on August 15, 2004, and bear a semi-annual interest at a rate of 6.35%. The principal of the bonds, together with linkage differences, is repaid in seven equal annual instalments, commencing in August 2007 and ending in August 2013. The interest is paid every six months. The balance of the bonds, as of the date of the Report, is approx. NIS 31 million. The bonds in this series are not secured and they are rated by Maalot. On December 14, 2011, Maalot announced the downgrading of the bonds (Series 4) to A with a stable outlook for the reasons described in Section 11.76.5 above. The bonds were issued pursuant to the conditions described in the trust deed, which was signed with Poalim Trust Services Ltd., which acts as the trustee of the bond-holders in this series. According to the trust agreement, the trustee has the right to make the outstanding balance of the bonds available for immediate repayment upon the occurrence of the causes for immediate repayment set forth above.

11.76.7. New Bond Series

On December 8, 2010 Maalot determined an A rating for a new bond series at a scope of up to NIS 200 million with a duration of 4-5 years, which shall be used to refinance costs and short-term credit in the group. Granite is examining the advisability of the issue, in accordance with market conditions and the group's plans. Until the Report Publication Date, no resolution was adopted by Granite's board of directors to issue any additional bonds. On December 14, 2011, Naalot announced the downgrading of Granite to A with a stable outlook for the reasons described in Section 11.76.5 above.

11.76.8. Liens and guarantees

A floating charge, unlimited in amount, on all of the assets of Sonol (including its fixed assets), and a fixed charge on its uncalled and/or unpaid share capital, reputation, securities and mortgaged documents have been placed in favour of the banks financing its operation. Pursuant to the floating charge Sonol and Supergas undertook not to create additional charges without the consent of the banks and subject to the conditions as set forth in the bonds. To the best of the Company's knowledge, there is an inter-bank agreement between the banks holding the charges, according to which they are holding the liens *pari passu* on the assets of Sonol as aforesaid. Additionally, there is a first-ranking fixed charge, unlimited in sum, on Sonol's proprietorship rights in several realties in favour of the Company's bondholders.

There is a floating charge, unlimited in sum, on all of Supergas's assets (including fixed assets), in favor of the banks which finance its business. There is also a fixed charge on its uncalled and/or unpaid share capital, goodwill and securities. Within the floating charge, Supergas undertook not to create additional liens without the banks' consent and subject to the terms as specified in the bonds. To the best of Supergas's knowledge, there is an interbank agreement between the banks holding the charges, whereby they possess a *pari passu* lien on Supergas's assets, as stated. For details as to the liens created by Supergas due to the issuance of bonds by a subsidiary of Supergas, see Section 11.73.4 above.

For details as to the lien on Via Maris's assets, see Section 11.75.1 above. As of the Report Publication Date and in accordance with agreements reached with the bank, part of the shares that Granite holds in Tambour will be released from the lien such that 51% of Granite's holdings in

Tambour will remain pledged to the bank. For further details see Section 11.75.3 above.

For liens granted to the trustees in favour of the holders of the bonds issued by the Granite Group see Section 11.56.4 above.

To secure the liabilities of Tambour vis-à-vis the banks for credit, Tambour placed the following securities in favour of the banks: (1) a first ranking mortgage, unlimited in amount, on approx. 100 dunam in Akko, which is registered in favour of the banks in equal ranking (*pari passu*); (2) a first ranking fixed charge, unlimited in sum, on the outstanding share capital and on its reputation and a first ranking floating charge on its plant, its business and all the assets and rights of any kind whatsoever that Tambour has or will have at any time in the future; (3) a first ranking pledge, unlimited in amount, of Tambour's holdings in the shares of Tambour Distributions Ltd. ("**Tambour Distributions**"); (4) a first ranking floating charge on the plant of Tambour Distributions, its business and all the assets and rights of any kind whatsoever that Tambour Distributions has now and will have at any time in the future and a first ranking fixed charge on the outstanding share capital of Tambour Distributions and on its reputation. With regard to the liens placed by Tambour as aforesaid, it was decided that the proceeds from the sale of the Company's assets will be distributed *pari passu* according to the extent of its debts to the banks.

Granite has given a perpetual guarantee, unlimited in amount, vis-à-vis Bank Leumi and a renewed guarantee, unlimited in amount, vis-à-vis HaBank HaBeinleumi for the full disposal of all the amounts that are due or will be due to Bank Leumi or HaBank HaBeinleumi from Tambour in the accounts in which the credit assigned to Tambour in November 2004 from Granite was managed (The balance of the assigned credit as of December 31, 2011 is approx. NIS 12 million). In July 2011, Tambord signed an undertaking to impose a fixed charge, unlimited in sum, on all of the equipment of the plasterboard plant owned thereby vis-a-vis the banks.. In addition, Tambord undertook to sign a perpetual guarantee, unlimited in sum, to secure all of Tambour's debts and liabilities vis-a-vis the banks.

With regard to additional guarantees given by the Granite Group, see this section above and Note 35 to the Company's financial statements in Chapter C of this Report.

11.76.9. Estimation of Granite with regard to the need to raise financing sources

According to the financing agreement for the expansion of Via Maris's desalination facility's, GES is required to provide equity at a rate of 20%, which amounts to approx. NIS 80 million (see Section 11.72.1 above). On February 29, 2012, GES provided a shareholder loan in the amount of NIS 40 million, 25 of which had been provided thereto by Granite, and with respect to the balance of the amount, a sum of NIS 40 million, Granite provided the Bank with a guarantee for the equity's provision, which is in force until December 2012. In December 2012, GES will be required to complete the equity injection and in the Company's estimation, based on the best knowledge of Granite's management, Granite will be required to provide GES with some of the amount as an additional shareholder loan. As of the publication of the Report, the amount that GES will be able to obtain from Via Maris's current sources and the amount that Granite will be required to lend GES as a shareholder loan, are not assessable. Furthermore, in December 2012, Granite is supposed to repay the short credits taken thereby, as stated in Section 11.72.1 above. As of the date of the Report, Granite has several liquid assets, however, as of the date of this Report, the sum which the Company will be required to raise beyond such cannot be estimated. In addition, it is possible that subsidiaries of the Granite Group will be required to raise additional sources of financing in the event of increases in the prices of Oil Distillates in the world or government policy to increase the excise duty, and for investments in subsidiaries and/or the making of new investments and execution of existing and/or new projects. With regard to the Bank of Israel Directives in relation to the “Single Borrower” or “Group of Borrowers” restrictions and the effect they may have on Granite, see Section 1.79.3 below.

This section includes forward-looking information, as defined in the Securities Law. Forward-looking information is uncertain information with respect to the future, which is based on information which exists at the Company on the Date of the Report, and includes estimates of the Company or its intentions as of the Date of the Report. The actual results may materially differ from the results estimated in or implied by this information.

11.77. **Material agreements**

The following is the detailing of the material agreements of the Granite Group that are not in the ordinary course of business of Granite:

11.77.1. In September 2002, the general meeting of Granite (in this Section 11.57.2 below: the "**Company**") approved the provision of advance indemnification to all officers of the Company and the Company’s subsidiaries (who serve as

such on behalf of the Company), including to controlling shareholders of the Company, commencing from January 1, 1995 and onwards, to the fullest extent permitted by the Companies Law (in this Section: the "**Entitled Officers**").

The maximum indemnification amount that the Company will pay to all of the aforesaid officers cumulatively shall not exceed 20% of the Company's equity according to the known financial statements at the actual time of indemnification, with the addition of sums that are received, if received, from insurance companies. The indemnification shall apply to certain events.

In addition, the general meeting of Granite has approved the exemption of all Entitled Officers, as aforesaid, to the fullest extent permitted by the Companies Law and the Company's Articles of Association.

On March 13, 2012, in furtherance of the resolutions of the Audit Committee and the board of directors of the Company, the shareholders' general meeting approved the extension of the indemnification given to directors and officers, in such manner so that it will also apply to events stemming from the increased efficiency of enforcement law, under the law's restrictions. In addition, the Company limited the retroactive indemnification amount to 20% of its equity as per the financial statements at the time of the actual indemnification. Furthermore, indemnification to Ms. Dana Azrieli, who is considered a controlling shareholder of the Company, was also approved.

11.77.2. On January 25, 2011 Granite's Audit Committee and Board of Directors approved the extension to 2011 of the Company's agreement with Canit Hashalom with respect to the provision of services, including: services for the management, optimization and improvement of the Company's assets, strategic consultation, financial consultation and business development, in consideration for a total annual fee in the amount of NIS 3,000,000, linked to the consumer price index. On March 13, 2012, after Granite's Audit Committee and Board of Directors had approved it, the general meeting of Granite's shareholders approved the extension of the agreement as stated for an additional 1-year period, without change in its terms, except for the amount of management fees, which was decreased by 20% and is currently in the amount of NIS 517 thousand.

11.77.3. On March 26, 2008, the Audit Committee and Board of Directors of Granite approved the payment of an annual remuneration to Mr. Menachem Einan, the chairman of the Board of Directors of Granite, and/or a company under his

control, in the amount of NIS 384,000 per annum, commencing from January 1, 2007, and for as long as he serves as the active chairman of Granite's Board of Directors and until it is otherwise decided (the "**Annual Remuneration**"). The Annual Remuneration is linked to the rise in the Consumer Price Index. The basic index is the index of February 2008. The Annual Remuneration is paid to the Chairperson of the Company's Board of Directors in 12 equal monthly payments and linkage to the Consumer Price Index is updated monthly. Payment of the Annual Remuneration does not derogate from the payment of participation fees to which the chairman of the Board of Directors is entitled according to a resolution of the general meeting as of May 8, 2007. Payment of the Annual Remuneration has been approved by the general meeting of Granite, held on July 13, 2008. In accordance with the undertaking of Granite in the report released in May 2009, in March 2010 the Audit Committee and Board of Directors, respectively, approved the Annual Remuneration to the chairman, as aforesaid, as an extraordinary transaction wherein the controlling shareholder has a personal interest. In April, 2010, said Annual Remuneration was approved by the general meeting of Granite.

11.77.4. For agreements during the ordinary course of business, see the description of the operating segments above.

11.77.5. Agreement for the purchase of electricity

The Company, Granite, including subsidiaries thereof (Via Maris Desalination Ltd., Tambour and GES) (the "**Group**") engaged in an agreement for the purchase of electricity with O.P.C. Rotem Ltd. ("**OPC**"), which is a private electricity producer, and in a parallel agreement between the Group companies, which regulates the relationship between them with respect to the said electricity purchase agreement, and according to which Granite will coordinate between the Group companies and itself and between them and OPC. In accordance with the agreement, OPC will sell electricity to the Group companies, which in consideration will pay it a variable tariff in accordance with actual consumption, which is based on the tariffs of the IEC, less a discount at various rates which were determined in the agreement, which are dependent on the scope of the companies' consumption. The agreement is for a supplied capacity of 83 mWh. The agreement is for a period of ten years which will begin on the date of commencement of supply of the electricity, which is expected to occur at the end of 2012. The agreement allows the Group to give notice of termination thereof prior thereto in the event of the construction of a power station

controlled by Granite under the conditions determined. The agreement also includes an option for extension thereof for a total period of 15 years. In the event that OPC's power station shall not function and shall not supply electricity for whatever reason, electricity shall be supplied directly from the IEC. The agreement determined the maximum and minimum scopes of consumption of electricity by the Group companies. In addition, various mechanisms were determined which allow flexibility in compliance with the said minimum and maximum scopes, in order to address a possible change in the demand for water from Via Maris' desalination plant. After the Date of the Report, in January 2012, the Group exercised an option that was granted thereto and increased the scope of the agreement to 116 mWh. The Group companies were granted an option to purchase an additional 100 mWh, in the event of the construction of an additional power station by OPC's parent company. Supergas was granted an option to purchase an additional 30 mWh, under similar conditions, exercisable until March 2012.

11.77.6. Granite and/or its subsidiaries have several agreements with interested parties in Granite and/or with companies which controlling shareholders hold personal interest in Granite, which are executed during the ordinary course of business and under market conditions, and which are negligible, in accordance with Granite's policy for negligible transactions, such as agreements on the following subjects: fuelling for vehicles fleets, lease and sale of paints.

11.78. **Legal proceedings**

The Granite Group is a party to many legal proceedings, including class actions that have been filed against the Granite Group. For details regarding the material legal proceedings of the Granite Group, see Note 36 to the Financial Statements of the Company in Chapter C of this Report.

11.79. **Granite Group insurance policies**

The Granite Group's insurance policies cover, subject to the terms of each policy, various risks, at the insurance amounts indicated in each policy.

On November 29, 2010, the audit committee and the board of directors approved Granite's engagement in a policy for liability insurance for officers, including directors and officers considered to be controlling shareholders in the Company and/or their relatives, with coverage of $40 million, with the addition of defence expenses in Israel of $8 million and an additional layer for Granite of $10 million, plus defence expenses in Israel of $2 million for an additional period of 18 months commencing from November 30, 2010. The engagement was approved

at the general meeting of Granite's shareholders which convened on March 2, 2011.

In addition, Granite purchased a "run off" insurance policy for a period commencing from February 1, 2007 until November 30, 2013 for insurance of liability to directors and officers (even though they do not serve as such in the Granite Group, as to date) in respect of measures taken by them in the context of their duties prior to the purchase of control by Canit in November 2006. The extent of the coverage stands at U.S. $ 30,000,000 per event and for the period. On March 29, 2007, the general meeting of Granite after receipt of approval of the Audit Committee and the Board of Directors of the Company approved the said commitment.

The rest of the insurances were executed in the various subsidiaries of the Company. Details of the main insurances, by company, are as follows:

11.79.1. Sonol

Sonol has property insurance policies, which include the Company's property, with total coverage of approx. $298 million. Sonol has third-party liability and product liability insurance. The extent of the coverage is $40 million. In addition, Sonol has arranged consequential loss insurance with respect to the output facility in Haifa totalling $18 million.

In addition, Sonol, has extended indemnification for aviation product liability of Paz Airline Services Ltd. and Airline Properties Ltd., with total coverage of $500 million. In addition, Sonol is included as an additional insurant in the product (airline-related) liability insurance of Mercury Israel Airlines Ltd. with a liability cap of $50 million. In addition, in the said policy, with a liability cap of $525 million, above $50 million indemnification is given to the Company also in respect of the activity of Mercury Israel Airlines Ltd. only. As stated above, Airline Services Ltd. and Mercury Airline Ltd. are companies that supply fuelling services to airplanes at Ben Gurion Airport. In addition, in the framework of the (aviation) product liability policy of ORL, with coverage of $500 million, Sonol is given extended indemnification in respect of its liability for bodily harm and/or property damage caused by defective product supplied by ORL.

11.79.2. Supergas

Supergas has property insurance, with total coverage of approx. $ 25 million. Supergas has third-party liability and product liability insurance, with a total coverage of $ 40 million. Supergas has consequential loss insurance with respect to its gas farm facility totalling approx. $14 million. Supergas has insurance for contractors' work in the segment of construction of solar electricity facilities in a total scope of NIS 150 million. In addition, there is a property policy covering the solar projects after their construction's completion and a third-party insurance for the solar operation segment with a liability limit of $2 million.

11.79.3. Tambour

Tambour has property insurance, with total coverage of approx. US $187 million. Tambour has third-party liability insurance with total coverage of $10 million and product liability insurance with a total coverage of $10 million. Tambour also has an insurance policy to cover consequential loss with total coverage of approx. $83 million.

11.79.4. GES

GES has property insurance, with total coverage of approx. $43 million. GES has third-party liability insurance with total coverage of $10 million and product liability insurance with a total coverage of US$5 million and contractor work with coverage of $10 million ($2.5 million per project). GES also has an insurance policy to cover consequential loss with total coverage of approx. $11 million.

11.79.5. Via Maris

Property insurance with coverage of $120 million. Loss of profits and mechanical breakage insurance with coverage of $36 million. Insurance for damages for breach of contract with coverage of $10 million. Third party insurance with coverage of NIS 84 million. Product liability insurance with coverage of NIS 80 million. Preliminary contractors' work insurance with NIS 20 million coverage.

In addition to the main insurance policies mentioned above, the Group's companies are insured in an array of additional policies, such as product liability insurance against employers' liability, finances, trust and vehicle.

11.79.6. The Granite Group has joint insurance against terrorism with liability limits of US$20 million.

11.79.7. In July 2011, the Company and its subsidiaries Sonol, Tambour, Supergas and GES separately renewed their

insurance policies. Pursuant to this renewal, it was determined that the insurance amount for earthquake risks will stand at US$600 million for the period and for flood and natural disaster risks will stand at US$500 million for the period, with these amounts being shared by Granite and the said four subsidiaries, and the Company. The policy determines the manner of division between the various insured companies in the event of damage in an amount exceeding the cap.

The Granite Group usually renews its policies as aforesaid each year for periods of a year.

As the Company has been informed, the management of Granite, based on the insurance advice it has received, is of the opinion that the extent of insurance is adequate.

11.80. **Goals and business strategies at the Corporation level**

The Granite Group is concentrating its business on its core activities, to strengthen the standing of the portfolio companies in their respective fields. Granite's goals are to examine new investments and indentify business opportunities in Israel and outside of Israel, in all of its main areas of activity and in areas of synergy for companies in the Granite Group, in particular, the expansion of activity in paint and building finishing, projects in the fields of energy and ecology, such as the treatment of water and industrial wastewater, sea-water desalination, "green" electricity production based on solar energy and integration in the field of infrastructures and conveying natural gas. Also, as a holding company, Granite, from time to time, examines investment opportunities in other areas.

In addition, the Company is continually taking steps to improve its operating profits, including efficiency, cost-reduction and effective allocation of Granite group's resources.

The Granite Group hopes to improve its financial position, the type and extent of its loans, including an audit of its assets that are not being used or that do not have any synergy with the activities of the companies in the Group, converting short-term credit to long-term credit, and more.

With regard to Oil Distillates, the Granite Group hopes to increase the its customer base through direct marketing, including by way of submission of applications for tenders and through continual improvement of service and compliance with the safety principles and the environmental quality. In Sonol's fuelling and commerce complexes segment, Granite aspires to increase its national layout of the Chain's fuelling stations, as well as to introduce additional convenience stores of the Sonol Chain. Also, Granite intends to improve the quality of service provided at the stations and expand the

types of services provided at the fuelling stations and the convenience stores, *inter alia*, through cooperation and to build retail complexes in proximity to the fuelling stations, to the extent possible, in order to broaden the range of products and services offered to the customer. Additionally, Sonol will act for the continuous improvement of profitability, including by way of increasing efficiency, an effective allocation of its resources and identifying new business opportunities in all its major operation segments. In this context, the Fuel Administration's decision to reduce the marketing margin, as described in Section 11.5 above, will be taken into account.

In the Supergas segment, Supergas's strategy is to expand the variety of energy solutions it offers it customers and to increase and vary its customers in its operation segments, including by way of submitting applications to tenders and increasing the number of LPG customers, penetration into natural gas marketing to industrial and institutional customers and initiating projects in the solar electricity production segment. Supergas also acts for the continuous improvement of customer service and observance of safety and environmental protection rules. Furthermore, Supergas will act toward identifying new business opportunities. Among other things, Supergas intends to be a contender in additional tenders in the segment of infrastructures and natural gas distribution in Israel.

In the Tambour segment, Tambour’s strategy is (1) to be a leading and professional player in the paint and building-finishing products segment and in the world of dry construction.(2) to invest in marketing initiatives intended to make colour fashionable and thereby increasing per capita consumption in Israel. (3) to increase sales of complementary products and plasterboard products and dry construction by the development of growth factors and increased activity on building sites and in front of construction companies. (4) to increase the business development and export in Tambour's core segments outside of Israel, including by way of distribution agreements, acquisitions, mergers and factories' construction. (5) to enhance and reinforce international cooperation. (6) cooperation, mergers and acquisitions in interfacing or complementary areas, in the domestic market and abroad.

In the water and wastewater segment, the Company’s strategy is to strengthen GES’s status as a leading supplier in the water desalination and wastewater treatment segments, increase exports and business development in GES’s core business, enhance and strengthen alliances, investment in marketing channels for the purpose of increasing GES's market share.

This section includes forward-looking information. Forward-looking information contains no certainty about the future, is based on estimates predicted by the Company, which are based on information available to the management of Granite on the Date of the Report, and Granite’s intentions as of the Date of the Report. The strategy that will

be actually adopted may be significantly different from that presented above, *inter alia*, due to market conditions. In addition, assessments that were used as a basis for the strategic decision are likely to turn out to be inaccurate or significantly different from those taken into account. It should be emphasised that the intentions and aspirations outlined above, *inter alia*, in relation to investments in new properties, are only goals and strategy and concrete decisions in respect thereof have not yet been made.

11.81. **Discussion of risk factors**

The operations of the Granite Group entail risk factors, which may have a material effect on the operations of the Company and its subsidiaries as well as on its business results and financial results, which stem from macro-economic risks, segment-related risks and risks which are exclusive to the Company.

11.81.1. Macro-economic risk factors

Economic slowdown – An economic slowdown in the global economy and in the Israeli economy leads to a fall in private consumption and business activity, including a fall in new construction, and as a result, is likely to lead to a fall in sales of the products, revenues and profits of the Granite Group.

Security and political situation – The security and political situation has a direct impact on the economic situation and global oil prices, and therefore, on the entire activities of the Granite Group, particularly in the area of refined oil, including a reduction, and even a break from importing of Oil Distillates and raw materials to Israel, and on the level of inventory which the Granite Group is required to hold. In addition, the security and political situation in Israel has a significant impact on the economic situation and on tourism in Israel, as aforesaid.

Changes in interest rates – Most of the credit received by the Granite Group from banks is at variable interest rates. Material changes in interest rates are liable to affect the extent of the Granite Group's liabilities via banks and its operating results.

Currency exposure – Granite has currency exposure in respect of assets and liabilities in foreign currency. Granite has partial currency protection. Accordingly, changes in the exchange rates of those currencies are liable to adversely affect its financial results.

Effect of changes in the consumer price index – Granite's index-linked liabilities exceed its index-linked assets. Granite

has partial protection, thus an increase in the consumer price index will have an adverse affect on its financial results.

Social protest – the social protest, which developed in 2011 in Israel, and the publications of the committee assigned to abate the cost of living in Israel (see Section 11.17.17 above), had a negative effect on the consumption of fuels in the market, brought to the increase of company tax and the freezing of its reduction, and instructed the examination of gasoline, diesel oil and LPG prices, which are marketed by the Granite Group, and recommended several measures in the fuel and LPG market. The Company estimates, based on Granite's management, that if and insofar as the social protest is exacerbated and focused on products sold by the Group, this could compromise its business results.

11.81.2. Industry risk factors

Changes in global oil prices – An increase in global oil prices leads to an increase in customers' balances and an increase in balances of inventory, and accordingly, to an increase in the total of bank credit, which increases Granite's financial expenses. In addition, such an increase is liable to adversely impact some of the Granite Group's business customers, particularly, those whose area of activity is dependent upon different fuels, such as haulage companies, and consequently, is liable to result in a fall in their total consumption and an impairment in the prospects of collection of the debts of the Granite Group. On the other hand, the fall in oil prices could lead to a loss on operating inventory held by Granite. In addition, the significant volatility in oil prices increases Granite's exposure. Due to such volatility, the Company's policy is to keep in storage an operating inventory of fuels for a period of several days of supply only. In recent months, there is governmental instability in several Arab countries, which are oil suppliers, and furthermore, sanctions have been imposed on Iran, which cause an increase in the oil price, which may also be exacerbated. For more details, see Section 6.1.9 above.

Increase in excise duty on diesel fuel – It is Government policy, backed up by an order, for the increase in excise duty on diesel fuel, with the desire to equalize it over the years to the excise duty levied on petrol. This policy causes and is likely to cause in the future an increase in the level of customer debts and an increase in credit risks. In addition, because of the time lapse between the date of transferring the excise duty to the State by the oil company and the date of collecting the debt from the customer, a financial burden is created for the Company, which will grow with the increase

in excise duty. The said policy will adversely affect Granite's results.

Credit lines - In the Oil Distillates operating segments, the Granite Group requires large credit lines due to the level and nature of the activity. It is possible that Granite will need to get additional credit, including by way of an increase in bank credit lines for the purpose of its day-to-day activities due to the increase in excise duty on diesel fuel as outlined above, if global oil prices rise, and due to investments that may be carried out. There is no certainty that the banks will respond favourably to such a request or that they will give allow Granite to provide, or that they will be prepared to place additional collateral additional restrictions on Granite. In addition, the aforesaid may compel the Company to prepare accordingly, including changing its credit policy for its customers.

The marketing margin in the Oil Distillates segment – The marketing margin from which the profitability of Oil Distillates' marketing companies, including the Company, is derived is a fixed amount, which is not affected by the price of oil, and is particularly low. There is a risk arising from changes in the marketing margin, both in relation to the products under supervision, and in relation to products that are not under supervision. In addition, since the marketing margin is particularly low on the one hand, and the levels of credit allowed for customers is particularly high, on the other hand, non-payment of customer debts are likely to have a significant adverse impact on Granite's results. For details with respect to the reduction of gasoline's marketing margin in September 2011, see Section 11.17.7 above. For details as to the examination of restoring diesel oil price control, see Sections 11.17.16 - 11.17.17 above. For details as to the examination of the effect of the control over LPG, see Section 11.17.11 above.

Environment – The requirements of the Ministry of Environmental Protection in connection with the fuelling stations, installations and plants, force Granite to allocate monetary resources on this issue. These requirements are liable to become more onerous, which could compel the Granite Group to allocate additional monetary resources to this issue.

Granite has no insurance policies for a liability that could be imposed on it as a result of continued environmental pollution which is not accidental.

Hazardous and toxic materials – Since the Granite Group is engaged in hazardous and toxic materials, it is exposed to

damage that is likely to be caused due to these products, including health hazards, environmental damage, damage as a result of inflammable materials catching fire, etc. Accordingly, the Granite Group is exposed to claims, including class actions. These claims are likely to adversely affect its operating results and impair its goodwill.

Product liability – Granite markets various Oil Distillates with particular sensitivity because of they are hazardous substances and due to the nature of their use. Several laws and regulations establish the rights of an injured party or a group of injured parties that may incur damage as a result of a product that has been manufactured, stored, marketed or sold by a supplier. If any damage is incurred, Granite is liable to be sued by those consumers, including by way of a class action, and is likely to have an adverse impact on its operating results. It should be noted that Granite has insurance coverage in relation to product liability. With regards to this matter, see Section 11.59 above.

Energy alternatives – There is trend throughout the world to develop alternative energies, for example, the use of natural gas, solar energy, wind power, and more. These energies represent an alternative to Oil Distillates which Granite markets, and therefore, their use is liable to reduce the volume of sales of the Granite Group. For example, natural gas is used for burning and is an alternative product for heating by diesel oil, crude oil and LPG marketed by the Granite Group. It appears that in the initial stages, the marketing of natural gas will be carried out to large business customers and not to the domestic customers, because of the absence of appropriate infrastructures. A further example is the development of electric cars. A transition to using vehicles driven by electricity or other energy sources is liable to impair the sales of Oil Distillates, particularly in the area of fuelling facilities. On the other hand, the development of energy alternatives could represent a business opportunity for Granite and it has started to operate in these segments, see also Section 11.53 above.

Regulatory developments – The Granite Group is affected by regulatory changes that apply, from to time, in relation to its products, including the supervision of products' prices and regulatory restrictions on commitments in connection with fuelling stations and the marketing of LPG. On this matter, see details in Section 11.17 above. In addition, restrictions may be imposed upon Tambour due to its having a monopoly, see below.

Dependence on ORL – As set forth in Section 11.13.4 above, the companies operating in the Oil Distillates operating

segment have a dependence on ORL, which is the principal supplier of the various Oil Distillates that these companies purchase. If ORL discontinues supplying Oil Distillates to Granite, the Granite Group will be compelled to locate alternative suppliers outside of Israel and import the distillates independently, which is likely to lead to an increase in the costs of purchase. There is no certainty that the Granite Group will succeed in importing the quantities of the various types of Oil Distillates that is required to continue its day-to-day activities.

The consequences of privatizing ORL – ORL has been split and privatized, the process that ended with the sale of ORA to Paz and the privatisation of ORL and its conversion to a public company. Paz, the purchaser of ORA, is a competing company that gains a relative advantage in the market from the purchase because of the total vertical integration. In addition, ORL is also entitled to engage in the marketing of Oil Distillates itself, which is liable to intensify competition in the market and introduce an additional major competitor, which is also totally vertically integrated in the Oil Distillates marketing segment.

Because the quantity of LPG produced in the oil refineries in Israel is limited and the purchase of imported LPG is at prices that higher than the price of LPG in Israel, Paz and ORL have a significant advantage over Granite and other competitors that do not own oil refineries, in the field of LPG. This is in addition to their anticipated advantage in the area of the marketing of fuels. Accordingly, it can be said that the privatisation of ORL, with its various implications, could have an adverse impact on the operating results of the Granite Group in the Oil Distillates operating segments.

Privatisation of Pi-Glilot – As set forth above, in the context of the process of the privatisation of Pi-Glilot, the three storage and output terminals of Pi-Glilot were sold to Delek, which is one of the Granite Group's competitors, which could give Delek a relative advantage over the other competitors.

Tenders - As outlined above, the Company’s business, institutional customers include customers to which sales have been made as a result of winning large tenders for defined and limited periods. There is no certainty that in the future, Granite group will continue to win such tenders, and accordingly, sales volume is likely to be significantly reduced.

Volatility in the building and renovation segment in Israel – A fall in the number of projects in the building segment, due an economic slowdown and slowdown in real estate

development will result in a drop in consumption of paint and building-finishing in Israel. The fall in the number of projects is liable to have an adverse effect on the operating results of the Granite Group.

Fluctuation in prices of raw materials in the paint and building-finishing segment – Drastic changes in the prices of the raw materials purchased in the paint and building-finishing segment are likely to impact the Granite Group's profitability. In addition, price of some of the raw materials are influenced by changes in oil prices (e.g., plastic packaging and monomers, etc.).

Competition in the operating segments – Sonol, Supergas and Tambour operate in markets which are characterized by extremely tough competition. In the Oil Distillates segment, the Company competes with large and strong competitors. The competition's influences may adversely affect Granite's business, financial position and operating results, including a reduction in revenues, a fall in profit and a loss of market share.

Absence of barriers to entry in the sales of Oil Distillates not in the fuelling stations – Granite is exposed to the entry of several competitors which will compete therein for the sales of Oil Distillates that are not in the fuelling stations, due to the absence of barriers to entry for this business.

Engagements with station owners – Because of the existence of stations in the Sonol Chain that are not under its ownership, it is possible that the owners of these stations, when their contract with Sonol reaches its term, will enter into an agreement with competing fuel companies. In additional, claims have been made against Granite by operators of the fuelling stations alleging restrictive practices. See also Section 11.17.19 above and Note 36 to the Financial Statements in Chapter C of this Report.

Development of similar products – Most of the products developed in the paint and building-finishing segment are not protected by patents. There is a risk that products similar to the products developed by the Granite Group will be developed by competitors in this segment or by other entities.

Failure to obtain approvals and licences required for operating the fuelling stations – Operating the fuelling stations of Granite requires approvals and licences on several grounds. With regard to some of the stations, Granite does not hold all of the necessary licences and approvals or sometimes, they have expired and need to be reduced. If the Company does not manage to obtain the said licences and

approvals, there could be an adverse impact on its operating results.

11.81.3. Risks unique to the Granite Group

Monopoly – Tambour is a monopoly, as this term is defined in the Restrictive Practises Law, 5748-1988 (for the details of the declaration of Tambour as a monopoly, see Section 11.31.4 above), and it is subject to the laws governing monopolies in Israel. The declaration as a monopoly is liable to result in the regulation of the prices of products or the imposition of other business restrictions, a fact that is liable to have an adverse effect on the Company's results.

Collective agreements – Many employees in the Granite Group are employed pursuant to the provisions of collective agreements. The fact that the Granite Group is dictated to by these agreements reduces its ability to make structural or organizational changes in employment terms.

Bank of Israel restrictions regarding "a single borrower" and "a group of borrowers" – The directives of the Supervisor of Banks in Israel include restrictions affecting the ability of banks in Israel to extend credit in excess of certain levels, including restrictions relating to the total debts of one group of borrowers and to the total indebtedness of a bank's six largest borrowers. The Granite Group, the controlling shareholders therein, and companies under their control are considered as belonging to one "group of borrowers" for this purpose. The definition of a group of borrowers also includes, *inter alia*, dependence on the financial stability between the borrowers in the group and borrowers in the group to other borrowers. The said directives could have an impact on the ability of the Granite Group to borrow additional amounts from the banking system in Israel, and their ability to make new investments for which the bank credit is required. However, it should be noted that, to the best of Granite's knowledge, it is not close to the "group of borrowers" restriction at present.

Claims – There are a number of claims pending against the Granite Group, some relating to restrictive practices, including claims which have petitioned for recognition as a class action and others. Therefore, Granite Group is exposed to the implications arising from these claims. (With regard to claims against the Granite Group, see Note 36 to the financial statements in Chapter C of this Report).

The Gas Farm at Kiryat Atta – Supergas's gas storage and refilling facility at Kiryat Atta has a poison permit, in force until May 2012, which allows Supergas to use the facility

subject to the conditions specified in the permit. Additionally, there are legal proceedings vis-a-vis the Kiryat Atta Municipality with respect to construction permits for gas tanks' interment and a business license for the farm. For more details as to the legal proceedings pertaining to the farm, see Note 36 to the financial statements and Section 11.34.2 above. If Supergas shall not have received construction permits for the interment of tanks on the farm, and the poison permit will consequently not be extended, Supergas will not be able to use the gas farm in the normal manner and will have to come up with other solutions for LPG storage and refilling, subject to the provisions of the law, which will enable it to continue providing services to its customers. Such solutions may increase the LPG marketing costs.

Dependence on branding and goodwill – The companies in the Granite Group have accumulated many years of goodwill. Impairment of this goodwill through various publications or other means could adversely affect Granite's results, even if the publications are not accurate.

It should be noted that even these factors can affect the business activity of the Granite Group and its operating results in the future positively or negatively depending on their orientation. The extent of the impact, if any, depends, *inter alia*, on the intensity of the event, their scope, how long they persist, and the ability of the Granite Group to deal with them.

The following is Granite's assessment with regard to the extent of the impact of the risk factors on Granite:

Extent of scope of risk factor on Granite			
	Large effect	**Medium effect**	**Small effect**
Macro risks			
Economic slowdown	√		
Security and political situation	√		
Changes in interest rates	√		
Currency exposure			√
Effect of changes in consumer price index		√	
Social protest		√	
Segment risks			
Changes in global oil prices	√		
Increase in excise duty on diesel fuel		√	
Credit facilities	√		
Marketing margins		√	
Environmental		√	

Extent of scope of risk factor on Granite			
	Large effect	**Medium effect**	**Small effect**
Protection			
Hazardous and toxic materials	√		
Product liability			√
Energy alternatives			√
Regulatory developments	√		
Dependence on ORL		√	
Privatisation of ORL		√	
Privatisation of Pi-Glilot			√
Tenders			√
Fall in number of projects in construction segment		√	
Fluctuations in prices of raw materials in Tambour segment			√
Competition in operating segment	√		
Absence of entry barriers in the Oil Distillates direct marketing segment		√	
Contractual engagements with station owners		√	
Development of similar products			√
Failure in obtaining approvals			√
Risks unique to the Group			
Monopoly			√
Collective agreements		√	
Bank of Israel restrictions			√
Claims	√		
Farm gas at Kiryat Atta		√	
Dependence on branding and goodwill			√

Part Six - Azrieli Group - Additional Business

12. Azrieli Group - Additional Business

12.1 Investments in available for sale financial assets in the banking and finance segment

12.1.1 Investment in Leumi Card

12.1.1.1 On May 26, 2008, the Company invested the sum of NIS 360 million, as a passive financial investment, in Leumi Card Ltd. ("**Leumi Card**") (the total investment less a dividend received as of the date of the report, is NIS 358 million), and in consideration for which Leumi Card issued shares to the Company representing 20% of the issued and paid-up capital of Leumi Card (post money and on a fully diluted basis) (the "**Investment Agreement**"). The Company's investment in Leumi Card is presented on its books as an available for sale financial asset, according to GAAP. The value of the Company's investment in Leumi Card as of December 31, 2011, in accordance with an independent valuation was approx. NIS 483 million.

Within the framework of the Investment Agreement, the Company undertook to comply with and fulfill regulatory requirements to be imposed, if any, on the shareholders of Leumi Card, in its capacity as an Auxiliary Corporation, as this term is defined in the Banking Law (Licensing), 5741-1981. To the best of the Company's knowledge, as of the Date of the Report, no regulatory requirements as aforesaid have been imposed on the Company.

On May 6, 2010, for the purpose of clarifying the lack of material effect of the Company on Leumi Card, the Company's board of directors decided to irrevocably waive the Company's voting rights in connection with two percent (2%) of the issued and paid-up capital of Leumi Card held thereby, such that, in view of the said waiver, the Company would hold 20% of the issued and paid-up capital of Leumi Card and 18% of the voting rights therein.

12.1.1.2 Within the framework of the Investment Agreement, the Company and Leumi Card undertook to one another, *inter alia*, as follows:

a. **Recommendation on the appointment of directors** – The Company will be entitled to recommend the appointment of two directors to the board of directors of Leumi Card, as well as their removal from office and the appointment of others in their stead, with one director serving as an outside director according to the provisions of Proper Conduct of Banking Business. The agreement provides that should the Company's holdings decline to less than 20% due to a sale of shares or transfer thereof to an unauthorized third party, or less than 18% as a result of a private placement of Leumi Card shares, or less than 15%, the Company will be entitled

to recommend the appointment of only one director. The Company's right to appoint directors shall expire in the event that its holdings decline to less than 10% due to a sale of shares or transfer thereof to an unauthorized third party or in any other event in which its holdings decline to less than 8%. On May 6, 2010, further to the said resolution of the same date, the Company's board of directors resolved to irrevocably waive the right to recommend the appointment of another director to Leumi Card, as an outside director. As of the Date of the Report, only one director holds office on behalf of the Company on the board of directors of Leumi Card, which comprises 12 directors (4 of whom are outside directors).

b. **Letter of indemnification** – In the agreement, the Company granted Leumi Card a letter of indemnification, under conditions back-to-back with the conditions of the letter of indemnification provided by Bank Leumi in favor of the directors holding office at Leumi Card (and as long as it shall not have been changed without the advance written consent of the Company), whereby in any event in which Leumi Card will be obligated to indemnify the directors holding office therein on behalf of the Company, the Company will indemnify Leumi Card, upon receiving its written demand, for any amount paid by Leumi Card as aforesaid.

c. **Rights upon a transfer of shares** – The Company will have the right to tag along in a sale and/or transfer of control in Leumi Card to a third party who is not an authorized transferee of Leumi Financial Holdings Ltd. ("**Leumi Holdings**"), Leumi Card's controlling shareholder, until the occurrence of certain events which are specified in the agreement, such as a public offering. In addition, Leumi Holdings was granted a right of first refusal and a bring-along right vis-à-vis the Company upon a transfer of shares.

d. **Shareholder financing –** The parties have undertaken to provide financing to Leumi Card proportionately to their holdings at such time, pursuant to a resolution of the board of directors of Leumi Card. The agreement sets forth dilution formulae for the dilution of a party which does not finance its share as aforesaid.

To the best of the Company's knowledge, in 2011, Leumi Card recorded net profit in the sum of approx. NIS 177 million. On May 24, 2010, the board of directors of Leumi Card approved a dividend policy whereby a dividend in a sum equal to 30% of Leumi Card's net current profit shall be distributed, subject to the directives of the Supervisor of Banks, to regulatory directives and to the requirements of the Companies Law. Further to the requirement of the Supervisor of Banks with respect to capital adequacy targets, the dividend distribution policy was changed and on May 22, 2011,

Leumi Card's board of directors determined that distribution of a dividend will be possible subject to risk appetite restrictions and the supervision requirements. Accordingly, the board of directors of Leumi Card approved, on February 23, 2012, the distribution of a dividend to the shareholders of Leumi Card in the sum total of NIS 40 million from Leumi Card's profits in 2011, to be distributed, in accordance with Leumi Card's publications, on March 29, 2012. Leumi Card's financials are publicly posted on Leumi Card's website and are available for inspection at the following link:

https://www.leumi-card.co.il/he-il/GeneralPages/Pages/FinancialReport.aspx

12.1.1.3 Concurrently, on May 26, 2008, the Company entered into a cooperation agreement with Leumi Card for the establishment of a program for the benefit of customers of the commercial centers and malls owned by the Company and/or affiliates of the Company, whose members would hold a Leumi Card card conferring special benefits and services (the "**Loyalty Program Agreement**"). The Loyalty Program Agreement is effective for seven years and is automatically renewed for additional one-year terms, unless written notice of termination by either party is received 90 days in advance, or if it expires earlier by a decision of Leumi Card to stop issuing Leumi Card cards. The aforesaid notwithstanding, the agreement may be terminated five years after the date of execution thereof, provided that written notice is given, twelve months in advance.

The Loyalty Program Agreement regulates the relationship between the parties, and, *inter alia*, sets forth provisions with regards to the terms of the loyalty card to be issued to the customers of the commercial centers and malls of the Company and its design, including the Company's rights to the loyalty program trademark and the member database, and registration thereof in its name.

On January 7, 2010, the Company entered into a licensing agreement with Leumi Card for the use of trademarks, whereby the Company granted Leumi Card an exclusive license to use all of the trademarks registered in the Company's name in connection with the "Multi Azrieli" mark, in connection with the operation and advertising of the loyalty program. The license is effective throughout the term of the Loyalty Program Agreement and subject to the conditions thereof. During 2011, the Company registered the trademark "Multi Azrieli" with the Registrar of Patents, Designs and Trademarks at the Ministry of Justice, including the registration of the Leumi Card as a licensee of the "Multi Azrieli" trademark, in accordance with the said licensing agreement.

In the agreement, the Company undertook to employ a management team to manage the Program's activities throughout the term of the agreement, at an annual cost that shall not exceed the amount of NIS 250,000, to be financed by Leumi Card. In addition, the Company neither has had, nor expects to have any revenues or benefits in connection with the Loyalty Program Agreement.

To the best of the Company's knowledge, as of the Date of the Report, the Loyalty Program comprises approx. 125,000 valid loyalty cards, out of, to the best of the Company's knowledge, approx. 2 million valid credit cards that are held by Leumi Card customers.

The loyalty card provides a discount of NIS 0.21 per liter and a 5% discount on some of the products at the convenience stores in Sonol fuelling station complexes. In addition, the card provides a discount at the rate of 10% at the parking lots adjacent to the Azrieli malls.

12.1.2 Investment in Bank Leumi

On April 30, 2009, the Company acquired from third parties, unaffiliated with the Company, as a passive financial investment, ordinary shares of Bank Leumi, a banking corporation whose shares are listed on TASE, representing approx. 4.8% of the issued and paid-up share capital of Bank Leumi, in consideration for a sum total of approx. NIS 742 million (as of the date of the report, the total investment less a dividend received is approx. NIS 676 million). The value of the Company's investment in Bank Leumi as of December 31, 2011 was approx. NIS 771 million. As of the Date of the Report, no change has occurred in the said holdings of the Company. The Company's investment in Bank Leumi is presented on its books as an available for sale financial asset, according to GAAP, and as of the Date of the Report, no decision has been made by the Company in connection with an increase or decrease of such holdings.

In 2011, due to significant fluctuations in the value of Bank Leumi's stock, the Company recorded a total loss due to this investment. For details, see Section 1.10 of the Board of Directors' Report.

The acquisition of the Bank Leumi shares was financed through loans taken by the Company. On the date of the acquisition, on April 30, 2009 (the "**Acquisition Date**"), the share price was 1055 (agorot). As of December 31, 2011, the share price was 1,091 agorot, whereas on March 14, 2012, the share price was 1,118 agorot.

To the best of the Company's knowledge, in 2011 Bank Leumi distributed a dividend to its shareholders, as specified below:

12.1.2.1 On December 28, 2010, the general meeting of Bank Leumi approved a dividend distribution for the first nine months of 2010 (after a previous distribution in respect of this year's profits of November 30, 2010) in the sum of NIS 500 million, at a rate of approx. 34% on the paid-up capital. The dividend is approx. NIS 0.34 for each share of par value NIS 1.0 of ordinary stock.

On January 27, 2011, the Company received approx. NIS 24 million as a dividend from Bank Leumi due to this distribution.

12.1.2.2 On May 24, 2011, the general meeting of Bank Leumi approved an additional cash dividend distribution to the bank's shareholders in the sum of NIS 400 million at the rate of approx. 17% of the bank's

net profit for 2010. The said dividend was approx. NIS 0.27 for each share of par value NIS 1.0.

On June 28, 2011, the Company received approx. NIS 19 million as a dividend from Bank Leumi due to this distribution.

12.1.2.3 Bank Leumi's financials are publicly posted on the distribution website of the ISA at www.magna.isa.gov.il and on the TASE website at www.tase.co.il.

12.2 Investing in high-tech start-up companies and investment funds

The Company from time to time invests in various high-tech start-up companies with a special emphasis on the medical, telecommunications, software and other such segments, which, in its estimation, have a large market potential and reflect innovation in their segments. The Company's investments in risk capital are made in amounts that are immaterial to the Company, with the intention of disposing of these investments upon the sale of the target company, the sale of its technology or its issue to the public. As a general rule, most of the Company's investments are in companies that have undergone the preliminary stage of development of the products and/or the services thereof. These investments are risk-intensive, and their results depend, *inter alia*, on many external factors over which the Company has no control. For details regarding the Group's risk factors, see Section 25 of the Report.

As of December 31, 2011, the Company has invested in approx. 10 active investment funds and start-up companies, which are presented at fair value in the sum of approx. NIS 16,737 thousand, and at fair value in the sum of approx. NIS 17,408 thousand as of December 31, 2010. Additionally, the Company has invested a total sum of approx. NIS 42,408 thousand in approx. 7 start-up companies, the investment in which was fully amortized in the Company's Financial Statements.

12.3 Holdings in other foreign companies

As of the Date of the Report, the Company has given notice of the exercise of a put option for the sale of all of its holdings (approx. 6.41%) in the issued and paid-up share capital of Health and Fitness Central Europe B.V ("**Fitness Europe**") that operates the "Holmes Place" chain of fitness centers in various countries in Europe. The notice regarding the exercise was given on November 7, 2011 and confers upon the Company the possibility to sell all of its holdings in Fitness Europe, at a price equal to the sum of its total investment in the company (which has not yet been repaid) plus 5% annual interest. In accordance with the terms of the Investment Agreement, the consideration for this exercise is supposed to be paid to the Company in 2012.

In addition, the Company holds approx. 3.8% of the issued and paid-up share capital of Health and Fitness East Med. B.V., which operates the "Holmes Place" chain of fitness centers in Greece.

In addition, as of the Date of the Report, the Company holds, through Otsem, full ownership of Azrieli Insurance Corporation in Barbados, which serves as a reinsurer for companies that provide property insurance services. As of the Date of the Report, Azrieli Insurance Corporation provides reinsurance services only with respect to insurance granted to the Group's companies.

Part Seven: Matters Common to the Group's Activities in All of its Operating Segments[25]

13. Fixed assets, land and facilities

The Company's offices are situated on the 48th floor of the Round Tower in Azrieli Center in Tel Aviv. The Company leases its offices, a gross area of 1,520 sqm[26], from Canit Hashalom for a long-term period, for immaterial amounts.

The Group's fixed assets primarily include furniture, office equipment, computers, vehicles and other assets. As of December 31, 2011, the Group's total fixed (net) assets was approx. NIS 44,909 thousand. The Group's fixed assets do not include the fixed assets in the Granite Hacarmel operating segment. For details concerning the Granite Hacarmel fixed assets, see Sections 11.12, 11.43, 11.44 and 11.64 of the Report.

14. Intangible assets

The Company and the Group companies' primary trade mark is a designed mark which includes the inscription "Azrieli Malls Group", in addition to the name of the mall and/or relevant commercial center, and the Group's logo:

As of the Report Publication Date, the Company has registered many trademarks, in the format as described above, in the Trademarks Register of the Patents, Designs and Trademarks Authority which is maintained by virtue of the Trade Marks Ordinance [New Version], 5732-1972 in connection with services in the Group's operating segment and services ancillary thereto.

As of the Report Publication Date, the Company owns approx. thirty registered trademarks, in the format as described above, in respect of all of the malls and commercial centers owned by the Group. In addition, the Group filed additional applications for registration of trademarks that are still in the process of registration and review, mainly due to new properties and properties under construction, including an application to register trademarks (including a 3D trademark) of the shape of the ball that appears at the entrance to some of the Company's malls.

Registration of trademarks is valid for 5 years and can be renewed, in a resolution of the Company, for additional periods of 10 years each, without restriction.

For details regarding the Company's trademark "Multi Azrieli" within the framework of the Company's loyalty program and Leumi Card, see Section 12.1.1.3 of the Report.

[25] The provisions of this part four "Matters Common to the Group's Activities in All of its Operating Segments" do not include the Granite Hacarmel operating segments unless explicitly stated otherwise.

[26] As of April 30, 2009, the Company has leased a gross area of 1,520 sqm. Likewise, as of December 31, 2009, the Company has leased, in a sub-lease, to Canadian Public Funds, an area of approximately 4.08% of the leased area, pursuant to terms identical to the lease terms borne by the Company.

15. Human capital

15.1 General

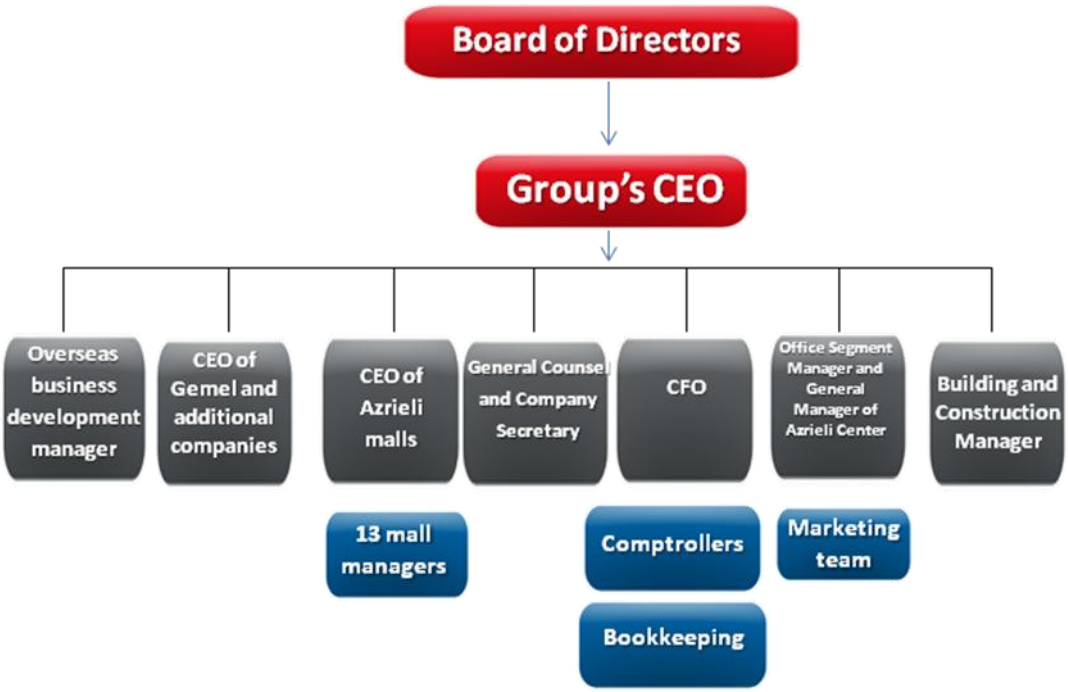
The Company places special emphasis on the quality of human capital, particularly at the Company's management level, by hiring a professional workforce with vast knowledge and experience in a variety of fields which are required within the framework of the Company's operating segments. Most of the Company's employees, mainly at its management level, have significant seniority in the Company, and vast experience in its operating segments.

The Company estimates that the activity, status, contacts, professionalism within the Company's operating segments and vast experience of Mr. David Azrieli, the Company's controlling shareholder and Chairman of the Company's Board of Directors, confer upon the Company, *inter alia*, knowledge and an advantage in its operating segment and are among the success factors that contributed to the Company's business results and which had and still have a positive effect on its success.

The Group's activity is carried out through its managerial headquarters including, *inter alia*, the Company's CEO, CEO of Azrieli Malls, CFO, VP Marketing and Manager of Azrieli Center, General Counsel and Company Secretary, Manager of the Building and Construction Department, Business Development Manager, managers and other officers who are directly subordinate to the Company's CEO. The people that belong to the Group's managerial headquarters are people with vast managerial experience, who have been by the Group's side for many years. The Company's representatives serve on the boards of directors and committees of the Group Companies and maintain current contact with the Group companies' management.

15.2 Organizational structure and workforce

The diagram below describes the Group's organizational structure:



As of December 31, 2011, the Group companies (excluding employees hired in the Granite operating segment) employ 226 employees. The segmentation of the employees is detailed below:

Department	Number of Employees as of December 31, 2011	Number of Employees as of December 31, 2010
Management Headquarters	32	32
Commercial Centers and Malls Segment	131	113
Office and Other Space for Lease in Israel Segment	62	63
Income-producing property in the U.S. Segment*	1	1
Total	226	209

* One employee from the management headquarters is attributed to the income-producing property in the U.S. segment.

The main increase in the number of Company employees in the commercial centers and malls segment derives from the construction and acquisition of new properties and *inter alia* hiring manpower for Azrieli Akko Mall and Azrieli Kiryat Ata Mall that were opened during Q3/2011.

The Group's management and headquarters employs 32 employees, including the Active Deputy to the Chairman of the Board of Directors, Vice Chairman of the Board of Directors, the Group's CEO, CFO, General Counsel and Company Secretary, CEO of Azrieli Malls and Manager of the Offices Segment and CEO of Azrieli Mall. 131 employees work for the Group's commercial centers and malls segment, of which 115 work on the management and maintenance teams of the commercial centers and malls, which engage in the current management of the commercial centers and malls, and 16 employees provide marketing services to all of the Group's commercial centers and malls.

62 employees work in the office and other space for lease in Israel segment, of which 58 work on the segment's management and maintenance teams which engage in the current management of the offices, and 4 engage in the provision of marketing services.

As of the Date of the Report, the income-producing property in the U.S. segment is managed by the Company's headquarters and the Overseas Business Development Manager. Management services and other services are provided to the Group in this segment by local professional management companies.

As of the Date of the Report, there are, between the Company and the Group companies, cooperation and agreements in connection with the provision of management services between themselves, including, *inter alia*, financial advice, strategic advice and current management advice, in consideration for a monthly payment. In addition, there are management agreements with the Group companies which derive, in part, as a percentage of such company's total expenses. The total payments that were made between the Group companies (including a management agreement between Granite Hacarmel and Canit Hashalom) for these management

services, in 2011 and 2010, amounted to the sum of approx. NIS 33.1 million and approx. NIS 26.3 million, respectively.

15.3 **Investing in training, instructing and developing the human capital**

The Group companies hold training and instruction workshops from time to time for their employees in accordance with the employee's position and the Group's needs. Employees of the Group companies keep abreast of fields touching on their responsibilities in the Group, from time to time, by participating in exhibitions, seminars, conferences and professional courses.

15.4 **Benefits given to employees and the nature of the employment agreements**

Employees in this Group are hired pursuant to personal contracts and no collective bargaining agreements apply.

The employment conditions of the Group's employees include, in some cases, *inter alia*, *per diems*, travel expenses / car maintenance / making a vehicle available to the employee, managers insurance / pension fund, advanced training fund, annual leave, recuperation pay, basic health insurance, payment for global overtime, reimbursement of expenses and a 13th salary.

Additionally, the Group's third party insurance policy is an extended policy that includes coverage for professional liability for the management companies and the Company's employees who are professionals, with a liability cap of $2 million per incident and per insurance period, as part of the policy's liability cap.

In addition to the above, all of the Company's and the Group Companies' liabilities are covered in respect of the employees' social rights and termination of the employment relationship by deposits that are made in severance pay funds and insurance policies and/or provisions that exist on the Company's books. For a description of the Company's liabilities in relation to the employees' social rights and termination of the employment relationship, see Note 23 to the Company's Financial Statements.

15.5 **Hiring officers and senior management employees in the Group**

As of the Date of the Report, members of senior management in the Group are hired as employees under personal employment agreements or through management agreements. For further details regarding employment agreements of senior officers in the Group, see Section 21 of Chapter D of the Report.

As aforesaid, the Group's business has developed, *inter alia*, on the basis of the know-how and vast experience accrued thereby over many years in the income-producing property in Israel segment, utilizing the experience and expertise of its main controlling shareholder, Mr. David Azrieli, who founded and established the Company from its inception. Therefore, in the Company's estimation, Mr. David Azrieli, who serves as Active Chairman of the Company's Board of Directors, has made a significant contribution to the Company's development and to its success in the Report Period, due to Mr. Azrieli's know-how, expertise, experience and contacts. In addition, Mr. Menachem Einan who serves as Active Deputy to the Chairman of the Board of Directors, and served as the Group's CEO for many years alongside Mr. Azrieli, has also made a significant contribution to the Group due to his know-how, expertise, experience and contacts. Over the many years that the Group has been in operation, Mr. Azrieli and Mr. Einan have trained a senior management team which has served in this

role for over a decade and which has led the Group during its development in recent years. Therefore, the Company estimates that although cessation of provision of the services by either Mr. David Azrieli or Mr. Menachem Einan to the Group may have a short-term effect on the Company until a replacement is found with the appropriate credentials, their ending their roles would not materially affect the Group's business results.

On January 16, 2011, the Company's Board of Directors, following the approval and recommendation of the Company's audit committee, approved that Mr. Menachem Einan, CEO of the Company, be promoted and appointed as an Active Deputy to the Chairman of the Board, while ceasing to act as CEO, from April 1, 2011. In this position, Mr. Einan will be considered as one of the two deputy chairman of the board of directors whom the board is entitled to elect, as provided in the Company's Articles of Association, in addition to Ms. Danna Azrieli, who has served as active deputy to the chairman of the board since June 2010. As Active Deputy Chairman to the Board, Mr. Einan will be responsible for the strategic areas related to the Group's continued business development and the realization of its long-term vision. In the framework of Mr. Einan's promotion, the terms of the management agreement with him, which are specified in Section 21 of Chapter D of the Report, were not changed.

Commencing from April 1, 2011, Mr. Shlomo Sherf serves as the Company's CEO (in lieu of Mr. Einan). During the last twenty years, Mr. Sherf served as CEO of Electra Ltd. and CEO of Electra Real Estate Ltd., companies traded on the TA-100 Index on the Tel Aviv Stock Exchange Ltd. For a description of the management agreement signed with Shlomo Sherf and his terms of employment, see the Company's immediate report as of January 16, 2011 (reference no. 2011-01-018405), which is included herein by way of reference, and Section 21 of Chapter D of the Report.

15.6 **The Group's employee compensation plan**

On June 10, 2010, the Company allotted 935,026 phantom units of a total financial value of NIS 28,350 thousand to senior officers and employees of the Company, including the Active Deputy to the Chairman of the Company, according to the allotment plan specified below:

On May 5, 2010, the Company's Board of Directors approved a Phantom Unit allotment plan pursuant to which the Company granted units representing theoretical shares ("**Phantom Units**) of a total value of between NIS 28 and 28.5 million, which were allotted to 32 senior officers in the Company (with the exception of the Chairman of the Company's Board of Directors and the deputy chairman of the Company) and the Company's employees (the "**Plan**"). The Phantom Units that were granted as aforesaid by virtue of the Plan will entitle the offerees to financial compensation in cash deriving from the increase in the value of the Company's shares on the basis of the mechanism detailed in the Plan. For details regarding the Phantom Units and the conditions of the Plan, see Note 25 of the Financial Statements.

In the opinion of the Company, the compensation mechanism for Company employees by way of the Phantom Units is an accepted method of incentivizing employees in companies of this type and a means of increasing the motivation of managers and staff. The mechanism determined for the vesting of the units links the compensation to the continued contribution to the Company and its results over time. In this framework, the compensation and/or the amount thereof is contingent upon improvement in the share price, which in turn reinforces the link between the offerees' contribution to the

Company's results and the share price and motivates the compensation recipients as aforesaid to promote the Company insofar as possible.

On June 8, 2010, the Company's Board of Directors appointed Mr. David Azrieli and Mr. Menachem Einan to the committee for implementation of the Plan.

In April 2011, the Company allotted to Mr. Shlomo Sherf, in accordance with the management agreement which was signed with him, an additional 284,527 Phantom Units according to a base price which was determined in accordance with the average price of the Company's stock in March 2011 (NIS 96.11, dividend-adjusted), according to a new plan, whose principles are identical to the plan described above. For further details see Section 21 of Chapter D of this Report.

For details concerning the compensation plan for senior officers and employees of Granite Hacarmel and its subsidiaries and affiliated companies, see Section 11.73.5 of the Report.

15.7 **Insurance, exemption and indemnification**

In accordance with resolutions of the Company's general meeting dated May 6, 2010, the directors and officers of the Company are insured under D&O insurance. In accordance with such resolution, in June 2011 the Company's Audit Committee and Board of Directors approved the renewal of the said insurance policy. In addition, the Company is issuing letters of exemption and indemnification to the officers therein, who are serving in the present and will serve in the future, in accordance with the provisions of the Companies Law and the Company's Articles of Association. On August 15, 2011, the Company's general meeting approved an amendment to the indemnification and insurance clauses set forth in the Company's articles of association as well as an amendment to the letters of indemnification, mainly in view of the taking effect of the Streamlining of Enforcement Proceedings at the ILA (Legislative Amendments) Law, 5771-2011. For a specification of these issues, see Section 29A of Chapter D of the Report. For details regarding the insurance for the liability of directors and officers serving in Granite Hacarmel, see Section 11.78 above.

16. **Working capital**

16.1 **Working capital**

As of December 31, 2011, the Group has positive working capital (without Granite) in the sum of approx. NIS 368 million compared with positive working capital in the sum of approx. NIS 1,460 million, as of December 31, 2010. The decrease in the working capital mainly derives from use of the IPO proceeds managed in marketable security portfolios for the financing of the acquisition and construction of investment property.

16.2 **Customer credit**

In the income-producing property segment there is no customer credit since the lease agreements with tenants contain provisions for payment of rent in advance and for monthly or quarterly periods. The Group collects the rent pursuant to the terms and conditions of the lease agreement, usually, by way of a standing order, bank transfers and postdated checks. The tenants, before the handing over of the leased premises thereto, provide securities for performance of their undertakings pursuant to the lease agreements and the management agreements (bank guarantees, deposits, promissory

notes, personal guarantees, etc.). The cases in which rent is not paid in advance are immaterial to the Group.

16.3 **Suppliers credit**

The Company receives credit from its suppliers (primarily contractors and maintenance service providers) for average periods ranging from 15 to 60 days, after the requested service has been completed (on average - a period of approx. 45 days). The scope of credit from suppliers in the Group (excluding Granite Hacarmel), as of December 31, 2011, amounted to approx. NIS 77 million, compared with a sum of approx. NIS 43 million as of December 31, 2010.

The data concerning the Group's working capital do not include financial data in Granite Hacarmel's operating segment. For details concerning Granite Hacarmel's working capital, see Section 11.14 of the Report.

17. **Financing**

17.1 **General**

The Group finances its activities from independent resources, from bank credit from financial institutions and non-bank credit, including through the issue of bonds from institutional bodies that are not listed on TASE.

The Group's financing section below does not include data in connection with financing in Granite Hacarmel's operating segment. For details concerning Granite Hacarmel's financing, see Section 11.75 of the Report.

The Group has long-term liabilities to banking corporations and non-bank financing sources amounting, as of December 31, 2011, to the sum of approx. NIS 4.3 billion (including current maturities). Most of the agreements include provisions pursuant to which the Company has the right to prepayment which is contingent, in most cases, upon the payment of a prepayment fine to the financing entity. Additionally, the loan agreements with banking corporations contain certain conditions, upon the occurrence of which, the banks may accelerate the loan amounts (primarily in the case of restructuring and a change of control in the Company, delinquent payments, receivership, and an adverse change in the value of the securities, if and insofar as securities were provided). To the best of the Company's knowledge, as of the Report Publication Date, the conditions for acceleration of the loans have not been fulfilled.

For details concerning the financial liabilities of the Group (excluding Granite) as of December 31, 2011, see Section 1.5 of the Board of Directors' Report. For details concerning projected payments per year, see T-126 as of March 22, 2012 which is published concurrently with this Report.

For further details concerning the Company's financing in general, see the Board of Directors' Report attached to this Report in Chapter B.

17.2 **The Group's loan balance (not intended for specific uses) as of December 31, 2011**

Set forth below is a specification of the average interest rate and the effective interest rate (which as detailed below, on the Date of the Report, is identical to the average interest) on long-term loans and short-term loans that were in effect during 2011, and

which are not intended for specific uses by the Group, while distinguishing between bank credit sources and non-bank credit sources:

As of December 31, 2011						
	Long-Term Loans			Short-Term Loans		
	Amount (NIS in thousands)	Average Interest Rate	Effective Interest Rate	Amount (NIS in thousands)	Average Interest Rate	Effective Interest Rate
Non-bank Sources - Index Linked Financing	1,167,401	4.86%	4.86%	---	---	---
Banking Sources - Index Linked Financing	504,025	4.74%	4.74%	---	---	---
Banking Sources - NIS Financing	31,250	5.5%	5.5%	---	---	---
Non-Bank Sources - NIS Financing	-			166,751	3.39%	3.39%
Total Financial Liabilities	**1,702,676**	**4.84%**	**4.84%**	**166,751**	**3.39%**	**3.39%**

17.3 Reportable credit made available to the Company

Set forth below is a specification of the balances of the material loans that were provided to the Company as of December 31, 2011 (NIS in thousands). The following data was updated versus the provisions of the Company's previous periodic statements and the Prospectus, such that they shall include specific reference to material loans only, in accordance with legal position 104-15 of the ISA regarding reportable credit[27]:

Date of provision of the Loan	Designation of the Loan	Type of Loan			Balance (including current maturities) as of December 31, 2011 (NIS in millions)	Type and rate of annual interest	Linkage	Guarantees / collateral (NIS in thousands)	Date for payment of long-term loans
		Banking corporation	Short-term	Long-term					
January 2010	Acquisition of Haifa Mall	Banking Corporation A		X	215		Linked to the consumer index	1) Fixed charge on the Company's rights in Azrieli Haifa Mall. 2) Fixed charge on the Company's rights in the lease agreements in Azrieli Haifa Mall; 3) First-ranking floating charge on all of the Company's rights in Azrieli Haifa Mall.	**Until October 2019**
June 2009	Acquisition of Givatayim mall	Banking Corporation A	X		167	Prime-0.6%	Not Linked	1) Undertaking to register a mortgage. 2) First-ranking pledge of contractual rights deriving from the mall. 3) First-ranking fixed charge on all of the rights deriving from the mall. 4) First-ranking floating charge on all of the rights in the mall. 5) Undertaking not to create a floating charge on all of the assets without receipt of the banking corporation's consent.	---
June 2009	Acquisition of Givatayim Mall	Banking Corporation A		X	141	3.2%	Linked to the consumer index	1) Undertaking to register a mortgage. 2) First-ranking pledge of contractual rights deriving from the mall. 3) First-ranking fixed charge on all of the rights deriving from the mall.	**Until December 2013**

[27] Legal position no. 104-15: Reportable Credit Event, of October 30, 2011, *http://www.isa.gov.il/Download/IsaFile_6187.pdf*.

Date of provision of the Loan	Designation of the Loan	Type of Loan			Balance (including current maturities) as of December 31, 2011 (NIS in millions)	Type and rate of annual interest	Linkage	Guarantees / collateral (NIS in thousands)	Date for payment of long-term loans
		Banking corporation	Short-term	Long-term					
								4) First-ranking floating charge on all of the rights in the mall. 5) Undertaking not to create a floating charge on all of the assets without receipt of the banking corporation's consent.	
March 2009	Acquisition of Givatayim Mall	Banking Corporation A		X	297	4.7%	Linked to the consumer index	1) Undertaking to register a mortgage. 2) First-ranking pledge of contractual rights deriving from the mall. 3) First-ranking fixed charge on all of the rights deriving from the mall. 4) First-ranking floating charge on all of the rights in the mall. 5) Undertaking not to create a floating charge on all of the assets without receipt of the banking corporation's consent	**Until March 2017**
March 2007	Current needs	Banking Corporation B		X	376	4.75%	Linked to the consumer index	Undertaking not to create a floating charge on all of the assets without receipt of the banking corporation's consent	**Until March 2017**
October 2011	Sarona Azrieli Center		X		190	Prime – 0.7%	Not linked	---	---

The Company has other non-material loans from banking corporations whose balance on the books, as of December 31, 2011, is approx. NIS 0.5 billion. These loans bear interest ranging between 3.85% and 5.8%, which shall be paid in 2013-2020. There are no financial covenants for these loans or for the material loans.

The Company undertook vis-à-vis some of the banking corporations not to create a floating charge on all of its assets without receipt of their consent, and that in the event of a breach vis-à-vis the banking corporations, they will be entitled to accelerate also other loans that shall have been given to the Company.

As of December 31, 2011, the total short-term and long-term credit received from Bank Hapoalim amounts to the sum of approx. NIS 579 million thousand, and the total short-term and long-term credit received from Bank Leumi amounts to the sum of approx. NIS 1,218 million.

As of December 31, 2011, the sum total of the Company's short-term loans taken thereby from banking corporations amounted to NIS 477 million, and long-term to NIS 1,450 million.

As of December 31, 2011, the scope of the Group's non-pledged income-producing properties is in the sum of approx. NIS 7.2 billion, as specified in Section 1.5 of the Board of Directors' Report, out of the sum total of the Group's income-producing properties in the sum of approx. NIS 14.8 billion.

17.4. Reportable credit made available to the Group Companies

Set forth below is a specification of the balances of the material loans that were provided to the Group companies as of December 31, 2011 (NIS in thousands):

Borrower Corporation	Date of Provision of the Loan	Designation of the Loan	Type of Loan			Balance as of December 31, 2011 (Company's share) (NIS in millions)	Annual Interest Rate	Linkage	Guarantees NIS in thousands/ Pledge	Date of Payment of Long-Term Loans
			Banking Corporation / Financial Institution	Short-Term	Long-Term					
Canit Hashalom	August 2001	Azrieli Center	Banking Corporation B		X	317	6%	Linked to the consumer index	Mortgage and Undertaking Not to Create a Floating Charge. The loan is secured by all of the collateral that was or shall be given to the banking corporation and any breach of another undertaking vis-à-vis the banking corporation confers a right to accelerate the loan.	**Until August 2013**
Canit Hashalom	August 2001	Azrieli Center	Banking Corporation A		X	551	5.975%	Linked to the consumer index	Mortgage and Undertaking Not to Create a Floating Charge	**Until August 2013**
Shareholders in the property[28]	February 2011	Acquisition of Three Galleria	Financial Institution A		X	497	5.998%	US Dollar	Pledge of the property and all of the rights relating thereto and deriving therefrom. Guarantee of the Company, forfeitable only in several specific instances defined in the loan agreement. The Company's undertaking to indemnify the financer for its damage in the event of certain breaches of the buyer's undertakings in the loan agreement	**Until February 2021**

[28] The loan was taken by Three Galleria Office Buildings, LLC, which is indirectly held 90% by the Company. The amount of the loan is in respect of 100% of the loan.

The Group has other non-material loans from banking corporations whose balance on the books, as of December 31, 2011, is approx. NIS 0.4 billion. These loans bear interest ranging between 4.35% and 7%, which shall be paid in 2013-2021. There are no financial covenants for these loans or for the material loans.

As of December 31, 2011, the Group companies' total long-term and short-term credit received from Bank Hapoalim amounts to the sum of approx. NIS 483 million, and the sum total of the Group companies' long-term credit received from Bank Leumi amounts to the sum of approx. NIS 562 million.

17.5 **Non-Bank Financing for the Company**

17.5.1 Issuance of Marketable Securities

17.5.1.1 On June 26, 2009, a framework agreement was signed between the Company and various institutional bodies of the type of the investors listed in the first schedule to the Securities Law, for the issuance of marketable securities (**"MS**"), which includes general conditions in connection with participation terms, immediate payment, expansion of the series, purchase of MSs by the Company and affiliated companies, tender mechanism, if any, and the issuance proceedings.

17.5.1.2 On July 1, 2009 the Company announced the issuance of an unrated MS series at a scope of up to NIS 65 million, with the Company having the right to increase or decrease the scope of the issue, at its sole discretion, while the Company exercised its right as aforesaid and increased the scope of the issue. The MSs were issued for a period of one year which is automatically renewed for four additional periods of one year each, considering daily exit points, by advance written notice of seven business days. The MSs bear annual interest at the Bank of Israel's interest rate plus 0.8%, paid at the end of each year. The principal is paid at the end of the period or in a payment upon utilization of an exit points. In 2009, the Company issued a total of approx. NIS 96 million. In 2010, the Company paid the principal of the marketable securities in the sum of approx. NIS 27 million. In 2011, the Company paid principal of the marketable securities in the total sum of approx. NIS 37 million. The securities which were paid as aforesaid have been written off. As of the Date of the Report and as of the Report Publication Date, the liabilities balance in respect of issuing marketable securities amounted to a sum of approx. NIS 32 million.

17.5.1.3 On July 1, 2009, the Company announced the issue of a series of MSs with a P-1 rating by Midroog Ltd., at a scope of up to NIS 135 million for a period of ninety days from the clearing date that is automatically renewed for another nineteen additional periods of ninety days each (in accordance with notice to be sent to investors), considering daily exit points by prior written notice of seven business days, as an off-floor transaction in accordance with the TASE Directives. On June 30, 2011, Midroog extended the validity of the rating with respect to this series until June 30, 2012. For details, see the Company's report of June 30, 2011 (ref. no.: 2011-01-198045). In January 2012, Midroog expanded the rating framework for this series from NIS 135

million to NIS 200 million (for details see the Company's report of January 12, 2012 (ref. no.: 2012-01-013743)). The MSs bear annual interest at the Bank of Israel's interest rate plus 0.6%, paid at the end of each ninety-day period or upon utilization of exit points, whichever is earlier. The principal is paid at the end of twenty periods of ninety days or upon settlement if the period was not renewed as aforesaid or settlement upon utilization of the exit points. This Series was listed on the trading system for classified investors of TASE's "Nesher" type [securities not listed for trade on TASE]. In 2009, the Company issued a total of approx. NIS 135 million MSs of this kind. In January 2012, after the date of the Statement of Financial Position, the Company issued an additional sum of NIS 65 million. During 2010, the Company paid principal of the rated marketable securities in the aggregate sum of NIS 5 million, and in 2011, the Company raised principal of the rated marketable securities in the aggregate sum of NIS 5 million. As of the Date of the Report, the balance of liabilities in respect of issuing marketable securities amounted to a sum of approx. NIS 135 million, and as of the date of publication of the Report to the sum of NIS 200 million. For details regarding restrictions to which the Company has committed, see Section 17.7.3 below.

17.5.2 Issuance of Series A Bonds

On March 21, 2007, the Company issued, in a private placement to institutional investors, NIS 725 million, par value Series A bonds of the Company, non-negotiable, registered, linked (principal and interest) to the consumer price index that was published for the month of February 2007, and bearing effective annual interest at the rate of 4.8%. On June 5, 2007, the Company issued an additional NIS 15 million, par value Series A bonds of the Company, whose conditions were identical to the conditions of the Company's Series A bonds, such that after the issue, the scope of the series was in the aggregate sum of NIS 740 million par value Series A bonds. The principal of the Company's Series A bonds will be paid in annual installments at a rate equal to 5% of the principal amount on March 31 of each one of the years 2008-2016 (i.e. 45% of the total principal) and payment of the principal balance at the rate of 55% of the principal sum will be made in a single installment on March 31, 2017. The interest on the Series A bonds will be paid each quarter (on June 30, September 30, December 31 and March 31), commencing from June 30, 2007 until March 31, 2017 (inclusive). The Bonds are not secured by any securities.

On the issuance date, the Company's Series A bonds were rated by Midroog Ltd. ("**Midroog**") with a rating of Aa2 and by Standard & Poor's Maalot ("**Maalot**") with a rating of AA\Stable. For further details regarding the current credit rating, see Section 17.11 of the Report.

The Series A bonds were listed on TASE's TACT institutional system, whereby the Company is entitled, at its sole discretion, to list the Series A bonds on TASE. The bonds will be accelerated upon fulfillment of certain conditions, including upon receivership, delinquent payments, change of control, the sale of rights in two of the following properties: Ayalon Mall, Hanegev Mall or the Jerusalem Mall, as a result of the sale of which a decline shall occur in the bonds' rating, as being at such time. The grounds for acceleration in relation to a

change of control, the sale of two of the Group's properties as stated above and a reduction of the bonds' rating below a BBB+ rating will be canceled upon the listing of the bonds. Within the framework of the issue of the Series A bonds, the Company undertook not to distribute dividends to its shareholders, if such a distribution would cause a decrease in the bonds' rating. In August 2008, the bondholders meeting approved the appointment of Clal Trust Finances 2007 Ltd. as trustee to replace the original trustee. The trustee is entitled to participate as an observer in the Company's shareholder meetings. As of December 31, 2011, the balance of the par value of the Series A bonds in circulation is NIS 592 million.

17.6 **Non-Bank Financing for the Group Companies**

17.6.1 Issuance of Series A Bonds of Canit Hashalom

17.6.1.1 On March 29, 2005, Canit Hashalom issued, in a private placement to institutional investors, NIS 500 million par value Series A bonds of Canit Hashalom, non-negotiable, registered, linked (principal and interest) to the consumer price index that was published for the month of April 2005, and bearing effective annual interest at the rate of 4.95%. On July 5, 2009, Canit Hashalom issued an additional NIS 89.5 million par value Series A bonds of Canit Hashalom, whose conditions were identical to the Canit Hashalom Series A bonds. An amount equal to 60% of the sum of the principal and interest of the Canit Hashalom Series A bonds will be paid in four equal annual installments (on September 30, December 31, March 31 and June 30), commencing from September 2005 until June 30, 2015 (inclusive). Payment of the principal balance at the rate of 40% of the principal amount will be made in a single installment on June 30, 2015. The Series A Bonds are rated with a Aa2 rating by Midroog. The Series A Bonds were listed on TASE's TACT institutional system. Within the framework of the indenture, Canit Hashalom undertook that insofar as its shares shall be listed, it will use its best efforts to list the bonds on TASE by and no later than 120 days after the date of the listing of its shares.

To secure its undertakings to the Series A bondholders, Canit Hashalom registered first-ranking fixed charges, unlimited in amount, on various properties of the Group companies, while as of the Date of the Report, the charges are as follows: (a) 16,083,900 ordinary shares without par value of Otzma & Co. Investments Maccabim Ltd. ("**Otzma Investments**"); (b) 53,969,250 ordinary shares without par value of Gemel Tesua Investments Ltd. ("**Gemel Tesua**"); (c) various bonds issued by Gemel Tesua and Otzma Investments as detailed in Sections 17.12.2 and 21.4 of the Report, that are secured by pledging the rights of Gemel Tesua and Otzma Investments in the following properties: all of the rights in Herzliya Business Park; 50% of the rights in Azrieli Mall Hod Hasharon; 40% of the rights in Holon Azrieli Mall; and 50% of the rights in K.M.T. Petach Tikva.

The bonds will be accelerated upon fulfillment of certain conditions, including upon receivership, delinquent payments, the sale of more than 50% of its rights in the "Azrieli Center" complex, if the sum of

NIS 50 million shall not be deposited in the reserved sum account that shall be pledged in favor of the trustee for the bondholders, within 3 months commencing from 2013. As of December 31, 2011, the balance of the par value of Series A bonds in circulation is approx. NIS 395 million.

17.6.1.2 Undertakings and conditions pertaining to the Canit Hashalom Series A Bonds:

a. As from 2013, the payment date of long-term loans that were provided to Canit Hashalom by Bank Leumi Le-Israel Ltd., Bank Leumi Investment Co. Ltd. and Bank Hapoalim Ltd., until the date of payment of the Series A bonds, the sum of NIS 50 million will be kept by the Company in an account that shall be charged in a first-ranking fixed charge in favor of the Series A bondholders.

b. To act in connection with a debt of Canit Hashalom to the Company that exists on the date of the raising of the Series A bonds, and any future debt of Canit Hashalom to the Company and/or any affiliated company, as defined in the Securities Law (the "**Debt**") such that the following conditions shall be fulfilled:

- The balance of the Debt, if any, will be paid, insofar as shall be paid, from Canit Hashalom's current surplus cash, except if the trustee shall have approved otherwise. For this purpose "surplus cash" - EBITDA to be calculated in accordance with GAAP, less payments on account of the bond principal and interest or bank debts and after tax payments (the "**EBITDA Mechanism**").

- In the event of dissolution of Canit Hashalom, the balance of the Debt to affiliated companies will be paid, insofar as shall be paid, only after payment of all of the amounts that are due to the Series A bondholders.

c. Canit Hashalom will be entitled to increase the bond series subject to the fulfillment of the following conditions: (a) after increasing the series, the asset-liability ratio shall exceed 1.35 and the bonds' rating shall not be prejudiced; (b) increasing the series is intended to finance and develop the backup properties.[29] and/or to improve them or to repay a loan that was taken for the purpose of improving the backup properties; (c) the scope of the series does not exceed 80% of the total financing that was used and/or will be used for development of the backup properties, in accordance with an opinion to be obtained on this matter.

17.6.1.3 In the framework of the rating report, Midroog rated the Series A bonds with a Aa2 rating, considering compliance also with the following conditions:

[29] "The Backup Properties" - the properties that were charged to secure the bonds of Gemel Tesua Investments Ltd. and Otzma & Co. Investments Macabim Ltd..

a. The loan from the Company, in an amount no less than NIS 130 million, will be an inferior loan, the date of payment of which, including in respect of principal, interest and linkage, will be after full settlement of the bonds;

b. Canit Hashalom will borrow additional amounts at a preference level identical to all of its debts, whether from the Company or third parties, at scopes that shall not exceed NIS 345 million. In the event that the Company shall transfer the said amounts, the priority level thereof will be equal to all of Canit Hashalom's other debts and repayment thereof will not be subject to the EBITDA Mechanism set forth in the indenture, as detailed above.

c. The rest of the financing in the sum of NIS 235 million will be transferred from the Company as a loan, subject to the EBITDA Mechanism, which amount will be added to the balance of the debt that is subject to the EBITDA Mechanism.

d. The loans will be repaid from the cash flow deriving from disposal of Granite Hacarmel shares (including disposal, refinancing etc.) according to the following order of preference: first, debts that are not subject to the EBITDA Mechanism, thereafter loans that are subject to the EBITDA Mechanism and lastly, inferior loans.

For the avoidance of any doubt, it is clarified that the additional financing that is expected to be received from the Company and/or banking corporations to finance additional projects, which is estimated to be approx. NIS 590 million, if taken, will not be subject to the EBITDA Mechanism.

In June 2011, Midroog announced the approval of an Aa2 rating, outlook stable, after this rating was also approved in August 2010. For details see the Company's immediate report of June 30, 2011 (ref. no.: 2011-01-198078).

17.6.2 Inter-Company Loans

Set forth below is a specification of the balances of loans provided between the Group companies as of December 31, 2011 (NIS in millions) in amounts exceeding NIS 20 million:

The Lending Corporation in the Group	The Borrowing Corporation in the Group	Date of Provision of the Loan	Original Loan Amount (NIS in millions)	Last Date For Payment	Annual Interest	Linkage	Balance Of Loan Amount As Of 31.12.11
Canit Hashalom (1)	Gemel Tesua	January 2009	74	January 2014	---	---	**74**
Canit Hashalom (2)	Gemel Tesua	April 2005	771	June 2015	---	---	**599**
Canit Hashalom (2)	Otzma Investments	April 2005	85	June 2015	---	---	**56**
Canit Hashalom (3)	AG Galleria Office Buildings LP	February 2012	99	Not yet determined	7.1%	U.S. $	**109**

*For a description of the balances of the loans provided by the Company to the Group companies, see Section 11 of Part D of the Report.

(1) Against the loan, Gemel Tesua issued a capital note in the sum of NIS 74 million to Canit Hashalom, bearing neither interest nor linkage, and the date of payment thereof will be no earlier than January 1, 2014, although the parties may agree to postpone the payment date. Payment of the capital note is not secured by any collateral and is inferior to other Gemel Tesua undertakings and precedes only the distribution of surplus assets upon dissolution.

(2) For details on the bonds that were assigned to Canit Hashalom, see Section 21.4 of the Report.

(3) The loan is in the sum of approx. U.S. $28 million.

17.7 Credit Restrictions

17.7.1 The Series A bonds issued by the Company included an undertaking not to distribute dividends to the Company's shareholders if the credit rating may be prejudiced. For further details, see Section 17.5.2 of the Report.

17.7.2 For a description of Canit Hashalom's undertaking in connection with the issue of the Series A bonds vis-à-vis the bondholders and the rating company, see Section 17.6.1 of the Report.

17.7.3 For the purpose of securing sufficient liquidity for payment of the marketable securities, the Company has undertaken to keep an amount of no less than approx. NIS 135 million in a deposit, which may not be offset against a bank loan, at a bank whose short-term rating is P-1 and/or in State of Israel bonds, free and clear of pledges, until the date of payment of the marketable securities.

As of December 31, 2011, and as of the date of publication of the Report, the Company meets all of the restrictions imposed thereon as stated above.

17.8 **Credit Facilities**

As of the Date of the Report, the Group has not been provided with any binding credit facilities or non-binding credit facilities.

17.9 **Bank and Non-Bank Credit Received Between the Date of the Financial Statements as of December 31, 2011 until Close to the Report Publication Date**

Borrower Corporation	Date of Provision of the Loan	Designation of Loan	Type of Loan			Amount of the Credit	Annual Interest Rate	Linkage	Guarantees/ Pledge (NIS in thousands)	Date of Payment of Long-Term Loans
			Banking Corporation / Financial Institution	Short-Term	Long-Term					
AG Plaza At Enclave LLC	January 2012	Acquisition of property in Houston	Foreign financial institution		X	$70 million	3.6% fixed	-	**(1)**	**February 1, 2017**
Azrieli Group Ltd.	January 2012	For current operations	MSs	X		NIS 65 million	Bank of Israel interest + 0.6%		**(2)**	**(2)**

(1) On January 10, 2012, after the date of the Statement of Financial Position, a U.S. corporation indirectly held at the rate of 100% by the Company (in this Section: the "**Buyer**"), engaged with a U.S. financial institution (in this Section: the "**Financer**"), whereby the Financer will provide the Buyer with a loan in the sum of approx. U.S. $70 million, for the purchase of a property in Houston, Texas, the details of whose purchase are described in Section 10.10 of the Report. For further details regarding the property, its financing and the agreement for the purchase thereof, see the Company's reports dated January 1, 2012 and January 11, 2012 (ref. no.: 2012-01-000444 and 2012-01-012534, respectively).

(2) In January 2012, after the date of the Statement of Financial Position, the Company issued an additional sum of NIS 65 million of MSs, after expansion of the rating framework to this MS series from NIS 135 million to NIS 200 million, all as specified in Sections 17.5.1.3 and 17.7.3 above.

17.10 **Loans that were repaid between the date of the Financial Statements as of December 31, 2011 and close to the Report Publication Date:** During the period between the Financial Statements as of December 31, 2011 and the Report Publication Date, short-term loans from banks in the sum of approx. NIS 105 million have been paid, over and above current payments in accordance with the payment schedule of each loan.

17.11 Credit Rating

17.11.1 Rating of the Company's Series A Bonds:

Rating Company	Date of the Rating	The Rating	Comments
Maalot	March 2007	AA	
Maalot	May 2009	AA	The rating is on the monitoring list with negative implications
Maalot	December 2009	AA – outlook stable	The Company was removed from the monitoring list
Maalot	December 2010	AA – outlook positive	
Maalot	**November 2011**	**AA stable**	**Present rating**
Midroog	March 2007	Aa2	
Midroog	August 2010	Aa2 outlook stable	
Midroog	**June 2011**	**Aa2 outlook stable**	**Present rating**

To inspect Maalot's annual monitoring report, see the Company's immediate report of November 23, 2011 (ref. 2011-01-336291). To inspect Midroog's annual monitoring report, see the Company's immediate report of June 30, 2011 (ref. 2011-01-198093). For further details regarding the rating of the Company's bonds, see Section 17.5.2 of the Report.

17.11.2 Rating of the Company's Marketable Securities:

Rating Company	Date of the Rating	The Rating	Comments
Midroog	July 2009	P-1	
Midroog	**June 2011**	**P-1**	**Present rating**. (Valid until June 30, 2012, including approval of this rating in connection with expansion of the series of the marketable securities in January 2012).

For further details regarding the rating of the marketable securities, see Section 17.5.1.3 of the Report. To inspect Midroog's annual monitoring report, see the Company's immediate report of June 30, 2011 (ref.: 2011-01-198045).

17.11.3 Series A Bonds of Canit Hashalom

Rating Company	Date of the Rating	The Rating	Comments
Midroog	June 2005	Aa2	
Midroog	August 2010	Aa2	
Midroog	**June 2011**	**Aa2, outlook stable**	**Present rating**

17.11.4 To inspect Midroog's annual monitoring report, see the Company's immediate report of June 30, 2011 (ref. 2011-01-198078). For further details regarding the rating of Canit Hashalom's bonds, see Section 17.6.1 of the Report.

17.12 **Pledges**

17.12.1 To secure the Group's undertakings to the banking corporations providing credit for the acquisition of the Company's real estate properties, the Company and/or the Group companies pledge, from time to time, in a first-ranking pledge, their rights in the various properties and their rights pursuant to the lease agreements. To secure the current liabilities of the partnerships that hold the properties in the U.S. vis-à-vis the financial institutions that provided the loans for the acquisition of the said properties, the partnerships pledged their rights in the properties in favor of the financial institution that provided the loan.

17.12.2 To secure its undertakings vis-à-vis the Series A bondholders of Canit Hashalom, as detailed in Section 17.6.1 of the Report, on June 29, 2005, Canit Hashalom registered a first-ranking fixed charge, unlimited in amount, and assigned by way of the charge all of its rights in the charged properties, as defined in the indenture. For further details, see Section 17.6.1.1 of this chapter of the Report.

17.12.3 See Section 17.3 above for the Company's undertakings vis-à-vis banking corporations not to create floating charges on their assets.

17.13 **Guarantees**

17.13.1 In the ordinary course of business, at the Company's request, bank guarantees are issued by banking corporations in connection with its properties, including guarantees to secure the undertakings of the Company and the Group companies, and performance guarantees which, as of December 31, 2011, are in the aggregate sum of approx. NIS 63 million.

17.13.2 In June 2009, the Company provided Bank Hapoalim with a guarantee to secure credit, whose balance as of the Date of the Report is approx. £4,133 thousand, which was provided to IC by the bank. In consideration for provision of the guarantee, the Company receives an annual commission at the rate of 0.25% of the total loan as aforesaid.

17.13.3 In December 2009, IC provided Bank Leumi Le-Israel Ltd. with a perpetual guarantee, unlimited in amount, to secure fulfillment of all of its undertakings and settlement of the existing and future debts of Urban to Bank Leumi in connection with all of the amounts that are or shall be or may be due to the bank from Urban. In consideration for provision of the guarantee, IC receives an annual commission at the rate of 0.75% of the sum of the balance of the credit that was provided to Urban, amounting, as of December 31, 2011, to the sum of NIS 10,477 thousand.

17.13.4 In March 2011, the Company provided a permanent guarantee vis-à-vis Mizrahi Tefahot Bank, unlimited in amount, to secure fulfillment of all of the undertakings and payment of the existing and future debts of Canit Northchase LP vis-à-vis Mizrahi Tefahot Bank, in connection with all of the amounts that are or shall be or may be due to the bank from Canit Northchase LP. The balance of the loan, as of December 31, 2011, is U.S. $7,750 thousand.

17.13.5 In February 2011, after the date of the Statement of Financial Position, the Company provided a guarantee to a U.S. financial institution (in this section: the "**Financer**"), which provided financing in the total sum of approx. U.S. $130 million to Three Galleria Office Buildings LLC, a company 90% held by the Company, for the purpose of acquisition of the office towers in Houston, U.S.A. The guarantee is only forfeitable in several specific cases defined in the loan agreement. The Company further undertook to indemnify the Financer for damage caused thereto in the event of certain breaches of the acquiring company's undertakings in the loan agreement.

17.13.6 In January 2010, after the date of the Statement of Financial Position, the Company provided a guarantee to a U.S. financial institution (in this section: the "**Financing Institution**"), which provided financing in the sum total of approx. U.S. $70 million to AG Plaza at Enclave, LLC, a company held at the rate of 100% by the Company, for the purchase of an office building in Houston, U.S.A. The guarantee is forfeitable only in several specific instances defined in the loan agreement. In addition, the Company undertook to indemnify the Financing Entity for its damage, if any, due to environmental issues in the property.

17.13.7 For information regarding additional guarantees and pledges of the Company and the Group companies, see Note 35 to the Financial Statements.

17.14 Credit at Variable Interest

The Group has several loans from banking sources in credit at variable interest. Most of the credit was taken in Shekel currency linked to Prime or Bank of Israel interest, and the remainder in foreign currency linked to the LIBOR, plus a margin determined in relation to each loan. The foregoing credit changes in accordance with changes in the LIBOR interest or the Prime or Bank of Israel interest.

Set forth below is a specification of the range of (nominal) interest for the periods of the Report, as well as the interest rate in proximity to the Report Publication Date in respect of the loans at variable interest:

Type of Credit	Currency	Scope of the Credit in Proximity to the Report Publication Date (NIS in millions)	Interest Rate in Proximity to the Report Publication Date (in %)	Interest Range in the Reported Periods (in %)		
				December 31, 2011	December 31, 2010	December 31, 2009
Bank Credit	NIS	372	3.3%-3.6%	3.55%-3.85%	2.9%	2.3% - 2.8%
Non-Bank Credit	NIS	232	3.1%-3.3%	3.35%-3.55%	2.6%-2.8%	1.6% - 2.5%
Bank Credit	**Pound Sterling**	25	**3.19%**	**3.19%**	**2.475%**	**2.625%**

The Company's management estimates that the Company will not be required to raise resources in addition to the IPO proceeds for the purpose of meeting the IPO targets or covering its current business operations.

17.15 **Regulatory Implications**

The instructions of the Supervisor of Banks in Israel include borrower group limits and "individual borrower" that affect the provision of credit beyond certain scopes, relative to the total liability of one group of borrowers and total liabilities of the six largest borrowers of the bank. Azrieli Group, together with Granite Group, and companies controlled thereby may be considered a one "group of borrowers" for this purpose. However, it should be noted that insofar as is known to the Company's management, as of the Date of Report, a borrower limit does not apply to the Azrieli Group and/or Granite.

18. Taxation

For details regarding the tax applicable to the Company and the Group companies (including Granite Hacarmel), see Note 33 to the Financial Statements.

19. The Environment

In the framework of its activities, the Group is required, *inter alia*, to meet the Ministry of the Environment's conditions and requirements, including in the field of land which may be expressed, *inter alia*, in the framework of approval of zoning plans and building permits, but also during the construction process itself and even thereafter. The Group companies are liable, by virtue of their owning or leasing land, under certain circumstances, pursuant to law, to the provisions of the environmental laws, including pursuant to the Water Law, 5719-1959, the Business Licensing Law, 5728-1968 and the Hazardous Substances Law, 5753-1993, the Planning and Building Law, 5725-1965, including the Planning and Building Regulations (Environmental Impact Surveys), 5763-2003, Abatement of Nuisances Law, 5721-1961, Sewage and Water Corporations Rules (Waste from Plants Discharged into the Sewage System), 5771-2011, Maintenance of Cleanliness Law, 5744-1984, Preservation of the Coastal Environment Law, 5764-2004, and the regulations promulgated thereunder, etc. To the best of the Group's knowledge, these conditions, as of the Date of the Report, had no material ramifications on the Group's business or business results, including its capital investments, profit and its competitive position.

In this context it is noted, that as of the Report Publication Date, several bills are pending which, if passed, will affect the Group's business, including: the Prevention of Soil Pollution and Treatment of Polluted Soil Bill, 5771-2011.

It shall be noted that in recent years, environmental activity, in Israel and worldwide, has significantly increased, as expressed, *inter alia*, in supervision and enforcement by government agencies and activity by environmental organizations. In the Group's estimation, this trend is expected to continue in the coming years. The Group is investing many resources in ensuring its compliance with the provisions of the environmental laws that apply thereto, and is acting to prevent and minimize the environmental risks from its activity.

The Group's policy is to comply with the provisions and requirements of the law, including the environmental laws, as well as the requirements of the various supervisory bodies. For this purpose, professional environmental consultants are assigned to each project of the Group, who assist the Group and advise it throughout the project.

Azrieli Kiryat Ata Mall complex – Due to the fact that in the past, a Tambour plant operated in this complex, the Ministry of the Environment and the Water Authority demanded, *inter alia*, the performance of soil surveys, a soil gas survey, ground-water sampling, as well as performance of protection of the building, or alternatively, performance of a hazard survey. These surveys and samplings were carried out between March-May 2010. Accordingly, the Group carried out the surveys on the soil, which indicated that the soil was polluted in a certain area of the complex, when the treatment of the polluted soil, including removal thereof to an authorized waste disposal site, was completed. On September 15, 2010, a building permit was duly received. It shall be noted that the results of the ground-water sampling that were received were normal. As of the Date of the Report, the Group continues to act in accordance with the Ministry of the Environment's instructions for examination of the condition of the soil, while the Group may take various additional samples in another complex on the same land, in accordance with the demands of the Ministry of the Environment, if any.

Complex at the Check Post intersection in Haifa - In accordance with the information leaflet that was received from the City of Haifa, the lot that is located at the Check Post intersection in Haifa may be affected by hazardous substances, and the Company may be required by the Ministry of the Environment to carry out various tests on the soil in the framework of the planning and building proceedings on the land.

Holon Azrieli Center complex – The Group carried out a soil survey in the complex including soil gas tests and the Company is not required to perform special actions in the complex. The soil survey and the soil gas tests were required due to the location of the land in Holon's heavy industry zone, and due to its proximity to polluting industrial uses, including garages, metal plating, processing and recycling plants, a historical textile factory site, etc., and the presence of contaminated ground-water in this area, which fact has caused the closure of several production drillings. In addition, there are signs at the site itself of illegal construction waste dumping and the presence of soil pollutants cannot be entirely ruled out, although, according to the historical soil survey performed at the site, the likelihood thereof is low.

Azrieli Akko Mall complex – The Group's mall in Akko was built in proximity to the Strauss plant. Due to the proximity to the Strauss plant, in which there are ammonia refrigeration systems, the Group was required, *inter alia*, by the Ministry of the Environment and the Fire Department, to carry out a hazard survey. This survey was submitted in December 2010. In the body of the hazard survey, which was performed by Hazmat, it is stated that the entity which is constructing the mall is handling this hazard and is acting for the minimization thereof by the installation of a PA system, installation of impermeability devices, continuous contact with the Straus plant, retention of security employees and preparation for emergency situations. On September 21, 2011, the Ministry of the Environment filed an appeal against the decision of the Akko local planning and building committee to grant the Akko Mall a certificate of occupancy, while cancelling the need for the Ministry of the Environment's approval, due to the mall's proximity to the Strauss plant, in which there are ammonia refrigeration systems. The Company filed its response to the foregoing appeal and is acting for the dismissal thereof against it. In view of the responses of the respondents to the appeal, including the Company, the committee joined Strauss as a respondent to the appeal. Its shall be noted that on March 2, 2012, an event of an ammonia leakage from the Straus plant had occurred, following which the mall was required to evacuate visitors of the mall to protected areas. The Company has no knowledge of any damage caused as a result of the event. A hearing of the appeal has been scheduled for May 8, 2012.

Sarona Azrieli Center: During the licensing process required for the construction work in the complex, various soil and groundwater tests were required. The Company carried out the tests and forwarded the findings to the authorities and is awaiting receipt of the appropriate

approvals. The Company will be required to perform various actions in accordance with the instructions of the competent entities in connection with the treatment of the soil.

Rental space for cellular - In some of the Group's income-producing properties, the Group leases to the Cellular Companies areas (the "**Leased Premises**") for the purpose of installing and operating cellular antennas and/or small offices (the "**Telecommunications Equipment**"). In accordance with most of the agreements between the Company and/or the Group's management companies and the Cellular Companies, responsibility for obtaining all of the approvals required by law to set up and operate the antennas and/or the offices, and responsibility for complying with the various environmental protection laws lies with the Cellular Companies, including holding, so long as they lease the Leased Premises, the approval of the Radiation Commissioner at the Ministry of the Environment regarding instructions and restrictions relating to the use of the telecommunication equipment, and acting in accordance with this approval, and they also undertake to comply with the safety instructions that shall be published by the Company or the management companies. Additionally, in the framework of these agreements, the Cellular Companies undertake to indemnify and compensate the Company and/or the management companies for any damage and/or expense that shall be caused as a result of the Cellular Companies' activities on the premises, and for their liability by law for any act or omission of the Cellular Companies, and they undertake to insure their liability under the law for any damage and/or harm that may be caused to a third party. Finally, pursuant to the provisions of most of the agreements as stated above, all of the Cellular Companies undertake to cooperate with the other Cellular Companies with which the Company has engaged, with respect to the operation of the telecommunications equipment in the Leased Premises.

Treatment of Waste water from Businesses in Azrieli Holon Mall and in Azrieli Tel Aviv Mall – On June 23, 2011 and September 5, 2011, warnings prior to the institution of legal proceedings pursuant to the Abatement of Environmental Nuisances Law (Civil Claims), 5752-1992 were sent to the Company on behalf of Malraz, claiming that according to reports on an industrial waste audit which was performed by the environmental unit of Dan Metropolitan Conurbation and carried out at the Company's malls in Holon and in Tel Aviv, deviations were found in the values of the waste discharged into the municipal sewage system. The Company responded to Malraz that the Company has no knowledge of the alleged existence of the nuisances mentioned in the letter, and that the Company places great importance on environmental issues and uses a professional consultant for this purpose.

For further details regarding the environment in Granite Hacarmel's operating segment, see Sections 11.34, 11.48 and 11.69 of the Report.

20. Restrictions and Monitoring the Corporation

Below is a brief overview of the laws, regulations, orders, restrictions and requirements with which the Group is obligated to comply in its various operating segments:

20.1 In Israel

20.1.1 Planning and Building Procedures

The Planning and Building Law, 5725-1965 (the "**Planning and Building Law**") prohibits construction without obtaining a building permit, and states that building without a permit or deviating from a permit constitutes a criminal offense pursuant to Sections 203-255 of the Planning and Building Law. For the purpose of construction of the various projects, the Company engages with architects and consultants, whose role is to prepare the requisite plans and to handle the approval thereof by the planning authorities, from modification of the zoning plan, if necessary, issuance of the building permits and preparation of the work plans required for the purpose of performance of the construction.

20.1.2 Israel Land Administration and Local Authorities

Approx. 90% of the land in Israel is owned by the Israeli government through the ILA, and therefore a large portion of the land on which the Group operates is leased from the ILA in a long-term lease. In addition, some of the land owned by the Group is leased directly from the local authorities in the areas in which the property is located. Hence, the rights in the land and the transactions in connection therewith are subject to the provisions of the contracts and the instructions in connection with a change of designation and utilization of the rights in the land, while any change of rights by virtue of the lease agreements, including extension of the lease periods, will be made in accordance with the provisions of the lease agreements and conditions that are acceptable to the ILA and the local authorities at that time. Thus, the Group may, in the framework of the lease agreements, bear various payments to the ILA such as permit fees, consent fees, lease fees and capitalization fees.

20.1.3 Land Taxes

In the framework of its business, the Group enters into transactions to acquire or sell land, and therefore it may bear various liabilities in accordance with the provisions of the Land Taxation Law (Appreciation, Sale and Purchase), 5723-1963, and the regulations promulgated thereunder.

20.1.4 The Land Law

With respect to rights in the land, registration thereof and joining third parties therein, the Group is subject to the provisions of the Land Law, 5729-1969, and the regulations promulgated thereunder.

20.1.5 The Lease and Loan Law

With respect to the income-producing properties that are leased by the Group to various tenants, the Group is subject to the Lease and Loan Law, 5731-1971.

20.1.6 General rules concerning the Group's operating segments

In the framework of its activities, the Company and the Group companies are subject to municipal bylaws in each one of the local authorities in which the Group's income-producing properties are located, insofar as relevant, including regarding the opening and closing of businesses. In addition, the Group is subject to the Prevention of Smoking and Exposure to Smoking in Public Places Law, 5743-1983.

Additionally, some of the Group companies purchase electricity from the IEC at high voltage according to the IEC's tariff for the purchase of high voltage electricity, and supplies the electricity to tenants according to the IEC's low voltage tariff. To the best of the Company's knowledge, as of the Date of the Report, the Ministry of National Infrastructures and the Public Utilities Authority are acting to regulate the licensing of electricity distribution in the commercial centers and malls throughout the country.

20.1.7 Business Licensing

In the framework of the Group companies' activities, some of the Group companies are required to obtain a business license pursuant to the Business Licensing Law, 5728-1968. In addition, in the lease agreements in which the Group engages with the various lessees, the lessee is required to hold a lawful business license for the operation of its business in the property. To the best of the Company's knowledge, as of the Date of the Report, all of the Group's buildings have the permits and licenses required pursuant to this law, except as specified below:

Azrieli Ayalon Mall – the mall has a temporary business license, valid until June 30, 2012. The Group acts in full cooperation with the relevant authorities for fulfillment of the conditions required to receive a business license.

Azrieli Haifa Mall – the mall has a temporary permit, valid until March 30, 2012. As of the Report Publication Date, the Group is acting to receive a permanent business license.

Azrieli Akko Mall – As of the Report Publication Date, the Company has received all of the approvals required for receipt of a business license in this property, with the exception of the approval of the Ministry of the Environment and the Ministry of Health, and is awaiting the results of the appeal, as specified in Section 19 above.

20.1.8 Antitrust

In the framework of expansion of the Group's activities, *inter alia*, by acquiring shares in companies that are companies owning the rights in real properties, the Company and the Group companies are required, under certain circumstances, to approve the merger pursuant to the Restrictive Trade Practices Law, 5748-1988.

On February 22, 2009, the Antitrust Authority approved the merger in connection with the acquisition of the Givatayim Mall, and on January 27, 2010, the Antitrust Authority approved the merger in connection with the acquisition of the Haifa Mall.

On January 8, 2012, the Company withdrew the merger application it had filed with the Antitrust Authority for approval of the acquisition of the "Ir Yamim" Mall in Netanya, in view of the Company's not consenting to the conditions presented by the Antitrust Authority for approval of the transaction. In accordance with the aforesaid, the closing condition for the acquisition of the "Ir Yamim" Mall was not fulfilled.

20.2 **Outside Israel**

The Group's activities in the USA and in England are subject to the laws and regulations in the said countries and *inter alia* in the field of land, planning and building and lease, the environment and laws on the municipal level and in connection with land taxation.

For further details regarding restrictions and monitoring of Granite Hacarmel's operating segment, see Section 11.17 of the Report.

21. **Material Agreements and Collaboration Agreements**

The Group is a party to collaboration agreements with third parties with respect to some of the projects within the Group's activities.

Below are details concerning the agreements to which the Company or any of the Group companies are a party and which are not in the ordinary course of the Group's business, and may be deemed material agreements as well as strategic collaboration agreements, that are not specified in this chapter above:

21.1 **Exemption and Indemnification for Directors and Officers**

The officers in the Company are insured in D&O insurance in the framework of the Company's insurance policies, and were granted letters of indemnification and exemption, all as detailed in Section 29A of Chapter D of the Report.

21.2 **Agreement with the Company's Controlling Shareholder**

For details regarding the Company's engagement in a management agreement with a management company in connection with services it will provide, as of the Date of the Report, through Mr. David Azrieli, see Section 22 of Chapter D of the Report.

21.3 **Issue of Bonds of the Company and the Group Companies**

For details regarding the issue of the Company's Series A bonds and the issue of Canit Hashalom's Series A bonds, see Sections 17.5.2 and 17.6.1 of the Report.

21.4 **Share Allotment Agreement and Assignment of Bonds**

On January 23, 2005, IC, Canit Hashalom, Otzma Investments, Gemel Tesua and Canit Developments Inc. (all jointly referred to below as the "**Azrieli Group**") engaged with Leumi Gemel Ltd. ("**Leumi Gemel**") in an agreement whereby Leumi Gemel assigned to Canit Hashalom all of its rights and obligations pursuant to the bonds issued thereto by Otzma Investments and Gemel Tesua in consideration for the sum of NIS 630 million, reflecting the discounted bond purchase amount (the "**Agreement**"). As of December 31, 2011, the balance of the bonds of Otzma Investments and Gemel Tesua vis-à-vis Canit Hashalom is in the sum of approx. NIS 655 million.

In the framework of the Agreement, the Azrieli Group and each one of the companies therein and/or any entity that shall replace them or in lieu of any of them, undertook to indemnify Leumi Gemel for any damage, loss, expense or liability caused thereto or to the provident funds due to any claim and/or demand and/or lawsuit filed against it in connection with Otzma Investments and Gemel Tesua's activities or in connection with the holding of their shares. The said indemnification does not apply in connection with its engagement with Leumi Gemel in the agreement and in connection with a claim by a member of the provident funds that was filed in his capacity as such.

For further details regarding material agreements and collaboration agreements in relation to Granite Hacarmel's operating segment, see Sections 11.18, 11.50, 11.71 and 11.75 of the Report.

21.5 **An agreement between Canit Hashalom and the City of Holon in connection with the construction of the Holon Azrieli Center**

For details see Section 7.8 above and Note 34B(3) of the financial statements in Chapter C of this Report.

22. Legal Proceedings

As of the Date of the Report, the Company and/or the Group companies are not a party to pending material legal proceedings, except as specified in this Report and in Note 36 to the Company's Financial Statements attached to this Report. In addition, as of the date of this Report, the Company and/or the Group companies are conducting various proceedings, as determined by law, *inter alia*, for the resolution of demands received from the various local authorities in respect of mandatory payments and levies, in a total amount that is immaterial to the Company, and in respect of which no provisions have been made in the Company's financial statements due to the low probability thereof, in the opinion of the Company's outside advisors, under the circumstances. For further details concerning legal proceedings in Granite Hacarmel's operating segment, see Section 11.76 of the Report.

23. Goals and Business Strategy

As a leading company in its operating segments, the Company focuses on real estate investments. The Group's business strategy is primarily to continue to expand its extensive activity in the segments of commercial centers and malls and office and other rental space in Israel and overseas. The Company intends to continue to act for the expansion of its business, as aforesaid, by acquiring land for the development and construction of properties and/or acquiring additional properties and/or improving existing properties, while exploring business opportunities on a current basis and preserving high financial strength and a relatively low leverage level:

The Company estimates that expansion of the Group's extensive business in the commercial income-producing real estate in Israel sector will be, *inter alia*, through completing projects that are in the planning and building phase, and through the purchase of land, the development and construction of malls and commercial centers and office buildings and know-how-intensive industrial parks throughout the State of Israel, while considering areas in demand, large population centers, primary traffic intersections and good accessibility to public transport.

The Company focuses, on a current basis, on improving the Group's existing properties, and acts to optimize the utilization of its commercial space and create a suitable and contemporary

tenant mix, while continuing to offer management services to its properties through the Group's management teams, maintaining the level of its tenants and renewing the lease agreements therewith for additional long-term periods.

The Group constantly acts to increase the number of visitors while maintaining and even improving the attractiveness of its malls and commercial centers and increasing the tenants' revenues.

For details concerning Granite Hacarmel's strategy and goals, see Section 11.79 of the Report.

Additionally, the Company from time to time investigates business opportunities in Israel and overseas in connection with the real estate sector. In the Company's estimation, in its acquisitions of leading, cash-generating target companies in its operating segments and in other segments, the Company takes advantage of its financial strength while leveraging the market conditions and/or crisis conditions. The Company's objectives as of the Report Publication Date are based on the management's estimates in connection with the market conditions as of such date, and there is no certainty that the aforesaid will indeed materialize. For further details, see the Board of Directors' Report in Chapter B of this Report.

24. Forecast for Development

As the Company reported in the past, during the Report Period until the Report Publication Date, the Group has continued exploring business opportunities, in Israel and overseas, in connection with the expansion of its business, in Israel and overseas, mainly in the real estate segment, including through the acquisition of land reserves, the acquisition of additional properties and the improvement of existing properties, some of which have materialized as stated in the Company's reports. In addition, the Company may, from time to time, look into further possibilities for expanding its operating segments, while taking advantage of market conditions and/or crisis conditions in leading, cash-generating target companies in other segments. As of the Date of the Report, the Company is holding initial contacts only with several entities, there being no certainty that they will develop into negotiations. The Company shall report in the future insofar as developments shall occur which mandate a report by law.

25. Discussion of Risk Factors

In the Company's estimation, the Group is exposed to several fundamental risk factors deriving from the economic environment and the Group's unique characteristics. For further details regarding the risk factors deriving from the economic environment and the unique characteristics in Granite's operating segment, see Section 11.79 of the Report.

It shall be clarified that the information concerning risk factors to which the Group is exposed is forward-looking information. The Company's expectations with respect to this issue are based on past experience, the Group's familiarity with the markets in which it is active and its estimations in relation to its economic and business development. However, the Group's expectations and forecasts may not be realized, *inter alia* due to dependence on external factors that are beyond the Group's control and which are detailed below:

25.1 Macro Economic and Financial Risks

25.1.1 The condition of the Israeli economy - The Company's business is dependent, *inter alia*, on the condition of the Israeli economy. A severe economic slowdown in the market may cause a reduction in the Company's business due to a reduction in the demand for rental space, and a slowing down of the pace of development and construction due to a decline in available resources in the

market and in demand. Deterioration of the condition of the economy in Israel may have a significant effect on the tenants in the Group's properties and their ability to meet their financial commitments to the Group. The Israeli economy may also be affected by a moderate prolonging of the global economic crisis, which may cause a slowdown in global financial activity and affect the condition of the capital market in Israel and overseas. The prolonged crisis may affect the Group's operating segments, its results of operations and its financial ability.

25.1.2 The security situation in Israel - Changes in and the worsening of the security situation and the political situation may affect the Company's business and harm its business results, both from the perspective of the willingness of visitors to visit the Group's commercial centers and malls and from the perspective of the demand for rental space, a shortage in manpower in the construction industry, an increase in construction costs etc.

25.1.3 A change in the building inputs index - An increase in the building inputs may affect the price of the Company's engagement with sub-contractors. While construction costs are usually linked to the building inputs index, income is usually linked to the consumer price index. Therefore, the Company may be exposed to negative effects in the event of changes in these indexes.

25.1.4 Changes in the economy's interest rates - Changes in the economy's interest rates and the banking corporations' conditions for provision of bank credit may affect the Group's financing costs in relation to each project, the yield from the properties, the value of the income-producing properties and the Group's profitability.

25.1.5 Regulatory changes in the Company's business environment – The Group's business is exposed to various regulatory restrictions, including in accordance with the antitrust laws, securities laws, the companies laws and the supervision of banks laws. The toughening of the regulation in the sectors relating to the Company, as well as possible repercussions of additional regulatory changes and legislation as a result of the conclusions of the Committee for Increasing Competitiveness in the Economy and the Committee for Socioeconomic Change (the Trajtenberg Committee), if any, may reduce and/or limit the Company's business, *inter alia* through organizational changes and the imposition of conditions on the Company's business activity and on its financial holdings.

25.1.6 Changes in the value of financial investments available for sale – In view of the condition of the capital market in Israel, the Company is exposed, to a certain extent, to adverse changes in the value of the companies in which it has invested as a financial asset available for sale. Impairment of these companies may adversely affect the value of negotiable investments which affect the comprehensive income of the Company and its equity.

25.1.7 The condition of the U.S. market – The Group's business in the U.S. is dependent, *inter alia*, on the condition of the U.S. market and the U.S. real estate market in particular. A slowdown in the U.S. real estate market may cause a decline in demand for rental space in its properties and a decline in revenues therein.

25.2 **Industrial Risks**

25.2.1 A decline in the demand for rental space – A decline in the demand for rental space and/or renewal of existing lease agreements may lead to a decline in occupancy rates in the Group's properties and a decline in income from rent and will necessarily harm the Company's business results.

25.2.2 A decline in the rent prices – A decline in the demand for rental space together with competition becoming fiercer in the industry may lead to erosion of the Company's rent and harm its financial results.

25.2.3 Strength of main tenants – Damage to the financial strength of tenants, and particularly main tenants, may lead to an increase in provisions for doubtful debts or alternatively, termination of lease agreements and/or eviction of tenants from the Group's properties, and therefore to a decrease in the Group's income from rent and necessarily harm the Company's business results.

25.2.4 Competition - The income-producing commercial property segment in Israel is subject to significant competition. For details regarding the effect of the Group's competitors on its business results, see Sections 8.3 and 9.3 of the Report.

25.2.5 Approvals from the authorities – Activity in the income-producing property segment is characterized by the need to obtain permits from various entities at the different authorities, particularly in the area of usage and rights confirmations (zoning plans), obtaining building permits, business licenses etc.. A delay in obtaining any permit or failure to obtain a permit could harm the profitability of the project or entail various financial expenses for the purpose of compliance with the requirements of the authorities for receipt of the approvals.

25.2.6 Legal and regulatory requirements, including with respect to environmental protection – the Group companies are subject to legal and regulatory requirements from various aspects and, *inter alia* on issues pertaining to the environment (nuisance, underground and above ground pollution, toxic waste etc.), and they are required to bear the costs involved in meeting the same, such that it may have an adverse effect on their results. These requirements could increase and multiply, which may force the Group to allocate additional financial resources to this issue.

25.3 **Unique Risks**

25.3.1 Fluctuations in the Consumer Price Index - The Group has loans and bonds that are linked to the Consumer Price Index and therefore the Group is exposed to fluctuations in the Consumer Price Index. However, most of the Group's revenues from rent in the commercial centers and malls segment and the office and other rental space segment are linked to the Consumer Price Index, while a rise in the Consumer Price Index may lead to an increase in the revenue from rent and reduce the exposure in relation to this risk.

25.3.2 Foreign Currency Risks - The Company has assets and liabilities that are stated in various foreign currencies. In view of the fact that the total foreign currency liabilities are not always equal in value to the total foreign currency assets, the Company is exposed to possible changes in the exchange rate of the foreign

currencies. As a result thereof, there is exposure to possible changes in the exchange rate of the foreign currency versus the NIS.

25.3.3 Dependency on Financing Sources - The Company's activity is also financed by external sources and an adverse change in the conditions for provision of credit and/or renewal of existing credit may materially harm the Company's results.

25.3.4 Variable interest - The Company has credit from banking and non-banking corporations bearing interest at variable rates. Changes in the variable interest rate and the interest margins in Israel may affect the Group's business results, the scope of the Company's financing expenses and the feasibility of investing in certain projects.

The aforesaid notwithstanding, it is noted that the Group's business is characterized by a large number of tenants, in multiple sectors, dispersed geographically. These characteristics allow the Group to minimize its exposure to changes in a certain operating segment and to minimize its exposure in relation to a specific tenant's business.

Set forth below are the main risk factors described above that were ranked, in accordance with the Company's estimate, according to the extent of the effect that they may have on the Company's business:

	The Extent of the Effect the Risk Factors may have on the Company		
	Large Effect	**Medium Effect**	**Small Effect**
Macro Economic Risks			
Economic situation In Israel	X		
Political Situation in Israel	X		
Changes in the interest rates in the economy		X	
Index Changes in the Building Index			X
Regulatory changes		X	
Changes in the value of available for sale financial investments			X
Condition of the U.S. market			X
Industrial Risks			
Decline in the demand for rental space	X		
Decline in rent prices	X		
Strength of main tenants			X
Competition	X		
Approvals from authorities			X
Environment and regulatory requirements		X	
Unique Risks			
Fluctuations in the Consumer Price Index			X
Foreign Currency Risks			X
Dependency on Financing Sources		X	
Variable Interest			X

CHAPTER B

Report of the Board of Directors

December 31, 2011

Azrieli Group Ltd.

Board of Directors' Report on the State of the Company's Affairs for the year ended December 31, 2011

The board of directors of Azrieli Group Ltd. hereby respectfully submits the board of directors' report for the year ended December 31, 2011 and for a period of three months ended on December 31, 2011 (hereinafter respectively: the "**Report Period**" and "**Q4/2011**"), pursuant to the Securities Regulations (Periodic and Immediate Reports), 5730-1970 (the "**Regulations**").

Azrieli Group Ltd. (the "**Company**"; the Company together with all of the corporations held by it, directly and/or indirectly, will be referred to below as the "**Group**" or "**Azrieli Group**"), engages both itself and through companies held by it, mainly in the income-producing property segment in Israel, while most of the Group's business activity is in the commercial centers and malls segment in Israel and in the office and other space for lease segment in Israel. In addition, the Company has income-producing properties abroad, and mainly lease space for offices in Houston Texas, USA. Also, the Company engages, through its holding in Granite HaCarmel Investments Ltd. ("**Granite**") in another business segment, which includes the energy, paint and building-finishing, water and environmental quality segments. The Company also holds minor holdings in financial corporations.

The Company belongs, as aforesaid, to the Azrieli Group and its business has developed, *inter alia*, on the basis of the extensive knowledge and experience that it has accumulated for many years in the income-producing property industry in Israel, while using the experience and expertise of the controlling shareholder, Mr. David Azrieli, who founded and established the Company from the beginning of its activity.

The data appearing in the board report are based on the consolidated financial statements as of December 31, 2011. The financial data and the business results of the Company are affected by financial data and business results of the companies held thereby. In some cases, details are presented which review events that occurred after the date of the financial statements and in proximity to the date of releasing the Report, with such fact indicated alongside them (the "Report Release Date") or additional details and data on the Company level only. The materiality of the information included in this Report was examined from the Company's point of view. In some of the cases additional detailed description was provided in order to give a comprehensive picture of the described topic, which is, in the Company's view, material for the purpose of this Report.

In light of the expansion in the Group's business in the USA in 2011, commencing from the financial statements as of December 31, 2011, the income-producing property business of the Company outside Israel (including adjustment of comparison numbers) will be presented in a sector separately reportable, which includes a number of office properties as well as one commercial center. For details see also note 41 of the consolidated financial statements as of December 31, 2011 and in Chapter A of the periodic report. Therefore, commencing from the financial statements of the Company as of December 31, 2011, the business segments of the Group reported as reportable business segments in the Company's financial statements are the commercial centers and malls sector in Israel, the office and other lease space sector in Israel and the income-producing property sector in the USA and the Granite Sector.

The financial statements attached are prepared according to the International Financial Reporting Standards (IFRS). For further details see Note 2 to the financial statements as of December 31, 2011.

The Company's management acknowledges the importance of transparency to the investors, the shareholders, the bond holders and analysts and sees all of these as its partners. Therefore, the Company had decided to adopt a policy according to which in the Company's board of directors' report disclosure shall be made regarding a summary of extended separate financial statements – i.e. – a summary of the Company's statements presented according to the IFRS standards, except for the Company's investment in Granite which is presented on the basis of the book value instead of the consolidation of its statements with the Company's statements (the other investments are presented with no change from the statement presented according to the IFRS standards). The Company's management believes that this Report adds a lot of information which helps in understanding the large contribution of the real estate activity to the total profit of the Company, while neutralizing material sections of the consolidated financial statements, deriving from the consolidation of Granite, such as clients, inventory, sales and more. The expanded stand alone statement is attached hereto as Annex E.

This report is not audited or reviewed by the Company's auditors.

Main emphases for the Report Period ended on December 31, 2011 (*)

Net Profit for 2011, net of unusual effects	• The profit for 2011 increased by 14% compared with the profit in 2010. For further details see Section 1.10 of the Report.
Approx. 11% additional growth in the NOI figures during the Report Period and approx. 14% increase in revenues from real estate	• Approx. NIS 982 million this year compared with a sum total of approx. NIS 882 million in 2010. Growth deriving mainly from an increase in the revenues from rental fees and from the purchase and construction of new properties. On the increase in revenues, see the Extended Standalone Statement, Annex E to this Report.
Approx. 5% growth in the Same Property NOI figures, in the malls and commercial centers in Israel segment	• In 2011 the same property NOI in the **Malls and Commercial Centers in Israel segment** totaled at approx. NIS 612 million compared with approx. NIS 584 million in the same period last year.
Approx. 10% growth in the same property NOI figures in the office and other space for lease in Israel segment	• In 2011 the same property NOI **in the Office and Other Space for Lease in Israel segment** totaled at approx. NIS 272 million compared with approx. NIS 247 million in the same period last year.
(Average) Occupancy rate remained very high	• Occupancy rate in the income-producing properties in Israel owned by the Group as of December 31, 2011 stands at close to 100%.
Value of Investment Property	• Contribution in the amount of approx. NIS 696 million to the profit after tax due to an increase in fair value of investment property during 2011 after update of the investment properties according to an independent appraiser's valuations as of December 31, 2011.
Approx. 12% growth in the FFO figures attributed to the income-producing property business	• The FFO for 2011 totaled approx. NIS 668 million compared with NIS 596 million last year. For details see Section 1.1.7.
Approx. 10.8% FFO yield attributed to income-producing property business	• Compared with the Company's value on TASE shortly before the release of this report (March 15, 2012). For calculation see Section 1.1.7.
Approx. 7.8% weighted cap rate deriving from the income-producing properties	• In the financial statements as of December 31, 2011. For calculation see Section 1.1.6.
Approx. 15% additional growth in the NOI figures during Q4/2011	• From a sum of approx. NIS 225 million during the same period last year to an amount of approx. NIS 258 million. Growth deriving mainly from growth in revenues from rental fees and the purchase and

	construction of new properties.
Effect of the decision to cancel the corporate tax rate reduction	• In the report period and in Q4/2011, one-time tax expenses were recorded in the sum of approx. NIS 601 million and carried to the income statement, plus another ~NIS 7 million carried to comprehensive income.
Impairment in the value of the holdings of Bank Leumi and Leumi Card shares	• In the report period, an impairment was recorded in the holdings value, which deducted approx. NIS 439 million from the comprehensive income (approx. NIS 83 million in Q4/2011).
Purchase of office buildings in Houston Texas, USA	• In February 2011 the Company increased the real estate holdings in the USA and purchased 90% of three office buildings with an overall area of approx. 99 thousand sqm. For details see Section 1.1.1.
Opening of the Azrieli Akko Mall and the Azrieli Kiryat Ata Mall in 2011	• During Q3/2011 the construction of both malls was completed. For details see Section 1.1.1.
Continued business initiation and development	• Significant progress in development of the projects under planning and construction. • In 2011 a plot of land was purchased which is designed for construction of the Azrieli Sarona center in Tel Aviv, as well as land for the construction of the Azrieli Ramla mall. For details regarding the projects under construction see Section 1.1.3.

(*) In the above emphases the Company included the main principles of this Report below. In the matter of forward looking information, and including in connection with the progress in the projects under construction, see Sections 1.1.1, 1.1.2 and 1.1.3 below.

1. Explanations of the board for the corporation's state of affairs

1.1 General

1.1.1 Main developments during the Report Period

The opening to the public of two new malls in Kiryat Atta and in Akko

In the beginning of the Q3/2011, the Group opened to the public the "Akko Azrieli Mall" at an overall marketing area of approx. 12,640 sqm and the "Kiryat Atta Azrieli Mall" at an overall marketing area of approx. 9,180 sqm. As of the date of release of the report, the occupancy rate at the Akko Azrieli Mall stands at approx. 98% and at Kiryat Atta Azrieli Mall at approx. 94%.

Transactions in respect of investment property

Azrieli Sarona, Tel Aviv:

On May 30,. 2011, the Company won a tender on behalf of the Israel Land Administration, for the purchase of the lease rights in a lot at an area of approx. 9.4 Dunam at the Southern Kirya, Tel Aviv (the "**Lot**"). The Lot is designated for building an office and commerce project at a scope of approx. 125 thousand sqm above-ground built area (gross) as well as approx. 61 thousand sqm underground floors. In consideration for leasing the Lot, the Company paid the Israel Land Administration an amount of NIS5 22 million (not including VAT) and approx. NIS 39 million development expenses. For further details see Section 7.8 of Chapter A of this Report.

Azrieli Ramla Mall

In May 2011, Otzem Initiation and Investments 1991 Ltd. completed the acquisition of the rights in a lot of an area of approx. 31,650 sqm in Ramla designated for the construction of a commercial center, in consideration for an amount of approx. NIS 100 million, and commenced the construction activity of Ramla Azrieli Mall. For further details see Section 7.8 of Chapter A of this Report.

Acquisition of office towers in Houston, Texas, U.S.A.

On February 4, 2011, Three Galleria Office Buildings, LLC, a U.S. company indirectly held by the Company at a rate of 90%, consummated the acquisition of three office towers in Houston, U.S.A, of a total area of approx. 99,000 sqm (1,065,789 sqf) in consideration for the total sum of U.S. $176 million. For further details see Section 10.9 of Chapter A of this Report.

Senior Management

Appointment of Mr. Menachem Einan as Active Deputy Chairman of the Board

On January 16, 2011, the Company's board of directors approved, after the approval and recommendation of the Company's audit committee, that Mr. Menachem Einan, CEO of the Company, be promoted and appointed as active deputy chairman of the Company's board *in lieu* of his position as the Company's CEO. In his said position, Mr. Einan will be deemed as one of the two deputy chairmen of the board who the board of directors is entitled to elect, as stated in the Company's articles, in addition to Ms. Danna Azrieli, who has been acting as of the date of this Report, as active deputy to the chairman of the board since June 2010. Mr. Einan will be responsible, in his new role, for the strategic areas related to the continued business development of the Group and realization of its long-term vision.

The appointment took effect on April 1, 2011. in accordance with the management agreement signed between the Company and Mr. Einan dated March 1, 2010, the terms and conditions of the management agreement with Mr. Einan remained unmodified, and all as specified in Section 21 of Chapter D of the Periodic Report as of December 31, 2011. For further details on the appointment of Mr. Einan, see immediate report of the Company dated January 16, 2011, ref. no. 2011-01-018351, which is included herein by way of reference as well as note 5 of the financial statement as of December 31, 2011.

Appointment of the Company's CEO and approving the terms and conditions of his office

On January 16, 2011, the Company's board of directors approved, after approval and recommendation of the Company's audit committee, the appointment of Mr. Shlomo Sherf to the position of CEO, commencing from April 1, 2011 and the terms and conditions of the engagement with him. For details on the management agreement that was signed with Mr. Sherf and the terms of his employment, see Section 21 of Chapter D of the Periodic Report as of December 31, 2011, an immediate report of the Company as of January 16, 2011, ref. no. 2011-01-018405, which is included herein by way of reference as well as Note 40C (7) of the financial statement as of December 31, 2011.

Current Operations

The Company has been consistently operating in recent years for the creation of growth engines additional to those existing in the Group in the core business, in order for them to constitute potential for significant future growth of the NOI of the Group – both through the purchase of land for initiation and development of new properties in the future as well as through the purchase of existing properties with growth potential. As the Company had reported in the past, during the

Report Period and until the date of release thereof, the Group has continued to review business opportunities in Israel and abroad, regarding the expansion of its activity especially in the real estate segment, including through acquisition of land reserves, acquisition of additional properties and betterment of the existing ones, some of which have been realized as stated in the Company's reports. In addition, the Company may review, from time to time, additional options for expanding its fields of business while utilizing market situations and/or crisis situations in leading and cash flow generating target companies in other segments.

As of the date of the Report, the Company is conducting with several entities in Israel and overseas initial contacts only, with regard to which there is no certainty that they shall mature to negotiations. The Company shall report in the future, to the extent that there shall be developments which shall require reporting according to law.

1.1.2 Main Developments after the date of the report on the financial condition:

Investment Properties Transactions

Acquisition of an office building in Houston Texas, USA

On January 10, 2012, after the date of the report on the financial condition, AG Plaza at Enclave, LLC, an American corporation indirectly held by the Company at a rate of 100%, completed the acquisition of an office building at an overall area of approx. 31,986 sqm (344,296 sqf) and at a 100% occupancy rate, in Houston Texas, USA, in consideration for a total amount of approx. US $107.5 million (in addition to transaction costs at a total of approx. US $750 thousand). For further detail see Section 10. 10 of Chapter A of this Report.

The non fulfillment of a condition precedent in agreements for the acquisition of the rights at the "Ir Yamim" Mall

On August 15, 2011 and on September 11, 2011, the Company engaged in contingent sale agreements for the purchase of the full rights in the "Ir Yamim" mall in Netanya (the "**Mall**") The agreements stipulated conditions precedent, including the obtaining of the Antitrust Commissioner's approval. On January 8, 2012, the Company withdrew the merger application it had submitted to the Antitrust Authority for approval of the acquisition of the Mall in light of the disagreement of the Company with the terms presented by the Antitrust Authority for approval of the acquisition thereof. Accordingly, the condition precedent for closing of the transactions of the acquisition of the Mall was not fulfilled.

1.1.3 **Update of Properties under Initiation and Development**

During the Report Period the Group continued to invest in the development and construction of new properties as well as in the expansion and renovation of existing properties. The overall investments of the Company during the Report Period stood at approx. NIS 360 million. Thus, the Company also continued to pro-actively manage its existing properties, the improvement thereof, maintaining the high occupancy rate unique to the Group and strengthening the cash flow generated from such properties.

As of the date of this Report, the Company operates towards the development of several properties under construction, as specified below. For further details regarding the development of the properties under construction, see Section 7.8 of Chapter A of this Report.

Set forth below is a summary of the data regarding properties under construction and expansions

Name of property	Location	Date of purchase	Usage	Rate of holding	Area of land (in sqm)	Sqm for marketing	Date of commencement of construction	Estimated date of completion	Cost of land and construction as of Dec. 31, 2011 (NIS in millions)	Estimated cost of completion of construction and (NIS in millions)
Sarona Azrieli Center	Tel Aviv	May 2011	Commerce and Offices	100%	9,400	125,000	Not determined yet. As of the date of release a building permit had been received for basements subject to the fulfillment of preliminary conditions.	2016	589	900-950
Azrieli Kiryat Ata (Phase B)	Kiryat Ata	Jan. 2009	Commerce and Offices	100%	2,700	4,000	May 2011	Q1/2013	6	45-55
Azrieli Rishonim	Rishon Lezion	Aug. 2008	Commerce and Offices	100%	19,000	48,000	December 2011 (permit for construction of temporary parking)	December 2014 (*)	83	415-445
Azrieli Center Holon (**)	Holon	Jun. 2008	Commerce Offices	83%	34,000	5,000 115,000	Phase A (***) – 2010 Phase B (***) – not yet determined	Phase A – 2013 Phase B – by 2016	112	500-535

Azrieli Ayalon Mall – additional floor	Ramat Gan	Aug. 1982	Commerce	100%	----	9,500(1)	Not yet determined	18 months from date of commencement of construction[1]	5	120-150
Ramla Azrieli Mall	Ramla	May 2011	Commerce	100%	31,650	22,000	Aug. 2011	2014	110	210-230
Total						328,500			905	2,190-2,365

(*) Contingent to approval of the city zoning plan.

(**) The figures are for 100%

(***) Phase A – construction of 62,500 sqm of above-ground areas and underground parking lots in an area of 81,000 sqm. Phase B – construction of the remaining of the areas (at least 80% of the building rights according to the city zoning plan).

[1] As of the date of the report, a decision had been made to commence the planning proceedings of an additional floor and a decision had not been made yet regarding the scope of the Project.

1.1.4 The NOI (Net Operating Income) index

The NOI figure is one of the important parameters in the valuation of income-producing property companies. The indication for determination of the value of income-producing property (over and above other indications such as: market value of similar properties in the same area, sale prices of similar properties in recent transactions that were performed etc.) is division of this figure by the accepted cap rate determined according to the character and location of the property. In addition, the NOI is used for measurement of the free cash flow available to service financial debt taken to finance the acquisition of the property. Current maintenance expenses for property preservation are offset against the total NOI.

We shall emphasize that these parameters do not present cash flows from current activity according to GAAP, do not reflect available cash for financing of all of the Group's cash flows (including its ability to perform a money distribution) and are not supposed to be deemed as a substitute for the net profit for assessment of the Group's results of operations.

For the purpose of calculation of the NOI, all revenues from lessees (including rental fees, management fees and other payments) were taken into account alongside the income, and the calculation of costs takes into account all of the operating expenses in respect of the properties, including management, maintenance and other costs. The Group is preparing its financial statements on the basis of the international standardization and therefore, in the calculation of the cost of leasing and operating the properties which are classified as investment property, depreciation was not taken into account. In addition, for the purpose of calculation of the above parameters, profit from revaluation of properties was not taken into account.

During 2007-2011, the Group recorded continuous growth of approx. 78.5% in the actual NOI values in all of its business segments in Israel and abroad.

Below are the NOI figures regarding income-producing properties, from the commercial centers and malls segment in Israel, from the office and other space for lease segment in Israel and from the income-producing property segment in the USA as of December 31 in the years 2010-2011:

NIS in millions	For the year ended		For the three months ended	
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2011	Dec. 31, 2010
Commercial centers and malls in Israel	662	614	175	160
Growth rate	8%		9%	

Office and other space for lease	272	247	71	59
Growth rate	10%		20%	
Income-producing property in the USA	48	21	12	6
Growth Rate	129%		100%	
Total NOI	982	882	258	225
Growth rate	11%		15%	
For explanations pertaining to the increase in NOI, see Section 1.11.1, 1.11.2 and 1.11.3 below.				

1.1.5 Same property NOI Index

(*) Same property NOI – NOI from similar properties that were held by the Group throughout the reported periods.

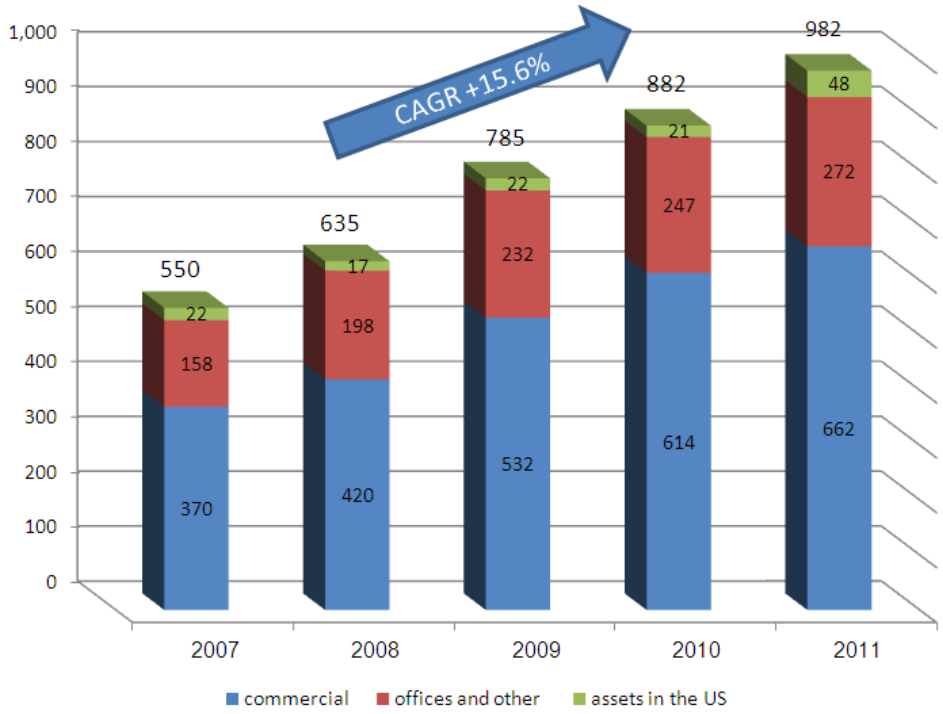
	For the year ended		For the three months ended	
NIS in Millions	Dec. 31, 2011	Dec.31, 2010	Dec. 31, 2011	Dec. 31, 2010
Commercial centers and malls segment in Israel	612	584	165	160
Office and other space for lease segment in Israel	272	247	71	59
Income-producing property in the USA	19	21	4	6
Total	**903**	**852**	**240**	**225**
Increase rate	**6%**		**7%**	
For explanations pertaining to the increase in same property NOI, see Section 1.11.1, 1.11.2 and 1.11.3 below.				

Development of actual same property NOI, according to quarters (NIS in millions):

	2011				2010
	Q4	**Q3**	**Q2**	**Q1**	**Q4**
Same property NOI in all of the periods (*)	240	237	231	230	225
NOI from acquired properties	18	13	8	6	-
NOI from properties	-	-	-	-	-

sold during the period					
Total NOI for the period	**258**	**250**	**239**	**236**	**225**
(*) In all of the Company's business segments.					

Actual NOI development – 2007 - 2011 (NIS in Millions)



1.1.6 Weighted cap rate

Following is a calculation of the weighted cap rate derived from the entire income-producing property of the Group as of December 31, 2011:

	NIS in millions
Total Investment property in the "Expanded stand alone" statement (See Annex E) (*)	14,766
Net of value attributed to construction rights not utilized yet	(1)
Net of value attributed to investment property under construction	(858)
Net of the value attributed to land reserves	(25)
Net of value attributed to down payments on account of property acquisition	**(17)**
Total value of income-producing investment property (including fair value of vacant space)	**13,865**
Actual NOI for the quarter ended on December	258

property (including fair value of vacant space)	
Actual NOI for the quarter ended on December 31, 2011	258
Addition to future annual NOI (**)	13
Pro-forma annual NOI based on standardized NOI	**1,083**
Weighted cap rate derived from income-producing investment property (including vacant space) (***)	**7.8%**

(*) In accordance with valuations received as of December 31, 2011.
(**) Adjustment to adjusted NOI that was included in appraisals as of December 31, 2011 for the income-producing property only (without properties under construction). The figure includes changes in rental fees that were renewed and signed until December 31, 2011 as well as the influence of the index as of December 31, 2011 which was not included in the NOI for 2011. In addition, estimates were included for an addition of NOI for vacant space for population for one year for which value was credited in the valuations as of December 31, 2011 and which have not been populated yet (mainly for Tower E in Herzliya of which population began during Q3/2010). This figure does not constitute Company's forecast for NOI in 2012 and does not include expected NOI from a property acquired in January 2012 in Houston, Texas. For details on sensitivity tests relevant to the cap rate, see Annex A of this Chapter of the Report.
(***) Annual standardized NOI rate out of the total income-producing investment property (including vacant space).

1.1.7 The FFO (Funds From Operations) Index for the real estate business (Calculated in NIS in millions):

For the purpose of providing further information about the results of operations, following is the FFO Index, which is in common usage around the world and provides an appropriate basis for comparison between income-producing property companies. The index expresses net reported profit net of income and expenses of a capital nature, plus the Company's share in depreciation from real estate and other amortizations. **In this Report the FFO index is presented for the Group's income-producing property only**. The Company's management believes that since the FFO index is an index customary in companies of which all of their business focuses on the income-producing property, therefore an adjustment of that index is required in companies of its kind to better reflect the Group's income-producing property business while neutralizing influences which are not from the real estate segment.

The Company's management believes that it is necessary to perform certain adjustments in respect of non-operating items which are affected by revaluation of fair value of assets and liabilities, mainly adjustments of fair value of investment property and property under construction, various capital losses and gains, deferred tax expenses and financing expenses in respect of appreciation of financial liabilities.

This index provides additional information over and above the NOI since it includes, *inter alia*, the cash flow financing expenses and tax

expenses of the Company. It should be emphasized that the FFO does not represent cash flow from current activity according to GAAP and does not reflect cash held by the Company and its ability to distribute the same and does not substitute the reported net profit. It is further clarified that this index is not a figure which is audited by the Company's auditors.

	For the year ended		
	Dec. 31, 2011	**Dec. 31, 2010**	**Dec.31, 2009**
Net profit for period attributed to shareholders	596	1,224	956
Discounting the net profit from Granite HaCarmel attributed to shareholders (including amortization of surplus costs)	(5)	(19)	(51)
Adjustments to profit (1):			
Increase of investment property value	(838)	(888)	(222)
Depreciation and amortizations	4	3	2
Net non-cash-flow finance expenses	92	90	132
Deferred tax expenses (revenues)	745	200	(325)
Adjustments for equity-investees	2	1	4
Interest and dividend from financial assets held for trade net of tax (5)	(49)	(21)	(7)
Impairment (appreciation) of financial assets available for sale and held for trade, net	99	(36)	(2)
Plus benefit recorded for employee option plan (6)	4	10	-
Others	-	-	(2)
Net of dividend received from financial assets available for sale	(44)	(26)	-
Total adjustments to profit	**15**	**(667)**	**(420)**
Plus interest paid for real investments - (2)	**62**	**58**	**58**
Total FFO attributed to the income-producing property business (3)	**668**	**596**	**543**
Annual FFO return for income-producing property in proximity to the Report Date (March 15, 2012)			
Company's value on the stock exchange	**10,540**		
Net of the value of cash and negotiable securities (according to book value as of December 31, 2011)	**(1,467)**		
Net of the value of the Company's holdings in Granite HaCarmel (according to stock	**(436)**		

exchange value)	
Net of the value of the Company's holdings in Bank Leumi (according to stock exchange value)	**(832)**
Net of the value of the Company's holdings in Leumi Card (according to book value according to the last valuation as of December 31, 2011 - the company is not traded)	**(483)**
Market value attributed to real estate alone	**7,322**
Net of value of properties under construction, land and down payments on account of real estate – according to book value as of December 31, 2011	**(901)**
Total market value of income-producing properties	**6,421**
Total quarterly real estate FFO (6)	**172**
Standardizing the quarterly FFO for a year	**688**
Annual income-producing property FFO return (4)	**10.7%**
Remarks and assumptions: 1. The adjustments to the profit below do not include adjustments due to Granite since its profits were discounted in full. 2. Calculated according to weighted interest of the Group due to the real investments, which include: Granite HaCarmel, Bank Leumi and Leumi Card, due to 65% of the investments costs. 3. Which is attributed to shareholder only. 4. The result deriving from dividing the FFO which is attributed to the income-producing property only with the market value which is attributed to the income-producing property only. 5. Net of interests and dividends in respect of transactions and actions in securities which were written off from the real estate operations. **6.** Calculated as FFO for 2011, net of the FFO released for the period ended on September 30, 2011.	

1.1.8 The EPRA indexes: Net Asset Value (EPRA NAV and EPRA NNNAV)

The Company is included in the EPRA index and is also a member of this association (European Public Real Estate Association) which incorporates the large income-producing property companies. In view of the aforesaid, the Company decided to adopt the position statement which was published by the EPRA, the aim of which is to increase the transparency, uniformity and comparativeness of financial information

which is released by the real estate companies.

The EPRA NAV reflects the Company's net asset value under the assumption of continued future activity which assumes the non-disposal of the real estate assets and therefore, various adjustments are required such as presentation by fair value of properties which are not so presented in the financial statements and cancellation of deferred taxes deriving from revaluation of investment property.

The EPRA NNNAV reflects the Company's net asset value under the assumption of immediate disposal of the "Spot" real estate business and therefore, various adjustments are required such as presentation by fair value of assets and liabilities which are not so presented in the financial statements and adjustments to the deferred taxes.

It shall be emphasized that the indexes which were specified above do not include the profit component anticipated due to the projects under construction which were assessed by an assessor at fair value on the basis of land value plus investments by the date of the Report.

These figures do not constitute a valuation of the Company, are not audited by the Company's auditors and do not replace figures in the financial statements.

EPRA NAV (NIS millions)	For the year ended	
	Dec. 31, 2011	**Dec. 31, 2010**
Equity attributed to the Company's shareholders in the financial statements	11,034	11,101
Together with a tax reserve due to revaluation of investment property and fixed assets to fair value (net of the minority share)	2,209	1,400
EPRA NAV	13,243	12,501
EPRA NAV per share (NIS)	109	103

EPRA NNNAV (NIS millions)	For the year ended	
	Dec. 31, 2011	**Dec. 31, 2010**
EPRA NAV	13,243	12,501
Adjustment of asset value to fair value (with no minority)	17	23
Adjustment of value of financial liabilities to fair value (with no minority)	(316)	(156)
Less a tax reserve due to revaluation of investment property and fixed assets to fair value (net of the minority share)	(2,209)	(1,400)
EPRA NNNAV	10,735	10,968
EPRA NNNAV per share (NIS)	89	90

1.1.9 Main market trends regarding income-producing property segment

The business environment in which the Group operates in Israel, is affected mainly by the financial situation in the Israeli economy, the increase in private consumption as well as by the condition of the global economy, the situation in the capital markets in Israel and worldwide and by material changes in the long-term interest rates and in the interest margins which affect the costs of raising long-term debt sources of the Group and the operating cap rates at which properties are revalued. The Group's business in the USA is also affected by the economic situation in the American market in general and in the income-producing commercial properties in particular.

In 2011, the effects of the financial crisis which commenced in the USA in 2007 and extended to a financial crisis which affected a large number of the Eurozone countries. The implications of this crisis are still evident, mainly in the U.S.A. and Eurozone countries, and are expressed, *inter alia*, in significant fluctuations in the financial markets (securities prices, bond rates, currency rates etc.). According to the estimate of the Company's board of directors, pursuant to the companies and businesses[2] survey, it appears that in Q4/2011 the business activity in the economy of Israel grew at a more moderate rate than that of Q3 and the recession concentrated mainly in industrial export and sales for services abroad. Expectations for Q1/2012 indicate that a slowdown is expected also in the local activity component of the industry and services sectors.

The consumer price index (known index) went down in Q4/2011 by approx. 0/2%, compared with an increase of approx. 0.65% in the same period last year. The exchange rate of the Dollar strengthened compared with the Shekel by approx. 2.93% during Q4/2011 and thus the exchange rate of the Canadian Dollar which strengthened compared with the Shekel by approx. 2.68%. It seems that the slowdown tendency which affected the income-producing property market about three years ago was stopped, expressed in a continued increase in the rate of demand and rent prices, and in most of the properties, increased proceeds were recorded in 2011. However, there still is difficulty in raising the rent in certain areas, where the competition is growing.

The economy of the USA continued to recover in 2011 from the recession it had encountered over two years ago. Even though during the years 2010 and 2011 recovery was apparent in the American market, in 2011 a slowdown in the said recovery became apparent as well as a slowdown in the expansion rate of the economic activity in the USA compared with 2010, while the growth in the second half of 2010 in the USA decreased from an annual rate of 2.75% to one percent in the first half of 2011.

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[2] For details regarding the companies and businesses surveys published by the Bank of Israel, see http://www.bankisrael.gov.il/publheb/publhslf.php?misg_id=9.

Despite the foregoing instability, as of the Report Release Date, this instability has no material effect on the Group's results of operations in its business segments, due to its financial strength, its high liquidity, its status in the financial market and the stability and even increase in private consumption in Israel. In the income-producing property segment, the Company even increased its income at a considerable rate compared with the same period last year, whilst maintaining high occupancy rates in its income-producing properties.

The Company's management estimates that the broad dispersion of the property portfolio held thereby, the active current maintenance and management of the properties, their location mainly in high-demand areas, the high business positioning of the properties, the high occupancy rates, the broad range of businesses that exists in the malls and commercial centers and the capital structure contribute to the reduction in the extent of the exposure of the Group's business to such crisis and/or instability.

However, in view of the worldwide uncertainty and instability in the financial markets, the Company is unable to assess, as of the date of approval of the financial statements, the expected effect of the events described above and the length of time in which such effects shall last.

1.1.10 Liquid means at Azrieli Group

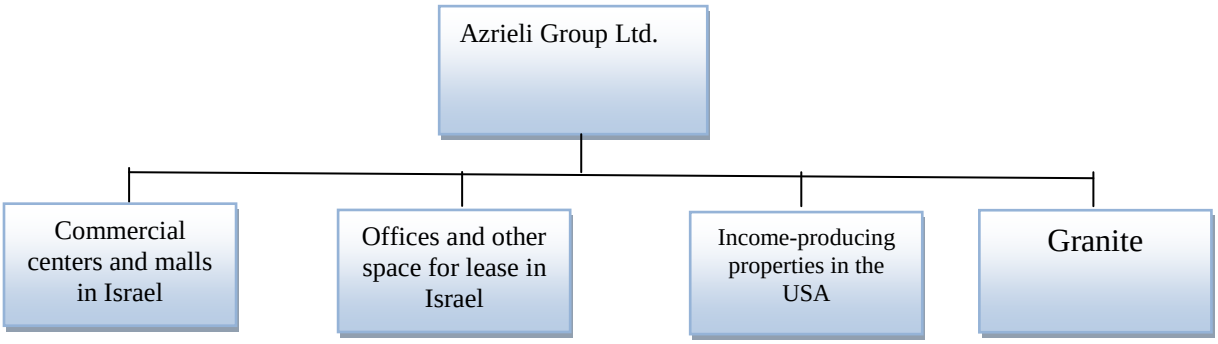
As of December 31, 2011 the aggregate scope of liquid means (cash and cash-equivalents, financial assets held for trade and short-term deposits) held by the Group amounted to the sum of approx. NIS 1.7 billion[3]. The Company regards its liquid means as important to its financial stability, great financial flexibility, due to its independence from the availability of outside sources also for the purpose of repayment of debts and the ability to take advantage of investment opportunities in different periods, in reference to additional possible liquid sources, the Company estimates that the Group is able to raise financing under convenient terms, also in the current economic conditions.

Until the date of the report, the Company managed the balance of the IPO proceeds in accordance with the policy announced by the Company in the Prospectus and in an immediate report dated August 29, 2010 (ref. no. 2010-01-601578), through portfolio managers according to the restrictions set forth in the said policy (The majority is managed in Israel and some is managed outside of Israel, in accordance with such instructions[4]). For details on the uses made of the IPO proceeds, see Regulation 10C in Chapter D – Further Details, of this Report. whilst the balance During the fourth quarter of 2011, the Company recorded financing revenues in a sum of approx. NIS 17 million due to a change in the value of negotiable securities and interests and dividends received from negotiable securities (total compared with NIS 25 million in the same period last year).

1.2 Main data from the Description of the Corporation's Business

1.2.1 Background

The Group's business activity focuses mainly on the income-producing property market in Israel and in the USA, as well as additional industries, *inter alia*, through the subsidiary, Granite. Below is chart specifying the Company's main operation sectors:



[3] For details in regard to NIS 135 million which the Company undertook to reserve within the framework of ratings renewal of commercial securities which it issued see Section 1.5 of this Report.

[4] After the date of the statement of financial position and the closing of the transaction for the acquisition of the towers in Houston, a very negligible amount remains under management overseas.

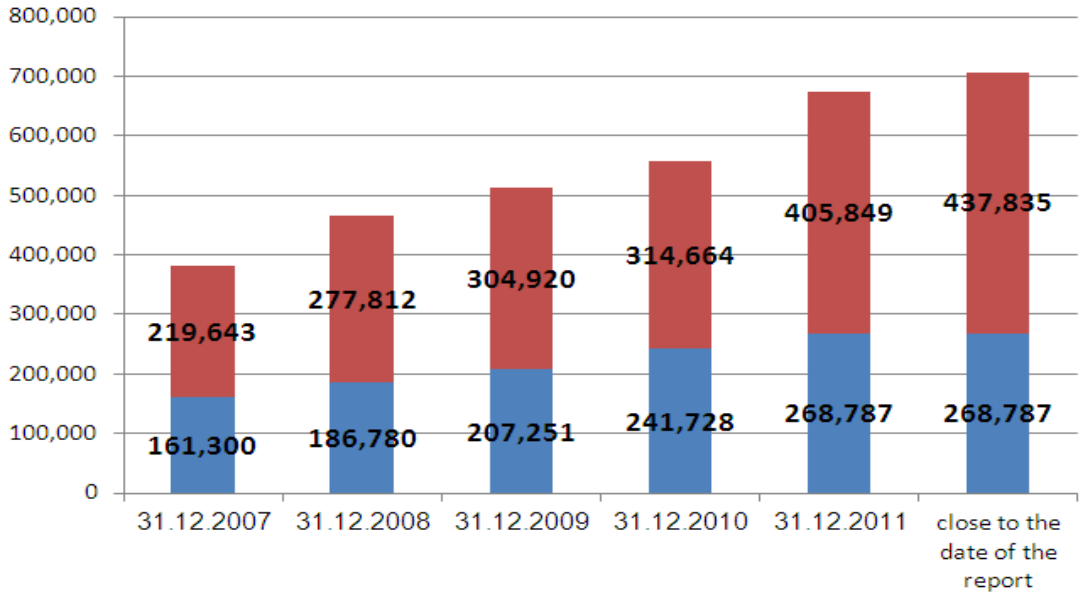
The Company's business condition, results of operations, capital and cash flows, are affected mainly by the state of the rental real estate industry, the business condition of Granite and changes in the value of the financial assets held for sale by the Company. In the board of directors' report, explanations will be presented regarding these effects on the Company for 2011.

The Company's strength is affected mainly by the broad dispersion of the income-producing property in Israel (commercial centers and office space for lease), the diverse lessee composition, the expertise in development, planning, management and construction of income-producing property and its business positioning. In addition, the Company estimates that it earns significant goodwill due to the fact that the commercial centers and malls owned thereby are characterized by high occupancy rates and revenues, immediately in proximity to the date of population thereof and so long as the Company manages them. In addition, the Group's financial strength derives, *inter alia*, from the scope of the cash flow from current activity and the rate of the Group's financial liabilities relative to its total assets which is lower than customary in the income-producing property industry.

During 2011, improvement occurred in the Group's main business activity in the income-producing property segments and growth in the Group's NOI figures, *inter alia* due to opening to the public of Azrieli Kiryat Atta Mall, Azrieli Akko Mall, the acquisition of office towers in Houston, USA and from growth in the Group's income from rental fees both from the commercial centers and the malls and from the existing office space for lease.

Set forth below is the dispersion of growth in sqm of commercial and office space for lease in Israel and abroad in the years 2007-2011:

The areas constituting the Company's share in the area of the property (apart from deduction of the negligible share of Mr. David Azrieli in the properties)



- Office and others
- Malls and commerce areas

The average occupancy rate in the income-producing property in Israel owned by the Group is very high and is close to 100% in the commercial centers and malls segment and approx. 99% in the office and other space for lease segment. The average occupancy rate in the income-producing properties in the USA is approx. 85%. In addition, the Group has land reserves which are intended for the construction of areas for rent.

In addition, Granite's gross profit rate improved in 2011The growth reflects an increase in profitability in all of the business segments except for Sonol, whose profitability was harmed by competition in the industry and mainly due to the decision on the decrease of the marketing margin for gasoline commencing in September 2011.

The Company from time to time looks into business opportunities in Israel and abroad in connection with expansion of its business, mainly in the commercial centers and malls segment and in the commercial property for office and other space segment, including through the acquisition of land reserves, the purchase of additional properties and betterment of existing properties. In addition, the Company from time to time looks into other possibilities for expansion of its business segments whilst taking advantage of market situations and/or crisis situations in leading cash flow-generating target companies in other segments.

The Company's management is acting with the intention of continuing to lead the income-producing property market, *inter alia*, through completion and population of projects in the income-producing property segments, the acquisition of land reserves and the purchase of

additional similar properties as aforesaid, which will cause further growth in the operating cash flow of the Company in the future, insofar as the Company's board of directors shall deem fit.

The main considerations of the Company's management in expansion of the real estate activity are based on:

The potential future demand for the lease of areas in a property which is examined, *inter alia*, based on existing and future data on the geographic region, population density, competing properties in the region, the socio-economic status of the population, access etc.

The construction risks which derive from the cost of construction and from the duration of the construction period which derives from regulatory arrangements and the construction period.

1.2.2 Summary of the Group's business segments

As aforesaid, in view of the expansion in the Group's activity in the USA in 2011, commencing from the financial statements as of December 31, 2011, the income-producing activity of the Company outside Israel (including adjustment of comparison numbers) is presented in a separately reportable segment, and as of this date, the Company has four main business segments which constitute its core business. Set forth below is a concise description of the Group's business segments:

Commercial Centers and Malls in Israel – In this business sector, the Group focuses mainly on development, construction, purchase, lease, management and maintenance of malls and commercial centers in Israel. As of the date of the Report, the Group owns 13 malls and commercial centers of a total leasable area of approx. 256 thousand sqm (the Company's share approx. 255 thousand sqm) which are leased to approx. 1,750 lessees, with most malls and commercial centers being located in the large cities in Israel.

In recent years the Company was and is acting to expand its business in this segment, *inter alia*, to preserve and strengthen its status as a leading company in the income-producing property segment. In this context, the Company completed in 2008 the construction of Azrieli Modi'in Mall; purchased Azrieli Givatayim Mall in 2009; acquired and improved Azrieli Haifa Mall at the beginning of 2010 and constructed and opened to the public the Kiryat Atta Azrieli Mall and the Akko Azrieli Mall in 2011. In addition, the Company is acting for the construction of Azrieli Ramla Mall and for receiving of the approvals for the construction of Azrieli Rishonim in Rishon Lezion, as specified in Section 7.8 of Chapter A of the Report.

In addition, the Company focuses on actions to preserve its ability to generate stable cash flows and to increase the scope thereof, *inter alia*, through modification of the composition of the areas intended for lease, maximum utilization of the areas through splitting large areas into small stores and marketing of areas for lease to well-known and reputable foreign chains. In this framework, the Company engaged, in 2011, in a lease agreement with the American fashion brand Forever 21 and it conducts negotiations with other international chains.

Office and Other Space for Lease in Israel – In this business segment the Company focuses mainly on development, construction, purchase, lease, management and maintenance of office buildings and office and knowledge-intensive industry parks in Israel. As of the date of the Report, the Group owns 9 income-producing properties in the office and other space for lease segment in Israel, of a total leasable area of approx. 282 thousand sqm (the Company's share, approx. 280 thousand sqm) leased to approx. 500 tenants.

In recent years the Company has been acting to expand its business in

this segment, *inter alia* through completing the utilization of existing building rights (such as completion of the Square tower in the Azrieli project in 2008 and completion of the construction of another office tower in the Herzliya Business Park project in 2010); the acquisition of land reserves which are intended for the construction of office towers (Azrieli Sarona Project at the Southern Kirya and Azrieli Holon Center, all as specified in Section 7.8 of Chapter A of the Report), the purchase of income-producing office towers (the purchase of the property in Houston, Texas, as specified in Section 9.2.10 of Chapter A of the Report) and the population of vacant office space for lease, thus preserving and even increasing the high occupancy rates which characterize the Group.

The Company estimates that these actions may continue to enhance the Group's financial strength and yield an increase in the Group's income and cash flow.

Income-Producing Property in the USA – in this segment, as of the report release date, the Company holds five (5) office properties for rent outside Israel, at an overall lease area of approx. 166 thousand sqm (the Company's share – 155 thousand sqm) leased to approx. 270 lessees, as well as one (1) commercial center at an overall leased area of 13 thousand sqm.

In recent years the Company expanded its activity in this segment, mainly through the purchase of additional income-producing properties (such as the acquisition of the office towers and the office buildings in Houston Texas, as specified in Sections 1.1.1 and 1.1.2 above) and through the population of areas free for lease for offices, and thus maintained, and even increased the high occupancy rate typical to the Group.

Granite – Granite is a public company which incorporated in Israel, whose shares are listed on the Tel Aviv Stock Exchange. Granite's main business, through the companies held thereby, is as follows: (1) Sonol fuelling and commerce complexes and direct marketing; (2) Supergas; (3) Tambour; (4) GES (water and waste water); (5) Others.

The Group has additional businesses, which include, *inter alia*, passive financial investments in corporations in the banking and financing segment, investments in start-up companies and investment funds as specified in Chapter A of the Periodic Report.

Thus, in light of the business opportunity that was created, the Company purchased during 2008 approx. 20% of the shares of Leumi Card and in 2009 passive minority holdings in Bank Leumi. The investments are presented in the financial statements as a financial asset available for sale. The passive financial investments are presented in the Company's financial statements according to the fair value and the change of value in respect thereof, net of the tax effect which was credited directly to the overall profit. The Company's management has

taken no decision regarding the increase or reduction of its holdings that are specified above.

Following are the changes in the main financial investments during the Report Period: (NIS in millions)

	Investment value in the financial statements as of Dec. 31, 2010	Investments during the year ended on Dec. 31, 2011	Total investment as of Dec. 31, 2011before adjustment for changes in the fair value during the Report Period	Fair value* of the investment as presented in the financial statements as of Dec. 31, 2011	Change in the fair value during the Report Period	Dividend that was received in 2011*
Investment in Bank Leumi le-Israel Ltd. (*)	1,284	-	1,284	771	(513)	43
Investment in Leumi Card Ltd. (**)	498	-	498	483	(16)	-
Total	1,782	-	1,782	1,254	(529)	43

* The fair value of the investment in Bank Leumi le-Israel was determined according to the value of the share at the stock exchange as of December 31, 2011. For details regarding the resolution of Bank Leumi's board of directors regarding the distribution of a dividend, see Section 12.1.2 of Chapter A of the Report – of the Description of the Corporation's Business chapter and Section 1.5 below;

** The fair value of the investment in Leumi Card Ltd. ("**Leumi Card**") was determined according to an independent appraiser, in accordance with the valuation as of December 31, 2011.

1.3 The business results and the total assets in the year ended December 31, 2011

Following is the contribution of the Group's business segments to the business results: (NIS in millions)

	Segment profit in the year ended:		Rate of the segment's profit from the total consolidated net profit in the year ended:	
	Dec. 31, 2011	**Dec.31, 2010**	**Dec. 31, 2011**	**Dec. 31, 2010**
Commercial centers and malls in Israel	662	614	106%	49%
Office and other space for lease in Israel	272	247	44%	20%
Income-producing property in the USA	48	21	8%	1%
Granite	200	177	32%	14%
Total attributed profit	1,182	1,059	190%	84%
Changes in fair value	849	891	136%	71%
Net financing expenses	(489)	(363)	(78%)	(29%)
Tax expenses	(876)	(292)	(141%)	(23%)
G&A income (expenses), net	(43)	(40)	(7%)	(3%)
Net profit per period	623	1,255	100%	100%

The Group's revenues for the Report Period amounted to approx. NIS 7,547 million, compared with approx. NIS 6,344 million in the same period last year, an increase of approx. NIS 1,203 million, deriving mainly from an increase in the income-producing property segment for commercial centers and malls in Israel in the sum of approx. NIS 60 million (mainly due to the opening of the Azrieli Akko Mall and Azrieli Kiryat Ata Mall in Q3/2011, at the end of the first quarter of 2009, the purchase of the Azrieli Haifa Mall during the first quarter of 2010, and an increase in revenues from existing properties), an increase in the income-producing property for office and other space for lease segment in Israel in the sum of approx. NIS 23 million (mainly from the increase in revenues from existing properties), from growth in the income-producing properties segment in the USA in the amount of approx. NIS 67 million (mainly due to the purchase of additional office buildings in February 2011) and an increase in the Granite segment in the sum of approx. NIS 1,053 million (Due to an increase in all of the business sectors of Granite).

The Group's revenues for the three months ended on December 31, 2011 amounted to the sum of approx. NIS 2,004 million, compared with the sum of approx. NIS 1,624 million in the same period last year, a rise of approx. NIS 380 million, which derives mainly from an increase in the income-producing property segment in the sum of approx. NIS 54 million (mainly due to the opening of the Azrieli Akko Mall and the Azrieli Kiryat Ata Mall in Q3/2011 and the purchase of 3 office buildings in Galleria, Texas, USA in February 2011) and from increase in the Granite segment in the sum of approx. NIS 326 million (Due to an increase in all of Granite's business sectors).

As of December 31, 2011, the total assets on the balance sheet were approx. NIS 23.2 billion, compared with approx. NIS 21.3 billion as of December 31, 2010.

Following is the share of the assets of the business segments from the total assets of the Group:

	The share of the segment's assets out of the total assets, on a consolidated basis, as of (NIS in millions)		The rate of the segment's assets out of the total assets, on a consolidated basis, as of	
	Dec.31, 2011	**Dec. 31, 2010**	**Dec. 31, 2011**	**Dec. 31, 2010**
Commercial centers and malls in Israel	9,424	8,445	41%	40%
Office and other space for lease in Israel	4,280	3,437	18%	16%
Income-producing property in the USA	1,092	281	5%	1%
Granite	5,497	4,921	24%	23%
Others	2,887	4,259	12%	20%
Total	**23,180**	**21,343**	**100%**	**100%**

1.4 **Summary of Balance Sheet Data from the Consolidated Statement**: (NIS in thousands)

	As of Dec. 31, 2011	As of Dec. 31, 2010
Current assets	4,072,143	4,364,252
Non-current assets	19,107,570	16,979,126
Current liabilities	3,863,385	2,992,780
Non-current liabilities	7,852,270	6,825,761
Capital attributed to the Company's shareholders	11,033,788	11,100,941
Capital attributed to the Company's shareholders from the total balance sheet (in percents)	48%	52%

The Group finances its business activity mostly by its equity, cash and marketable securities and by using non-bank credit (mostly bonds), bank credit (short- and long-term) and commercial securities. The Group's financial stability and the fact that most of the Group's debt is in long-term loans and bonds provides the Group with available sources for obtaining finance under convenient terms.

1.5 **Financial Condition, Liquidity and Financing Sources**

Liquid Means in the Group

As of December 31, 2011, the cumulative scope of cash, cash equivalents, and financial assets held for trade and short-term deposits and investments

amounted to approx. NIS 1.7 billion[5].

The Company estimates that its liquid means, the considerable cash flow from current operations and its non-pledged assets (in a total value of approx. NIS 9.2 billion in addition to NIS 1.7 billion specified above), allow it a high financial flexibility and an ability to use investment and capital raising opportunities in good conditions.

The following is a table of the assets that are not pledged and are available to serve as collateral against the obtaining of credit[6]:

Assets	Value of assets as of Dec. 31, 2011 (NIS in millions) as presented in the financial statements
Property in commercial centers and malls segment in Israel	5,536
Property in the office and other space for lease segment in Israel	1,669
Company's holdings in Leumi Card	483
Company's holdings in Granite	768
Company's holdings in Bank Leumi	771
Total	**9,227**

In addition, the Company holds pledged income-producing properties, the loan rate for which is considerably lower than their far value. (Such as the Azrieli Center project, which was appraised by an independent appraiser as of December 31, 2011 (Without the square tower which was included in the non-pledged assets) at approx. NIS 3.8 billion, whereas the loans for it, as of December 31, 2011 (without the square tower), amounted to approx. NIS 839 million).

Dividends:

The Company:

On March 29, 2011, the Company's board of directors approved, after having accepted the recommendation of the finance committee, a distribution in cash in the total amount of NIS 240 million (NIS1.979 per share) which constituted approx. 48% of the net profit to the shareholder in 2010 after discounting revaluation profits and after a discounting the tax effects thereon. On April 27, 2011, the Company distributed to its shareholders the said amount.

On March 21, 2012, after the date of the report on the financial condition, the board of directors of the Company approved, after accepting the recommendation of the finance committee, a cash distribution at an overall amount of NIS 240 million (NIS 1.979 per share) which constitutes approx.

[5] For details in regard to an amount which shall not be less than NIS 135 million which the Company undertook to reserve within the framework of ratings renewal of commercial securities which it issued see Section 1.5 of this Report.

[6] The assets in the table do not include income-producing properties held by Granite.

48% of the net profit for the shareholders in 2011 after discounting revaluation profits, discounting unusual effect of changing the rate of the corporate tax (following the Trachtenberg Committee) and discounting the tax effect thereon and approx. 36% of the FFO for the real estate business as specified in Section 1.1.7 above.

The Company's board of directors approved that the dividend distribution fulfills the profit test which is set forth in Section 302 of the Companies Law, 5759-1999, and that there is no reasonable concern that the distribution of the aforesaid dividend will deny the Company the ability to meet its existing and projected liabilities, as they become due. For purposes of adoption of the resolution on the dividend distribution, the board of directors examined figures which were provided by the Company's management, including the Company's cash balances, the Company's total liabilities for payment in the next two years and a surplus of current assets over liabilities in the next two years. In addition, in view of the Company's main business at this stage being in income-producing property, while considering its goals and the business strategy declared thereby, the Company's board of directors examined the profit appropriate for distribution, while also considering the profit which is based on the FFO index[7] which better expresses the permanent cash flow deriving from the real estate business. For further details see immediate report dated March 22, 2012, which released concurrently with this Report.

According to the Company's financial statements as of December 31, 2011, the Company has surplus of approx. NIS 8.4 billion.

Granite: According to the dividend distribution policy set forth for the held company Granite, Granite shall distribute every year cash dividend in such sum that shall constitute 40% to 50% of the net annual profit after tax of Granite, except for one-time profits not resulting from current operations, subject to the provisions of any law. In the Report Period, the Company received a dividend from Granite in the sum of approx. NIS 9 million.

Leumi Card: To the best of the Company’s knowledge, on May 24, 2010, the Leumi Card's board of directors adopted, annual dividend policy according to which each year an amount which shall equal 30% of Leumi Card's net current profit shall be distributed, subject to the instructions of the Supervisor on the Banks, regulatory provisions and the requirements of the Companies Law. This policy was updated on May 22, 2011 so that the dividend distribution will be allowed subject to limitations of a “risk appetite” policy which was approved by the board of directors of Leumi Card, according to which a capital to risk components ratio would be maintained at a range of between 14% and 14.5% and a capital core ratio which would be no less than 12% as well as the requirements of supervision on the banks which determine that the Company must adopt Bank Leumi’s capital adequacy objectives.

[7] It shall be clarified that the FFO does not represent a cash flow from current activity according to generally accepted accounting standards, and does not reflect cash which is held by the Company and its ability to distribute the same and does not replace the reported net profit). It is further clarified that this index is not a figure which is audited by the Company's auditors.

On February 23, 2012, Leumi Card decided on the distribution of a dividend in the amount of NIS 40 million (the Company's share - NIS 8 million) for the profits of 2011, which, according to the publications of Leumi Card, will be distributed on March 29, 2012. During the Report Period the Company did not receive a dividend from Leumi Card.

Bank Leumi: On January 27, 2011, and June 28, 2011 the Company received approx. NIS 43 million as a dividend from Bank Leumi for year 2010. Cash flows

Net cash flows generated for the Group from current operations for the year ended on December 31, 2011, amounted to the sum of approx. NIS 1,687 million, compared with the sum of approx. NIS 1,044 million which were used for current operations in the same period last year (an increase of approx. NIS 2,731 million).

The cash flow in the Report Period derived mainly from the operating profit of the income-producing property (approx. NIS 982 million), with the addition of cash flows generated from current operations from the sale of financial assets held for trade in the sum of approx. NIS 809 million.

The main increase in cash flows from current operations in the year ended on December 31, 2011 compared with the same period last year resulted from the sale of financial assets held for trade in the sum of approx. NIS 809 million in the Report Period, compared with the purchase of financial assets held for trade in the sum of approx. NIS 2,193 million in the same period last year. In addition, an increase occurred in cash flows deriving from an increase in the operating profit of the income-producing property (approx. NIS 100 million), compared with the same period last year.

In addition, in the Granite segment a decrease of approx. NIS 290 was recorded, deriving mainly from changes in working capital as follows: (1) increase in trade receivables and inventory, mainly due to the increases in the prices of oil distillates and expansion of the operation volumes in all of the business segments of Granite. (2) increase in trade payables this year, mainly due to increases in the prices of oil distillates and expansion of the operation volumes, as aforesaid, compares with a decrease in trade payables last year, mainly due to a reduction in the purchases of oil distillates.

The cash flow derived by the Group from current operations (net of investment in financial assets held for trade) in the year ended on December 31, 2011, together with cash originating from the IPO , were used by the Group mainly for financing investments required for projects under construction and purchase of income-producing properties and land.

Net cash flows used by the Group for investment activity in the year ended on December 31, 2011, amounted to approx. NIS 1,831 million, compared with approx. NIS 447 million in the same period last year.

The increase in the sum of NIS 1,384 million in the Report Period resulted mainly from the purchase of, and investment in investment properties and

investment properties under construction in the sum of approx. NIS 1,708 million compared with approx. NIS 474 million in the same period last year, and changes in short-term deposits in the sum of approx. NIS 160 million compared with the same period last year.

Net cash flows derived by the Group from financing activity in the year ended on December 31, 2011, amounted to approx. NIS 191 million, compared with net cash flows deriving from financing activity in the sum of approx. NIS 1,583 million in the same period last year. The decrease in the sum of approx. NIS 1,392 million resulted mainly from the IPO proceeds (net of IPO costs) in the sum of approx. NIS 2,481 million in the same period last year, from the distribution of a dividend in the amount of approx. NIS 240 million during the Report Period, and conversely an increase in short- and long-term loans/bonds received (net of loans repaid) in the sum of approx. NIS 1,415 million compared with the same period last year.

Following is the composition of the Group's financing sources:

	December 31, 2011		December 31, 2010	
	NIS in millions	% of total balance sheet	NIS in millions	% of total balance sheet
Short-term credit from banking corporations and other credit providers	2,445	10.5%	1,772	8.3%
Long-term credit from banking corporations and other credit providers	3,758	16.2%	3,300	15.5%
Bonds	1,707	7.4%	1,836	8.6%
Total	7,910	34.1%	6,908	32.4%

Increase in the sum of approx. NIS 1,002 million in the Report Period results mainly from an increase in credit from banking corporations and other credit providers in the Granite segment in the sum of approx. NIS 427 million, which resulted mainly from the additional working capital required for financing the increase in trade receivables and inventory in light of the increases in the oil distillates prices and in light of the expansion of the business in all of the business sectors of Granite except for the fueling complexes of Sonol, from the receipt of short-term credit for the purchase of Azrieli Sarona Center in the amount of approx. NIS 310 million, from the receipt of long-term credit for the purchase of the property in Galleria, Texas, USA in the sum of approx. NIS 497 million, and conversely repayment of long-term loans/bonds according to the payment schedules during the Report Period.

Bonds and commercial securities and the rating thereof

The Company's bonds are rated by Maalot, The Israeli Securities Rating Corporation Ltd. ("Maalot") and Midroog Ltd. ("Midroog"). During Q4/2011 Maalot updated the rating and raised it to stable AA. As of the date of the Report, the rating was as follows: the rating of Midroog: Aa2 with a stable horizon; the rating of Maalot: AA- stable. To review Midroog's annual

monitoring report see the Company's report of June 30, 2011, ref. no. 2011-01-198093. To review Maalot's annual follow-up report and the raise in the rating, see the Company's immediate report of November 23, 2011 (ref. no. 2011-01-336291).

On June 30, 2011, Midroog extended the rating of commercial securities (the "**Commercial Securities**") which the Company had issued, until June 30, 2012, at the rating of P-1. In order to ensure sufficient liquidity for the repayment of the Commercial Securities, the Company undertook to reserve an amount which shall not be lower than NIS 135 million in a deposit, which may not be offset against a bank loan, in a bank whose short term rating is P-1 and/or in State of Israel bond which are free and clear of charges, until the date of repayment of the Commercial Securities. For details see the Company's report of June 30, 2011, ref. no. 2011-01-198045. On January 12, 2012, Midroog expanded the rating frame of commercial securities of the Company from NSI135 million to NIS 200 million. For detail see immediate report dated January 12, 2012, reference 2012-01-013743.

For details regarding updated balances of bonds and commercial securities, see Chapter A of the Report (the Description of the Corporation's Business chapter).

Liabilities and Financing

Financial liabilities of the Group (except for Granite) as of December 31, 2011, in millions of NIS:

	Fixed Interest			**Variable Interest**		**Total**		**Total**
	Index linked	**USA Dollar Linked**	**Not Linked**	**Sterling Linked**	**Not Linked**	**Fixed Interest**	**Variable Interest**	
Short Term Loans	-	-	-	25	644	-	669	669
Long Term Loans	3,607	684	31	-	-	4,322	-	4,322
Total	**3,607**	**684**	**31**	**25**	**644**	**4,322**	**669**	**4,991**

The Company's policy is to finance its operations, beyond the positive and stable cash flow from current operations and current assets, by long-term loans, index-linked with a fixed interest, in order to minimize market risks resulting from changes in the interest rates in the economy and neutralize the market risk resulting from changes in the Consumer Price Index, while using the fact that most of the Company's revenues are index-linked.

Nonetheless, in light of the low interest rates for short-term loans with variable interest, the Company decided to finance its activity also by using short-term loans as specified above.

As of December 31, 2011, short-term loans accounted for approx. 13% of the Group's total financial liabilities (except for Granite). According to the Company's estimation, this rate is low and conservative in light of the low leverage ratio and the sum of the non-pledged assets as specified above.

According to the Company's policy, from time to time, it considers the opportunities for converting the short-term debt to a long-term debt with fixed interest. The Company's management considers on an on-going basis the payment sources for financing the existing and expected liabilities as they become due, including with respect to the cash flow and the sum of the non-pledged assets.

In the Report Period, the sources for financing the financial liabilities are mainly the following:

- The Group has a positive cash flow from current activity for many years (excluding consideration or investment in financial assets that are listed for trade). This cash flow amounted to the sum of approx. NIS 878 million in the year ended December 31, 2011, compared with the sum of NIS 1,144 million in the same period last year (the decrease in the sum of approx. NIS 290 million is attributed to Granite – see explanation regarding the cash flows, above, while the increase in the sum of approx. NIS 24 million is attributed mainly to the real estate business).

- A material part of the real estate property of the Group (not including Granite) is not pledged (approx. NIS 7.2 billion) and allows the Group, if necessary, to raise additional credit beyond the surpluses of the current cash flow, the balance of cash and securities.

- After the IPO, the Company received the IPO proceeds, in the framework of the IPO prospectus of the Company's shares, in the sum of approx. NIS 2.5 billion, which were used by the Company, *inter alia*, to repay the financial liabilities. The balance of the cash and financial assets held for trade as of December 31 , 2011 is approx. NIS 1.7 billion.

- The Company has financial assets that are available for sale and not pledged (such as: its entire holdings of Leumi Card shares whose value in the financial statements as of December 31, 2011, was approx. NIS 483 million, as well as Bank Leumi shares (that were purchased in April 2009), whose value in the financial statements as of December 31, 2011was approx. NIS 771 million).

- The Group's entire holdings of Granite shares which are not pledged and whose value in the financial statements as of December 31, 2011, was approx. NIS 768 million.

- In addition, the Group has income-producing pledged properties, the rate of the loan for which is considerably lower than their fair value.

<u>Analysis of sensitivity tests and effects on fair value of protection transactions, exchange rates, interest and financial instruments</u>

In accordance with the main market risks specified above and in accordance with the provisions of the Second Schedule to the Regulations, the Group is performing sensitivity tests regarding changes in market risks affecting the fair value of "sensitive instruments". For details see, attached hereto, Annex A to

this board of directors' report and also Note 39 to the financial statements.

Set forth below are the bottom lines of the sensitivity test tables as of December 31, 2011:

	Profit (Loss) from Changes in Parameters in respect of which the Sensitivity Test was Performed (NIS in thousands)						
		Rise in Parameter		Decline in Parameter		Absolute increase	Absolute decrease
	Fair Value	10%	5%	10%	5%	2%	2%
Sensitivity to changes in the NIS interest rates	56,135	(2,399)	(1,190)	2,332	1,169	(14,118)	11,781
Sensitivity to changes in the U.S. dollar interest rates	(736,998)	24,930	12,623	(26,236)	(12,950)	80,004	(95,032)
Sensitivity to changes in the real interest rates	(4,062,169)	26,351	13,221	(26,698)	(13,305)	210,078	(236,036)
Sensitivity to changes in the consumer price index	(5,832)	49,300	24,650	(49,300)	(24,650)		
Sensitivity to changes in dollar exchange rates	(1,052,492)	(37,298)	(18,650)	37,298	18,650		
Sensitivity to changes in other currencies exchange rates	48,618	11,408	5,685	(11,408)	(5,685)		
Sensitivity to changes in CAD interest rates	55,525	(854)	(427)	854	427		
Sensitivity to changes in securities rates	1,401,787	140,178	70,089	(140,178)	(70,089)		
Sensitivity to changes in the cap rate of investment property	13,834,354	(1,267,891)	(663,965)	1,550,234	734,563	(2,886,881)	4,934,879

Set forth below are the bottom lines of the sensitivity test tables as of December 31, 2010:

	Profit (Loss) from Changes in Parameters in respect of which the Sensitivity Test was Performed (NIS in thousands)						
		Rise in Parameter		Decline in Parameter		Absolute increase	Absolute decrease
	Fair Value	10%	5%	10%	5%	2%	2%
Sensitivity to changes in the NIS interest rates	291,111	(5,293)	(2,637)	5,193	2,609	(28,026)	26,783
Sensitivity to changes in the dollar interest rates	(202,606)	2,469	1,255	(2,639)	(1,297)	8,967	(10,488)
Sensitivity to changes in the real interest rates	(4,310,328)	28,459	14,290	(28,937)	(14,480)	269,260	(305,973)
Sensitivity to changes in the consumer price index	(1,064)	62,500	31,250	(62,500)	(31,250)		
Sensitivity to changes in dollar exchange rates	(487,683)	(993)	(496)	993	496		
Sensitivity to changes in other currencies exchange rates	36,008	4,848	2,424	(4,848)	(2,424)		
Sensitivity to changes in CAD exchange rates	237,878	23,788	11,894	(23,788)	)11,894(		
Sensitivity to changes in securities rates	2,310,423	231,042	115,521	(231,042)	(115,521)		
Sensitivity to changes in the cap rate of investment property	11,997,550	(840,319)	(310,346)	1,599,849	896,848	(2,868,625)	4,525,107

The Company's linkage balance sheet as of December 31, 2011 and 2010

For details regarding the Company's consolidated linkage balance sheet as of December 31, 2011 and 2010, see Note 39C to the financial statements.

1.6 Quality of Profit

The Company's net profit mainly includes and is affected by the following components:

- Profit from the income-producing property business – the commercial

centers and malls segment in Israel, the office and other space for lease segment in Israel and the Income-producing property segment in the USA;

- Changes in the fair value of the Group's investment property;
- The Company's share in the profits of Granite's sector;
- The Company's HQ business which includes net financing expenses, G&A expenses;
- Deferred and current tax expenses including the effect of changes in the tax percentage.

The profit from the real estate segment is affected almost entirely by the rental income in the various properties, which is mainly affected by the supply and demand for rental space.

There may be high volatility in the Company's profits between different report periods, mainly due to changes in the value of the income-producing property as aforesaid, which is affected, *inter alia*, by changes in the cap rates and changes in the scope of the income, which is mainly affected by a rise in the consumer price index. In addition, the financing expenses at the Company are affected by changes in variable interest and changes in the consumer price index.

At least once a year the Company examines the fair value of the investment property and whenever there are indications for material changes in the value. The fair value is determined, mainly, based on valuations that were performed by appraisers independent of the Company. The fair value is measured based on the discounting of projected cash flows, reliable estimates of future cash flows which are supported by the terms and conditions of the existing lease contracts and by external evidence such as current rent for real estate in similar locations and condition, as well as usage of cap rates which reflect the market assessments of the uncertainty with respect to the amount and the timing of the cash flows. The Company examines, each quarter, the need for updating the value of the investment properties by an examination of macro-economic changes, changes in the surroundings of the property and revenues deriving therefrom, and speaks with an independent real estate assessor to examine changes in the capitalization rates. In addition, with regard to investment properties under construction, the costs which were actually invested during the period, the updated forecast of costs for completion and the lease contracts that were executed during the period, are taken into account. In the event that the management estimates that there may be material changes in the value of the properties, updated valuations are performed for the relevant properties, by the Company or an independent assessor. A valuation is performed by an independent appraiser for each investment property at least once a year.

Changes in the assumptions that are being used by outside experts and/or changes in the estimates of the Company's management which relies on its aggregate experience may lead to changes in the fair value that was carried to

the income statement, and thus affect the Company's financial condition and results of operations. For further details see Note 3(C) (1), (8) and (9).

For details regarding the fair value of the investment property according to business segments see Section 1.11 of the Report and also see Note 14 of the attached financial statements.

1.7 General and Administrative Expenses

The Company's consolidated administrative expenses (without Granite) amounted to approx. 71 million in 2011 versus NIS 69 million in 2010. The increase in the amount of approx. NIS 2 million derives mainly from an increase in compensation, consulting and other expenses of approx. NIS 9.5 million and on the other hand a decrease in donations in the amount of approx. NIS 3.5 million and a decrease in management fees to the chairman of the board, in the amount of approx. NIS 4 million.

The total consolidated amount of donations of the Company (without Granite) in 2011 amounted to approx. NIS 7.8 (out of which approx. NIS 4.2 million in Q4/2011)[8].
The Company's consolidated management expenses (without Granite) totaled to approx. NIS 22 million in Q4/2011 compared with approx. NIS 21 million in the same period last year.

1.8 Net Financing Expenses

The Group's net financing expenses as of the year ended on December 31, 2011, amounted to the sum of approx. NIS 489 million, compared with approx. NIS 363 million in the same period last year. The increase in the financing expenses results mainly from losses from negotiable securities (net of interest and dividend therefrom) in the amount of approx. approx. NIS 31 million during the Report Period compared with a profit of approx. NIS 74 million in the same period last year, as well as from the increase in the rate of the rise of the known index during the Report Period at a rate of approx. 2.55% compared with an increase of approx. 2.28% in the same period last year.

In addition, the increase in the scope of the Company's activities during the period (purchase of income-producing property and land) which led to an increase in the scope of the Company's debt and as a result to an increase in the financing expenses.

1.9 Taxes on Income

The Group's income tax expenses for the year ended December 31, 2011, amounted to the sum of approx. NIS 876 million, compared with tax expenses in the sum of approx. NIS 292 million in the same period last year. The

[8] For details regarding correction of *lapsus calami* in the Company prospectus regarding the rate of the total contributions of the Company to the Azrieli Foundation (Israel) (registered association) out of the net profit of the Company, see the immediate report of the Company dated February 20, 2012 (reference 2012-01-046971).

increase in the expenses in the sum of approx. NIS 584 million resulted mainly from a one-time extraordinary expense (consolidated) that was recorded in 2011 at an amount of approx. NIS 601 million due to the cancellation of the reduction in corporate tax rate.

1.10 Summary of the Company's Results (Consolidated) – NIS in millions

	For the year ended		
	December 31, 2011	Dec. 31, 2010	Dec. 31, 2009
Net profit for the period attributed to the Shareholders	596	1,224	956
Net profit attributed to the Shareholders and rights which do not confer control	623	1,255	1,000
Basic profit per share (NIS)	4.91	11.33	10.52
Total profit for Shareholders and rights which do not confer control	204	1,317	1,478

Main causes for the change in the Net Income (NIS millions)

	For the year ended on		
	Dec. 31, 2011	Dec. 31, 2010	Difference
Consolidated Net Profit	623	1,255	(632)
Unusual effects:			
Change in Tax percentage	601	-	601
Profit from real estate value increase net of tax	(696)	(730)	34
Loss (Profit) from negotiable securities net of tax	75	(35)	110
Interest and dividend from negotiable securities net of tax	(56)	(19)	(37)
Dividend from financial assets available for sale	(45)	(31)	(14)
Total unusual effects (consolidated)	(121)	(815)	694
Total increase in profit net of unusual effects	502	440	62

Total profit (loss)

The Company's capital and total profit are also affected by various capital funds, mainly capital funds due to adjustment to the fair value of investments treated as financial assets available for sale.

The total profit for the year ended December 31, 2011 amounted to the sum of approx. NIS 204 million, compared with a net profit (including rights which do not confer control) in the sum of approx. NIS 623 million in the same period. The aforesaid difference results mainly from a loss in the sum of approx. NIS 432 million due to a negative change in the fair value of financial assets available for sale (mainly change in the fair value of the investment in Bank Leumi le-Israel and Leumi Card and net of tax.

1.11 Contribution to the Company's Results According to Business segments

The Company implemented in its financial statements the International Financial Reporting Standard 8 concerning Operating Segments (IFRS8). The Company's division into segments is based on the managerial and internal reports of the Company. In addition, the contribution to the results takes into account the Company's share in the results of the held company Granite, which constitutes a business segment.

1.11.1 Commercial Centers and Malls Segment in Israel

Summary of the segment's business results:

	For the three months period ended		For the year ended	
	Dec. 31, 2011	**Dec. 31, 2010**	**Dec. 31, 2011**	**Dec. 31, 2010**
		NIS in millions		
Revenues	219	194	814	754
% change	13%		8%	
NOI	175	160	662	614
% change	9%		8%	

The NOI figure is one of the important parameters in valuations of income-producing property companies. For details concerning the manner of calculation of this figure, see Section 1.1.4 above.

The increase in the NOI results mainly from an improvement in the revenues of the existing commercial centers and malls and from the revenues of commercial centers and malls that were added to the Group due to the purchase and/or the completion of construction and occupation thereof in the course of 2011-2010 (mainly, Azrieli Haifa

Mall, Azrieli Akko Mall and Azrieli Kiryat Atta Mall).

Following is the development of the segment's NOI (NIS in millions)

	For the three months period ended		For the year ended	
	Dec. 31, 2011	Dec. 31, 2010	Dec. 31, 2011	Dec. 31, 2010
For the assets owned by the Company as of the beginning of the period in 2010[9]	165	160	612	584
For assets that were purchased or whose construction was completed in 2010	-	-	33	30
For assets that were purchased or whose construction was completed in 2011	10	-	17	-
Total	**175**	**160**	**662**	**614**

In the Quarter ended December 31, 2011, the NOI increased compared with the same quarter last year, resulting mainly from the increase in revenues from existing properties and from the opening of Azrieli Akko and Kiryat Atta Malls .

In the year ended December 31, 2011, the NOI increased compared with the same period last year, resulting mainly from an increase in revenues from existing properties and from the opening of Azrieli Akko and Kiryat Atta Malls at the end of Q3/2011, the purchase of Azrieli Haifa Mall at the end of January 2010.

In the Company's estimation, the same property NOI in the malls and commercial centers segment in Israel was favorably affected primarily by:

- A real increase in the rent at the time of renewal of contracts in the various properties (pursuant to option exercise by the tenants and/or execution of new agreements).
- Most lease contracts are linked to the consumer price index (which rose in the period of the report by 2.55% (known index)).
- Replacement of stores such as the removal of the cinemas and introduction of H&M in the Azrieli mall and the Azrieli Jerusalem mall.
- Operational streamlining in the management companies.

[9] Same-property NOI – NOI from similar properties that were held by the Group throughout all of the reported periods.

In the Company's estimation, the same property NOI in the malls and commercial centers segment in Israel was adversely affected primarily by:

- Temporary vacation of leased properties in order to perform changes in the tenant mix (in Azrieli Hanegev mall).

The balance of the assets of commercial centers and malls segment in Israel – amounted as of December 31, 2011, to the sum of approx. NIS 9.4 billion, compared with approx. NIS 8.4 billion on December 31, 2010. The increase results mainly from the completion of construction of Akko Azrieli Mall and Kiryat Ata Azrieli Mall as well as from the purchase of land for building Ramla Azrieli Mall and the commerce part in the Sarona Azrieli Center. All in addition to the adjustment of the value of the assets to their fair value according to valuations of an independent appraiser.

Profit due to the adjustment of fair value of investment property and investment property under construction of the segment –

The profit from the fair value adjustment of investment property and investment property under construction of the segment amounted in the Report Period to the sum of approx. NIS 555 million, compared with a profit of approx. NIS 776 million in the same period last year.

For details regarding transactions with respect to real estate during the Report Period and after the date of the financial statements, see Section 7.8 of Chapter A of the Report.

1.11.2 Office and Other Space for Lease Segment in Israel:

Summary of the segment's business results:

	For the three months ended		For the year ended	
	Dec. 31, 2011	**Dec. 31, 2010**	**Dec. 31, 2011**	**Dec. 31, 2010**
	NIS in millions			
Revenues	84	75	325	302
% change	12%		8%	
NOI	71	59	272	247
% change	20%		10%	

The increase in revenues derives mainly from revenues from office and other space for lease which was added to the Group pursuant to the purchase thereof and/or the finishing of construction and occupation thereof during 2010 and in the Report Period (especially the Givatayim offices and Tower E in Herzliya), an improvement in revenues from existing office space for lease, and the lease of vacant space.

Following is the development of the segment's NOI (NIS in millions):

	For the three months period ended		For the year ended	
	Dec. 31, 2011	**Dec. 31, 2010**	**Dec. 31, 2011**	**Dec. 31, 2010**
Due to the segment's assets owned by the Company at the beginning of the period in 2010[10]	71	59	272	247
Due to assets which were purchased or whose construction was completed in 2010	-	-	-	-
Due to assets which were purchased or whose construction was completed in 2011	-	-	-	-
Total	**71**	**59**	**272**	**247**

The NOI figure is one of the important parameters in valuations of income-producing property companies. For details regarding the manner of calculation of the figure, see Section 1.1.4 above.

The same property NOI in the office and others segment in Israel was favorably affected primarily by:

- A real increase in the rent at the time of renewal of contracts in the various properties (pursuant to option exercise by the tenants and/or execution of new contracts).
- Most lease contracts are linked to the consumer price index (which rose in the period of the report by 2.55% (known index)).
- Continuation of occupation of Tower E in Herzliya Business Park.
- Completion of construction of an additional office floor over the Givatayim Mall.
- Operational streamlining of the management companies.

The balance of the Group's investment property in the office and other space for lease segment in Israel – amounted on December 31, 2011 to the sum of approx. NIS 4.3 billion, compared with approx. NIS 3.4 billion on December 31, 2010.

The increase derives mainly from the adjustment of the properties' value to the fair value thereof according to valuations of an independent appraiser.

Profit from adjustment of fair value of investment property and investment property under construction, of the segment –

The profit from the fair value adjustment of investment property and

[10] Same-property NOI – NOI from similar properties that were held by the Group throughout the reported periods.

investment property under construction of the segment amounted, in the Report Period, to the sum of approx. NIS 218 million, compared with a profit of approx. NIS 109 million in the same period last year.

For details regarding transactions with respect to real estate during the Report Period and after the date of the financial statements, see Section 7.8 of Chapter A of the Report.

1.11.3 Income-producing property segment in the USA:

Summary of the business results of the segment:

	For a period of three months ended on		For the year ended on	
	December 31, 2011	**December 31, 2010**	**December 31, 2011**	**December 31, 2010**
			NIS millions	
Revenues	29	8	102	35
Percentage of change	262%		191%	
NOI	12	6	48	21
Percentage of change	100%		129%	

The increase in revenues derives mainly from revenues of office and other space for lease which were added to the Group due to their acquisition during the Report Period (the three office buildings at Galleria), from the improvement of revenues from existing office space for lease and the lease of vacant space.

Following is the development of the segment's NOI (NIS in millions):

	For the three months period ended on		For the year ended on	
	Dec. 31, 2011	**Dec. 31, 2010**	**Dec. 31, 2011**	**Dec. 31, 2010**
Due to the segment's assets owned by the Company at the beginning of the period in 2010[11]	4	6	19	21
Due to assets which were purchased or whose construction was completed in 2010	-	-	-	-
Due to assets which were purchased or whose construction was completed in 2011	8	-	29	-
Total	**12**	**6**	**48**	**21**

The NOI figure is one of the important parameters in valuations of income-producing property companies. For details regarding the manner of calculation

[11] Same-property NOI – NOI from similar properties that were held by the Group throughout the reported periods.

of the figure, see Section 01.1.4 above.

The same property NOI in the income-producing property segment in the USA was favorably affected mainly from:

- Increase in the American exchange rate (which increased during the report period by 7.67%).

The same property NOI in the income-producing property segment in the USA was adversely affected primarily by:

- Increase in the operation expenses.

The investment property balance of the Group in the segment – totaled on December 31, 2011 in the amount of approx. NIS 1.1 billion compared with approx. NIS 0.3 billion on December 31, 2010. The increase mainly derives from the purchase of three office buildings (Galleria) in Houston, Texas, USA.

Profit from the adjustment of fair value of investment properties of the segment -

Profit from the adjustment of fair value of investment properties of the segment totaled during the report period to the amount of approx. NIS 76 million, compared with a profit of approx. NIS 7 million, in the same period last year.

For detail regarding transactions pertaining to real estate properties during the report period and after the date of the financial statements, see Sections 7.8, 10.9 and 10.10 of Chapter A of the Report.

1.11.4 Granite Segment

The Company's share (without rights which do not confer control) in the Granite segment results amounted, in the year ended on December 31, 2011, to a profit of approx. NIS 5 million, compared with a profit of approx. NIS 20 million in the same period last year.

Following is a summary of data from Granite's consolidated statement : (NIS in millions)

	For the year ended on		Increase
	Dec. 31, 2011	Dec. 31, 2010	
	NIS in millions		%
Revenues	6,305	5,252	20%
Operating Profit	208	211	(1%)
Net Profit	39	56	(30%)

Summary of Granite's business results:

The main rise in Granite's revenues during the Report Period compared with the same period last year derived from: (1) an increase in sales in the field of the oil distillates; (2) "Sogood" chain of convenience stores - recorded an increase in sales; (3) an increase in the quantities sold by Supergas and in the prices of LPG; (4) an increase in the quantities of the paint and materials for the end-of-construction which were sold in the local market, and for export, and from the new activity in the field of gypsum; (5) a rise resulting mainly from the desalination facility Via Maris.

Gross profit

Granite's gross profit amounted in the year ended on December 31, 2011 to a sum of approx. NIS 1,101 million, compared with approx. NIS 1,084 million in the same period last year. An increase at a rate of approx. 1.6% during the Report Period which was influenced mainly by: (1) At the fueling and commerce complexes the gross profit decreased as a result of a decrease in quantities and a decrease in margins, including due to a decrease of the supervised marketing margin of the fuel in the gas stations, Since September 2011, according to an Amendment of the Order for Supervision of Maximal Prices at Fueling Stations. The decrease was set-off by the positive effects of the increase in inventory profits[12] (which amounted to approx. NIS 8.5 million compared with approx. NIS 7.6 million last year) and of the increase in the profit of the convenience stores in the Sogood in a sum

[12] Inventory profits/losses are profits or losses created due to price changes in the purchase of oil distillates, due to the amount of distillates in stock. Profits are recognized upon the realization of the inventory while losses are recognized on the price change date.

of approx. NIS 10.3 million. Sonol initiated several actions in order to reduce the negative effects of decreasing the marketing margin, *inter alia*, reducing the discounts granted to customers and other streamlining actions.

(2) In direct marketing an increase in profit was recorded, mainly due to the increase in the quantities of diesel oil sold and due to the increase in inventory profits (totaled at approx. NIS 4.5 million compared with approx. NIS 1.0 million last year).

The gross profitability in the distillates segment was favorably affected from the decline in the exchange rate of the dollar, which is the purchase currency of oil distillates. Granite protects against such changes through future currency transactions that are performed as economic protection. The results of the transactions are included in the finance item and offset most of the effect of the exchange rate changes.

(3) In Supergas the gross profit grew at a rate of approx. 10% compared with the same period last year due to the increase in the LPG sold, although there was a decline in the marketing margins. In the business in the solar field, Supergas recorded this year for the first time an immaterial profit.

(4) In Tambour – the gross profit grew at a rate of approx. 8% compared with the same period last year, mainly due to the increase in amounts of paint and complementary products and due to the new business in the gypsum field.

(5) In GES – the gross profit grew at a rate of approx. 36% compared with the same period last year, mainly due to the influence of Via Maris and due to the increase in profit in the Projects segment.

Sales, general and administrative expenses

In 2011 selling, general and administrative expenses in the Granite segment amounted to approx. NIS 895 million compared with approx. NIS 899 million in last year.

1.12 Note with regard to forward-looking information

The Company's intentions mentioned in the introduction of the board of directors' report, the main emphases to the Report and in Sections 1.1 through 1.5 of the board of director's report, *inter alia*, in connection with taking advantage of business opportunities and expansion of the activity, liquidity, sources of financing, progress of the projects under construction and pertaining to the possibility of conversion of the short-term debt into long-term debt; are forward looking information, as defined in the Securities Law, 5728-1968, which is based on the Company's plans as of the date of the Report, the Company's estimates in respect of market developments, levels of inflation and the anticipated cash flows, and on the conditions of and possibilities for raising credit on the date of the Report. Such estimates may not be realized, in

whole or in part, or may be realized in a materially different manner than such which the Company estimated. The main factors which may affect the same are: changes in the capital market which will affect the conditions of and possibilities for raising credit, changes in the Company's plans, including use of liquid balances which will exist, for purposes of taking advantage of business opportunities, changes in the merit of holding various investment channels or in the merit of using various financing channels, and the Company or any of the Group's members encountering financing or other difficulties, in the manner which will have an effect on the Company's cash flow.

2. Qualitative Report on the Exposure to and Management of Market Risks

2.1 General

Risk management at the Company and the held companies in the Group is determined and performed directly by their managements.

The following specification pertains to the Company and subsidiaries wholly owned thereby as well as to material held companies of the Company whose exposure to market risks may materially affect the Company.

2.2 The Person Responsible for Market Risk Management

The person responsible for market risk management at the Company is the Company's CFO, Mr. Yuval Bronstein. For details on his education, qualifications and business experience, see Chapter D – Additional Details on the Corporation - of this Report.

2.3 Description of Market Risks

The main risks at the companies of the Group are mainly those specified below:

Exposure to fluctuations in market value of held and other companies

The Company has a material holding in the shares of Bank Leumi, whose shares are traded on the stock exchange.

Changes in the rates of the said security may affect the equity, cash flows and value of the Company. Such changes may also have an effect on parameters which are taken into account by the rating companies. The Company does not usually protect against such exposures.

The Company's holdings in Granite, whose shares are traded on the stock exchange, are long-term and are not presented in the balance sheet at their fair value, and are therefore not affected by market cap fluctuations.

Changes in interest rates

The Company and the companies held thereby have NIS loans with variable interest and are therefore exposed to changes in the bank interest in Israel. As of the date of the financial statements, the Group does not protect against the exposure to changes in the interest rates.

The Company's policy is to exchange some of the short term credit with long term loans according to the market conditions, when such is, according to its estimate, economically advisable.

The Company reviews from time to time the protection possibilities available on the market and the economic advisability thereof.

Exposure to a rise in the Consumer Price Index

A considerable portion of the Group's long-term loans and bonds are in NIS linked to the consumer price index in Israel. Therefore, a rise in the rate of the index may lead to a significant rise in the Company's financing expenses.

As of the date of the financial statements, the Group has surplus liabilities linked to the price index in the sum of approx. NIS 3,912 million.

The majority of the Group's income in the income-producing property segments is linked to the consumer price index, such that a rise in such index leads to an increase in income from rent and reduces this exposure. In addition, a rise in the rate of the index affects the calculation of the value of the Group's investment property such that a rise in the index usually leads to an increase in the value of the investment property. Granite partially protects its index-linked surplus liabilities by buying forward contracts written on the consumer price index according to an outline that shall have received the approval of the balance sheet committee and the approval of its board of directors. For further details see also Note 39C to the financial statements.

Changes in exchange rates

The Company's financial statements are prepared in the currency of the main economic environment in which it operates – NIS. However, the Company has business and transactions which are performed in a different currency, therefore, the Company is exposed to a financial exposure in respect of changes in the exchange rates.

The Company is exposed to changes in exchange rates of foreign currency within the framework of its assets abroad, an exposure which derives both from the current operations abroad and from the financing methods of the investments thereof abroad (mainly to USA Dollar).

In addition, there are exchange rate risks at Granite. Most of Granite's income in the field of oil distillates is in NIS, and conversely, a considerable portion of its costs are in dollars. Granite's policy is to hedge the material currency exposures. As part of Granite's efforts to protect against the balance sheet exposure, Granite applies a policy of balancing in the field of oil distillates between its dollar assets and its dollar liabilities, including off-balance sheet liabilities, *inter alia* by financing dollar assets with dollar credit. For protection against Granite's cash flow exposure in the field of oil distillates, Granite uses financial instruments. For further details, see also Annex B to this Report.

As of the date of the financial statements, the Group has surplus foreign currency-linked liabilities in the sum of approx. NIS 987 million.

Indirect Exposure to Changes in the prices of raw materials

A significant part of Granite's inventory comprises oil distillates. The prices of the oil distillates of the products in Israel are updated once a month and are

based on CIF Lavera port, Italy prices (average price of the distillate in the Mediterranean basin on the dates determined towards the end of each month). From inquiries made by Granite through outside consultants it transpires that the global financial instruments market does not currently offer an appropriate protection instrument for such prices, such that Granite has no effective possibility of hedging its risks in respect of changes in the prices of oil distillates. Therefore, as part of the risk management policy, Granite is not taking action to hedge this exposure but is acting to reduce the quantities of the exposed inventory. Moreover, each month, Granite adjusts the quantities of the oil distillates inventory in accordance with the sales forecast so as to minimize the inventory which is exposed to fluctuations.

Granite examines, from time to time, the protection mechanisms available on the market and the degree of effectiveness thereof.

It shall be stated that the exposure to changes in the prices of oil distillates mainly affects profits or losses from the holding of inventory. The distillates which are bought and sold during the month are not exposed to this risk since the purchase and sale prices are determined each month on the same basis. The continued increases in the prices of oil distillates in the period from the end of the Report year until the Report Release Date is expected to positively affect the gross profit in Sonol due to inventory profits. Granite retains outside consultants for current examination of the said exposures and the hedging thereof. The balance sheet committee of the board of directors of Granite holds discussions on the issue and monitors the exposures and the protection policy according to the outline determined.

Regulatory Risks

The Group is affected by regulatory changes which may occur from time to time regarding its products and business, including supervision over product prices, the water desalination issue, quality of the environment and so forth.

On August 31, 2011, Sonol received an Amendment to the Supervision Order of Maximal Prices at Fueling Stations, according to which the marketing margin for 95 Octane gasoline was reduced from September 1, 2011.

On July 22, 2010 an Amendment for the Fuel Sector (Competition Promotion) Law was approved, pertaining to the imposition of a duty on the fuel companies to install a general automatic fueling system which allows fueling with all of the fuel companies, while the fueling shall be carried out with any company with whom the customer had executed an engagement contract. On October 23, 2011 regulations were published for implementation of such law, imposing, *inter alia*, a prohibition on the fueling companies to unreasonably refuse an engagement with a customer in an agreement for the purchase of fuel.

In September 2011, the Committee for Change in the Social-Economic priorities (Trachtenberg Committee) filed its recommendations, including, *inter alia*, recommendations for immediate release of several fueling stations from their obligation to the fuel companies, for implementation of the use of a

universal automatic fueling system, for implementation of immediate supervision on transportation diesel oil prices, for examination of a mechanism requiring the sale of stations to small companies, for the imposition of supervision on the LPG prices and for the establishment of a team for examination of a reform in the LPG industry.

In December 2011 the Electricity Authority decided on a gradual rate decrease for the electricity outputs from facilities for production of electricity through solar technology. Similarly to equivalent activity of regulators in other countries based on decrease in prices of the construction and operation costs of photo-voltaic facilities.

Fluctuations in the prices of securities and market value

As aforesaid, upon completion of the IPO pursuant to the Prospectus and the Private Placement of the Company's shares, during the month of June, 2010, the Company began managing the IPO proceeds in accordance with the policy and restrictions announced by the Company in Chapter V of the Prospectus and in the immediate report dated August 29, 2010 (ref. 2010-01-601578). Since the IPO date and during the report period, and until investments made with the IPO proceeds and the Company's other means as specified in Regulation 10C in Chapter D of this Report, part of the IPO proceeds were invested in marketable securities, and therefore the Company might have been exposed to fluctuations in the securities' prices and the market value of its investments therein, which may affect the value of the managed portfolio, the cash flow and the liquid means of the Company. In addition, a small part of the funds are managed overseas in the Canadian dollar currency, and the Company may therefore be exposed to fluctuations in the currency exchange rates. As a rule, and other than as specified by the Company in the Prospectus, the Company does not take protective action against such exposure. For further details see also Note 39 of the financial statements attached to this Report.

2.4 The Company's Market Risk Management Policy

The person responsible for market risks, together with the Company's managers examine the market risks in the field of interest, index and exchange rate and act to reduce the financial exposure to these risks, whilst examining cost-benefit considerations, such as changes in the composition of long-term and short-term bank credit.

The Company's risk management policy as specified above is implemented for the Company itself and its subsidiaries, with the exception of Granite which determines its risk management policy independently. During 2011 Granite used derivative financial instruments for protection of its surplus exposure. See Annex B of this Report.

2.5 Means of Supervision and Implementation of the Policy

The finance committee and the board of directors deliberate, at least once every quarter, the Company's exposures to market risks and the actions which

the Company's management has taken, and insofar as required determines quantitative criteria and limitations. With respect to management of the IPO proceeds and the uses made thereof, see Regulation 10C in Chapter D of this Report. The Company's management examines the control procedures on a current basis and updates the same in accordance with the scope of the business and the risk deriving from the business.

2.6 **Positions in derivatives**

For details see Annex B of the board of directors' report.

2.7 **Analysis of sensitivity tests and fair value effects of protection transactions, exchange rates, interest and financial instruments**

In accordance with the main market risks specified above and in accordance with the provisions of the Second Schedule to the Regulations, the Group is performing sensitivity tests regarding changes in market risks affecting the fair value of "sensitive instruments". For details see, Annex A attached hereto.

2.8 **Linkage bases table**

See Note 39C to the financial statements.

3. Corporate Governance Aspects

3.1 Report on Directors with Accounting and Financial Expertise

On August 24, 2010 the Company's general meeting approved the office of Prof. Niv Ahituv as an expert outside director with accounting and financial expertise. After the Company's becoming a public company, the Company's board of directors determined, considering, *inter alia*, the Company's type, its size, the scope of its business and its complexity, that the minimum number of directors required on the board of directors who are required to have "accounting and financial expertise", as defined in the Companies Regulations (Conditions and Tests for a Director with Accounting and Financial Expertise and for a Director with Professional Qualifications), 5766-2005, is one director (in addition to an outside director with accounting and financial expertise). In the Company's opinion, considering all of the relevant circumstances as specified above, the minimum number determined as aforesaid allows the board of directors to meet the duties imposed thereon pursuant to law and to the incorporation documents, particularly with respect to its responsibility for checking the Company's financial position and for preparing the Company's financial statements.

As of the date of the Report, two (2) directors, on the basis of whose education and experience, as they declared before the board of directors, have accounting and financial expertise, hold office on the Company's board of directors: Mr. Joseph Ciechanover and Prof. Niv Ahituv (outside director).

For further details, including the education, qualifications and business experience of the Company's directors, see Chapter D – Additional Details on the Corporation - of this Report.

3.2 Independent Directors

As of the date of approval of the financial statements, except for the outside directors, another independent director (as such term is defined in the Companies Law, 5759-1999), Mr. Joseph Ciechanover, of whose classification as an independent director was approved by the Company's audit committee and board of directors on May 25, 2011, serves at the Company. The Company has not adopted a provision regarding the rate of the independent directors in the corporation in its articles.

3.3 Outside Directors

As of the date of the Report, two (2) outside directors hold office at the Company – Messrs. Efraim Halevy and Prof. Niv Ahituv. For further details, including the education, qualifications and business experience of the directors at the Company, see Chapter D of this Report.

3.4 Compensation of Senior Officers

Within the meeting held on March 21, 2011 by the board of directors for the approval of the financial statements for the year 2011, the board of directors

extensively discussed the compensation and/or management agreements of each of the senior officers and interested parties in the Company, according to the requirements of Regulation 21 of the Regulations, as detailed in Chapter D of this report. For the purpose of the aforesaid review, the board of directors had considered the relevant compensation and management agreements, the data forwarded ahead of time in relation to each of the Company's relevant officers and interested parties (as detailed below), the relevant sections of the law, including Regulation 21 of the Regulations and legal position no. 101-13 of the ISA dated February 13, 2011 pertaining to the quality of the disclosure required as per Regulation 10(b) (4) of the Regulations.

For the purpose of the discussion, the board of directors reviewed the overall data presented to it regarding each of the officers, while relying on all previous discussions held during the said year, in which the board was given opportunities to closely review the Company's officers' contribution to its business and achievements.

The members of the board approved the view of the audit committee which had determined that the review of the connection between the reasonableness and fairness of the compensation given to all officers in 2011 and their contribution to the Company shall be made, *inter alia*, by the following criteria:

The officer's contribution to the Company's business and profits;

The valuation of his performance and contribution by the chairman of the board and/or the CEO;

The importance of preserving a skillful management backbone with unique expertise, and the position of the said officer within this policy.

The level of the officer's responsibility, its scope and complexity;

Changes in circumstances related to the position and the scope of responsibility during the last year, so far as such changes occurred;

Special challenges of importance to the company, with which the officer dealt during the year.

Within the review of all the above criteria, the board of directors considered the significance of major events in the Company's business during 2011, beyond the extensive ongoing activity over the years, events which contributed to larger and fuller scopes of activity than before. Among others, the following events were reviewed: the opening of the two new malls in the North – Azrieli Akko mall and Azrieli Kiryat Ata mall, the negotiation and maturation of a huge project in South HaKirya in Tel Aviv (Azrieli Sharona center) following the winning of the tender on behalf of the Israel Land Council, as well as the negotiation for the purchase of Ir Yamim mall in the south of Netanya, a large transaction which the Company's management decided not to materialize due to the Company's disagreement with the conditions imposed by the Anti-trust authority. At the same time, 2011 was a year of regulatory changes following

legislation by the Knesset and accordingly special input was required of the members of the Company's management in order to confront the reality taking shape on the level of the Company's conduct as a publicly traded company. All the above greatly influenced the scopes of performance of all senior officers reviewed within this discussion, and therefore, as per their request, the members of the audit committee and thereafter the members of the board of directors, received in advance all relevant data in relation to each of the officers, including the management's analysis and position regarding the qualifications and contribution of each of them. Following the discussions by the audit committee, the board of directors reviewed the decisions made regarding the bonuses approved for some of the officers for 2011, within discussions previously held.

The audit committee recommended to the board of directors to place importance on the basic common rule "Pacta sund servanda" (agreements must be kept) and any desire to deviate therefrom shall be followed only upon weighty reasons. The Company's business and corporate culture, as designed along the years, even prior to the Company's becoming a public company, put special emphasize on fairness and honesty in its interactions with both customers and people in its service, a culture which had allowed the Company's owners and managers to lead it to its current position. The outcomes of this culture are reflected in the rate of leverage, significantly lower than the rate customary in companies of the same size as the Company.

The management agreement of the chairman of the board of directors, through companies under his control, was presented to the members of the audit committee and board of directors, and its details were reviewed. The audit committee reported to the board of directors that it is satisfied that since the approval of the management agreement, with an emphasis on 2011, the scope of services rendered as per the agreement had grown, in light of both the Company's business development and the growth in income producing properties and architectural and development projects, and that as per the Company's real business results the terms of the agreement, as determined in 2010 – upon its signature, are reasonable and fair.

In this context, the audit committee wishes to draw the board of directors' attention to the data presented before it by the Company's CEO regarding the level of profits for the year under review. During 2011 the State had sharply, significantly and immediately changed the policy of company taxation, while applying the said change within a short period of time. As a result, and considering the tax planning and calculation manners, the company had to record a loss of over NIS 600 million, and deduct this amount from its annual profits. The Company's achievements in 2011, prior to the aforesaid tax deduction (as well as after the said deduction), are significant and commendable. This fact was considered by the committee as a supporter of its principled view in relation to those heading the Company, and its senior management backbone.

In addition, a review was given to the board of directors of the plan for phantom options[13] which were granted to officers of the company and the subsidiaries thereof (except for Granite) concurrently with the IPO procedure and/or thereafter. In the opinion of the company's board of directors, the phantom bonus is a fair and reasonable mechanism under the circumstances and is accepted as an incentive and a means for increasing motivation in companies of the company's type. The graduated mechanism for vesting of the phantom units ties the compensation to continued contribution to the Company and to changes in the price of the Company's share over time, an necessarily strengthens the connection between the contribution of the offerees and the interests of the Company's shareholders. The board of directors stated regarding each of the officers, that the compensation to the said officers in 2011 was given considering the standing, position and contribution of each one of them and his contribution to the group's operations and business, relative to the company's achievements based on its results in 2011.

Following is the summary of the explanations of the Board of Directors:

Mr. Menachem Einan, Active Deputy Chairman of the Board –

For details regarding the compensation given to Mr. Einan, see Section 21 of Chapter D (Additional Details) of this report.

Until March 2011 and for 19 years, Mr. Einan served as the CEO of the group. For the whole duration of his office, including year 2011, he acted to increase the scope of its operations and expand its business, led many moves of the group, including the restructuring of the Group, the acquisition of the financial holdings in Leumi Bank and Leumi Card and a unique and significant IPO process which were efficiently and successfully managed whilst continuing to manage a large company and lead it to continued growth in most of the relevant parameters and achievement of the goals determined. Since April 2011, Mr. Einan serves as an active vice chairman of the board, a position within the framework of which he is responsible for the strategic fields related to the continued business development of the Group, and the realization of the long term vision thereof. During the report year, which was significant and intensive he made a significant contribution in the strategic field, assisted and supported the integration of a new CEO for the Group, supported the new CEO in the continued expansion of the Company's business, initiation of new projects, promotion of existing projects and conduct vis-à-vis the toughening regulation.

The board of directors examined the growth in the scope of the group's business in 2011 and accordingly in the complex responsibilities of Mr. Einan and found that considering the aforesaid, taking into account the weight of the responsibility and degree of complexity of the position and changes which occurred in the Company and the scope of business thereof, the many

[13] For details regarding the granting of phantom units to employees of the company, including to the said officers, and for further details regarding the cost of the expense in respect of the granting of the options, including in respect of the share of the company's CEO, see Section 15.6 of Chapter A of the report and Note 25 to the financial statements in Chapter C of this report.

challenges faced thereby in light of the state of the economy in Israel, both in the social-political aspect and in the economic aspect, and against all of these, the results presented by the company, the compensation in respect of 2011 is reasonable, proper and fair.

Mr. Shlomo Sherf, CEO –

For details regarding the compensation given to Mr. Sherf, see Section 21 of Chapter D (Additional Details) of this report.

Mr. Sherf has been serving as the Company's CEO since April 2011, concurrently with material changes in the market condition and the social atmosphere (the Summer 2011 Protest), and the toughening regulation and the continued increase in the scopes of business and fields of complex responsibility of the CEO of the largest real estate group in Israel. During the report year, Mr. Sherf acted towards the increase in the scope of the operations and expansion of the business thereof, as well as realization of the Groups business strategy. Mr. Sherf led many strategic moves of the Group, including expansion of the activity abroad, completion of the construction of the two malls in the north of Israel and the opening thereof during Q3, winning the Southern Kirya tender and conducting the receipt of the authorizations and permits for commencement of construction as well as facing the toughening regulation. In 2011 Mr. Sherf led the Group's staff, acted successfully towards retaining the Company's management and retaining a talented and veteran team, and for the creation of motivation throughout the whole Group for continued growth and increase in most of the relevant parameters, and achievement of goals that were set.

The board of directors examined the scope of the responsibility and functioning required of Mr. Sherf in view of the increase in the regulatory requirements and the condition in the markets, the scope of projects under development and construction, the scope of the business in the Group and stated the contribution of Mr. Sherf to the Company and to the achievement of the goals presented to the board of directors.

The board of directors found that considering the aforesaid, the compensation in respect of 2011, including the phantom options component which ties the compensation to his continued contribution and changes in the price of the Company's share (and which, as of the date of the report, is significantly out of the money), is reasonable, proper and fair.

Mr. Yuval Bronstein, CFO –

For details regarding the compensation given to Mr. Bronstein, see Section 21 of Chapter D (Additional Details) of this report.

Mr. Bronstein manages the entire system of finance and accounting reporting in the group in accordance with the changing regulation. In the framework of his position, Mr. Bronstein manages the issue of raising the group's financing sources, management of its free funds and market risks, preparation for and

assimilation of the issue of the effectiveness of internal controls in the company until the required implementation thereof at the end of 2011, and accompanies all of the proceedings for acquisition of properties and financing of projects under construction.

The board of directors examined the growth which occurred in the scope of the responsibility and functioning required of Mr. Bronstein in view of the growth in the scope of the company's business, the increase in the regulatory requirements in connection with the accounting reporting and the internal controls systems, the relationship with the banking system in view of the condition in the markets and the relationship with the capital market which was added after the company's successful IPO. The board of directors stated the company's achievements in the IPO and in transactions in 2011 and Mr. Bronstein's significant contribution to this success and the meeting of the work plans' targets.

The board of directors found that considering the aforesaid, taking into account the scope of his authorities, the scope of operations and the complexity of the Group's operations, considering the condition of the markets and the Israeli economy and Mr. Bronstein's great involvement in significant processes which the company had undergone, the compensation in respect of 2011, including the phantom mechanism which ties the compensation to his continued contribution and to the company's results, is reasonable, proper and fair.

Mr. Peer Nadir, CEO of Azrieli Malls –

For details regarding the compensation given to Mr. Nadir see Regulation 21 of Chapter D (Additional Details) of this Report.

Mr. Nadir manages the Group's income-producing properties in the commerce centers and malls, at an overall scope of 254,416 sqm area for rent. During recent years, Mr. Nadir acted for maintaining an occupancy rate of 100% in the commerce centers and malls, including during the economic crisis years and the social protest period in 2011. The Company reached nice achievements in the mall sector under the management of Mr. Nadir, while successfully meeting the objectives of continued growth in NOI figures as stipulated in the work plans.

The board of directors examined the growth which occurred in the scope of responsibility and functioning required from Mr. Nadir in light of the increase in the scope of operations of the Company. Mr. Nadir has contributed to the NOI results of the Group and to the constant growth presented thereby in recent years in general and in 2011 in particular. In the end of August 2011 and the beginning of September 2011, the Company opened two malls in Akko and in Kiryat Ata which were constructed and marketed within a significantly shorter period than that taken into account in the Company's budget from the beginning of the way, resulting, according to the Company's board estimate, especially due to unusual efforts and special skills demonstrated by Mr. Peer Nadir regarding a record marketing of the stores in

the said malls and the opening thereof at an occupancy rate of over 85%. In addition, in light of the social protest and the government committees established in order to make recommendations regarding the economic-social situation in Israel, Mr. Nadir was required to face difficulties of lessees at a much larger scope than in previous years.

The board of directors found that considering the aforesaid, taking into account the scope of authorities thereof, the scope of the complex operations of the Group and considering the condition of the markets and the Israeli economy and Mr. Nadir's great involvement in significant processes which the company had undergone, the compensation in respect of 2011, including the phantom mechanism which ties the compensation to his continued contribution and to the company's results, is reasonable, proper and fair.

Compensation to interested parties of the company:

The management agreement with companies controlled by David Azrieli, chairman of the board of directors and the controlling shareholder:

For details regarding the compensation given to the management companies controlled by Mr. Azrieli and the terms and conditions of the agreement and the methods of approval thereof, see Section 21 of Chapter D (Additional Details) of this report.

In considering the performance of David Azrieli during 2011, in view of the data required as per Regulation 21 of the Regulations, and the criteria set by the audit committee and the board of directors, the audit committee had diligently reviewed the evaluation of the managerial and professional skills of the Company's founder and chairman during its 30 years of existence, his contribution to the Company in 2011 and the estimation of reasonableness and fairness of the compensation given to him in 2011, prior to forming its recommendation to the board of directors.

It would not be superfluous at all to note that for thirty years, since its foundation, the chairman is leading the group, and for over a quarter of a century he is forming its vision and manner of conduct. His attitude can be evidenced, inter alia, by the fact presented to us that the company never distributed dividend prior to becoming a public company, and its coffers were used for the Company's investments with the goal of magnifying its activity and allowing it to credit itself for the construction of malls which turned into icons in the Israeli landscape, including, *inter alia*, the first mall in Israel, Azrieli Ayalon mall, Azrieli Jerusalem mall (Malcha) and the Azrieli center in the heart of the city of Tel Aviv.

From the early days to this date, the chairman is involved, way beyond his duty as a chairman of the board, in the formation of the Company's strategy and the guidance of its management towards achieving the various goals expanding over the years. His daily involvement in the details of planning, and specifically in the architectural aspects which are the core of the business, are a rare asset of the Company. His expertise and long experience keep serving

the company as they did in previous years and it is clear that he is essential to the Company.

The chairman's significant contribution to the Company grew further in 2011 due to the materialization of some of the projects which were successfully completed, as well as the initiation of new moves in the area of real estate overseas, where an evident acceleration is recognized. Above all, the chairman's courage was evident in his decision, together with the other leaders of the Group, to participate in the tender of "South Hakirya", which the Company had won. The project of "South Hakirya" is a huge project which required strategic business consideration side by side with careful consideration of the Company's ability to take on another project of this large scale and capital investment-intensity. At the same time, the chairman kept fulfilling his responsibilities as the chairman of the board, lead its discussions and resolutions confidently, while strictly preserving the low leverage, a policy that is not common in the Israeli business arena.

In considering their position regarding the compensation to the chairman in 2011, the audit committee and board of directors deem fit to consider the following data: the reasonableness and fairness of the compensation were reviewed by the board of directors in 2010, prior to the Company becoming publicly traded. This issue was carefully discussed within the prospectus and the numerous discussions with the ISA staff. In light of the difficulty in identifying other companies whose value is similar to that of the Company, a review was made at the time of the prospectus according to comparative figures in similar companies regarding the ratio of the annual General & administrative expenses out of the total annual operational income.

In the discussion held by the audit committee on March 19 2012, and the discussion held by the board of directors on March 21, 2012, one of the facts considered was that material part of Mr. Azrieli's compensation is conditioned on the achievement of goals and is derived from the EBITDA which reflects the Company's results and potential over a long period of time in a good way. The committee recommends to adhere to the terms of the agreements, which were evaluated as reasonable and fair at the time of their determination, without protest by anyone.

Among its considerations, the audit committee and board of directors insisted that the Company approved the compensation of last year whole heartedly, that the volume of activity and gravity of decisions required exceeded in 2011 in comparison to those of last ear; that the business in 2011 was carried under unstable conditions in the market on the whole which drove a number of leading companies into material difficulties, whereas the Company again excelled this year in extraordinary financial solidity. The Company's profits in this problematic year still enable it to distribute dividend, in spite of the major decrease in profit which was caused, by a significant amount, by the sudden legislative change in relation to the cancellation of companies' tax reduction.

These achievements in themselves are significant. Mr. Azrieli holds a signed and valid agreement, and as per Amendment 16 of the Companies Law 5759-1999 it will expire in May 2013. The audit committee and the board of

directors resolved that no reason was found to deviate from the agreement in a year in which the qualities and contributions of the chairman were especially evident, specifically in light of the fact that the total amount of compensation to Mr. Azrieli in 2011 is approx. NIS 4 million lower that the compensation to which he was entitled in 2010.

Due to the aggregate weight of all these considerations, which are all based in clear business data, the audit committee and the board of directors saw fit to confirm that Mr. Azrieli's compensation for 2011 is fair and reasonable, just and right. The audit committee and board of directors noted that they are aware that the compensation to which Mr. Azrieli is entitled is relatively high in comparison to companies with similar equity, but beyond the fact that the clear source of the compensation is in a duly approved valid agreement, it reflects the unique contribution of Mr. Azrieli to the Group, its business and impressive development which is hard to compare to other similar officers in companies of similar scopes. The board of directors and the audit committee noted that Mr. Azrieli benefits the Company on a daily basis, and successfully builds a team of highly qualified, honest, effective and loyal people, and is leading the entire enterprise towards further achievements, while this activity boosts the national economy in this time which is characterized by no little uncertainty.

Ms. Danna Azrieli, Active Vice Chairman of the Board (not included in the five highest compensation receivers in the Company) –

For details on the compensation given to Ms. Azrieli and the terms of the agreement and the manner of approval thereof, see Section 21 of Chapter D (Additional Details) in this report.

Danna Azrieli, has legal education and has been managing her areas of responsibility with great success for many years already, through constant investment and coping with changing conditions Ms. Azrieli invests and contributes extensive working input and assists the chairman of the board and the CEO in forming the Group’s strategy and policy, in business development, in projects under development and construction and in the transactions examined in the framework thereof and the corporate responsibility. , Ms. Azrieli acted tirelessly for the benefit of the Company and in 2011, her investment in the significant procedures undergone by the Company was apparent, including involvement and leadership in strategic proceedings, participation and involvement in management meetings and managerial meetings of the Group’s 13 malls. In 2011 Ms. Azrieli invested extensive resources in the Company’s relations with the Israeli and foreign capital markets, participated and preformed presentations for the promotion of the Company’s image and the strength thereof. Ms. Azrieli also managed the issue of the Group’s social involvement.

The board of directors noted that in view of the expansion of the Company’s scope of business, a significant addition of active malls and projects under construction, the changing regulation and the need for investment of extensive input in the Company’s relations with the market, as well as in light of the

changes in the market conditions, the authorities and areas of responsibility of Danna Azrieli since the date of approval of the compensation and until the end of 2011, which require involvement and investment of extensive input and resources, her contribution to moves which had a direct impact on the Company's results and achievements in 2011 was extensive.

Considering the aforesaid, the compensation for 2011 is reasonable, proper and fair.

Additional Directors at the Company

The Company's board and the audit committee further stated that the compensation granted to the other directors in the Company, who are not outside and independent directors, as specified in Regulation 21 of Chapter D (Additional Details) of this Report, are fair and reasonable considering the requirements of the duties of the directors in a large and complex company, and the scope of activity and responsibility required therefrom in the fulfilling of their duties.

3.5 **Internal Auditor**

In 2010 the Company adopted an internal audit procedure (the "**Internal Audit Procedure**"), the purpose of which is to define the status and fields of activity of the internal audit in the Company, and the ways and means for the fulfillment of its tasks. Such procedure was approved by the Audit Committee, in its meeting of November 15, 2010, and by the Company's board of directors, in its meeting of November 24, 2010.

Identity of the Internal Auditor

Mr. Gali Gana, CPA, was appointed to the position of the internal auditor of the Company and companies of the Group (with the exception of Granite) and began his service at the Company in December 2009.

Mr. Yaron Aloni acts as the internal auditor at Granite.

The Internal Auditor's Compliance with Legal Requirements

To the best of the knowledge of the Company's management, in accordance with the internal auditor's declaration, he meets the requirements of Section 146(b) of the Companies Law and the provisions of Section 3 and 8 of the Internal Audit Law, 5752-1992 (the "**Internal Audit Law**").

Holding of Securities of the Company or of a Body Affiliated therewith

As of the date of this Report, as the internal auditor informed the Company, he does not hold securities of the Company or a body affiliated therewith.

The Internal Auditor's Ties with the Company or with a Body Affiliated therewith

To the best of the knowledge of the Company's management, as the internal

auditor informed the Company, the internal auditor has no material business ties or other material ties with the Company and the internal auditor's other business ties do not create a conflict of interest with his position as internal auditor at the Company.

The Internal Auditor's other Positions at the Company

The internal auditor is an outside service provider to the Company on behalf of Rosenblum-Holtzman & Co., CPA. In accordance with the Internal Audit Procedure, the auditor and the audit employees shall have not other position in the Company in addition to the internal audit. As of the date of the Report, apart from his position as the Company's internal auditor, the internal auditor is not employed by the Company nor does he provide it with additional outside services.

Other Positions of the Internal Auditor outside of the Company

Mr. Gali Gana is a partner at the firm Rosenblum-Holtzman & Co., CPA.

Manner of Appointment of the Internal Auditor

Mr. Gali Gana was appointed to act as the Company's internal auditor by the Company's CEO in November 2009 after thorough examination of his education, qualifications and his many years of experience in internal audit within reference to the duties, authorities and roles imposed on the internal auditor by law. Mr. Gana was found to be appropriate to act as the Company's internal auditor, *inter alia* considering the scope of the Company's business and its complexity. In the framework of the Internal Audit Procedure that was approved by the Company's audit committee and board of directors in November 2010, from now the board of directors will appoint the internal auditor and determine his position and salary conditions.

Identity of the Internal Auditor's Supervisor

The internal auditor's organizational supervisor is, as of the date of the Report, the Chairman of the Company's board of directors, with coordination with the Company's audit committee.

The Audit Plans

According to the Internal Audit Procedure, the internal auditor submits a proposal for an annual work plan, in coordination with the Chairman of the board and the Company's CEO. The audit committee is required to discuss the plan and approve it and thereafter the plan is forwarded to the board for approval. The internal auditor's audit plan is an annual plan which derives from a multi-year work plan, *inter alia* according to the following considerations: a recently made mapping of operations, efficiency and savings potential, risks inherent in the Company's business, regulation and rules that apply to the Company and weaknesses that are currently visible to the Company's board, management or internal auditor.

The internal audit's annual work plan also includes performance of an audit of

the monitoring of implementation of the recommendations of the internal auditor and the audit committee by the Company's management. The audit is performed according to the plan under the supervision of the internal auditor, and is adjusted according to developments and findings which are discovered in the course of the audit. The work plan leaves the auditor discretion to change the issues audited, subject to the formal approval of the audit committee.

In the Company's board meeting of November 24, 2010, the audit plan for 2011 was approved after being presented by the auditor to the Company's board, following the audit committee's recommendation to approve the plan and in accordance with the multi-year plan.

At the Company's board meeting of March 21, 2012, the audit plan for 2012 was approved after being presented by the internal auditor to the Company's board, following the audit committee's recommendation to approve the plan and according to the multi-year plan.

Material Transactions

The internal auditor receives an invitation, including background material, to meetings of the Company's audit committee at which transactions are examined and approved, as stated in Section 270 of the Companies Law, 5759-1999. At his choice, after receiving appropriate details, he attends the meetings or receives updates thereon. In addition, the internal auditor receives, upon his demand, minutes of meetings of the Company's board of directors at which such transactions were approved. In 2011, the internal auditor examined transactions which were carried out in the Company pursuant to Section 270 of the Companies Law.

Audit of Held Corporations

The internal auditor also acts as the internal auditor of the subsidiaries in the Group, except at Granite Group.

With respect to the audit of corporations held by a material holding, the multi-year plan of the Company is intended to encompass the range of audit issues, once every few years in each materially held company in which an internal auditor had not been appointed, including abroad.

The Scope of Engagement of the Internal Auditor's

The scope of the internal auditor's engagement was approved by the audit committee in accordance with the audit plan that was approved thereby. In 2011 the internal audit hours at the Company and at the companies held thereby (with the exception of Granite) amounted to approx. 850 hours (all in respect of activity in Israel) by the internal auditor Gali Gana on behalf of accounting firm Rosenblum Holtzman, CPA. Management may expand the scope of engagement according to the circumstances.

The Company estimates that the scope of the internal auditor's work for 2011

is appropriate.

The scope of the hours for the audit work at the Company and at the subsidiaries was determined in accordance with the audit plan proposed by the internal auditor in cooperation with the management and approved by the audit committees of the various boards of directors. The annual scope of the audit plan at Granite Group amounts to approx. 650 working days of outsourcing, not including the working days of the internal auditor retained by Granite.

According to the Internal Audit Procedure, the office of the Company's internal auditor shall not exceed six years, unless the audit committee and the board adopted other resolution.

Guiding Professional Standards in Performance of the Audit

The internal auditor and his team perform the audit work while complying with necessary standards for the holding of a professional and reliable audit which is independent of the auditee. In accordance with information provided to the Company's management by the internal auditor, the audit reports are based on the audit's findings and the facts documented in the audit performed according to accepted professional standards in accordance with Section 4(b) of the Internal Audit Law, in accordance with the IIA's professional standards (standards series 1000 and 2000), according to the professional directives of the Israeli Institute of Internal Auditors. The board of directors relied on the internal auditor's reports regarding his compliance with the professional standards according to which he carries out the audit.

Free Access for the Internal Auditor

The Company's internal auditor has free access, after coordination, to documents, information and the relevant information systems of the Company and of held companies, including financial data, and independent status. With respect to held companies overseas, the Company's internal auditor carries out an audit based on reports that he receives from the subsidiaries' auditors overseas. The internal auditor undertakes to maintain in confidence, not to deliver to others and not make any use for himself or for others of any information pertaining to the Company.

The Internal Auditor's Report

The internal audit reports are submitted in writing and discussed on regular basis with the Company's management and CEO.

The dates on which a report was filed regarding the findings of the internal auditor to the CEO are: March 3, 2011, June 19, 2011, June 22, 2011, December 20, 2011, January 18, 2012, January 30, 2012 (2 reports) and on February 5, 2012.

The dates on which a discussion was held at the audit committee regarding the findings of the internal auditor are as follows: March 27, 2011, June 28, 2011 and February 22, 2012.

The Assessment of the Company's Board of Directors of the Internal Auditor's In the estimation of the Company's board of directors, the qualifications of the internal auditor and his staff, the scope, nature and continuity of the internal auditor's activity and his work plan are reasonable under the circumstances, and fulfill the goals of the internal audit at the Company.

The Internal Auditor's Compensation

The payment to the internal auditor of the Company and subsidiaries in Israel is made according to actual working hours and in accordance with the work plan approved by the audit committee and the progress in the audit work of each and every issue. At the beginning of each year, the auditor submits a proposal for an annual audit plan, which includes a planned framework of hours.

The audit committee determines the audit plan and the quota of hours. The auditor shall not deviate from the quota of hours without the approval of the audit committee. In the event that additional tasks shall be imposed upon the auditor in the course of the audit year – the audit committee shall determine the quota of hours for the additional tasks.

In 2011 the payment to the internal auditor and his staff amounted to the sum of approx. NIS 165 thousand (plus VAT). The cost of the internal audit at Granite Group for 2011, including the cost of outsourcing, amounted to the sum of approx. NIS 1,430 thousand.

In the Company's estimation, due to the fact that the compensation is on the basis of working hours, the said compensation does not affect the exercise of the internal auditor's professional discretion. The Company has determined the independence of the internal audit as an essential policy, and therefore the internal auditor is in no way dependant on the Company and the management thereof.

3.6 The Auditor

Identity of the Auditor

The chief auditors of the Company and the held companies (with the exception of Granite) are the accounting firm Brightman Almagor Zohar & Co., CPA (the "**Auditor**").

It shall be stated that the firm leases offices from the Company in Azrieli Center in Tel Aviv at amounts which are immaterial to the Company. However, in order to ensure that its independence is not prejudiced, the auditor (in the framework of an agreement with the ISA) took upon itself parameters to be examined from time to time in connection with the engagement, including in connection with the specificity of the terms and conditions of the lease agreement and non-modification thereof; fee agreements in writing and at market conditions; separation between the identity of the service providers and the decision makers in connection with the lease agreement; restrictions in

connection with settlement of accounts between the lease agreement and the services, and an agreement that in the event of disputes, the Auditor will act to terminate its office.

The Auditor's Fee

In 2010 and 2011 the auditors' fee in respect of audit services, audit-related services and tax services and in respect of consulting services was as follows:

2011:		**Audit Services, Audit-Related Services and Tax Services**		**Other Services**		**Total**	
Company	**Auditor**	**NIS in thousands**	**Hours**	**NIS in thousands**	**Hours**	**NIS in thousands**	**Hours**
Azrieli Group Ltd.	Brightman Almagor Zohar & Co., CPA	1,100	7,820	155	550	1,255	8,370
Azrieli Group Ltd.	Other auditors	-	-	205	850	205	850
Granite	Somekh Chaikin KPMG (auditors)	2,600	17,500	850	3,000	3,450	20,500
Granite	Other auditors	300	2,250	10	25	310	2,275
2010:		**Audit Services, Audit-Related Services and Tax Services**		**Other Services**		**Total**	
Company	**Auditor**	**NIS in thousands**	**Hours**	**NIS in thousands**	**Hours**	**NIS in thousands**	**Hours**
Azrieli Group Ltd.	Brightman Almagor Zohar & Co., CPA	1,548(*)	8,450(*)	42	15	1,590	8,465
Granite	Somekh Chaikin KPMG (auditors)	3,000	18,000	1,900	6,000	4,900	24,000
Granite	Other auditors	490	2,500	80	240	570	2,740

(*) Including fees due to prospectus. The expenses for the other services included mainly consultation regarding preparation for implementation of ISOX, approvals, tax assessments hearings, tax counseling and varied guidance.

Determination of the Auditor's Fee

The Company's board of directors, after receiving the recommendation of the Company's audit committee, was authorized in the Company's articles of association to determine the fee of the auditor. The fee is determined on the basis of the required work and past experience, while adaptation thereof to

changes in regulation and scope of work, the development of the Company and events which occurred during the passing year. Accordingly, the Company's board of directors approved, on November 23, 2011, the auditor's fee for 2011, after accepting the audit committee's recommendation.

3.7 **Negligible Transaction Classification Procedure**

3.7.1 On November 24, 2010, the Company's board of directors decided to adopt guidelines and rules with regard to the classification of transactions which are not irregular, of the Company or a consolidated company thereof, with controlling shareholders or its interested parties, as a negligible transaction. Such guidelines were determined, *inter alia*, while considering the scope of the Company's assets, the variety of its activities, the nature of the transactions performed thereby and the level of their effect on the Company's business and results.

Such rules and guidelines will serve, on the one hand, to examine the need for certification of the transaction by the relevant institutions of the Company, and on the other hand, to examine the duty and/or scope of the disclosure in the periodic report and the prospectus (including in shelf offering reports)[14], and/or issuance of an immediate report in respect of such transaction[15]. It shall be clarified that nothing in this procedure addresses transactions of public companies which are held by the Company, *inter alia*, since they themselves are reporting companies, and the Company will report in accordance with their reports, if and insofar as necessary, pursuant to the law.

The Company's board of directors determined that a negligible transaction in the Company is a **transaction which is not irregular**[16] (in other words – it is performed in the course of ordinary business, in the Company's best interests, and under market conditions) with controlling shareholders and/or another person in which the controlling shareholder has a personal interest, if it fulfills the following tests:

1. For purposes of the duty of issuing an immediate report – a single negligible transaction in the Company or in a subsidiary controlled thereby, does not exceed 0.1% of the Company's consolidated equity pursuant to the latest financial statements; in case of on-going transactions (including rents, leases, etc.), according to the monthly transaction amount or the total transaction amount for the entire engagement period, whichever is shorter/lower. For purposes of an immediate report, the negligibility of a transaction shall be examined based on the

[14] With regard to a transaction with a controlling shareholder or which the shareholder has a personal interest in approval thereof as determined in Regulation 22 of the Periodic Reports Regulations and in Regulation 54 of the Securities Regulations (Details of the Prospectus and Prospectus Draft – Structure and Form), 5729-1969

[15] As determined in Regulation 37(a)(6) of the Periodic Reports Regulations.

[16] It is clarified that a transaction which is not in the ordinary course of business or which is not under market conditions or which may have a material effect on the Company's profitability, assets or liabilities, will not be classified as a negligible transaction.

single specific transaction, and insofar as the same shall exceed the negligibility threshold, the Company shall report the transaction in an immediate report.

2. For purpose of providing specifications in the annual report – the total sum of all of the transactions of a specific type in the Company or in a subsidiary controlled thereby, in a calendar year, did not exceed the 0.5% of the Company's consolidated private equity pursuant to recent annual reports. The Company shall include the types of transactions and their aggregate amount in its annual report only if the sum total exceeds the rate indicated above. For purposes of reporting in the periodic report, financial statements and prospectus (including shelf offering report), the negligibility of the aggregation of all transactions of the same type of the Company with the interested party or corporations under the control of an interested party, shall be examined on an annual basis.

When classifying transactions as negligible, each transaction shall be examined in itself, but the negligibility of transactions which are combined or interdependent or transactions of the same type, shall be examined in the aggregate as a single transaction. In respect of multi-annual transactions (agreements for a period of several years), the scope of the transaction will be calculated for purposes of examining the negligibility threshold, on an annual basis (namely, the annual monetary amount which derives from the transaction exceeds such negligibility threshold). In insurance transactions the premium shall be examined as the transaction amount, irrespective of the insurance coverage provided. Multi-annual insurance transactions shall be measured based on the annual insurance fees, which are paid or collected.

The transactions that were classified as negligible by the Company's held companies shall be deemed as negligible also at the Company's level, whereas those classified thereby as non-negligible, shall be examined at the Company's level. In the event that the Company has no available information that enables examination of the classification of the transactions that were classified thereby as non-negligible, as negligible transactions, then the conjunction of all of the transactions of the same type shall be deemed as a negligible transaction, unless in view of the data known to the Company, one of the two conditions has occurred: (1) From the point of view of the above quantitative parameters, the transaction itself as a single transaction is not negligible; (2) The aggregation of the transactions is material to the Company.

Notwithstanding the aforesaid, a quantitative examination of the qualitative considerations of a negligible transaction may lead to the classification thereof as a non-negligible transaction, if in view of its nature, essence and effect on the Company it is conceived as a significant event by the Company's management and serves as a basis

for the making of important managerial decisions or if in the framework of an interested parties transaction, the interested parties are expected to receive benefits, reporting of which to the investing public is important. It is clarified that even if an interested party transaction has met the quantitative test below, it would not be deemed negligible if such qualitative considerations attest to a material aspect thereof.

The certifying function

Pursuant to Section 22.3 of the Company's articles of association, the board of directors has determined that the examination of the classification of an interested party transaction as a negligible transaction shall be made by the CFO and the Company's secretariat together with legal counsel, if required, and in every certification of a transaction as a negligible transaction, the process of examination and classification shall be documented.

In addition, the board of directors authorized the Company's CEO, or the CFO, to certify performance of transactions which are not irregular (and which are not related to terms of office and employment, including exemption, insurance or indemnification), including transactions that comply with the definition of negligibility pursuant to this procedure (provided that both of them do not have personal interest in such transactions, since in such case the chairman of the audit committee shall authorize the transaction, provided that the transaction does not concern the terms of office and employment of an officer).

Supervision and control:

Every year the audit committee shall review the manner of the application of the provisions of this procedure by the Company and shall make a sample examination of transactions that were classified as negligible transactions pursuant to the provisions of the procedure. In the framework of the sample examination, the audit committee shall examine, *inter alia*, the prices determination methods and the other transaction conditions, as the case may be, and shall examine the effect of the transaction on the Company's business condition and operations results. In the periodic report, the Company shall include a disclosure regarding the holding of the review, the manner of performance of the examination, and the results and conclusions thereof. For details regarding transactions examined by the audit committee as aforesaid, see Chapter D – Further Details, of this Report.

The Company's board of directors shall examine the need to update this procedure from time to time, in consideration of the interested party transactions in which the Company engages, material changes in the Company's scope of operations and the relevant financial data and changes in the relevant provisions of law.

After discussion of the implementation of the provisions of negligible

transactions procedure and review of the consideration of the negligible transactions executed in 2011 and their other characteristics compared with the market conditions, held on March 19 and March 21, 2012, respectively, the audit committee and the board of directors determined, that all of them were carried out at arm's length and may not materially affect the business condition of the Company and the business results thereof. They also determined that all of the transactions reviewed as aforesaid, were found as transactions that comply with the definition of a "negligible transaction" according to the Company's procedure regarding negligible transactions, and that such procedure was properly implemented by the Company.

3.8 **Independent Signatory**

As of the date of the Report, Mr. David Azrieli is an independent signatory of the Company and his signature alone can bind the Company.

3.9 **Donations**

The Company has a deep commitment to improving and promoting the community in Israel. The social responsibility, the integration and giving to the community are strategic goals which are an integral part of the business work plan of the Company, which allocates financial resources to the issue in the annual work plan. The activity for the community is performed with the involvement of the employees and the internalization of social responsibility and environmental values.

In addition, the Company has for many years helped public corporations and institutions whose goals include activities for welfare, charity, sports, medical assistance for the needy, education etc. During 2011 the Company donated, itself and through consolidated companies (excluding Granite), donations in cash and in finished products at a total value of approx. NIS 7.8 million. For details see Section 1.7 above.

With respect to the resolutions that the Company adopted in connection with its donation policy, through the Israel Azrieli Fund, R.A., see Section 22 of Chapter D of the Report.

3.10 **Process of approval of the financial statements in the corporation**

The committee

The Company's board of directors has appointed the finance committee to act also as the financial statement review committee. The audit committee does not act as a financial statement review committee.

The members of the committee

As of the date of the report, the four members of the committee for review of the financial statements are:

Prof. Niv Ahituv (chairman of the committee and outside director), with

accounting and financial expertise, *inter alia* based on his education and experience, as follows: holds an MBA from the Tel Aviv University and acts as a member of the investment committee of Migdal Insurance and Financial Holdings Ltd. and as an outside director in several public companies and also served in the past as chairman of the board of directors and chairman of the rating committee of Maalot, a company for rating.

Mr. Josef Ciechanover, director (who on May 25, 2011, the members of the Company's audit committee and board of directors approved his classification as an independent director as such term is defined in the Companies Law) , with accounting and financial expertise, *inter alia*, based on his education and experience, as follows: holds a BA in business administration from the Hebrew University in Jerusalem (completed his studies towards a Masters degree in business administration at the Hebrew University in Jerusalem) and serves as a director in several public companies.

Mr. Yossi Kucik, director, with professional qualifications and the ability to read and understand financial statements who served, *inter alia*, as vice chairman of Direct Insurance Financial Investments House Ltd. and serves as a director in Meitav Investments Ltd. Mr. Kucik declared that neither he nor his relative, partner, employer, anyone to whom he directly or indirectly reports, or a corporation of which he is the controlling shareholder, on the date of the appointment or in the two years prior to the date of the appointment, has a link with the Company, the controlling shareholder of the Company on such date or another corporation.

Mr. Efraim Halevy, outside director, with professional qualifications and ability to read and understand financial statements, who served, *inter alia*, as head of the Shasha Center for strategic studies at the Hebrew University and holds a Masters degree in Law, from the Hebrew University in Jerusalem.

Immediately before their appointment the four committee members issued a declaration to the Company pertaining to their education and experience, as specified in Article 26 of Chapter D of this Report and pursuant to Section 3 of the Companies Regulations (Instructions and Conditions regarding the Proceeding of Approval of the Financial Statements), 5770-2010, according to which the Company deems them as having accounting and financial expertise or the ability to read and understand financial statements, as the case may be.

Proceeding of approval of the financial statements

The Committee convened on March 19, 2012 to review the financial statements as of December 31, 2011 and to form its recommendations to the Board of Directors regarding approval of the statements. An advanced draft of the Annual Report, with all parts thereof including the Company's financial statements, as well as the Company's presentation on the main financial results and material issues for discussion were delivered to the Committee members several days prior to the date scheduled for the committee meeting.

At the committee meeting of March 19, 2012, all of the committee members specified above participated. Also attended the meeting, according to the

committee chairman's request, Mr. Shlomo Sherf, the Company CEO, Mr. Yuval Bronstein, the CFO, Ms. Danna Azrieli, Active Vice Chairman of the Board, the internal auditor, Mr. Gali Gana, the General Counsel, Ms. Michal Kamir, the Company's auditor, the valuator of the Company's assets as well as relevant office holders at the Company, such as the Company's comptroller and the Assistant CEO, as well as an external attorney of the Company. During the meeting, the Company CEO and CFO reviewed the reports and additional issues and answered questions of the committee members, to the extent such was required.

During the meeting the Committee discussed, *inter alia*, the financial results, including estimates and assessments made in connection with the financial statements, internal controls related to financial reporting, the completeness and fairness of the disclosure in the financial statements, and the manner of presentation of figures and the comparison thereof to parallel figures in the previous reporting year. The Committee further discussed the accounting policy adopted in the financial statements and whether there were any changes thereto, the accounting treatment applied to material issues of the corporation and valuations, including the assumptions and estimates underlying the same, on which figures in the financial statements are based. The Committee also discussed the aspects of the effectiveness of the control on the financial reporting and disclosure, including in the very material processes for the purposes of reporting.

In the course of the discussion, the Committee members raised issues that require clarifications and received answers and clarifications from the CFO and from officers of the Company who attended the meeting, as well as from the auditors who also attended the meeting.

After a deliberation, as specified above, was held at the committee, the committee chairman put to the vote the committee's recommendation to the board and asked whether any of the committee members still had questions or issues regarding which no answer was provided. At that meeting, the committee decided to recommend to the board of directors to approve the Company's financial statements as of December 31, 2011. The recommendations of the finance committee sitting as a committee for review of the financial statements, were forwarded to the members of the board on March 19, 2012, according to the timeframe determined as "reasonable" by the board of directors (approx. 2 business day) in light of the scope and complexity of the recommendations, in preparation for the board meeting which took place on March, 21, 2012.

On March 21, 2012, the Company's board of directors, which is the organ responsible for oversight at the Company, approved the financial statements of the Company as of December 31, 2011. For details regarding the board members see article 26 of Chapter D in the Periodic Report of the Company as of December 31, 2011. Advanced drafts of the financial statements, the notes thereto, the board report and annexes thereto, and any report and presentation related thereto are sent to the board members several days prior to the date scheduled for the board meeting.

The board meeting of March 21, 2012 was also attended by the persons invited to the meeting of the Committee as specified above. The members of the board of directors who were present at the aforesaid meeting were: Mr. David Azrieli, chairman of the board of directors, Ms. Danna Azrieli, active vice chairman of the board of directors, Mr. Menachem Einan, active deputy chairman of the board, Ms. Sharon Azrieli, director, Ms. Naomi Azrieli, director, Mr. Yossi Kucik, director, Mr. Josef Ciechanover, independent director, Prof. Niv Ahituv (outside director) and Mr. Efraim Halevy (outside director). The representatives of the Company's auditor commented and responded, insofar as required, to questions which were addressed to them by the members of the board pertaining to material issues which derived from the figures presented in the financial statements contemplated in the deliberation. In the context of presentation of the statements to the board of directors, the material developments in the period and the financial results were reviewed, in comparison to previous periods, during which questions were answered. At the end of the deliberation by the board of directors, a vote was held in which the financial statements of the Company for 2011 were approved.

3.11 **Internal Enforcement Plan at the Company**

As of the date of release of the report, the Company has commenced a proceeding for adoption of an internal enforcement plan at the Company. During the first half of 2012, the Company's board of directors intends to approve an enforcement outline adapted to the unique structure of the Company and the line of business thereof, to review the appointment of a head of internal enforcement at the Company as well as the appointment of a designated committee of the board for the matter. The Company is acting these days towards the adaptation of the working procedures currently prevailing at the Company into updated procedures which shall constitute part of an overall enforcement system at the Company as well as the formulation of new working procedures in additional fields, to the extent required. Within the framework of adoption of the outline, the Company's management updated the timetables for implementation of the milestones required for completion of the plan adoption process, subject to the possibility of changes in the timetables, due to extensive scope of work on the plan and due to various factors which may not be estimated in advance.

4. Provisions on Disclosure in connection with the Company's Financial Report

4.1 Critical accounting estimates

Preparation of the financial statements according to accepted accounting principles in Israel, which are the International Financial Reporting Standards – IFRS, requires the Company's management to perform assessments and estimates which affect the reported values of the assets, liabilities, revenues and expenses, as well as disclosure in connection with contingent assets and liabilities.

For a review of the main principles of the Company's accounting policy, see Note 2 to the financial statements. The Company examined the disclosure provisions set forth in FAQ14 and in Section 10(b)(8) of the Securities Regulations (Annual Financial Statements), 5770-2010, and no significant disparities were found in the estimates specified in Note 3 to the financial statements.

4.2 Disclosure pertaining to very material valuations

The guideline of the Securities Authority determines that a material valuation is a valuation which fulfills one of the tests: (1) The subject matter of the valuation constitutes at least 5% of the company's total assets as the same are presented in the report on the consolidated financial condition as of the last day of the report (the "**Balance Sheet Test**") (2) The effect of the change in value as the result of the valuation on the net or total profit, as the case may be, constitutes at least 5% of the total amount of the net or total profit, respectively, of the company for the period of the report. In addition, the guideline determines that a very material valuation, which should be attached to the financial statements of a reporting corporation, is a valuation which fulfills double materiality (10% instead of 5%).

The Securities Authority further determined that where the valuation fulfills the quantitative tests but qualitative considerations led to a different decision of the corporation and it was decided not to attach the same, the corporation will examine the effect of the valuation on the net or total profit of the current year, as the case may be, in respect of the equity which is attributed to the owners of the corporation (effect on equity without rights which do not confer control) or on any other accepted criterion in the industry (the "**Additional Test**"). Insofar as after the application of the Additional Test the corporation adopts a resolution whereby a valuation is not very material, it shall disclose its resolution, while specifying the results of the quantitative tests, including the Additional Test and the reasons and considerations which constituted the basis for this resolution.

As of the Report date, the Company's board of directors determined that there is an obligation to attach a valuation of an asset whose value is at least 10% of the Company's total consolidated assets, or that the change in its fair value constitutes, in the absolute value thereof, at least 10% of the consolidated

profit/loss of the Company (of the Company's profit or loss before financing, tax and excluding profit or loss from revaluation of investment properties in the current reported period), provided that the change in the fair value constitutes, in its absolute value, at least 4% of the Company's capital, as the same is presented in the Company's consolidated balance sheet.

As of the date of the Report and after the above determination was examined, attached is the very material valuation only in respect to the Azrieli Towers in Tel Aviv (which is included in the valuation of the entire Azrieli Center, along with its components – namely- including the Azrieli Mall) - attached as Annex C of this Report. As of December 31, 2011, Azrieli Jerusalem Mall (without the office component) met the quantitative tests for a very material valuation, since the effect of the change in the fair value thereof net of the tax as a result of the valuation on the net profit (which included a one-time irregular effect of cancelation of the reduction of corporate tax, as specified in Section 1.10 above) constitutes approx. 11% of the net profit of the Company as of December 31, 2011. However, after qualitative review of the influence of the valuation, such valuation was not attached to the Company's financial statements: (a) since the influence of the change in the fair value on the net profit of the Company in its financial statements for the year 2011 does not comply with the quantitative consequential presumption regarding the net profit of the previous reporting year and is not expected to meet the expected net profit of the coming report year, due to the one-time tax effects on the net profit for 2011, deriving from the cancellation of the expected tax reduction of the corporate tax; and (b) since the change in the fair value of this asset constitutes in its absolute value0.6% of the Company's capital, as presented in the consolidated balance sheet of the Company, and less than 4% according to the board resolution, as specified above.

As of December 31, 2011, the value of the Company's assets whose fair value was determined through a very material valuation (made as of December 31, 2011) was in the amount of approx. NIS 4.3 billion (which is attributed both to Azrieli Center's towers and Azrieli mall,), out of a fair value of investment properties in the amount of approx. NIS 14.8 billion (approx. 29% of the Company's total investment properties).

4.3 Events after the date of the financial statements

See Note 44 to the financial statements.

4.4 Financial figures attributed to the Company as a parent company

Pursuant to Regulation 9C of the Periodic Reports Regulations, financial figures from the consolidated financial statements attributed to the Company as a parent company are hereby attached as Annex D of the board of directors' report, together with an auditor's opinion.

4.5 Issues to which the Company's auditors drew attention in their opinion on the financial statements

Without qualifying their opinion, the auditors drew attention to:

The provisions of Note 36 pertaining to legal actions in material amounts, cumulatively, against consolidated companies, regarding which a motion was filed to recognize the same as class actions and pertaining to various arguments and claims in material financial scopes, cumulatively, against a consolidated Company regarding which it was argued that the agreements thereof with its clients constitute a restrictive arrangement.

The Company's board of directors and management express their great appreciation for the Company's officers, the managements of the Group's various companies and their employees, on their blessed contribution to the Group's achievements in the year ended December 31, 2011.

David Azrieli	**Shlomo Sherf**
Chairman of the Board of Directors	**CEO**

Date: March 21, 2012

Annex A

Sensitivity Tests

December 31, 2011

Annex A – Sensitivity Tests

The following tables should be read in view of the following remarks:

1. The recorded instruments are not necessarily presented in the financial statements at fair value.
2. For details on the interest rates that were used in the determination of the fair value, see also Note39F(2) to the financial statements.
3. Sensitivity to 2% absolute change in the interest constitutes an extreme scenario in the Company's estimation, after reviewing severe but conceivable scenarios.

Table on sensitivity for financial instruments as of December 31, 2011 in accordance with changes in market factors:

Sensitivity to changes in the NIS interest rate

	Profit (loss) from the changes in the market factor			**Fair value of asset (liability)**	**Profit (loss) from the changes in the market factor**			**Value determination method**
	NIS in thousands	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	
Rate of Change	2% absolute increase	10% increase	5% increase		5% decrease	10% decrease	2% absolute decrease	
Marketable securities	(28,207)	(5,746)	(2,873)	390,328	2,873	5,746	28,207	market value
Interest Swap Transaction	1,704	287	143	(182)	(148)	(285)	(1,992)	market value
Long-term loans that were received	11,588	2,727	1,371	(323,411)	(1,382)	(2,775)	(12,442)	DCF model
Financing leases	797	333	169	(10,600)	(174)	(354)	(1,992)	DCF model
Total	(14,118)	(2,399)	(1,190)	56,135	1,169	2,332	11,781	

Annex A – Sensitivity Tests
(continuation)

Table on sensitivity for financial instruments as of December 31, 2011 in accordance with changes in market factors:

Sensitivity to changes in the US dollar interest rate

	Profit (loss) from the changes in the market factor			Fair value of asset (liability)	Profit (loss) from the changes in the market factor			Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of Change	2% absolute increase	10% increase	5% increase		5% decrease	10% decrease	2% absolute decrease	
Forward Transactions purchase Dollar/NIS	(916)	(14)	(7)	5,136	7	14	936	market value
Loans granted	(102)	(28)	(14)	1,934	14	29	115	DCF model
Loans that were received	76,401	23,028	11,654	(700,754)	(11,942)	(24,180)	(90,461)	DCF model
Financing leases	4,621	1,944	990	(43,314)	(1,029)	(2,099)	(5,622)	DCF model
Total	80,004	24,930	12,623	(736,998)	(12,950)	(26,236)	(95,032)	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2011 in accordance with changes in market factors:

Sensitivity to changes in the real interest rate

	Profit (loss) from the changes in the market factor			Fair value of asset (liability)	Profit (loss) from the changes in the market factor			Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of Change	2% absolute increase	10% increase	5% increase		5% decrease	10% decrease	2% absolute decrease	
Marketable securities	(37,963)	(6,024)	(3,012)	500,702	3,012	6,024	37,963	market value
Limited Investments	(5,129)	(293)	(147)	22,037	148	297	6,838	DCF model
Long-term loans that were granted	(4,813)	(1,900)	(963)	59,912	990	2,008	5,561	DCF model
Long-term loans that were received	184,510	28,373	14,275	(3,111,661)	(14,455)	(29,096)	(209,972)	DCF model
Bonds	150,321	24,649	12,409	(2,046,020)	(12,580)	(25,336)	(172,032)	DCF model
Receivables in respect of a franchise arrangement	(75,874)	(18,690)	(9,465)	517,610	9,713	19,681	95,322	DCF model
Financing Leases	731	251	130	(4,278)	(139)	(287)	(1,138)	DCF model
Embedded financial derivative	291	68	35	(289)	(36)	(72)	(364)	Yield curve discount
Interest Swap Transaction	(1,996)	(83)	(41)	(182)	42	83	1,786	Forward Formula
Total	210,078	26,351	13,221	(4,062,169)	(13,305)	(26,698)	(236,036)	

Annex A – Sensitivity Tests
(continuation)

Table on sensitivity for financial instruments as of December 31, 2011 in accordance with changes in market factors:

Sensitivity to changes in exchange rates NIS/dollar

	Profit (loss) for the changes in the market factor		Fair value of asset (liability)	Profit (loss) from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	10% increase	5% increase		5% decrease	10% decrease	
Exposure on the balance sheet linkage	(105,739)	(52,870)	(1,057,390)	52,870	105,739	Book Value
Forward purchase transactions Dollar/Shekel	61,748	38,874	5,136	(38,874)	(61,748)	Market Value
Embedded financial derivative	6,693	3,346	(238)	(3,346)	(6,693)	Yield curve discount
Total	(37,298)	(18,650)	(1,052,492)	18,650	37,298	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2011in accordance with changes in market factors:

Sensitivity to changes in consumer price index

	Profit from changes in market factor		Fair value of liability	Loss from changes in market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of Change	10% increase	5% increase		5% decrease	10% decrease	
Interest swap transaction	3,320	1,660	(182)	(1,660)	(3,320)	Market value
Future index transactions	45,980	22,990	(5,650)	(22,990)	(45,980)	Market value
Total	49,300	24,650	(5,832)	(24,650)	(49,300)	

Sensitivity changes of interest rates in the CAD

	Profit from the changes in the market factor		Fair value of asset	Loss from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of Change	10% increase	5% increase		5% decrease	10% decrease	
Marketable Securities	(854)	(427)	55,525	427	854	Market value
Total	(854)	(427)	55,525	427	854	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2011 in accordance with changes in market factors:

Sensitivity to changes in exchange rates of other currencies

	Profit from changes in the market factor		Fair value of asset	Loss from changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	10% increase	5% increase		5% decrease	10% decrease	
Exposure on the balance sheet linkage	4,919	2,460	49,188	(2,150)	(4,252)	Book Value
Embedded financial derivative	6,031	3,015	(544)	(3,015)	(6,031)	Yield Curve Discount
Forward purchase transactions Euro/NIS	495	247	11	(247)	(495)	Market Value
Sale of put options Euro/NIS	(37)	(37)	(37)	(273)	(630)	Market Value
Total	11,408	5,685	48,618	(5,685)	(11,408)	

Sensitivity to security rates

	Profit from the changes in the market factor		Fair value of asset	Loss from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	10% increase	5% increase		5% decrease	10% decrease	
Shares	24,898	12,449	248,985	(12,449)	(24,898)	Market value
Governmental bonds	51,586	25,793	515,859	(25,793)	(51,586)	Market value
Corporate bonds	51,884	25,942	518,844	(25,942)	(51,884)	Market value
Convertible bonds	10	5	105	(5)	(10)	Market value
Participation certificates in trust fund	10,630	5,315	106,305	(5,315)	(10,630)	Market value
Others	1,170	585	11,689	(585)	(1,170)	Market value
Total	140,178	70,089	1,401,787	(70,089)	(140,178)	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2011 in accordance with changes in market factors:

Sensitivity to changes in the interests of investment property cap rates

	Loss from changes in the market factor			Fair value of asset	Loss from changes in the market factor			Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	2% absolute increase	10% increase	5% increase		5% decrease	10% decrease	2% absolute decrease	
Weighted cap rate								
7% - 7.5%	(1,430,656)	(609,713)	(319,373)	6,699,132	352,992	745,204	2,495,265	DCF model
7.51% - 8%	(810,232)	(355,372)	(185,995)	3,836,572	206,246	435,053	1,384,521	DCF model
8.01% - 8.5%	(468,915)	(216,887)	(113,607)	2,344,178	125,637	265,121	772,687	DCF model
8.51% - 9%	(157,895)	(76,190)	(39,909)	817,620	44,110	93,121	253,401	DCF model
9.51% - 10%	(19,183)	(9,729)	(5,081)	136,852	5,578	11,735	29,005	DCF model
Investment properties and investment properties under construction	(2,886,881)	(1,267,891)	(663,965)	13,834,354	734,563	1,550,234	4,934,879	

Annex A – Sensitivity Tests

Sensitivity to index linked security rates as of December 31, 2011

	Profit from changes in market factor		Fair value of asset	Loss from changes in market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	**2% increase**	**1% increase**		**1% decrease**	**2% decrease**	
Index linked bonds	10,026	5,013	501,306	(5,013)	(10,026)	Market value
Index linked convertible bonds	2	1	105	(1)	(2)	Market value
Total	10,028	5,014	501,411	(5,014)	(10,028)	

Sensitivity to nominal security rates as of December 31, 2011

	Profit from changes in the market factor		Fair value of asset	Loss from changes in market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	**2% increase**	**1% increase**		**1% decrease**	**2% decrease**	
Bonds	9,072	4,536	453,578	(4,536)	(9,072)	Market value
Shares	4,938	2,469	246,912	(2,469)	(4,938)	Market value
Trust funds	276	138	13,760	(138)	(276)	Market value
Others	1,666	833	83,255	(833)	(1,666)	Market value
Total	15,952	7,976	797,505	(7,976)	(15,952)	

Annex A – Sensitivity Tests

(continuation)

The following tables should be read in view of the following remarks:

1. The recorded instruments are not necessarily presented in the financial statements at fair value.
2. For details on the interest rates that were used in the determination of the fair value, see also Note 42E(2) to the financial statements.
3. Sensitivity to absolute change in the interest of 2% constitutes an extreme scenario in the Company's estimation, after reviewing severe but conceivable scenarios.

Table on sensitivity for financial instruments as of December 31, 2010 in accordance with changes in market factors:

Sensitivity to changes in the NIS interest rate

	Profit (loss) from changes in the market factor			Fair value of asset (liability)	Profit (loss) from changes in the market factor			Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	2% absolute increase	10% increase	5% increase		5% decrease	10% decrease	2% absolute decrease	
Marketable securities	(40,509)	(8,627)	(4,314)	646,141	4,314	8,627	40,509	Market value
Long-term loans granted	(337)	(176)	(90)	11,577	92	185	366	DCF model
Long-term loans received	11,112	2,863	1,438	(349,533)	(1,455)	(2,923)	(12,046)	DCF model
Financing leases	1,708	647	329	(17,074)	(342)	(696)	(2,046)	DCF model
Total	(28,026)	(5,293)	(2,637)	291,111	2,609	5,193	26,783	

Sensitivity to changes in the dollar interest rate

	Profit (loss) from the changes in the market factor			Fair value of asset (liability)	Profit (loss) from the changes in the market factor			Value determination method
	NIS in thousands	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	
Rate of Change	2% absolute increase	10% increase	5% increase		5% decrease	10% decrease	2% absolute decrease	
Marketable securities	(1,105)	(273)	(137)	9,401	137	273	1,105	Market value
Loans to trade receivables	(120)	(54)	(27)	10,043	28	57	133	DCF model
Loans received	5,365	1,006	505	(180,248)	(510)	(1,025)	(5,847)	DCF model
Financing leases	4,827	1,790	913	(41,802)	(952)	(1,944)	(5,879)	DCF model
Total	8,967	2,469	1,255	(202,606)	(1,297)	(2,639)	(10,488)	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2010 in accordance with changes in market factors:

Sensitivity to changes in the real interest rate

	Profit (loss) from the changes in the market factor			Fair value of asset (liability)	Profit (loss) from the changes in the market factor			Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	2% absolute increase	10% increase	5% increase		5% decrease	10% decrease	2% absolute decrease	
Marketable securities	(57,918)	(6,765)	(3,382)	629,324	3,382	6,765	57,918	Market value
Deposits	(692)	(28)	(14)	21,423	14	28	730	DCF model
Long-term loans granted	(6,478)	(2,699)	(1,371)	67,494	1,414	2,876	7,573	DCF model
Long-term loans received	233,221	31,192	15,707	(3,349,411)	(16,001)	(32,089)	(264,610)	DCF model
Bonds	184,464	25,082	12,619	(2,248,463)	(12,777)	(25,717)	(213,389)	DCF model
Convertible bonds	67	10	5	(21,543)	(5)	(10)	(68)	Market value
Receivables in respect of a franchise arrangement	(84,772)	(18,754)	(9,491)	598,407	9,726	19,694	108,006	
Financing leases	1,368	421	218	(7,559)	(233)	(484)	(2,133)	
Total	269,260	28,459	14,290	(4,310,328)	(14,480)	(28,937)	(305,973)	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2010 in accordance with changes in market factors:

Sensitivity to changes in exchange rates NIS/dollar

	Profit (loss) from the changes in the market factor		Fair value of asset (liability)	Profit (loss) from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	10% increase	5% increase		5% decrease	10% decrease	
Loans granted	629	314	6,285	(314)	(629)	DCF model
Loans received	(25,500)	(12,750)	(255,000)	12,750	25,500	DCF model
Trade payables	(33,225)	(16,612)	(332,247)	16,612	33,255	Book value
Fuel administration	12,357	6,178	123,569	(6,187)	(12,357)	Book value
Short term credit from banking corporations	(7,878)	(3,939)	(78,777)	3,939	7,878	Book value
Trade receivables	5,962	2,981	59,617	(2,981)	(5,962)	Book value
Financial assets designated at fair value through profit and loss	1,513	757	15,130	(757)	(1,513)	Book value
Other current assets	3,979	1,990	39,793	(1,990)	(3,979)	Book value
Other current liabilities	(5,582)	(2,791)	(55,818)	2,791	5,582	Book value
Future transactions	46,752	23,376	(10,235)	(23,376)	(46,752)	Market value
Total	(993)	(496)	(487,683)	496	993	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2010 in accordance with changes in market factors:

Sensitivity to changes in consumer price index

	Profit from the changes in the market factor		Fair value of liability	Loss from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of Change	10% increase	5% increase		5% decrease	10% decrease	
Future transactions	62,500	31,250	(1,064)	(31,250)	(62,500)	Market value
Total	62,500	31,250	(1,064)	(31,250)	(62,500)	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2010 in accordance with changes in market factors:

Sensitivity to exchange rate NIS/CAD

	Profit from the changes in the market factor		Fair value of asset	Loss from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of Change	10% increase	5% increase		5% decrease	10% decrease	
Exposure on the balance sheet linkage	23,788	11,894	237,878	(11,894)	(23,788)	Book value
Total	23,788	11,894	237,878	(11,894)	(23,788)	

Sensitivity to changes in exchange rates of other currencies

	Profit from the changes in the market factor		Fair value of asset	Loss from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	10% increase	5% increase		5% decrease	10% decrease	
Exposure on balance sheet linkage	4,848	2,424	36,008	(2,424)	(4,848)	Book value
Total	4,848	2,424	36,008	(2,424)	(4,848)	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2010 in accordance with changes in market factors:

Sensitivity to security rates

	Profit from the changes in the market factor		Fair value of asset	Loss from the changes in the market factor		Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	10% increase	5% increase		5% decrease	10% decrease	
Shares	25,134	12,567	251,342	(12,567)	(25,134)	Market value
Governmental bonds	103,101	51,551	1,031,013	(51,551)	(103,101)	Market value
Corporate bonds	78,050	39,025	780,501	(39,025)	(78,050)	Market value
Convertible bonds	847	423	8,466	(423)	(847)	Market value
Participation certificates in trust fund	16,868	8,434	168,684	(8,434)	(16,868)	Market value
Other	7,042	3,521	70,417	(3,521)	(7,042)	Market value
Total	231,042	115,521	2,310,423	(115,521)	(231,042)	

Annex A – Sensitivity Tests

(continuation)

Table on sensitivity for financial instruments as of December 31, 2010 in accordance with changes in market factors:

Sensitivity to changes in the interests of investment property cap rates

	Loss from changes in the market factor			Fair value of asset	Loss from changes in the market factor			Value determination method
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	
Rate of change	2% absolute increase	10% increase	5% increase		2% absolute increase	5% decrease	10% decrease	
Weighted cap rate								
7% - 7.5%	(1,171,322)	(492,538)	(252,186)	5,543,087	304,417	629,102	2,097,621	DCF model
7.51% - 8%	(599,712)	(265,050)	(134,561)	3,005,334	147,619	311,102	1,030,063	DCF model
8.01% - 8.5%	(1,106,974)	(196,963)	(88,076)	2,483,590	164,084	311,177	848,025	DCF model
8.51% - 9%	(143,570)	(68,118)	(34,256)	780,056	44,160	89,902	237,451	DCF model
9.51% - 10%	152,953	182,349	198,734	185,484	236,569	258,566	311,947	DCF model
Investment property and investment property under construction	(2,868,625)	(840,319)	(310,346)	11,997,550	896,848	1,599,849	4,525,107	

Annex B

The Group's Positions in Derivatives
December 31, 2011

Annex B
The Group's Positions in Derivatives
As of December 31, 2011

The Group's positions in derivatives as of December 31, 2011:

Granite HaCarmel and consolidated companies perform, as aforesaid, financial protection on the rise of the index due to the difference between the liabilities and index-linked NIS assets.

Below is a specification of the transactions as of December 31, 2011:

Amount in thousands	Currency	Date of expiry/payment/exercise	Fair Value (NIS in thousands)
459,800	NIS	May 2012 – October 2012	(5,650)

The maximum holding of derivatives, during the period of the report, of all of the NIS purchase positions was NIS 625,000 thousand.

A consolidated company of Granite HaCarmel entered into interest swap contracts whose payment dates correspond to the payment dates of certain loans, and they were therefore recognized as hedge accounting.

Below is a specification of the transactions as of December 31, 2011:

Amount in thousands	Currency	Date of expiry/payment/exercise	Fair Value (NIS in thousands)
31,300	NIS	2014-2016	(182)

During the year, consolidated companies of Granite HaCarmel entered into future currency transactions for protective purposes (which were not recognized as hedge accounting).

Below is a specification of the engagements as of December 31, 2011:

Amount in thousands	Currency receivable	Currency payable	Date of expiration/payment/exercise	Fair Value (NIS in thousands)
161,500	Dollar	NIS	January-April 2012 (mainly January-February 2012)	5,136
2,250	Euro	NIS	January-April 2012	(26)

The maximum holding of derivatives, during the report period, of all of the purchase positions for purposes of protection of the dollar-NIS exchange rate was US$180,500 thousand, and of the total purchase positions for purposes of protection of the Euro-NIS exchange rate was €3,200 thousand.

Collection of the figures for purposes of the aforesaid measurements was performed

on the basis of the par value thereof at the time of measurement. The measurement is tracked at a frequency of at least once a month.

Annex C

Azrieli Center Valuation

December 31, 2011

March 21, 2012

Our reference: 3415-06

CANIT HASHALOM INVESTMENTS LTD.

1 Azrieli Center, Tel Aviv

Expert Professional Opinion

Comprehensive Land Valuation - "Azrieli Center"

1 Azrieli Center, Tel Aviv

At your request, which was received by our firm on December 22, 2011, by Yuval Bronstein, CFO of the Azrieli Group Ltd., submitted hereby is a Professional Opinion to assess the value of the rights of Canit Hashalom Investments Ltd. (the "Company") in Azrieli Center and its components (parking lot, mall and offices) (the "Property").

We agree that our Opinion will be released in the framework of the financial statements of the Company and/or the Azrieli Group Ltd. that will be released to the public.

Over the years we have performed appraisal assignments for the Azrieli Group Ltd. and companies controlled thereby. The income from these assignments is not material to our firm and no dependency was thereby created of our firm on the Company and/or Azrieli Group Ltd.

We received a letter of indemnity from Azrieli Ltd. that was signed by Menachem Einan and Yuval Bronstein on March 23, 2010. According to the letter of indemnity the Company undertakes to indemnify the appraisers if they are charged with a financial liability in connection with an appraisal as a result of incorrect documents or information provided by the Company or other companies on its behalf and/or as a result of non-transfer of documents or other information required for the valuation (except for documents held by the authorities and/or the public).

The duty to indemnify shall not apply if the appraisers acted negligently or maliciously with respect to the Opinion.

This valuation was made according to Standard No. 17.1 of the Real Estate Appraisers Council and according to the International Valuation Standard (IVS) Edition 2007, and especially IVA1 standard (INTERNATIONAL VALUATION APPLICATION 1).

Expert name:	**Adina Greenberg**
Address:	**65 Yigal Alon, St., Toyota Tower, Tel Aviv.**
Occupation:	**Certified Real Estate Appraiser, certificate No. 237, since 1990.**

Education:

1985-1987	Tel Aviv University - Real Estate Appraisal and Property Management studies.
1975-1979	Technion - Civil Engineering studies in the framework of the academic reserve.
December 2001	Mediation course of the Israel Center for Negotiation & Mediation (ICNM).

Professional Experience:

Since October 1994	Partner at Real Estate Appraisals firm Greenberg Olpiner & co.

Expert name:	**Ronen Katz**
Address:	**65 Yigal Alon St., Toyota Tower, Tel - Aviv.**
Occupation:	**Certified Real Estate Appraiser, certificate No. 616, since 1997.**

Education:

1993-1995	Tel Aviv University - Real Estate Appraisal and Property Management studies.
1990-1993	Faculty of Agriculture of the Hebrew University of Jerusalem, B.A. in Agricultural Economics and Management.

Professional Experience:

2001 -	Partner at Greenberg Olpiner & co.
1995-2001	Greenberg Olpiner & Co. A Trainee until 1997 and since that date as a Real Estate Appraiser.

And this is the question:

The market value estimate of the Company's rights in Azrieli Center and its components (parking lot, mall and offices), in the free market, in the criterion of a willing buyer from a willing seller.

We were informed by the Company, the owner of the Property, that the Property contemplated in the Opinion is defined as an investment property according to International Financial Reporting Standards (IFRS), International Standard IAS 40.

Market value is defined according to IVS1 International Standard as:

"The estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing, wherein the parties had each acted knowledgeably, prudently and without compulsion".

The effective date for the valuation – December 31, 2011.

Documents and representations received from the Company:

- Underlying agreement between the City of Tel Aviv - Yafo and the Company.
- Compromise agreement between the City of Tel Aviv – Yafo and the Company.
- Lease agreements between the City of Tel Aviv - Yafo and the Company regarding the parking lot, the mall, the Round tower, the Triangular tower and the Square tower.
- Company report for the actually received rental fees for the years 2009-2011.
- Report of the management companies' figures for the years 2009-2011 and forecast for 2012.
- Forecast for leased areas and forecast for income from rental fees and management fees for 2012, based on signed contracts (see clarification in Section 4.1 below).
- Data on the business activity of the parking lot for the years 2009-2011 and income forecast for 2012, based on signed contracts (see clarification in Section 4.2.6).
- Document of undertaking to populate the Square tower dated February 28, 2008.
- The Company's document regarding the cost of building the tunnel and the bridge.

- Disclosure document[1].

[1] See separate chapter in the valuation.

And hereby is our professional Opinion:

1. Property information

Block:	7106, 7102
Parcel:	59, 49
Parcel area:	31,992 sqm, 903 sqm.
Total built-up area:	326,233 sqm (according to building permit application plans)
Rights:	Lease from the City of Tel Aviv – Jaffa

2. Description of the Property and the surroundings

Site visit performed by the undersigned on January 23, 2012.

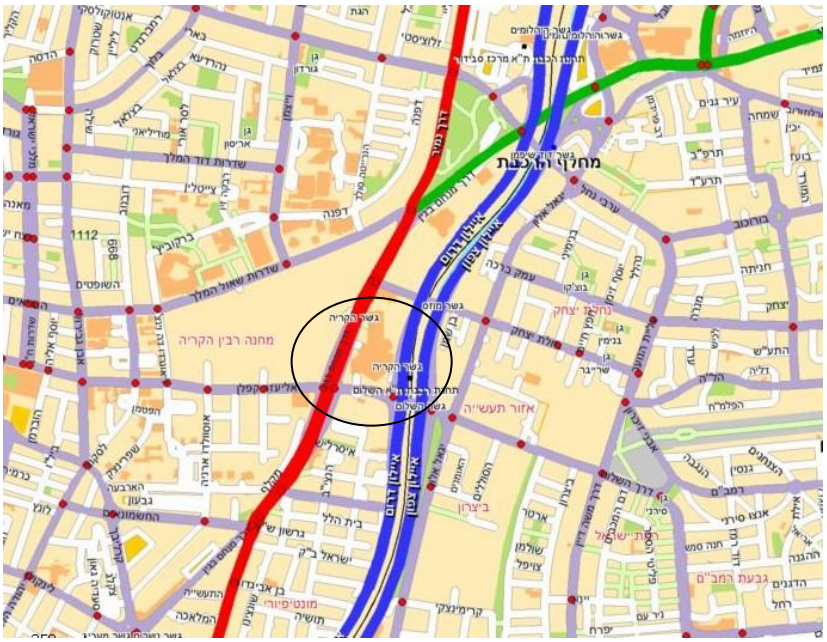
2.1 Description of the surroundings

The surroundings are known as the northern CBD of Tel Aviv. Bounded on the west by Menachem Begin Rd., Parashat Derachim St. on the north, the Ayalon Highway on the east and Ha'Shalom Rd. on the south. The accessibility is excellent due to its proximity to main traffic roads (Ayalon Highway, Ha'Shalom Rd. and Haifa Rd.). Ha'Shalom railway station, located in Ha'Shalom interchange is adjacent to Azrieli Center, which is the subject matter of the Opinion.

At the south-west corner of Petach Tikva Rd. and Ha'Shalom Rd. junction is located the Government Compound Tower, which includes areas used by the governmental offices and areas leased to private entities.

In the last few years new plans where approved allowing, whereby in the surroundings are planned some projects for offices, high-tech industries, employment and trade, combined with residential upper floors up to building rate of about 450%. The projects that are planned in the surroundings are the "Echtman Bldg." (At initial stages of construction, located north of the subject matter of the Opinion), "Karden House", Gazit Paz House (existing building, a building addition is planned on the building's roof), the "Yediot Aharonot", "Egged", "Kupat Holim", "Tenuva" and "Hatzeerim Tower" complexes designated for commerce and residence, located north of the subject matter Property.

Map of the surrounding area:



2.2 The business environment

In the last two decades several office towers were built in the area that include, *inter alia*: the Government Compound Tower, the office towers in Ha'Arbaa St. (Platinum, Ha'Tichon and Millennium), 2 office towers planned on the intersection of Ha'Arbaa St. and Ernie (are at initial construction stages by Hagag Group), office tower is designed in Max Payne School's complex (south of the subject matter of the Opinion), an office tower adjacent from the south to the Government Campus (will be constructed by the Company).

Another focus of employment areas in the vicinity under formation is along Yigal Allon St. (the southern part of the street, south of Ha'Shalom Rd.). The Toyota office tower and the Elco Tower are in the area, HaArgaz complex (the purchase of the complex by B.S.R Group and Harel and Migdal was recently closed for construction of 2 office towers) are at preliminary stages of population. There are also in the immediate area several large land complexes designated for office towers, such as: "Shmei bar" complex, "Machshirei Tnua" complex, the "Cinerama", the "ACE" complex, etc.

Town plan TA/3000 (South Kirya complex) declares the Sharona colony, which is located southwest of the subject matter of the valuation, as a conservation park in an area of approx. 40 dunam that includes 37 Templar stone houses. The area was marketed approximately two years ago to several companies and there is currently on site at stages of construction a project for commercial and public uses.

6 residential towers which will include about 650 residential units (as well as commercial areas and offices on lower floors) on a total main

area of approx. 90,000 sqm planned to be built west and south to the park on the first line to it. 3 residential towers were marketed to Gindi Holdings, are currently in construction stages.

9 towers of offices, commercial use and hotels (the lot, under hotels designation, had been marketed during the past year to Nitsba) (some of them, such as the Kirya Tower, Platinum, Millennium, Hatichon Tower are already built) on a total main area of about 400,000 sqm are planned in the second line.

2.3 Description of the plots

The subject matter of the Opinion is the "Azrieli Center" project, which is built on parcel 59 in block 7106 and parcel 49 on block 7102, which constitute a plot of land on a total area of 32,894 sqm, with a regular rectangular shaped plot, with three fronts, on a level surface.

Plan:

[Translator's note: Image not copied from Hebrew due to size of file.]

Borders:

South -Front facing the Givat Ha'Tachmoshet St. (which connects Kaplan St. on the west to Ha'Shalom Rd. on the east), constitute a major traffic artery connecting the Tel Ha'Shomer junction (on Route No. 4) on the east with Tel Aviv City Center on the west. The Max Payne School is located across the street.

West - Front facing Menachem Begin Rd., a major traffic artery connecting the Tel Aviv City Center with Jabotinsky Rd. in Ramat Gan until Petach Tikva. The "Camp Rabin" army base is across the street.

East - Southbound Ayalon highway - Road no. 20 (in the mentioned segment between Rakevet Tzafon interchange and Ha'Shalom interchange in the south) constitute a national highway connecting the city of Tel Aviv With the cities of Jerusalem, Rishon LeZion, Holon, Bat Yam, Haifa, etc.

North- The "Yediot Aharonot" House.

2.4 Description of "Azrieli Center"

2.4.1 General

"Azrieli Center" is the largest business center in Israel. The center was designed as an independent urban unit capable of providing its users and visitors a full range of services that are required for the management of their businesses, the welfare of the employees, and the convenience of the customers.

The center includes underground parking lot for 3,200 vehicles, a mall and three towers: the "Round" and "Triangular" towers are offices area and the "Square" tower partially occupied by a hotel and the other part as office space. In addition, the center provides complementary services and areas, such as a conference hall, “Holmes Place” fitness center, a travel agency, taxicab stand, laundry, etc.

On top of the Round tower there is an observatory overlooking the Dan metropolitan and the surrounding cities. The visit to the observatory is accompanied with vocal guidance, telescopes, etc.

The construction on the project began in 1995. The underground parking lot and the mall are operating since April 1998, the Triangular tower is populated since 1999, the Round tower was populated in 2000 and the Square tower was populated in 2008 and 2009.

The project is located at a major transportation crossroads and therefore the accessibility is very good. There are entrances and exits for vehicles from the Northbounds and Southbounds Ayalon Highway, from Menachem Begin Rd., from Givat Ha'Tachmoshet St. and from Noah Mozes St. There is a pedestrian bridge that links the Ha’Shalom railway station with the first floor of the mall, and another pedestrian bridge across Menachem Begin Rd. to the first floor of the mall. In addition there is a heliport on top of the Round tower.

Following are details of the Azrieli Center’s construction areas, as transpires from approved building permit plans[2]:

Designation	**Main Area in sqm**	**Service area in sqm**	**Total in sqm**
Underground parking lot, storerooms, open floor and IEC control station	2,564	119,691	122,255
Bridges (above Petach Tikva Rd., Hashalom railway station)		1,365	1,365
Mall and public areas	29,992	28,657	58,649
Round tower	45,436	10,274	55,710
Triangular tower	39,631	8,049	47,680
Square tower	28,787	11,787	40,574
Total	**146,410**	**179,823**	**326,233**

[2] For details on as made permit plans that have been submitted in full to the engineering administration at the City of Tel Aviv, which include changes to these areas, see Section 2.6 below.

The construction and finishing standard includes, *inter alia*:

- Mall and the office towers - reinforced concrete structure, a combined marble tiled facade with screen walls.

- The public areas and passages in the mall are spacious, covered with marble flooring, centrally air conditioned, ceilings combined with decorative elements, there are 8 skylights, PA system, fire detection system, etc.

- In the mall's areas and the public floor a fully finishing level, including marble/ ceramic/ parquet/ wood tiled floor, decorative ceiling, immersed lighting, glass display cases, interior plaster/ paint/ decorative wall cover, central air conditioning system, etc.

- The mall's public level includes a terrace paved with precast paving stones, landscape lighting, public benches and transparent environmental sculptures that are used in addition to bring daylight to the mall's space.

- In the offices area a fully finishing level, including marble/ parquet/ wall-to-wall carpets, internal division using plaster partitions, decorative ceiling, immersed fluorescent lighting, central air conditioning system, communication systems and computers.

- At the Hotel areas – in lodgin rooms parquet flooring, air conditioning system, fire detection system, work area including a PC. In bathrooms a table sink, a bathtub and shower.
  In public areas - wall-to-wall carpet/ marble flooring/ parquet, air conditioning system, fire detection system, etc.

- In the parking lot epoxy color coated smooth concrete floor, forced ventilation system, fire detection system, PA system, CCTV.

2.4.2 The mall and the public areas

A national mall which serves large populations coming from all over Israel. The occupancy rate nowadays and throughout all of the operating years is approx. 99%. There are approx. 343 sqm free (area formerly leased to Markedo restaurant) divided into approx. 204sqm commercial area plus approx. 139sqm commercial gallery.

The mall includes 3 commercial floors and one public floor.

The parking lot levels are linked to the commercial center's levels via 11 passenger elevators and 2 escalator systems.

The mall was ranked third in the Globes newspaper's annual rating of the leading and strongest malls for the year 2011.

About 184 businesses are operating in the mall in a wide range of shops in the fields of fashion, footwear, jewelry, gifts, communications, electronics and computers, optics and more, such as: Steimatzky, Mega Sport, Adidas, Domo, Castro, Golf, Renour, Fox, Polgat, Hanes, Nike, Puma, Honigman, Aldo, Royalty, Happening, Tzomet Sfarim, Kravitz, Michal Negrin, Miller, café café, Rikushet, Opticana, Crazy Line, Lucci, and more.

8 businesses lease relatively large areas : Shufersal, Mango, Hamashbir Lazarchan, Superpharm, GAP, H&M, Zara and Forever 21.

The Public floor (the third mall's floor above ground) includes "Holmes Place", the Wall Street and Kidum schools, area designated for a restaurant (currently vacant – formerly the Markedo restaurant) and the conference center. The center's roof area is being used for activities for children and adults.

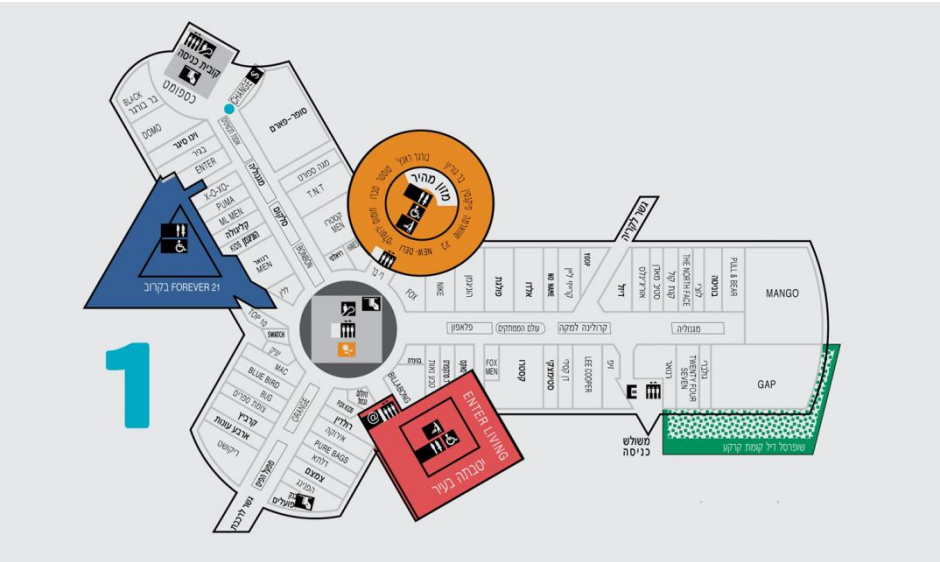
A summary of the commercial areas by marketing mix segmentation:

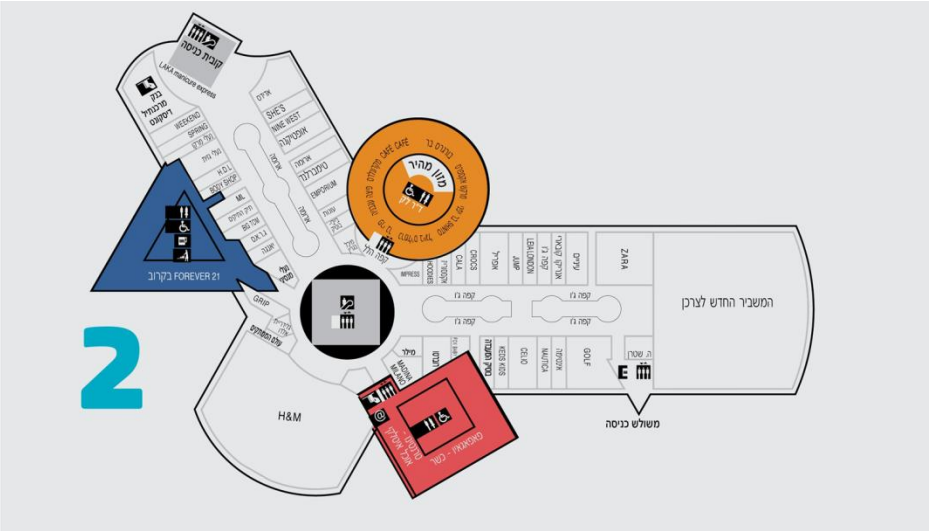
Item	**Area for lease in sqm**	**%**
Shufersal, H&M, Hamashbir, Superpharm, Mango, GAP, Zara and Forever 21	12,645	38.9%
Shops and other businesses	15,991	49.2%
Public floor	3,886	11.9%
Total	**32,521**	**100.0%**

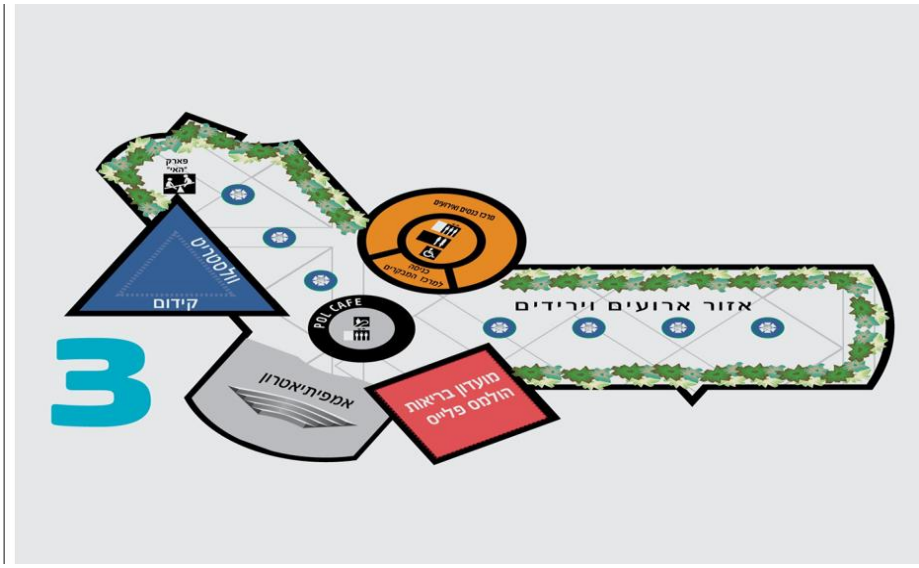
According to the data provided to us, the leasable areas are the store area, plus loading of public areas at a variable rate ranging between of 10%-15%.

Representative pictures:

Layout:


1
בקרוב FOREVER 21
ENTER LIVING
עברה בעיר
GAP
MANGO
משולש כניסה


2
בקרוב FOREVER 21
H&M
ZARA
המשביר החדש לצרכן
משולש כניסה


3
קידום
אמפיתיאטרון
אזור ארועים וירידים
POL CAFE

2.4.3 The Round tower

Includes 39 office floors and a roof which is used as a tourist attraction - public-access observatory and restaurant.

The gross total area of the tower is about 55,709 sqm.

The top office floor on a leasable area of approx. 1,520 sqm is self used by the Azrieli Group Ltd. **The Opinion does not include this floor**.

According to the marketing plans, the average area of a floor is approx. 1,520 sqm. The total area for lease is approx. 58,128 sqm (excluding an area for Azrieli Group's own use).

Main lessees in the tower are law firms, accounting firms and other liberal professionals.

There are 12 passenger elevators in the tower.

As of the effective date the building is leased in its entirety.

The tower's image:

Typical floor layout:

2.4.4 The Triangular tower

Includes 35 office floors and 2 service floors. The gross total area of the tower is about 47,672 sqm.

According to the marketing plans, the average area of a floor for marketing is approx. 1,430 sqm. The total area for marketing is approx. 48,094sqm.

The main lessees in the building are Bezeq that leases an area of about 22,300 sqm (about half of the building), the IDB Group, law firms, accounting firms and other liberal professionals.

The finishing standard in the areas leased to Bezeq is average. In the framework of an addendum to the lease agreement with Bezeq which was signed on October 20, 2010, the lessor shall forward to Bezeq a budget for renovation works in the Property in the sum of approx. NIS 660 per sqm to be spread over 5 years for area renovation.

There are 10 passenger elevators in the tower.

As of the effective date, the building is leased in its entirety.

Typical floor layout:

2.4.5 The Square tower

Includes 13 floors leased for use as the "Crown Plaza City Center" hotel and 18 office floors above the hotel's floors. The gross total licensed area of the tower is about 40,867 sqm.

The hotel:

The hotel's lobby is located in the ground floor of the building and in 13 floors, total 273 rooms and public areas. The internal division – public floor which includes a dining hall, bar, 3 conference rooms, central kitchen and operational areas. above such floor there are 8 typical floors that include 24 rooms each, total of 192 rooms. Above them a floor that includes 17 rooms and a business lounge, on top of them 3 floors for rooms - total of 64 rooms.

The total leasable area – approx. 18,000 sqm.

The offices:

18 typical floors – the area of a typical floor for lease is approx. 1,384 sqm and the total leasable area is approx. 25,170 sqm.

The offices are leased to liberal professionals, lawyers, bank managements, IBM offices, etc.

There are 12 passenger elevators in the tower – 6 elevators to the hotel and 6 elevators to the office floors.

Typical floor plan:

2.4.6 The parking lot that serves the Property and its components

According to data provided by the client commissioning the Opinion, the parking lot includes 3,200 parking spaces, with the following breakdown:

Floor	No. parking spaces
Ground	200
-1	650
-2	750

-3	800
-4	800
Total	**3,200**

The operation of the parking lot:

From the Company's data there are currently about 3,100 active subscribers, average monthly subscription fee - NIS 800 + VAT.

There are approx. 11,000 vehicle entrances to the parking lot on average per day, divided to approx. 8,000 casual parker entrances and approx. 3000 subscriber entrances.

Approx. 62% of the causal parker entrances are for a period of up to two hours. 21% of the causal parker entrances are for a period of 3 hours. The rest are for a period of over 3 hours.

The parking fee for casual parkers:

First hour NIS 14, each additional quarter of an hour NIS 3, up to a maximum of NIS 70 for all-day parking. Evening's, weekends' and holidays' rate is NIS 10 with no time limit. The rates include VAT.

Storerooms:

Total storeroom areas according to building permit plans are approx. 2,500 sqm, of which areas for marketing are approx. 2,076 sqm. The remaining of the area is used for operation.

Additional revenues:

In accordance with the Company's figures, there are revenues due to management fees from the subscribers, advertising on the parking lot's pillars, the taxicab stand and the car wash facility.

2.5 Licensing

The built-up areas were built in several construction phases, and according to many building permits.

Following are some of the main building permits:

Building	Permit No.	Date	Substance
Parking Lot	4-980345	April 6, 1998	Changes in 4 parking levels, versus permit no. 4/950764 dated August 28, 1995 and permit no. 4/970405 dated May 26, 1997.

Mall	4-980991	October 20, 1998	Changes versus permit no. 4/960594 dated July 4, 1996 (the base, commercial and public floors) and permit no. 4/980184 dated June 10,1998 (health club).
Round	4-980606	June 25,1998	Office floors – Round tower - changes during construction – variance application. Changes versus permit no. 4/960595 dated July 7, 1996.
	3-220843	November 4, 2002	Changes in the visitors' level.
Triangular	4-980476	May 21, 1998	Floors 5-27 - changes during construction. Changes versus permit no. 4/961072 dated December 4, 1996.
	4-970717	August 20, 1997	Triangular tower, floors 28-40. Floors 28-40 for offices. Floors 39-40 continuation of core only.
	4-980603	June 25, 1998	Changes on all floor levels. Floor 39 – new office floor, changes technical areas on floor 40.
Square	20060074	January 30,2006	Construction changes and additions on the ground floor of the Square tower which include – changes and addition of main areas on the ground floor, construction of a gallery, kitchen storeroom and a kitchen service elevator from the parking lot level to the gallery level. Re-designation from offices to hotel entrance lobby, synagogue and a kitchen storeroom on the ground floor.
	20060075	January 30, 2006	13 hotel floors, 18 office floors and 2 technical floors in the Square tower at the Ha'Shalom center, above 4 existing floors and basement floors.
	20060076	January 30, 2006	Changes and building additions in the basement and ground floors.

Forms 4 and construction completion certificate:

Building	**Form 4**	**Completion certificate**
Parking Lot	Issued on March 31, 1998	Issued on November 21, 2002
Mall	Issued on March 30,	See reference in the Square tower

	1998	
Round	Issued on December 27, 1999 for floors 29, 36, 37, 38, 39, 42, 43	Issued on November 26, 2002 for a total area of 33,890 sqm.
	Issued on August 29, 2001 for floors 5-12, 19-22, 27-28, 30-31, 33-34, 40-41, and parts of floors 13-14, 16-18, 32, and in any case no more than 25,155 sqm.	
Triangular	Issued on January 17, 1999 whereby it is possible to populate 21,975 sqm.	Issued on May2, 2002 for Phase A in the Triangular tower (23,152 sqm) without floors 26-27. Issued on May 2, 2002 for Phase B in the Triangular tower (area of 12,946 sqm) without floor 34.
	Issued on August 29, 2001 to the upper part of the Triangular tower for floors 29-33, 35-39 and parts of floor 28, and in any case no more than 12,574 sqm.	
Square	Issued on March 20, 2008 for Phase A which includes floors 18-35 for offices and technical areas only, and does not include the hotel floors.	As informed, the Company is working nowadays to receive a completion certificate for the mall and the Square tower.
	Issued for the hotel on May 1, 2008.	

Business License

For the parking lot, the mall and the amphitheatre have a business license that expires on December 31, 2013.

The hotel has a temporary business license that expires on July 11, 2012.

2.6 Plans for application for a permit for interior changes to areas of Azrieli Center

As we were informed by the Company, in the context of the proceedings for receipt of a completion certificate for the mall areas and the Square tower, the Company was required to perform as-made permit plans that shall include also renewed applications for changes made in accordance with applications submitted in the past, including in respect of the parking lot and the mall.

The main changes:

Item	**Change**
Level -1 of the Square tower (parking lot)	Addition of main area of approx. 143 sqm and changes to the service areas on level -1 for the purpose of adjustment thereof to the hotel's usage.
Mall	Interior changes from cinemas to commerce – preparation of H&M store, addition and/or replacement of galleries in Zara, H&M and Superpharm stores.

As informed, the applications for a building permit have been filed to the local authority and not approved yet.

Summary of the areas in accordance with the permit plans and as-made plans (insofar as shall be approved):

Designation	**Main Area in sqm**	**Service Area in sqm**	**Total in sqm**	**Comments**
Underground parking lot, storerooms, open floor and IEC control station	2,708	119,550	122,258	According to as-made plan
Bridges (above Petach Tikva Rd., Hashalom railway station)		1,365	1,365	According to building permit plans
Mall and public areas	31,167	28,004	59,171	According to as-made plan
Round tower	45,436	10,274	55,710	According to building permit plans
Triangular tower	39,631	8,049	47,680	
Square tower	28,787	11,787	40,574	
Total	**147,729**	**179,029**	**326,758**	

To the best of our understanding, no betterment levy is expected in respect of approval of the permit application plan since the limit of areas of a public nature set forth in the zoning plan (4,000 sqm) is kept in the framework of the application (see further details regarding areas of a public nature in Section 5.1 below) on the one hand, and on the other hand there is no deviation in the main building area designated for commerce, compared with the commercial area approved for construction in the zoning plan.

2.7 The Management Companies

The mall and the office towers are managed by two separate management companies. The lessees in the mall are paying to the management company management fees based on actual costs + 10%-

15%. The lessees in the offices are paying (except for Bezeq) management fees based on actual costs + 15%.

We reviewed the 2012 expense budget.

The main items in the management costs of the mall are:

Item	Total Budgeted Expenses
Security, cleaning and maintenance	NIS 10,465,296
Salaries, bookkeeping, legal	NIS 4,204,795
Advertising and marketing	NIS 1,635,000
Insurance and miscellaneous	NIS 1,135,650
Public electricity	NIS 3,779,475
Total	**NIS 21,220,216**
Revenues to owners	NIS 3,553,526
Total	**NIS 24,773,742**

These costs reflect approx. NIS 63 on average per sqm for lease per month.

These costs were found compatible with the standard in similar commercial centers.

The main items in the management costs of the offices are:

Item	Total Budgeted Expenses
Security, cleaning and maintenance	NIS 15,817,899
Salaries, bookkeeping, legal	NIS 5,562,498
Advertising and marketing	NIS 193,000
Insurance and miscellaneous	NIS 1,457,824
Public electricity	NIS 6,043,816
Total	**NIS 29,075,037**
Revenues to owners	NIS 9,348,883
Total	**NIS 38,423,920**

These costs reflect approx. NIS 21 on average per sqm for lease per month.

These costs were found compatible with the standard in offices towers at this level.

The accounting firm Brightman Almagor Zohar & Co. audited the profit and loss figures for the management operations of the property in 2010. The responsibility for the information lies with the Company.

We were also presented with the management companies' revenue and expenditure figures for 2011, from the Company's submitted trial balance sheet. These figures have not yet been checked nor audited by the auditors.

2.8 Electric power services to lessees

A step down power transformer is installed in the Property. The Company is collecting from the lessees electric consumption according to low voltage rate and pays to the IEC according to high voltage rates. From such settlement of account the Company derives an annual cash flow surplus, see specification in Section 4.2.7 below.

3. Description of legal rights

3.1 Information from the Rights Registry

According to information from the Rights Registry dated January 10, 2012, which was produced via the website of the Ministry of Justice, the following details arise:

3.1.1 Block 7106, parcel 59

Land area - 31,992 sqm.

Owner - the City of Tel-Aviv.

Lessees - Canit Hashalom Investments Ltd. for a period of 200 years.

Expiration date February 6, 2195.

Mortgages There are mortgages registered on the lease of Canit Hashalom Investments Ltd. in favor of an investment company of Bank Leumi, Bank Leumi Le'Israel B.M. and Bank Hapoalim Ltd.

Caveats –

Caveats are recorded in favor of:

Bezeq the Israel Telecommunication Corporation Ltd.

Ha'Yarden hotels M.H.Y Ltd.

Israel Electric Corporation Ltd. on an electric sub-stationand an easement on the transported and on the tunnel and basements[3].

NTA - Metropolitan Mass Transit System Ltd.

Easement - An easement is registered in favor of the City of Tel Aviv-Jaffa for free public passage through passageways on the ground floor, first floor and second floor.

3.1.2 Block 7102 parcel 49

Land area - 903 sqm.

[3] An area leased to the IEC which is designated for the building of a sub-station. This area was not taken into account in the calculation of the valuation which is specified below.

Owner -	The City of Tel Aviv-Jaffa.
Lessees -	Canit Hashalom Investments Ltd. for a period of 200 years. Expiration date February 6, 2195.
Caveat -	A caveat is registered on an antiquity site.

3.2 Lease agreements

3.2.1 Underlying Agreement

On August 18, 1992, an agreement was signed between the City of Tel Aviv-Jaffa and Canit Hashalom Investments Ltd. (an underlying agreement that defines the undertakings of the parties in connection with the Property of the contemplated project).

It transpires from the provisions of the agreement, *inter alia*, that separate lease agreements will be signed for parts of the project, as follows:

- For the first stage – the parking lot, the commercial center and one tower with minimum floor area of 20,000 sqm.

- Separate lease contract for every additional tower.

On April 24, 2002 a compromise agreement was signed between the parties to the underlying agreement, following which, in accordance with information provided by the Company, a consideration was paid to the City due to the removal of the marketing limitation for 50,000 sqm of offices designated for vacation that were set forth in detailed Plan No. 2401 which is specified in Section 5.1 below. Detailed Plan 2401C that was approved in 2005 includes the removal of the limitation as aforesaid (See Section 5.2 below).

3.2.2 Lease agreement no. 1 (parking lot, commercial center and Round tower)

The main principles of a lease agreement dated October 23, 1996 between the City of Tel Aviv-Jaffa and Canit Hashalom Investments Ltd. which was presented to us:

- The leased property - The boundaries of the plot of land and the plot of the Round tower. Until the completion of the construction of the shopping center, the Developer will be considered a licensee in the area of the other plot on which the Company shall build parts of the parking lot and the shopping center.

- The lease period – 200 years commencing on February 7, 1995 and expiring on February 6, 2195.

- Lease fees - Lease fees were paid for the leased area for the entire lease period, and no annual lease fees shall apply.

- Consent fees – In any case where the Developer shall transfer or grant to others any rights under this contract, provided that such transfer or grant are permitted according to the provisions of this agreement, the Developer shall not be required to pay the City any consent fees or similar payment.

- Charge and assignment – If the Developer has fulfilled its undertakings under this agreement for construction of the parking lot and the shopping center, the Developer will be entitled to charge them as it deems fit, provided that it shall be assured that whomever acquires the leased area by virtue of exercise of the charge, will meet the criteria that guided the City in choosing the Developer according to the agreement, and the continued construction of the project and the operation, maintenance and management thereof in accordance with the provisions of the agreement are assured. If the Developer has fulfilled its undertakings under this lease agreement and contract for the building of a tower or towers, the Developer will be entitled to charge the tower or towers as it deems fit.

3.2.3 Lease agreement no. 2 (Triangular tower)

Following are the main principles of a lease agreement dated December 28, 1997 between the City of Tel Aviv-Jaffa) and Canit Hashalom Investments Ltd. which was presented to us:

The leased property – The land within the plot area of the Triangular tower and anything to be built thereon. The leased property is designed to enable the Developer to build the Triangular tower.

The lease period – for 200 years commencing on February 7, 1995 and ending on February 6, 2195.

The remaining sections of the agreement are similar to those specified in agreement no. 1 above.

3.2.4 Lease agreement no. 3 (Square tower)

The main principles of a lease agreement dated December 28, 2008 between the City of Tel Aviv (and Canit Hashalom Investments Ltd.:

The leased property – The land within the plot area of the Square tower and anything to be built thereon. The leased property is designed to enable the Developer to build the Square tower.

The lease period – for 200 years commencing on February 7, 1995 and ending on February 6, 2195.

The remaining sections of the agreement are similar to those specified in agreement no. 1 above.

3.3 Undertaking to populate the Square tower dated February 28, 2008

We were presented with a letter of undertaking dated February 28, 2008 addressed to the Local Committee for Planning and Construction of Tel Aviv, from Canit Hashalom Investments Ltd. with the following main principles:

- In view of the fact that on November 3, 2002 a permit was issued for the vehicle tunnel connecting Menachem Begin Rd. with Azrieli Center in the basement parking level +7.40, but the permit was not realized due to the Company’s estimate that for reasons of transportation and security there is no need for another entrance, it was agreed, after further discussion with the City that the occupancy permit is granted subject to the Company’s statement that a mechanism to exhaust the review of the need for the tunnel will be determined, in accordance with the Municipal Engineer's application to the Ministry of Transport for receipt of its professional position on the necessity of the tunnel. As notified, as of the date of the valuation, the position of the Ministry of Transport regarding the tunnel has not been received yet.

- After hearing the arguments of Canit Hashalom on this subject and if it is found that building the tunnel is necessary, the Company shall act in proximity thereto to build the tunnel, whether by itself or by a third party, and in any case no later than two years after receiving the Ministry's position, subject to obtaining the appropriate permits from the competent authorities.

- The Company further undertook to build, at its own expense, the bridge connecting the Azrieli project to the southern side of Ha'Shalom Rd., if it is decided to build a railway station at the site and/or a connection to the Shefa-Tal complex is required, in accordance with the timetables as determined by the Municipal Engineer, and to submit to the City the calculations of the building areas of the construction as actually performed on the basis of measurement plans, within 3 months from the date of signing this undertaking. As notified, it has been agreed between the Company and the City that the planning stage has not matured yet for making a decision.

3.4 Guarantees for Developer's Undertakings

To secure all of the developer's undertakings, the Company deposited unconditional bank guarantees in the (nominal) amount of NIS 16,000,000. As of December 31, 2011 the amount is approx. NIS 30,000,000.

4. The economic activity in the Property

4.1 Actual revenues according to the Company's financial statements:

A table specifying the actual revenues from rental fees over the years, as transpires from the Company's financial statements and income forecast for 2012 based on signed contracts and subjective estimates of the Company's management based on past experience and indications received from lessees as of the date of the valuation, with respect to changes in the terms and conditions of the existing contracts or renewals of contracts which expired during 2012.

The mall:

Item/Year	**2009**	**2010**	**2011**	**2012 forecast (***)**
Income from rental fees	NIS 95,428,000	NIS 101,833,000	NIS 105,453,000	NIS 110,063,000
Income from additional revenue	NIS 160,000	NIS 252,000	NIS 205,000	NIS 220,000
Income from casual stalls	NIS 0	NIS 0	NIS 361,000	NIS 603,000
Total	**NIS 95,588,000**	**NIS 102,085,000**	**NIS 106,021,011**	**NIS 110,886,000**

The towers:

Tower/Year	2009	2010	2011	2012 forecast (***)
Round (*)	NIS 61,190,667	NIS 59,456,000	NIS 63,999,000	NIS 66,677.000
Triangular	NIS 45,112,000	NIS 47,659,000	NIS 46,657,000	NIS 48,161,000
Square (**)	NIS 42,168,000	NIS 44,933,000	NIS 47,347,000	NIS 47,480,000
Total	**NIS 148,470,667**	**NIS 152,048,000**	**NIS 158,003,000**	**NIS 162,318,000**

(*) Doesn't include the area self-used by Azrieli Group Ltd.

(**) The population of the Square tower commenced in the second half of 2008 and ended during 2009.

(***) See reference in Chapter 10 below.

4.2 An analysis of the data upon which the valuation is based

4.2.1 Basis of the data

The data in respect of the rental fees was received from the Company's collection system in respect of each and every lessee in the Property.

The commercial areas are leased to 184 lessees. The occupancy rate is approx. 99%, there are approx. vacant 343 sqm (formerly an area leased to the Markedo restaurant) divided into approx. 204sqm commercial area plus approx. 139 sqm commercial gallery.

The office areas and the hotel approx. 149,390 sqm (excluding an area used by the Azrieli Group) are leased to 178 lessees. The occupancy rate is approx. 100%.

We checked 20% of the contracts on a random basis and found them to match the data received from the Company, and also the contract between the Company and Bezeq, as a primary lessee, was checked.

4.2.2 The lease period

Mall – commercial areas:

Segmentation of the expiration dates of the lease agreements:

Year	No. of contracts expiring	%
2012	18	9.8%
2013	42	22.8%
2014	34	18.5%

2015	33	17.9%
2017-2020	57	31.00%
Total	**184**	**100.0%**

During 2012, 18 contracts (approx. 1,400 sqm) are expected to expire. A considerable part of the lessees have an option to extend the contract, and as was informed based on past experience they will probably exercise it. With respect to some of the lessees, the commercial conditions have been agreed and the contracts extended.

The average rental fees in areas, the contracts for which are expected to expire during 2012, are similar to the average rental fees in the mall and it is therefore reasonable that also other lessees would pay these rental fees.

Towers – the office areas

Round tower - The lease agreements expire during 2012-2019. During 2012, 23 lease agreements are expected to expire. The lessees have an option to extend the contract, and as was informed based on past experience they will probably exercise it. With respect to some of the lessees, the commercial conditions have been agreed and the contracts extended.

Triangular tower - The lease agreements expire during 2012-2018. During 2012, 7 lease agreements are expected to expire. The lessees have an option to extend the contract, and as was informed based on past experience they will probably exercise it. With respect to some of the lessees, the commercial conditions have been agreed and the contracts extended.

Square tower - The lease agreements are expected to expire during 2012-2020. During 2012, 4 lease agreements are expected to expire, the lessees have an option to extend the contract, and as stated, according to past experience, they will probably exercise such. In respect of another part of the lessees, the commercial terms had been agreed upon and the contracts were extended.

4.2.3 The rental fees

The mall – It transpires from the data that the rental fees for the commercial areas range widely between NIS 38 per sqm per month (storerooms) and approx. 3,400 per sqm per month (stalls), where the average, including large stores, is approx. NIS 282 per sqm per month.

It transpires from an analysis of the gaps that the difference derives, *inter alia*, from the difference in the location of the stores (proximity to entrances and crowd-attracting stores

which provide higher/greater exposure, versus rear and lateral location, location on the public floor versus the first and second mall floors), the size of the store, the type of activity and the date of the commencement of the lease (old contracts versus new contracts).

The office towers - Average rental fees (not including the area leased to Bezeq) is approx. NIS 99 per sqm per month. These rental fees were found to be appropriate and match similar/substitute properties.

We have carried out for the purpose of preparing the opinion, a distinction between 2 types of lessees and leased properties:

- Long-standing and significant contracts – lessees who hold more than half a floor and have been in the property for over 6 years (there are several lessees who have been in the place since the beginning of occupation thereof, and lease significant areas at rental fees lower than the average rental fees at the property).

- Other contracts and lessees at the towers.

The dispersion of the areas:

Item	**Area in sqm**	**Average rental fee**
Long-standing and significant contracts that were populated until December 31, 2005	35,735	NIS 88
The other contracts	73,357	NIS 104
Total	**109,092**	**NIS 99**

Bezeq's areas are leased in consideration for approx. NIS 72 per sqm per month. These rental fees are lower than appropriate rental fees.

Hotel - The hotel is leased at an average rental fee of NIS 63 per sqm per month. The lease period expires in October 2020. The hotel was leased as a shell. The lessee performed all of its finishing and adjustment work at its expense since the rental fees are low, there is no impediment for leasing the hotel for a higher rental fees to a substitute lessee.

4.2.4 Changes that occurred over the last year - 2011

Commerce:

In the end of 2011 the Forever 21 store began operation. During 2011 approx. 4,250 sqm were leased (including Forever 21 in an area of 2,200), at average rent of NIS268 per sqm per month (the average rent net of the area leased to Forever 21 is at the range of NIS 371 per sqm per month). In addition storerooms and stalls were leased.

Offices:

Approx. 13,200 sqm of offices was rented for average rental fees of approx. NIS 100 per sqm per month.

4.2.5 Forecast for the next year - 2012

No significant changes are expected in the commercial areas and the offices.

4.2.6 Parking and storerooms that serve the Property and its components

The parking lot's business activity figures (excluding V.A.T), based on signed contracts and subjective estimates of the Company's management based on past experience and indications received from lessees as of the date of the valuation, with respect to changes in the conditions of existing contracts or renewals of contracts expiring in 2012.

According to the Company's data it transpires that the segmentation of the revenues from subscribers and casual parkers over the years is similar, and therefore it is possible to assume that this trend will continue also in the future.

Parking lot:

Item/Year	**2009**	**2010**	**2011**	**2012 Forecast (***)**
Income from subscribers	NIS 20,557,000	NIS 23,090,000	NIS 23,830,000	NIS 25,268,000
Income from casual parkers	NIS 20,427,000	NIS 21,890,000	NIS 22,463,000	NIS 24,428,000

Operation costs	NIS -13,395,000	NIS -13,545,000	NIS -13,289,000	NIS -14,176,000
Operating profit	**NIS 27,589,000**	**NIS 31,435,000**	**NIS 33,004,000**	**NIS 35,520,000**

Storerooms:

Item/Year	**2009**	**2010**	**2011**	**2012 Forecast (***)**
Income – from storerooms and others	NIS 6,200,000	NIS 1,631,000	NIS 2,454,000	NIS 2,040,000

(***) See reference in Chapter 10 below.

4.2.7 Surplus from electric services to lessees

As stated above, there is a difference between the cost of electricity which is paid by the Company to the IEC and the sum charged to the lessees.

The annual cash flow surplus:

Year	**2009**	**2010**	**2011**	**2012 forecast**
Annual surplus	NIS 3,981,000	NIS 4,253,000	NIS 3,299,000	NIS4,150,000

5. Description of planning figures

The sources for the information: information existing in our firm and information from the City of Tel Aviv

5.1 Detailed Plan No. 2401

The plan was published for validation in Official Gazette No. 4265 dated December 4, 1994.

The purpose of the plan, *inter alia*:

- To redesign the area in order to create a Central Business District along the "Ayalon" highway.
- To build a Central Business District on a building area of approx. 150,000 sqm that includes areas of offices, commerce, recreation and entertainment. The building rights allow the conversation of up to 15,000 sqm office area to residence and hotel area.
- To determine several basements designated mainly for parking, above which up to four above-ground levels will be allowed

covering up to 80% of the lot area. Above them, the construction of 3 high-rise buildings will be permitted.

Lot use: Central Business District.

Uses - Offices, industry (causing no nuisance), commerce, personal services, entertainment, public uses, as well as residences and hotel accommodation. The office areas will be at least 70% of the total construction area. Up to 15,000 sqm of office area may be converted to construction of residential apartments and/or hotels. The conversion of the areas shall be made according to a key of 1 sqm of residences and/or hotels equalling 1 sqm of office space. The residences and/or hotel, if built, will be according to the following conditions: residences will be incorporated only in the top floors of the high-rise buildings, no lower than the 20th floor above the Petach Tivka Rd. level. This limitation shall not apply to the hotel. Residence and hotel areas will have a separate entrance, separate elevators and separate parking. Commercial, entertainment and personal service areas will be up to 25% of the total construction area. Public uses, such as conferences halls, museums, halls for sports and cultural activities and similar uses will be at least 4,000 sqm.

The building rights - The total building area will be 100,000 sqm for main uses above the entrance level. In addition, 50,000 sqm will be permitted for main uses above the entrance level for offices designated for vacation, as defined below. The service areas will include the following areas: shelters and restrooms for maintenance on the floors of up to 20 sqm per floor. Machine rooms, electricity, ventilation shafts and piping, elevators, escalators, parking lots, areas and passageways for loading/unloading, etc. The service areas will include the public passageways in accordance with the legal regulations, except for passageways wider than 3m, where tables and chairs related to the commercial uses may be placed. In this case, 10% of the said area will be considered as main area. Lobbies, stairways and entrance halls will be considered as service areas in their entirety, provided that no commercial use will be made therein. The total service areas will not exceed 202,500 sqm, 150,000 sqm of which below the entrance level.

Height and land coverage - Construction of up to 5 basement floors for parking will be allowed. Up to 4 levels above ground level will be allowed, each one of which covering no more than 80% of total lot area. A transparent cover above the public space will be allowed on the top floor. Above the aforesaid levels three high-rise buildings will be allowed, covering in total no more than 30% per floor of the total lot area. The building height is as follows: up to 175m from street level (up to 44 floors from street level), up to 158m from street level (up to 40 floors from street level) and up to 140m from street level (up to 36 floors from street level).

Offices for vacation[4] - 50,000 sqm of office space designated for vacation of offices from residential areas. The office towers shall be designed according to such planning and technical specifications enabling 50,000 sqm thereof to be suitable for occupation by occupants to be vacated from offices designated or vacation.I n the first stages, building permits will be issued for areas not exceeding 100,000 sqm. The building permits for building the office buildings on an area of 50,000 sqm designated for the offices, which are designated for vacation will be issued gradually, only for the sold or leased to occupants having vacated offices designated for vacation, who shall have vacated in practice.

Transport - Implementation of the plan will be conditioned upon the implementation of transport requirements relating to the peripheral roads outside the area of the plan, as marked in the transport annex and in accordance with the stages of construction. It was determined that: construction of over 100,000 sqm will be carried out through an additional entrance from Petach Tikva Rd. from south to north (the tunnel).

5.2 Detailed Plan No. 2401C

The plan was published for validation in Official Gazette No. 5379 dated March 15, 2005.

The purpose of the plan - Redistribution of construction areas in Plan 2401 and change of requirements for the vacation of offices from residential areas in the city, by changing requirements for populating the office areas and other changes in the building instructions.

- Section 8.1.2 in Plan 2401 will be cancelled and replaced by the following language: to build a central business district on construction area of 150,000 sqm, which includes office, recreation and entertainment areas. In the framework of the building rights 16,000 sqm of main area may be converted to residence and/or hotel.

- The maximum main area for construction in the CBD will be 150,000 sqm above-ground.

- The transfer of 17,500 sqm of service areas from the levels below the entrance level to levels above the entrance level will be permitted, provided that there will be no deviation from the total service areas permitted for construction in accordance with Plan 2401.

- It is possible to transfer up to 3,000 sqm from the main areas above-ground to underground for all the purposes permitted by Plan 2401, except for residential use.

[4] See amending plan in Section 5.2.

- An addition of two partial floors above the Petach Tikva Rd. street level (two closed galleries) will be allowed, without changing the building shell as approved in Plan2401, provided that the total main and service areas permitted for construction will not be changed.

- An addition of one floor in the three high-rise buildings (in addition to the 2 partial floors, as aforesaid). In the buildings named the Triangular and the Round the roof level may be raised by 3m each relative to Plan 2401. The roof level without the banister and/or technical facilities will not exceed 161m in the Triangular tower and 178m, in the Round tower.

- In the Square tower, the roof level may be raised by 6m relative to Plan 2401. The roof level without the banister and/or technical facilities will not exceed 146 meters.

- In the framework of the service areas that are permitted by virtue of this plan, the Municipal Engineer may permit the inclusion of storerooms in the tower cores and on the technical floor.

6. Principles of the valuation

There are 3 main valuation approaches that are customary for the valuation of real estate properties.

6.1 The income capitalization approach

In the income capitalization approach, expression is given to the value of the property according to the cash flow generated by the property during its economic lifetime. The cap rate used to discount the cash flow is determined according to the type of property, the risk level and the uncertainty regarding the receipt of the projected cash flow, the size of the property, etc.

This approach is customary in the valuation of income-producing properties.

The mall and office towers are by definition a property producing a current income.

6.2 The comparison approach

The comparison approach is the best and preferred approach for assessing the value of property.

According to this approach, the value of a property is estimated based on comparison data for similar properties in the vicinity while making the necessary adjustments (for location, size, standard, etc.).

Nevertheless, commercial centers, malls and office towers are unique properties. There are purchase transactions of malls but in light of the complexity of the property and the many adjustments required, the use of this approach could cause a distortion of the results.

6.3 The cost approach

In the cost approach, expression is given to the value of the property as the sum of the value of its components. Property value using this approach includes the value of the land with the added cost of constructing the property, while taking into account physical, planning depreciation with the addition of developer's profit which is set according to the type of property, its physical state, the state of the market, etc.

In the case subject matter of the Opinion, the cost approach is irrelevant and constitutes an indication to the total investments in the Property.

7. Principles, factors and considerations in the valuation

The main principle in the valuation of real estate property is the principle of the highest and best use (HBU) of the property. We have examined the Property contemplated in the valuation according to this principle and have formed the general opinion that the present use is the highest and best use.

In the valuation of malls, commercial centers and office towers the following general factors and considerations are taken into account:

Location

One of the most important factors/elements in the valuation of commercial properties is the location. Transport accessibility and convenient access to public transport, within residential neighbourhoods, adjacent to/within areas of employment, on main traffic arteries (arterial roads), and others.

Supply & demand and occupancy rates

It is of great importance to assess the market's characteristics, whether the real estate market is on a downwards trend in demand or whether the market is seeing an upswing.

In assessing value using the income capitalization approach, the relevant factors and considerations are:

The leased area

The characteristics of the leased area include the following factors which affect rental fees value: the size of the leased area; the gross/net ratio; the relative location - floor (especially when this involves a multi-storey structure); the standard of finishing and construction; the property's goodwill; the management.

The rental fees

In light of the fact that malls/ commercial centers/ office towers are income-producing properties, their valuation derives from the future flow of receivables. Therefore, it is required to undertake a comprehensive examination of the rental fees levels in the past and in the present, which shows whether the rental fees being obtained from the Property are appropriate. Should the rental fees be higher than those customary in the vicinity, without good justifications, then there is the possibility that the rental fees in the future years will get in line with the customary rental fees in the vicinity. This possibility must be expressed in the income flows for future years, and, as may be required, apply a discount to the rental fees.

On the other hand, there is a possibility that the present rental fees are low, in which case one may assume that in future it will be possible to lease the Property at a higher rent that matches the market.

In this context, it is required to mention the importance of the mechanism used to update rental fees.

Identity of the lessees and the mix

As stated above, as the value of the property is set mainly on the basis of the flow of income paid by the lessee, it is required to carefully examine the financial strength of the lessees.

It is possible to separate the mix of stores in the commercial centers into several categories, such as: store size and type of activity; chain stores compared to local stores, an individual store.

The lease period

A long-term lease reduces the level of uncertainty regarding the ability of the investor to lease the Property in the coming years. The investor is assured, with a high degree of probability, a fixed cash flow for a long period of time. In most commercial centers and office towers, the lease period ranges in the vicinity of 5 years with options to the lessee, especially in light of the large investment that the lessees invest in their store/office.

The cap rate

The capi rate reflects the yield required in order to be attractive for capital investment. Therefore, the choice of the suitable rate constitutes a decisive factor.

The customary cap rate in the market is set at a particular point in time, for a particular type of property, and in the context of the interest rates in the economy at that time.

The cap rate may be both empirically inferred from known market data (the value of properties and rental fees in respect thereof in the free market)[5] and assessed using theoretical methods.

The cap rate elements

Risk-freemarket interest, illiquidity, transaction costs, management and collection, depreciation, inflation and real change, risk and entrepreneurship, land taxation.

[5] The basic cap rate used in the value calculation specified below originates from the market, from an analysis of comparison transactions made.

Summary of use of the valuation approaches:

	Valuation approaches
Commercial area/ the mall	Income capitalization approach Compare value to other commercial areas
Offices	Income capitalization approach Compare value to other office areas
Parking Lot	Income capitalization approach

8. Factors and considerations

In assessing the value of the Property, we have taken into account *inter alia*, the following factors and considerations:

- The location of the Property in the Tel Aviv City Center, in vicinity to central traffic arteries and near the Ha'Shalom railway station.

- The project's areas, the finishing standard, segmentation and mix of the lessees and uses.

- The Property's rights are capitalized lease rights from the City of Tel Aviv for a lease period of 200 years.

- Company's undertaking to build the tunnel and the bridge – insofar as shall be decided on its necessity, in accordance with the Company's estimate, the construction cost is estimated in the range of the sum of approx. NIS 4,000,000. The Company estimates that no decision will be made to build the aforesaid in the coming years, if at all. In light of the above, for reasons of conservatism and in reference to the Company's estimate of the low probability of building the tunnel and/or the unknown future construction date, we have deducted one half of the said amount, i.e., NIS 2,000,000, from the value of the Property specified below.

  - The actual revenues for previous years and 2012 revenue forecast, based on signed contracts and subjective estimates of the Company's management based on past experience and indications received from lessees as of the date of the valuation, with respect to changes in existing contracts and/or renewals of contracts expiring in 2012.

- Parking and storage areas in the basement:

  - As aforesaid, parking at Azrieli Center is for pay. In addition, storage areas, advertising areas and an area for a car wash facility are leased.

  - The operating profit from the operation of the parking lot, as specified above.

- The Mall:

- By definition, the mall is a property producing current income ("**Income Property**"), both from rental fees from the various areas in the mall and from management fees.
- The commercial center has started operating during April 1998 and is fully occupied.
- The total areas for marketing are as specified above.

- The Round, Triangular and Square towers:
  - As of the effective date, all of the areas in the office buildings are leased.
  - A self-used area by Azrieli Group of approx. 1,520 sqm on the top office floor of the round tower is not included in this Opinion.
- Investments in the Property:
  - We depreciated future investments in the Property.
  - In addition, according to the lease agreement with Bezeq, the Company has undertaken to provide a fund for the renovation of the Bezeq areas. The current value of the instalments balance (4 years) was depreciated.
- Other revenues:

  As aforesaid, the Company has revenues from the management company and from the sale of electricity.

  - The mall and the office towers are managed by management companies. In an income-producing property all revenues from the property, including the management company, are required to be considered as a single whole. In this case we have added the profitability of the management companies. Since the profitability of the management companies derives from business activity and changes in profit may occur as a result of changes in the scope of the expenses of the management companies, the full profit as aforesaid cannot be attributed to the Property. Cap rate embodies higher risk factors.
  - Revenues from sale of electricity – We discounted the revenues from the sale of electricity at a cap rate of 12%, which reflects the risks involved in operating such systems and the depreciation.

9. Comparison data

9.1 Malls and commercial centers

Most of the major income-producing property companies in Israel, are veteran companies with properties at a large scope, with high occupancy rates and with high-quality management. Alongside such, insurance companies, mainly Clal, Migdal and Harel and investment funds such as Reit 1, Sela Capital and others are also active in the market.

Some of the purchases are done aiming to better and improve the performance of the commercial center/mall, and some are done based on a consideration of secured return.

Comparison figures for the purpose of determination of the **cap rate for commerce** based on transactions carried out and published by the public companies on the market in the past year:

- Transactions not materialized (taken into account under required adjustments)

- According to reports on the MAYA site, on the dates August 16, 2011 and September 11, 2011, Azrieli signed contingent purchase agreements for the purchase of the "Ir Yamim" mall in Netanya, which is under advanced construction stages and is expected to be opened to the public in the beginning of 2012. As of September 11, 2011, lease contracts for approx. 70% of the areas for marketing had been signed, for which annual rental fees of approx. NIS 42,000,000 shall be paid. In the company's estimate, the annual NOI after leasing all of the areas, will be approx. NIS 61,000,000. The group purchased the mall in its state in two stages, half of the rights in the mall were purchased on August 16, 2011 for NIS 350,000,000 and the second half was purchased on September 11, 2011 for NIS 370,000,000. In addition, further costs are expected to apply to the group entailed in the completion of the mall, if any, estimated at approx. NIS 80,000,000 – 90,000,000. The calculated cap rate is approx. 7.62%. The transaction did not mature, in light of the disagreement of Azrieli Group to the conditions presented by the Antitrust Commissioner and the property is being remarketed.

- On August 3, 2011, Malisron reported that it was holding contacts for the sale of its entire rights and obligations in the Savionim Mall in Yahud, in consideration for approx. NIS200,000,000. According to complementary information held in our office, the calculated cap rate in the transaction is approx. 7.8%. On September 27, 2011 Malisron reported the cessation of the negotiations.

- On August 3, 2011 British Israel Company reported that it was holding contacts for the sale of all of its entire rights and obligations in Hazafon Mall in Nahariya, in consideration for approx. NIS 159,000,000. According to complementary information held in our office, the cap rate calculated in the transaction is approx. 8.2%. On September 27, 2011 British Israel reported cessation of the negotiations.

- According to a report on the MAYA site, on June 19, 2011, British Israel Ltd. purchased 50% of the rights in the Lev Hadera Mall, in Hadera, in consideration for NIS 260,000,000 (reflects a value of NIS 520,000,000 for the mall in its entirety). The annual NOI as of December 31, 2010 stands at approx. NIS 38,500,000. The calculated cap rate is approx. 7.4%.

- According to a report on the MAYA site, on April 5, 2011, Sela Capital Real Estate Ltd. Purchased 2 commercial centers at Rosh Ha'ayin, known as the Afek Center and Tal Center, at an overall commercial area of 6,100 sqm, for NIS 93,750,000. The properties are leased at an occupancy rate of 89% for 40 lessees, for annual rental fees of NIS 6,700,000. The seller undertook to ensure for the company minimal annual rental fees in the amount of NIS 7,360,000 in the first year. The calculated cap rate, considering the seller's undertaking, 7.85%.

- According to a report for quarter 2 of Africa Israel Properties Ltd., during April it completed the sale of its rights in the commercial center known as "Merkaz HaBama" at Ganei Tikva, for NIS 35,000,000. The calculated cap rate according to information held by our office is 8.4%.

- According to a report on MAYA site dated January 16, 2011 REIT 1 Ltd. purchased the "Globus Center" in Netivot in consideration for NIS 56,000,000. The center is approx. 5,500 sqm and includes approx. 25 stores, which are leased on the date of the transaction with 100% occupancy, the annual NOI is approx. NIS 5,000,000. The purchase will be made in two stages, stage B being contingent, *inter alia*, on the approval of a new zoning plan for the land which will permanently authorize the commercial use thereof. According to the report, the weighted yield for stages A and B is 8.95%.

- On December 31, 2010 it was published in the press that Supersal was purchasing from Azorim its share at the "Azorim Center" mall in Rehovot, in consideration of approx. NIS 34,000,000. The mall has area for marketing of 2,760 sqm + additional building rights, while Azorim holds 69% of the property. Net annual rental fees totaled to NIS2,600,000. The calculated cap rate – 9%.

- According to a report on the MAYA site on December 31, 2010, M. Aviv signed an agreement for the sale of a commercial building which is in construction proceedings, at the Lev Ha'ir project at Bait Intersection in Jerusalem for approx. NIS 47,000,000. The building is designated for a supermarket (Supersal) and is destined to include approx. 2,550sqm of commerce areas and storerooms, approx. 700sqm service areas and 120 parking spaces. The sale agreement cancels and replaces a lease agreement which was signed with the buyer in July 2009 for the lease of the building for 10 years + 2 option terms of 7 years each, in consideration for

monthly rental fees of NIS 298,000, linked to the consumer price index (approx. NIS 310,000 on the date of signing the sale agreement). The transaction reflects a return of 7.9% compared with the rental fee (approx. NIS 82 per sqm per month) in the cancelled lease contract.

- In the end of 2010, Amot consummated the purchase of BARAN's shares in Ness-Pan Ltd. According to a report dated November 17, 2010, the properties of the company in Israel include two commercial centers in Be'er Sheba and an employment and office complex at Beit Dagan. The occupancy rate at the properties – 96.6%. The transaction consideration – NIS 460,000,000. From the analysis of the information we have collected in respect of the transaction, the following details appear:

  - Commercial Center – B7 complex in Beer Sheba (adjacent to the Big Complex) serving as a shopping and entertainment center in a marketing area of approx. 23,400 sqm on a land in the area of 54 Dunams, purchased according to a return rate of 9.5%. It is expected that the center will be renovated and that the rental fees paid therein shall be improved.

  - "Nave Ze'ev" commercial center in Be'er Sheba – a neighbourhood center in a marketing area of 8,200 sqm which includes commerce, offices and clinics, built on approx. 10 Dunams of land, purchased according to an 8% rate of return.

  - The Beit Dagan ParkTech Employment Complex was purchased at an 8% rate of return.

9.2 Offices

- According to various releases, in the course of 2010 the following areas were leased in the Electra Tower on Yigal Alon st. in Tel Aviv:

  - In December 2011, an area of approx. 1,750 sqm on the 20-21 floors and 30 parking spaces were leased to Forex, at a rental fee of NIS 95 per sqm per month and NIS 750 per month for a parking space.

  - In March 2011, an area of approx. 8,000sqm, on the 26-31 floors was leased to Google, at a rental fee of NIS 105 per sqm per month.

  - In September 2010, an area of approx. 3,000 sqm, on floors 18-19 was leased to EBay., fully finished, fully finished al fees of NIS 100 per sqm per month.

- In September 2010, an area of 750 sqm, on the 40th floor, was leased, to the investment fund FIMI for rental fees of NIS 100 per sqm per month.

- In March 2010, an area of approx. 4,125 sqm on floors 34-36 was leased, fully finished, to Beit HaPraklitim for rental fees of NIS 100 per sqm per month.

- An area of 250sqm is offered for rent, at a high floor, fully finished, in consideration for NIS100 per sqm per month.

- An office at an area of 600 sqm is offered for rent, between the 20th to the 30th floor, fully finished, in consideration for NIS130 per sqm per month.

- Areas of 200-600 sqm are offered for rent, on the 43rd floor, fully finished, in consideration for NIS110 per sqm per month.

- In the Platinum Building, an office at an area of 370 sqm on the 20th floor is offered for rent, fully finished, in consideration for NIS120 per sqm per month.

- At the Millennium Building an office in the area of 250sqm, on the 19th floor is offered for rent, fully finished, in consideration for NIS140 per sqm per month.

- According to the financial statements of Electra Real Estate for Q4/2011, it appears that the value of an average sqm for offices at the Electra Tower on 86 Yigal Alon, is within the boundaries of NIS16,330. We shall state that the average price reflects that approx. 35% of the areas were leased at the shell level and approx. 65% of the areas were leased at a full finishing level.

- According to the financial statements of Meshulam Levinstein Real Estate for Q4/2011 it appears that the value of an average sqm for offices at the Levinstein Building on Menachem Begin St. in Tel Aviv, is within the range of NIS15,000.

- According to the financial statements of Meshulam Levinstein Real Estate for Q4/2011, it appears that the value of an average sqm for the offices at the Discount Building on Yehuda Halevi ST. in Tel Aviv is within the range of NIS 17,400.

9.3 Data for capitalization and office areas

Comparison data for purposes of determining the cap rates for the office areas based on transactions made and announced by the public companies in Israel during the past year:

- According to publication in the press, from December 27, 2011, Migdal purchased 50% in two office buildings in Ra'anana, leased in their entirety to Nice , in consideration for NIS106,400,000.

According to the publication, the transaction was carried out on the basis of an approx. 7.3% cap rate.

- According to a report on the MAYA site, on September 27, 2011, Isralom Assets Ltd. sold all of its rights at the "Vered House" in Givata'im, approx. 1,500sqm of offices, approx. 300 parking spaces and storerooms, in consideration for NIS 45,400,000. According to information held in our office, the transaction reflects a cap rate for the property, of approx. 8.6%.

- In April 2011 Electra Real Estate sold its share at "Beit Reinhold" at 26 HaBarzel St. in Tel Aviv. From information we have collected it appears that the rental fees paid are at the range of NIS85 per sqm per month for a very high finishing level, and that the transaction was carried out according to an 7.75% cap rate.

- According to a report on the MAYA site, on March 1, 2011, Sela Capital Real Estate purchased in a Lease Back transaction an office building which is used by the Bezeq management in the Romema neighbourhood in Jerusalem (Block 30075 Parcel 136), at an area of approx. 12,500sqm and approx. 400 parking spaces in consideration for approx. NIS115,000,000. The Company shall lease the building to the seller for a period of 10 years, in consideration for annual rental fees of approx. NIS10,650,000, the calculated cap rate is approx. 9.26%.

- According to a report on the MAYA site, on February 16, 2011, Kamur Ltd. Sold all of its rights (40% unspecific) in an office and commerce building, at a built area of approx. 16,300sqm, on 16 HaMasger St. in Tel Aviv, in consideration for NIS43,000,000. The 6 office floors are leased to the State of Israel and the ground floor, including two levels thereof, is leased to the car importer "Kamur Motors". The rental fees from the property for 2010 totaled at NIS 2,976,000. The calculated cap rate is approx. 6.92%.

- According to a publication in the press, on February 13, 2011, Migdal Insurance purchased the 3 office floors, at an area of approx. 2,370sqm and 39 parking spaces constituting the office foundation beneath the exclusive residential tower 1 Rothschild in Tel Aviv, in consideration for approx. NIS 40,000,000. According to publications, the entire area was leased in August 2010 to Bank Leumi, in consideration for rental fees ranging between NIS70 to 100 per sqm per month. The bank carried out finishing work at a very high level. According to an analysis we carried out, it appears that the average rate of return in the transaction is lower than 7%.

- According to a report on the MAYA site dated December 28, 2010, Orad Ltd. Sold, in a Lease Back transaction, a property at 4 Hamashbir St., in Holon, at a built area of approx. 8,000 sqm gross (out of that, half at the basement level), in consideration for NIS 32,800,000. The company shall lease the building in consideration

for NIS 218,000 per month for a period of 10 years, with an option for extension of the lease by 5 additional years. The calculated cap rate is approx. 8%.

- According to a report on the Maya website, on October 11, 2010, REIT 1 purchased one non-specific half of all of the rights in the property known as parcel 268 in block 6638 and in a 6-story office building built thereon, whose address is 6 Hanechoshet St., Ramat Hachayal, Tel Aviv, with an above-ground area of approx. 5,100 sqm in consideration for NIS 55,500,000. The building is leased to three main lessees for periods of up to two years. On the date of purchase of the object of sale, the occupancy rate is 51% and the annual rental fees deriving from the object of sale is approx. NIS 2.5 million. Indicates a cap rate of approx. 8.83%.

9.4 **Hotels**

The following comparison data have been taken into account:

- According to information held in our office, a lease agreement was signed between Isrotel and Electra, for the lease of 230 rooms, a spa and related areas, at a hotel in the Sea One project (Royal Beach Tel Aviv) in consideration for NIS 15,400,000 per year (the rental fees are minimal rental fees, the agreement includes an addition of revenues as a function of the business activity). The property will be handed over to Isrotel at a full finishing level, including fixtures and furnishing of the rooms and of the related public areas. The transaction reflects approx. NIS 5,580 per month per room (grosses up the spa and the related areas).

- According to information held at our office, lately a lease agreement for approx. 162 hotel units had been signed in a project which is destined to be built at the Herzliya Marina, according to a key of approx NIS 4,900 per month for a finished and ready to be occupied hotel room (including furniture).

- According to information published in the financial statements of Ogen Real Estate, on December 31, 2010, Fatal Hotels rented at the Wietzman Business Center located in the heart of T.M.R Park in Rehovot (adjacent to the Weitzman Institute and the Weitzman Employment Park at Ness Ziona) an area of approx. 6,654 sqm + 20 underground parking spaces, for a period of 15 years + an option for 10 more years, for the purpose of operating a hotel, at a rental fee of NIS 42 per sqm per month (the parking spaces included) + management fees in the amount of NIS 8 per sqm per month. The property was leased in a shell condition, all of the adjustment work will be borne by the lessee alone. According to information held at our office, a hotel including 116 rooms had been completed at the location, at an investment cost of approx. NIS28,000,000. The agreement reflects rental fees of approx. NIS 2,400 per room per month, at the shell level.

- Fattal leased (in 2008) a building on 17 HaBarzel St. in Tel Aviv, at an area of approx. 8,700sqm – Tel Aviv Leonardo Boutique Hotel, including 167 rooms, in consideration for $1,100,000 per year (approx. NIS2,200 per month per room). The company leased the building at a shell finishing level and carried out on its account all of the finishing costs, estimated at approx. NIS40,000,000 (approx. NIS240,000 per room).

9.5 Parking Lots

- According to publications in the press, dated December 7, 2011 it appears that Emed who held 50% of the parking lot on Hayetzira st. in Ramat Gan, purchased approx. one month ago additional 50% in the parking lot, in consideration for NIS 42,000,000 and completed its full ownership over the parking lot which includes 610 parking spaces. The transaction reflects approx. NIS 137,000 per parking space.

- According to a report on the MAYA site on September 27, 2011, Isralom Properties Ltd. Sold all of its rights at the "Beit Havered" in Givataim, approx. 1,500sqm of offices, approx. 300 parking spaces and storerooms for NIS 45,400,000. According to information held at our office, the value of a parking space was determined within the framework of the transaction at approx. NIS 90,000.

- According to the financial statements of Electra Real Estate for Q4/2011, it appears that the value of a parking space at the Electra Building parking lot on Yigal Alon st. is within the range of NIS 147,000.

- According to the financial statements of Africa Israel Properties as of December 31, 2010, it appears that the value of a parking space at the Government Campus parking lot at the range of NIS105,000.

- On June 21, 2011, Edri-El reported the purchase of 2 commercial floors as well as part of a parking lot space (173 parking spaces) at the Opera Tower in Tel Aviv, in consideration for NIS70.7 million. According to information held at our offices, the value of a parking space in the transaction was determined according to NIS 90,000.

- According to a publication in the press, on November 21, 2011, it appears that negotiations are being held for the purchase of the Mea (the "Hundred") Parking Lot, on Ibn Gavirol St. in Tel Aviv, which includes approx. 500 parking spaces, in consideration for NIS 43,000,000. Reflecting approx. NIS 86,000 for a parking space.

- Subscription asking and actual prices for roofed parking lots in the area:

Parking Lot	Monthly subscription price including VAT
The Millennium Tower	NIS 1,200
HaTichon Tower	NIS 700
Platinum Tower	NIS 900
The Government Campus	NIS 1,100
Heichal HaTarbut	NIS 900

10. The calculation of the valuation

We estimated the Property's value by the income capitalization approach.

The cap rate used in the calculation of the value originates from the market from an analysis of comparison transactions that were made. The information we have before us while analysing the transactions includes the rental fees that are paid in the current year and the price of the property as set in the transaction.

Therefore, when we analyse an income-producing property sale transaction, the multiplier (the total cap rate) which is calculated by dividing the reported annual rental fees by the transaction value, actually reflects all of the relevant components in the market by investors, buyers and sellers, and *inter alia*, future changes in the rental fees deriving from changes in the lease contracts and Index rise, projected macroeconomic changes in the market (inflation, interest rate, etc.) as well as the lease periods characteristic of the type of properties.

I.e, in order to use the multiplier / total cap rate in a property valuation with the same characteristics, it is necessary to use the rental fees known on the effective date (without any changes and future forecasts).

The rental fees:

The information base is the rental fees as of the effective date, based on actual lease agreements and appropriate rental fees for vacant space.

The calculation of the total rental fees was provided to us by the Company. No modifications were made by us to the figures.

The Cap Rate:

The cap rate – we have not find indications for changes in the cap rate that may change the cap rate used in the last opinion, i.e. a cap rate of 7.25% for the commercial areas.

The cap rate due to income from revenues and casuals in the commercial areas was taken in the rate reflecting the risk, an addition of 1% to the basic cap rate.

The cap rate for the office areas was set at weighted 7.5% – reflecting a cap rate of 7% for the long-standing and significant contracts (in light of a lower risk component) and a cap rate of 7.75% for the other contracts. This cap rate matches the office and employment areas in office buildings.

Cap rate for Bezeq areas and the hotel areas was set at a cap rate lower by approx. 0.25% than the weighted cap rate for offices, in light of the lower risk.

The cap rate for the parking lot was set according to 7.75%.

For the income from revenues and sale of electricity we set a cap rate which reflects risk and uncertainty.

We deducted a cost which is attributed to the transportation task.

Item	**Annual Income**	**Cap Rate**	**Value**
Mall-commercial areas	NIS 110,063,000	7.25%	NIS 1,518,100,000
Mall- Additional income from revenue and casual	NIS 823,000	8.25%	NIS9,970,000
Leased offices – excluding Bezeq	NIS 129,260,000	7.50%	NIS1,723,400,000
Bezeq offices	NIS19,390,000	7.25%	NIS 267,400,000
The hotel	NIS 13,660,000	7.25%	NIS 188,400,000
Vacant spaces (*)	NIS580,000	8.00%	NIS 7,200,000
Storerooms	NIS2,040,000	7.75%	NIS26,300,000
Parking lot	NIS35,520,000	7.75%	NIS458,300,000
Total	**NIS311,336,000**	**7.4%**	**NIS 4,199,070,000**
Profit from electricity	NIS 4,150,000	12%	NIS 34,500,000
Profit from management	NIS 12,800,000	9.4%	NIS 135,900,000
Future investments in the Property			NIS - 61,100,000
Deduction of transportation task			NIS -2,000,000

Total, rounded off			**NIS 4,306,400,000**

(*) approx. 343sqm (formerly area leased to Markedo restaurant) divided into approx. 204sqm commercial area plus approx. 139sqm commercial gallery.

The total value indicates average commercial area value of approx. NIS 46,000 per sqm, average office value of NIS 15,000 per sqm and parking space value of NIS 140,000. These figures match the market figures.

Sensitivity analysis

The results of a sensitivity analysis for changes in the cap rate:

	7.00%	**7.50%**	**8.00%**
Value of the Property	NIS 4,614,500,000	NIS 4,306,400,000	NIS 4,036,600,000

11. The valuation

In light of the aforesaid, our assessment of market value of the Company's rights in the Property (excluding the area self-used by Azrieli Group) in the free market, in the criterion of a willing buyer from a willing seller, free of any debt, charge, mortgage, including third-party rights, is in the range of **NIS 4,306,400,000**.

12. General

- The value does not include V.A.T.
- We have not related to taxation that may apply, insofar as shall apply, at the time of selling the Property.
- In our Opinion we referred to such forward-looking information that was provided to us by the Company's management, with respect to the 2012 forecast and income forecast, and is based on information available as of the date of the valuation and subjective estimates of the management, materialization of which is uncertain due to reasons beyond the Company's management control.
- The value fo the property in the Company's books – NIS 4,137,366,000.
- We have valuated the Property in the past for purposes of their inclusion into the Company's financial statements:

Effective date	**Value of the Company's Rights**	**Comments**
December 31, 2008	NIS 3,596,100,000	Commenced the population of the Square building during this year

December 31, 2009	NIS 3,725,100,000	
December 31, 2010	NIS 4,014,000,000	
June 30, 2011	NIS 4,133,100,000	

13. Disclosure Document

According to Standard 17.1 we requested from the Company a disclosure document pertaining to several issues.

On February 8, 2012 our firm received a disclosure document for the purpose of valuation of Azrieli Center, 1 Azrieli Center, Tel Aviv, for December 31, 2011, from the Company. A summary of the document:

- There are no protected tenants in the property pursuant to the Tenant Protection Law, 5732-1972.
- There are no tenants in the property without a valid lease agreement.
- There are no tenants in the property who are interested parties of the corporation, such as: a subsidiary[6], affiliates[7], etc, excluding the So-Good store at an area of approx. 103 sqm on the ground floor of the triangular tower.
- There is an undertaking which was made to the City of Tel Aviv regarding the construction of a tunnel under Begin Rd. and the construction of a bridge above Ha'Shalom Rd.
- There is no liability for compensation in respect of damage caused by the Property to third party land.
- There is no other material liability related to the land which affects the value of the Property and is not specified in the sections above.

14. Declarations

- We declare that to the best of our knowledge, the facts upon which this Opinion has been based are correct.
- The analysis and the conclusions are limited to the assumptions and conditions specified above.
- We declare that the legal information presented in this document is the legal information on which the valuation is based.
- We declare that we have no personal interest in the Property contemplated in the valuation, in the right owners therein or in the client commissioning the Opinion.
- The fees for this valuation not conditioned upon the results of the valuation have no material influence on our firm's income.

[6] A company in which another company holds 50% or more of its issued share capital or the voting rights.

[7] A company which is owned or controlled, indirectly, by the owner of the Property.

- The report was prepared according to the Real Estate Appraiser Regulations (Professional Ethics), 5726-1966 and according to the professional standards of the Appraisal Standards Committee.
- We declare that we have the necessary knowledge for making this valuation.
- The valuation was performed by the undersigned, without assistance.

Sincerely,

Annex D

Separate Financial Information

December 31, 2011

The Azrieli Group Ltd.

Separate Financial Information

For the Year 2011

Prepared pursuant to the provisions of Section 9C of the Securities Regulations (Periodic and Immediate Reports), 5730-1970

The Azrieli Group Ltd.
Separate Financial Information
For Y2011

Contents

To
The Shareholders of
Azrieli Group Ltd.
1 Azrieli Center
Tel - Aviv

Ladies and Gentlemen

Re: Special Audit Report on separate financial information in accordance with Regulation 9C of the Securities Regulations (Periodic and Immediate Reports) – 1970

We have audited the separate financial information, which is presented in accordance with Regulation 9C' of the Securities Regulations (Periodic and Immediate Reports) – 1970, of **Azrieli Group Ltd.** (hereinafter- "the Company") as of December 31, 2011 and 2010 and for each of the three years, the last of which ended on December 31, 2011. The separate financial information is the responsibility of the Company's Board of Directors and Management. Our responsibility is to express an opinion on the separate financial information based on our audit.

We did not audit the separate financial information from the financial statements of investee companies, the sum of the investments in which amounted to approximately NIS 461 million and approximately NIS 449 million as of December 31, 2011 and 2010, respectively, and the profit from such investee companies amounted to approximately NIS 18 million, approximately NIS 31 million and approximately NIS 55 million, for the years ended December 31, 2011, 2010 and 2009 respectively. The financial statements of those companies were audited by other auditors whose reports were furnished to us, and our report, in so far as it related to the amounts that have been included in respect of those companies, is based upon the reports of the other auditors.

We conducted our audit in accordance with generally accepted auditing standards in Israel. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by the Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and on the reports of the other auditors, the separate financial information has been prepared, in all material respects, in accordance with the provisions of Regulation 9 C' of the Securities Regulations (Periodic and Immediate Reports) – 1970.

Brightman, Almagor, Zohar & Co.
Certified Public Accountants

Tel Aviv, March 21, 2012

Azrieli Group Ltd.

Information on the Financial Position

	As of December 31	
	2011	2010
	NIS in thousands	NIS in thousands
Current assets		
Cash and cash equivalents	109,398	83,105
Financial assets held for trade	1,322,083	2,234,857
Trade receivables	5,279	6,500
Other receivables	34,100	11,570
Total current assets	1,470,860	2,336,032
Non-current assets		
Available for sale financial assets	1,256,346	1,789,993
Financial assets designated as at fair value through the statement of income	16,737	17,408
Investment property and investment property under construction	6,152,957	5,333,219
Investments in investee companies	4,401,133	3,876,883
Loans to investee companies	1,517,786	1,209,180
Fixed assets	5,276	4,127
Other receivables	25,129	8,786
Total non-current assets	13,375,364	12,239,596
Total assets	14,846,224	14,575,628
Liabilities and capital		
Current liabilities		
Credit from banking entities and other providers of credit	831,238	547,873
Trade payables	15,776	6,519
Other payables	38,713	38,493
Liabilities in respect of current taxes	2,646	15,069
Total current liabilities	888,373	607,954
Non-current liabilities		
Loans from banking entities	1,309,484	1,414,533
Bonds	651,359	677,355
Other liabilities	18,001	18,401
Deferred tax liabilities	927,399	744,464
Employee benefits	17,819	11,980
Total non-current liabilities	2,924,062	2,866,733
Capital		
Share capital	18,223	18,223
Premium	2,477,664	(*) 2,477,664
Capital reserves	143,030	(*) 564,394
Retained earnings	8,394,872	8,040,660
Total capital attributed to the holders of the Company	11,033,789	11,100,941
Total liabilities and capital	14,846,224	14,575,628

(*) Reclassified

March 21, 2012

Date of approval of the separate financial information	David Azrieli Chairman of the Board of Directors	Shlomo Scharf CEO	Yuval Bronstein Chief Financial Officer

Azrieli Group Ltd.

Information on the Comprehensive income

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Income			
From rental, management and maintenance fees	429,467	403,920	340,957
Net gain on the adjustment of the fair value of investment property and investment property under construction	188,839	429,078	123,342
Financing income	102,337	144,728	144,355
Other	44,855	25,970	365
Total income	765,498	1,003,696	609,019
Costs and expenses			
Cost of income from rental, management and maintenance fees	10,283	8,493	12,623
Selling and marketing	968	956	961
Administrative and general	53,910	57,662	36,139
Financing	212,601	180,138	186,357
Total costs and expenses	277,762	247,249	236,080
Income before Company's share of the profits of investee companies	487,736	756,447	372,939
Share of profits of investee companies, net of tax	444,675	611,295	450,441
Income before taxes on income	932,411	1,367,742	823,380
Tax on income – benefit (expense)	(336,557)	(143,562)	132,977
Net income for the year	595,854	1,224,180	956,357
Other comprehensive income (loss), net of tax			
Change in fair value of available for sale financial assets, net of tax	(439,145)	83,071	470,259
Actuarial gain (loss) in respect of defined benefit plan, net of tax	(18)	135	167
Translation differences in respect of foreign operations	3,991	(1,139)	(1,166)
Share of other comprehensive income (loss) of investee companies, net of tax	12,416	(13,178)	5,122
Other comprehensive income (loss) for the year, net of tax	(422,756)	68,889	474,382
Total comprehensive income for the year attributed to the holders of the Company	173,098	1,293,069	1,430,739

Azrieli Group Ltd.

Information on Cash Flows

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Cash flows from operating activities			
Net income for the year	595,854	1,224,180	956,357
Depreciation and amortization	713	448	192
Capital gain on the disposal of fixed assets	(7)	-	(24)
Net gain on the adjustment of the fair value of investment property and investment property under construction	(188,839)	(429,078)	(123,342)
Financing and other expenses, net	(37,093)	41,478	43,314
Dividend received from available for sale financial assets	43,145	25,970	-
Interest and dividends received from financial assets that are held for trade	68,642	26,763	8,345
Share of profits of investee companies, net of tax	(444,675)	(611,295)	(450,441)
Tax expenses (income) that have been recognized in the statement of income	336,557	143,562	(132,977)
Income tax paid, net	(67,768)	34,711	(11,956)
Change in financial assets that are held for trade	912,774	(2,234,678)	148,659
Change in trade receivables	(12,525)	7,063	(11,213)
Change in trade and other payables	4,613	(18,722)	13,319
Change in provisions and employee benefits	2,709	1,740	3,832
Change in financial assets that have been designated as at fair value through the statement of income	1,443	5,454	(1,346)
Benefit share-based payment	2,587	6,350	-
Net cash generated (absorbed) by operating activities	1,218,130	(1,776,054)	442,719
Cash flows from investment activities			
Consideration from the disposal of fixed assets	460	-	54
Investment in investment property and investment property under construction	(622,322)	(345,809)	(766,810)
Purchase of fixed assets	(2,315)	(2,153)	(702)
Extension of long-term loans	(9,033)	-	-
Investments in investee companies	(1,306)	(1,853)	(3,929)
Investment in available for sale financial assets	-	-	(743,150)
Repayment of investment (investment) in financial assets that have been designated as at fair value through the statement of income	(1,674)	396	(2,983)
Collection (extension) of long-term loans to investee companies	(213,676)	208,234	73,696
Investment in a company consolidated for the first time	(67,453)	-	-
Collection of long term loans and receivables, net	(8,187)	-	-
Net cash absorbed by investment activities	(925,506)	(140,585)	(1,443,824)

Azrieli Group Ltd.

Information on Cash Flows

(Continued)

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Cash flows from financing activities			
IPO proceeds (net of IPO expenses in the sum of approx. NIS 44 million)	-	2,480,697	-
Dividend distribution to shareholders	(240,000)	-	-
Repayment of bonds	(42,764)	(41,054)	(39,635)
Receipt of long-term loans from banking entities	-	225,000	930,000
Repayment of long-term loans from banking corporations	(137,605)	(524,055)	(114,733)
Short-term credit from banking entities, net	277,667	(47,801)	332,752
Deposits from customers, net	(811)	1,067	5,388
Interest paid	(123,560)	(121,404)	(103,498)
Net cash generated by financing activities	(267,073)	1,972,450	1,010,274
Increase in cash and cash equivalents	25,551	55,811	9,169
Cash and cash equivalents at the beginning of the year	83,105	31,727	25,652
Impact of changes in exchange rates on cash balances that are held in foreign currency	742	(4,433)	(3,094)
Cash and cash equivalents at the end of the year	109,398	83,105	31,727

Azrieli Group Ltd.

Additional information for the Separate Financial Statements

A. General

Definitions

The Company	-	The Azrieli Group Ltd.
Investee company	-	As defined in Note 1 to the Company's consolidated financial statements as of December 31, 2011.

B. The manner of the preparation of the financial data

The financial data, from the consolidated financial statements, which relate to the Company itself, as a parent company (hereinafter: "the financial data"), have been prepared in accordance with the provisions of Regulation 9 C of the Securities Regulations (Periodic and Immediate Reports) – 1970, including the details that are detailed in the Tenth Addition to the said regulations (hereinafter – "the Tenth Addition").

Moreover, disclosures are presented within the framework of the notes that are presented below, in respect of additional significant information, in accordance with the said disclosure requirements in the said Regulation and as detailed in the Tenth Addition, in so far as that information is not included in the consolidated financial statements in a manner that relates specifically to the Company itself as a parent company.

(1) The manner of the preparation of the financial data

The amounts are presented in respect of assets and liabilities, which are included in the consolidated financial statements, which relate to the Company itself as a parent company, and which have been detailed in accordance with the types of assets and liabilities, have been classified in the same manner as they were classified in the consolidated statements of financial position.

Moreover, these data reflect the mutual balances between the Company and the investee companies, which were eliminated within the framework of the consolidated financial statements. For this matter, those date have been presented in accordance with the provisions of International Accounting Standard 1, and according, in so far as is relevant, to the manner of the detail provided in the statement of financial position.

(2) Income and expenses that are included in the consolidated financial statements that relate to the Company itself as a parent company

Amounts are presented in respect of income and expenses, which are included in the consolidated financial statements, with a split between gain or loss, which relate to the Company itself as a parent company, and with details in accordance with the type of income and expenses. These data have been classified in the same manner as the manner in which they were classified in the consolidated statements of income.

Moreover, these data reflect the results of the activities between the Company and the investee companies, which were eliminated within the framework of the consolidated financial statements. For this matter, those date have been presented in accordance with the provisions of International Accounting Standard 1, and according, in so far as is relevant, to the manner of the details provided in the statements of income.

(3) Cash flows that are included in the consolidated financial statements that relate to the Company itself as a parent company

Amounts are presented in respect of cash flows, which are included in the consolidated financial statements, which relate to the Company itself as a parent company, have been taken from the consolidated statements of income, with a split between cash flows from operating activities, cash flows from investment activities and cash flows from financing activities and with details of the components thereof. These data have been classified in the same manner as the manner in which they were classified in the consolidated financial statements.

Azrieli Group Ltd.

Additional information for the Separate Financial Statements

C. Financial assets and liabilities

(1) Analysis of groups of financial assets and liabilities according to the linkage base and the type of currency:

The Group's exposure to index and foreign currency risk, based on denoted values, is as follows:

	As of December 31, 2011					
	Israeli Currency		Foreign Currency			
	Unlinked	Index linked	Dollar	Other(*)	Others	Total
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Current assets						
Cash and cash equivalents	103,129	-	3,333	2,936	-	109,398
Financial assets held for trade	760,979	470,232	11,048	79,824	-	1,322,083
Trade receivables	5,279	-	-	-	-	5,279
Other receivables	21,998	1,110	-	7,337	3,655	34,100
Total current assets	891,385	471,342	14,381	90,097	3,655	1,470,860
Non-current assets						
Investments in investee companies	-	-	-	-	4,401,133	4,401,133
Loans to investee companies	421,265	1,096,521	-	-	-	1,517,786
Other receivables	-	-	-	-	25,129	25,129
Available for sale financial assets	1,253,533	-	-	2,813	-	1,256,346
Financial assets designated as at fair value through the statement of income	1,364	-	15,373	-	-	16,737
Investment property and investment property under construction	-	-	-	-	6,152,957	6,152,957
Fixed assets	-	-	-	-	5,276	5,276
Total non-current assets	1,676,162	1,096,521	15,373	2,813	10,584,495	13,375,364
Total assets	2,567,547	1,567,863	29,754	92,910	10,588,150	14,846,224
Current liabilities						
Credit from banking entities and other providers of credit	653,868	177,370	-	-	-	831,238
Trade payables	15,776	-	-	-	-	15,776
Other payables	33,047	-	-	-	5,666	38,713
Current taxes	-	-	-	-	2,646	2,646
Total current liabilities	702,691	177,370	-	-	8,312	888,373
Non-current liabilities						
Loans from banking entities	25,000	1,284,484	-	-	-	1,309,484
Employee benefits	-	-	-	-	17,819	17,819
Bonds	-	651,359	-	-	-	651,359
Other liabilities	-	17,819	-	-	182	18,001
Deferred tax liabilities	-	-	-	-	927,399	927,399
Total non-current liabilities	25,000	1,953,662	-	-	945,400	2,924,062
Total liabilities	727,691	2,131,032	-	-	953,712	3,812,435
Net balance sheet balances	1,839,856	(563,169)	29,754	92,910	9,634,438	11,033,789

(*) Mainly CAD and Euro.

C. Financial assets and liabilities: (Continued)

(1) Analysis of groups of financial assets and liabilities according to the linkage base and the type of currency (Continued)

The Group's exposure to index and foreign currency risk, based on denoted values, is as follows:

	As of December 31, 2010					
	Israeli Currency		Foreign Currency			
	Unlinked	Index linked	Dollar	Other	Others	Total
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Current assets						
Cash and cash equivalents	74,994	-	1,208	6,903	-	83,105
Financial assets held for trade	1,325,132	637,350	9,402	262,973	-	2,234,857
Trade receivables	6,500	-	-	-	-	6,500
Other receivables	405	8,603	-	-	2,562	11,570
Total current assets	1,407,031	645,953	10,610	269,876	2,562	2,336,032
Non-current assets						
Investments in investee companies	-	-	-	-	3,876,883	3,876,883
Loans to investee companies	915,504	293,676	-	-	-	1,209,180
Other receivables	-	-	-	-	8,786	8,786
Available for sale financial assets	1,781,545	-	-	8,448	-	1,789,993
Financial assets designated as at fair value through the statement of income	2,278	-	15,130	-	-	17,408
Investment property and investment property under construction	-	-	-	-	5,333,219	5,333,219
Fixed assets	-	-	-	-	4,127	4,127
Total non-current assets	2,699,327	293,676	15,130	8,448	9,223,015	12,239,596
Total assets	4,106,358	939,629	25,740	278,324	9,225,577	14,575,628
Current liabilities						
Credit from banking entities and other providers of credit	333,987	213,886	-	-	-	547,873
Trade payables	6,519	-	-	-	-	6,519
Other payables	11,144	21,409	-	-	5,940	38,493
Current taxes	-	-	-	-	15,069	15,069
Total current liabilities	351,650	235,295	-	-	21,009	607,954
Non-current liabilities						
Loans from banking entities	18,377	1,396,156	-	-	-	1,414,533
Employee benefits	-	-	-	-	11,980	11,980
Bonds	-	677,355	-	-	-	677,355
Other liabilities	-	18,214	-	-	187	18,401
Deferred tax liabilities	-	-	-	-	744,464	744,464
Total non-current liabilities	18,377	2,091,725	-	-	756,631	2,866,733
Total liabilities	370,027	2,327,020	-	-	777,640	3,474,687
Net balance sheet balances	3,736,331	(1,387,391)	25,740	278,324	8,447,937	11,100,941

(*) Mainly CAD and Euro.

C. Financial assets and liabilities: (Continued)

(2) The management of liquidity risk

Tables in respect of interest and liquidity risk

Financial liabilities that do not constitute derivative financial instruments

The following tables detail the Company's remaining forecast repayment times in respect of financial liabilities, which do not constitute derivative financial instruments. The tables have been prepared on the basis of the undiscounted cash flows for the financial liabilities, based on the earliest times at which the Company could be required to repay them. The tables include cash flows both in respect of interest and also in respect of principal.

	As of December 31, 2011					
	Carrying value	Forecast cash flows	2012	2013	2014	2015 forth
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Financial assets						
Cash and cash equivalents	109,398	109,398	109,398	-	-	-
Financial assets held for trade	1,322,083	1,322,083	1,322,083	-	-	-
Trade receivables	5,279	5,279	5,279	-	-	-
Other receivables	31,628	31,628	31,628	-	-	-
Available for sale financial assets	1,256,346	1,256,346	-	-	-	1,256,346
Financial assets designated as at fair value through the statement of income	16,737	16,737	-	-	-	16,737
Loans to investee companies	1,517,786	1,847,431	-	-	-	1,847,431
	4,259,257	4,588,902	1,468,388	-	-	3,120,514

	As of December 31, 2010					
	Carrying value	Forecast cash flows	2011	2012	2013	2014 forth
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Financial assets						
Cash and cash equivalents	83,105	83,105	83,105	-	-	-
Financial assets held for trade	2,234,857	2,234,857	2,234,857	-	-	-
Trade receivables	6,500	6,500	6,500	-	-	-
Other receivables	9,008	9,008	9,008	-	-	-
Available for sale financial assets	1,789,993	1,789,993	-	-	-	1,789,993
Financial assets designated as at fair value through the statement of income	17,408	17,408	-	-	-	17,408
Loans to investee companies	1,201,195	1,474,118	-	-	-	1,474,118
	5,342,066	5,614,989	2,333,470	-	-	3,281,519

C. Financial assets and liabilities (Continued)

(2) The management of liquidity risk (Continued)

	As of December 31, 2011						
	Carrying value	Forecast cash flows	2012	2013	2014	2015	2016 forth
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Non-derivative financial liabilities							
Credit from banking entities and other providers of credit(*)	647,618	647,618	647,618	-	-	-	-
Loans from banking entities(*)	1,455,833	2,068,965	225,056	328,210	168,649	163,454	1,183,596
Bonds(*)	694,653	838,641	75,118	73,031	70,944	68,858	550,690
Deposits from customers	17,819	17,819	-	-	-	17,819	-
Total	2,815,923	3,573,043	947,792	401,241	239,593	250,131	1,734,286

	As of December 31, 2010						
	Carrying value	Forecast cash flows	2011	2012	2013	2014	2015 forth
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Non-derivative financial liabilities							
Credit from banking entities and other providers of credit(*)	371,561	371,561	371,561	-	-	-	-
Loans from banking entities(*)	1,556,830	2,233,615	222,978	217,784	318,229	162,979	1,311,645
Bonds(*)	719,569	892,905	75,281	73,246	71,211	69,176	603,991
Deposits from customers	18,231	18,231	-	-	-	18,231	-
Total	2,666,191	3,516,312	669,820	291,030	389,440	250,386	1,915,636

(*) The carrying value in the accounting records include current maturities and accumulated interest as of December 31, 2011 and 2010.

C. Financial assets and liabilities (Continued)

(3) Details in respect of investments in other companies:

Details in respect of available for sale financial assets

For details in respect of the Company's investments in Bank Leumi Le'Israel Ltd. and Leumi Card Ltd., see Note 12 A' (1) and (2) to the consolidated financial statements as of December 31, 2011.

D. Taxes on income

(1) Details in respect of the tax environment in which the Group operates:

For details in respect of the tax environment in which the Company operates, see Note 33 A' to the consolidated financial statements for the year ended December 31, 2011.

(2) Taxes on income benefits (expenses), which have been recognized in the statement of income:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Current tax benefits (expenses):			
In respect of the current period	(56,630)	(49,300)	(35,355)
Adjustments in respect of previous years, net	1,278	(1,992)	3,158
	(55,322)	(51,292)	(32,197)
Deferred tax benefits (expenses)	(281,205)	(92,270)	165,174
Total taxes on income benefit (expenses)	(336,557)	(143,562)	132,977

(3) Tax assessments:

In December 2010, the Company received an assessment to the best of judgment for 2006.As of the date of approval of the financial statements, immaterial amounts were paid and final tax assessments closed for the Company up to and including the tax year 2007.

D. Taxes on income (Continued)

(4) Taxes on income in respect of the components of other comprehensive income (loss):

	2011			2010			2009		
	Amounts before taxation	Taxation benefit (expense) (1)	Amounts net of taxation	Amounts before taxation	Taxation benefit (expense)	Amounts net of taxation	Amounts before taxation	Taxation benefit (expense)	Amounts net of taxation
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Gain in respect of the re-measurement of available for sale financial assets	(528,013)	(2) 88,868	(439,145) (2)	95,562	(12,491)(2)	83,071	561,832	(2) (91,573)	470,259
Actuarial gain(loss) in respect of defined benefit plan	(24)	6	(18)	165	(30)	135	223	(56)	167
Translation differences in respect of foreign operations	3,991	-	3,991	(1,139)	-	(1,139)	(1,166)	-	(1,166)
Share of other comprehensive income (loss) of investee companies, net of tax	14,653	(2,237)	12,416	(15,924)	2,746	(13,178)	5,518	(396)	5,122
Total other comprehensive income (loss)	(509,393)	86,637	(422,756)	78,664	(9,775)	68,889	566,407	(92,025)	474,382

(1) Including the impact of the change in the tax rates.

(2) The deferred taxes have been calculated in 2011 in accordance with a tax rate of 25% and in 2010 in accordance with a tax rate of 18%.

D. Taxes on income (Continued)

(5) Deferred taxes:

Deferred tax **assets and liabilities that have been recognized:**

The deferred taxes have been calculated in accordance with the tax rate that is expected to apply at the time of the reversal of the balances, as detailed above.

The deferred tax assets and liabilities are attributed to the following items:

	Real estate property and fixed assets (3)	Employee benefits	Financial instruments (1), (3)	Deductions and losses carried forward for tax purposes	Others (2), (3)	Total
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Deferred tax asset (liability) as of January 1, 2010	(587,876)	1,991	(96,823)	11,272	30,154	(641,282)
Changes reflected in the statement of income	(83,817)	947	(8,279)	(96)	(1,024)	(92,269)
Changes reflected under other comprehensive income	-	(30)	(12,492)	-	(40)	(12,562)
Other changes	1,649	-	-	-	-	1,649
Deferred tax asset (liability) as of December 31, 2010	(670,044)	2,908	(117,594)	11,176	29,090	(744,464)
Changes carried to income statement	(37,886)	1,676	22,650	(408)	1,708	(12,260)
Changes carried to other comprehensive profit	-	(6)	94,593	-	-	94,587
Other Changes	-	-	-	-	9,408	9,408
Effect of the change in the tax rates, which has been reflected in the statement of income	(274,457)	360	1,782	3,363	7	(268,945)
Effect of the change in the tax rates, which has been reflected in other comprehensive profit	-	-	(5,725)	-	-	(5,725)
Deferred tax asset (liability) as of December 31, 2011	(982,387)	4,938	(4,294)	14,131	40,213	(927,399)

(1) Primarily in respect of available for sale financial assets.

(2) Primarily in respect of the capital reserve that has been created in respect of credit that has been extended to subsidiary companies other than on market terms.

(3) The deferred taxes as of December 31, 2011 have been calculated in accordance with a tax rate of 25% (As of December 31, 2010 – 18%).

E. Significant commitments and transactions with investee companies:

(1) **See** Note 10 A to the consolidated financial statements as of December 31, 2011 in respect of investments in companies, which are held directly by the Company.

(2) **The** Company has made a loan available to Canit Hashalom Investments Ltd. (a company in which there is a holding of approximately 99.1%), whose balance was approximately NIS 1,355 million as of December 31, 2011 (December 31, 2010 – NIS 1,150 million). Of this amount an amount of approximately NIS 1,097 million (December 31, 2010 – NIS 856 million) is index linked and bears interest at a rate of 4.8% a year and the balance bears interest of 3.8% (interest of 3% in 2010).

The credit as of December 31, 2011 is presented after having been measured at fair value at the time of initial recognition in accordance with the present value of the forecast returns. The difference between the fair value, which was measured at the time of the initial recognition and the amount of the loan that was actually extended is reflected under a capital reserve on transactions with controlling interests and amounts to approximately NIS 163 million (December 31, 2010 – approximately NIS 164 million). As of December 31, 2011 a balance in an amount of approximately NIS 1,519 million has no restrictions attached and no repayment time has been set for it. Of the said amount, approximately NIS 506 million will be repaid out of the Company's cash surpluses.

(3) **Significant arrangements between the Company and the investee companies**

a. Agreements exist between the Company and a number of companies that are held by it and other companies in the Group, according to which the Company is entitled to management fees at a fixed rate of the generality of the expenses of those companies. In the years 2011 and 2010 the company received management fees, as aforesaid, in overall amounts of approximately NIS 18,886 thousand and approximately NIS 13,466 thousand, respectively.

b. Agreements exist between the Company and a number of companies that are held by it, according to which the Company is entitled to amounts for a depreciation and replacement reserve for the replacement and/or comprehensive repair of facilities and equipment, which are used by the generality of the tenants on the Company's realty. In the years 2011 and 2010 the company received receipts, as aforesaid, in overall amounts of approximately NIS 6,684 thousand and approximately NIS 5,612 thousand, respectively.

c. The Company has made loans available to a number of companies that are held by it. See Note 10 A to the consolidated financial statements as of December 31, 2011 and section E(2) above. The interest and the linkage differentials that have accumulated in respect of these loans and which have been presented in the Company's statement of comprehensive income for the years ended December 31, 2011 and 2010, amount to the overall sums of approximately NIS 91 million and approximately NIS 83 million, respectively.

d. The Company bears the office, insurance, salary and ancillary expenses of the senior employees in the Group (hereinafter – the Group expenses). Agreements exist between the Company and a number of companies that are held by it and other companies in the Group according to which the Company is entitled to a refund in respect of amounts that have been paid by it for the companies. In the years 2011 and 2010 the Company received receipts, as aforesaid, in overall amounts of approximately 20,055 thousand and approximately NIS 13,346 thousand, respectively.

F. Guarantees:

(1) On June 1, 2009 the Company made a guarantee in an unlimited amount available in favor of Bank Hapoalim in respect of a loan that was taken by a subsidiary. As of December 31, 2011 the balance of the loan was approximately NIS 24.8 million.

(2) On March 30, 2011 the Company made a guarantee available in favor of Bank Mizrahi-Tefahot, in the amount of the loan, in respect of a loan that was taken by a limited partnership thereof. The balance of the loan was approximately NIS 29.6 million as of December 31, 2011.

(3) On February 4, 2011, the Company provided a guarantee in favor of a U.S. financial institution in the amount of a loan taken by a limited partnership thereof, which is exercisable only in several cases defined in the loan agreement. The balance of the loan as of December 31, 2011 is NIS 496.7 million.

G. Contractual restrictions and financial covenants:

See Notes 22 B (1), 22 B (5) and 22 D (1) to the consolidated financial statements as of December 31, 2011 for details in respect of contractual restrictions assumed by the Company.

H. Dividends from companies that are held directly by the Company:

The companies that are held directly by the Company do not have contractual restrictions on the distribution of dividends.

I. Charges:

(1) The Company has given an undertaking to banks not to create a floating charge on the generality of its assets. Moreover, the Company has given an undertaking to a banking entity that it has not created and that it will not create a floating charge over its assets, whether they are owned by it or whether they will be owned by it, including over its goodwill and share capital and it has also undertaken not to give a commitment in any way whatsoever to create a floating charge, as aforesaid, unless concurrently with its creation it will also create a floating charge in favor of the bank.

(2) As at December 31, 2011 the Company has real estate assets for investment and real estate for investment under construction which are not pledged of NIS 4,462 million and a balance of approx. NIS 1,699 million is charged under a fixed charge as collateral for loans from banks, whose balance was approximately NIS 900 million as of December 31, 2011.

(3) As at December 31, 2011 the Company has financial assets available for sale which are not pledged of NIS 1,256 million. See also Note 12 to the consolidated financial statements as at December 31, 2011.

J. Commitments with related parties and interested parties:

See Note 40 to the consolidated financial statements as of December 31, 2011 in respect of commitments with related parties and interested parties.

Annex E

Extended Standalone Financial Statements

December 31, 2011

Annex E

Extended Standalone Financial Statements

The Company's extended standalone financial statements are the condensed Company's reports presented according to the IFRS rules, except for the investment in Granite which is presented on the basis of the balance sheet value method *in lieu* of consolidation of the reports thereof with the Company's reports (the remaining investments are presented with no change to the report presented pursuant to the IFRS rules). These reports do not constitute separate reports in their meaning in the international accounting standard 27 and do not constitute separate financial statements pursuant to Regulation 9C of the Securities Regulations (Periodic and Immediate Reports), 5730-1970. The reports are not part of the information that is required to be published according to securities laws, however, the Company's management believes that analysts, investors, shareholders and bond holders might receive valuable information from the presentation of such figures.

The figures in this annex have not been audited and reviewed by the Company's auditors.

Balance sheet:

	As of December 31	
	2011	**2010**
	NIS in thousands	**NIS in thousands**
Assets		
Current Assets		
Cash and Cash equivalents	145,072	115,929
Financial Assets held for Trade	1,322,083	2,234,857
Trade Receivables	30,101	29,348
Other Receivables	62,139	19,710
Current Taxes Assets	6,599	6,471
Total Current Assets	1,565,994	2,406,315
Non Current Assets		
Investment in Investee Companies	767,112	768,370
Loans and Debit Balances	30,579	26,973
Financial Assets Available for Sale	1,256,346	1,789,993
Financial Assets designated in fair value through profit and loss	16,737	17,408
Investment Real Estate and Investment Real Estate under Construction	14,766,056	12,137,437
Fixed Assets	44,909	42,558
Deferred Taxes Assets	1,723	1,672
Total Non Current Assets	16,883,462	14,784,411
Total Assets	18,449,456	17,190,726

Annex E

Extended Standalone Financial Statements

Balance Sheet:

	As of December 31	
	2011	2010
	NIS in thousands	NIS in thousands
Liabilities and Equity		
Current Liabilities		
Credit from Banking Corporations and other credit providers	1,004,671	813,029
Trade Payables	76,900	42,794
Other Payables	81,013	64,203
Current Taxes Liabilities	35,019	26,350
Total Current Liabilities	1,197,603	946,376
Non Current Liabilities		
Loans from Banking Corporations and other Credit Providers	2,912,228	2,472,274
Bonds	1,074,461	1,136,463
Other Liabilities	38,229	34,819
Employee Benefits	22,155	15,668
Deferred Taxes Liabilities	2,111,119	1,450,909
Total Non Current Liabilities	6,158,192	5,110,133
Equity		
Ordinary "A" Share Capital	18,223	18,223
Premium on Shares	2,518,015	2,518,015
Capital Funds	102,678	524,043
Surplus	8,394,872	8,040,660
Equity attributed to the Parent Company	11,033,788	11,100,941
Rights that do not Confer Control	59,873	33,276
Total Equity	11,093,661	11,134,217
Total Liabilities and Equity	18,449,456	17,190,726

Annex E

Extended Standalone Financial Statements

Income Statement:

	For the year ended On December 31	
	2 0 1 1	**2 0 1 0**
	NIS in thousands	**NIS in Thousands**
Revenues		
From rent, management and maintenance fees	1,245,546	1,094,466
Net profit from the adjustment of fair value of investment and under construction real estate	848,638	891,777
Financing Revenues	4,222	65,369
Share in the results of Affiliated Companies, Net of Taxes	24,228	43,678
Other	44,855	26,584
Total Revenues	2,167,489	2,121,874
Costs and Expenses		
Cost of revenues from rent, management and maintenance fees	259,833	209,141
Sales and Marketing	2,480	2,158
General and Administrative	70,705	69,138
Financing Expenses	369,460	316,592
Other	34	211
Total Costs and Expenses	702,512	597,240
Profit before Tax on Income	1,464,977	1,524,634
Income Tax Expense	(841,965)	(269,530)
Net Profit for the Period including the Minority	623,012	1,255,104

CHAPTER C

Audited Consolidated Financial Statements

December 31, 2011

Azrieli Group Ltd.

Consolidated Financial Statements

For the Year 2011

Azrieli Group Ltd.

Consolidated Financial Statements

For the Year 2011

Contents

Independent Auditors' Report to the Shareholders of
Azrieli Group Ltd.
Regarding Audit of Components of Internal Control over Financial Reporting pursuant to
Section 9B(c) of the Securities Regulations (Periodic and Immediate Statements), 5730-1970

We have audited components of internal control over financial reporting of **Azrieli Group Ltd. and subsidiaries** (jointly, "the Company") as of December 31, 2011. These components of control were determined as explained in the paragraph below. The board of directors and management of the Company are responsible for performance of effective internal control over financial reporting and for evaluating the effectiveness of the components of internal control over the financial report attached to the periodic statement as of December 31, 2011. Our responsibility is to express an opinion on the components of internal control over financial report of the Company, based on our audit. We did not check the effectiveness of the components of internal control over financial reporting of consolidated subsidiaries whose assets and revenues that are included in the consolidation constitute approx. 22% and approx. 75%, respectively, of the respective amounts in the consolidated financial statements as of December 31, 2011 and the year ended on that date. The effectiveness of the components of the internal control over financial reporting of such companies was audited by other auditors whose reports were provided to us and our opinion, insofar as it relates to the effectiveness of components of internal control over financial reporting of such companies is based upon the other auditors' reports.

The components of the internal control over financial reporting that were audited by us were determined pursuant to Audit Regulation 104 of the Institute of Certified Public Accountants in Israel "Audit of Components of Internal Control over Financial Reporting" ("Audit Regulation 104"). These Components are: (1) Organization level control, including control over the financial closing and reporting process and ITGC control; (2) control over investment property; (3) control over revenues from rent from investment property (all of these jointly are referred to below as the "Audited Components of Control").

We conducted our audit pursuant to Audit Regulation 104. Pursuant to this Regulation, we were required to plan and perform the audit with the purpose of identifying the Audited Components of Control, and to obtain reasonable assurance as to whether these components of control were performed effectively in all material respects. Our audit included obtaining an understanding regarding internal control over financial reports, identification of the Audited Components of Control, evaluation of the risk that a material weakness exists in the Audited Components of Control, and examination and evaluation of the effectiveness of the planning and operation of such components of control, based on the estimated risk. Our audit regarding such components of control also included performance of other such procedures that we thought were necessary under the circumstances. Our audit only referred to the Audited Components of Control, as opposed to internal control over all of the material processes in connection with the financial reporting, and therefore our opinion refers only to the Audited Components of Control. In addition, our audit did not refer to the mutual influences between the Audited Components of Control and those that are not audited, and therefore, our opinion does not take into consideration such possible influences. We believe that our audit provides a reasonable basis for our opinion in the context described above.

Due to obvious limitations, internal control over financial reporting in general, and components thereof in particular, may fail to prevent or disclose a material misstatement. In addition, future conclusions based on any current effectiveness evaluation is exposed to the risk that the control will become unsuitable due to changes in circumstances, or that the degree of performance of the policies or the procedures will change for the worse.

In our opinion, based on our audit, and the other auditors' reports, the Company effectively performed the Audited Components of Control in all material respects, as of December 31, 2011.

Pursuant to the accepted Audit Regulations in Israel, we also audited the consolidated financial statements of the Company as of December 31, 2011 and 2010, and for each of the three years in the period ending on December 31, 2011, and our report as of March 21, 2012, includes an unqualified opinion on those financial statements based on our audit and on other auditors reports as well as the drawing attention to the provisions of Note 36 to the financial statements regarding legal claims in material amounts, in the aggregate, against consolidated companies in respect of which a motion for class certification has been filed and regarding various claims and suits in material financial scopes, in the aggregate, against a consolidated company whose agreements with its customers have been argued to constitute a restrictive arrangement.

Brightman Almagor Zohar & Co
Certified Public Accountants

Tel Aviv March 21, 2012

Auditors' Report to the Shareholders of

Azrieli Group Ltd.

We have audited the attached consolidated statements of financial position of the **Azrieli Group Ltd.** (the " Company") as at December 31, 2011 and 2010 and the consolidated statements of comprehensive income, the changes in capital and the cash flows for each of the three years in the period ended December 31, 2011. These financial statements are the responsibility of the Company's Board of Directors and Management. Our responsibility is to express an opinion on these financial statements based on our audit.

We did not audit the financial statements of consolidated subsidiaries, whose assets that are included in the consolidation constitute approx. 22% and approx. 21% of the total consolidated assets as of December 31, 2011 and 2010, respectively, and whose revenues that are included in the consolidation constitute approx. 75%, approx. 72% and approx. 79% of the total consolidated revenues for the years ended December 31, 2011, 2010 and 2009, respectively. Moreover, we did not audit the financial statements of the associates under the equity method, the investment in which amounted to approx. NIS 46 million and approx. NIS 43 million as of December 31, 2011 and 2010, respectively and the share of whose losses amounted to approx. NIS 18 million, approx. NIS 21 million and approx. NIS 7 million for the years ended December 31, 2011, 2010 and 2009, respectively. The financial statements of those companies were audited by other auditors whose reports were furnished to us, and our report, in so far as it relates to the amounts that have been included in respect of those companies, is based upon the reports of the other auditors.

We conducted our audit in accordance with generally accepted auditing standards in Israel, including standards that were set in the Accountants Regulations (Mode of Operation of Accountants) 5733-1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by the Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and on the reports of the other auditors, the abovementioned financial statements present fairly, in all material respects, the financial position of the Company and of the Company and its subsidiaries as of December 31, 2011 and 2010 and the results of their operations, the changes in their capital and their cash flows for each of the three years in the period ended December 31, 2011 in accordance with International Financial Reporting Standards (IFRS) and the provisions of the Securities Regulations (Annual Financial Statements), 5770-2010.

We have also audited, in accordance with Audit Standard 104 of the Institute of Certified Public Accountants in Israel “Audit of Components of Internal Control over Financial Reporting”, components of the internal control over the Company’s financial reporting as of December 31, 2011 and our report as of March 21, 2012 included an unqualified opinion on the effective existence of such components.

Without qualifying our opinion, we draw attention to the contents of Note 36 to the financial statements, on the subject of legal claims in material amounts, cumulatively, against consolidated companies, in respect of which an application for recognition as a class action has been presented and on the subject of various claims in material amounts, cumulatively, against a consolidated company, in which it is alleged that its agreements with its customers fall within the bounds of a restrictive arrangement.

Brightman, Almagor, Zohar & Co.
Certified Public Accountants

Tel Aviv March 21, 2012

Azrieli Group Ltd.

Consolidated Statements of Financial Position

	Note	As of December 31	
		2011	2010
		(NIS in thousands)	
ASSETS			
Current assets			
Cash and cash equivalents	4	224,430	177,858
Financial assets held for trade	5	1,401,786	2,310,423
Short-term deposits and investments	6	84,271	48,274
Trade receivables	7a	1,719,764	1,339,109
Other receivables	7b	144,684	95,233
Receivables for work in progress	8	32,649	34,982
Inventories	9	439,933	346,054
Current tax assets	33	24,626	12,319
Total current assets		4,072,143	4,364,252
Non-current assets			
Investments in associates	10	13,140	15,309
Loans to associates	10	33,080	27,648
Investments, loans and other receivables	11	122,126	119,533
Restricted investments	11d	50,930	49,448
Financial assets available for sale	12a	1,305,184	1,828,302
Financial assets designated at fair value through profit and loss	12b	16,737	17,408
Long-term receivables in respect of a franchise arrangement	13	534,596	527,075
The Fuel Administration		132,720	123,569
Investment property and investment property under construction	14	14,839,570	12,210,264
Fixed assets	15	1,427,028	1,419,748
Intangible assets	16	540,406	551,517
Lease fees paid in advance	17	36,603	39,454
Deferred tax assets	33	55,450	49,851
Total non-current assets		19,107,570	16,979,126
Total assets		23,179,713	21,343,378

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Financial Position
(Continued)

	Note	December 31 2011	December 31 2010
		(NIS in thousands)	
LIABILITIES AND CAPITAL			
Current liabilities			
Credit from banks and other credit providers	22	2,445,422	1,772,313
Accounts payable	18	854,724	682,783
Other payables	19	385,849	366,170
Deposits from customers	20	105,995	103,366
Provisions	21	29,288	32,883
Current tax liabilities	33	42,107	35,265
Total current liabilities		3,863,385	2,992,780
Non-current liabilities			
Loans from banks and other credit providers	22	3,757,837	3,300,137
Bonds	22	1,706,726	1,835,675
Employee benefit	23	59,312	54,311
Other liabilities	22	100,122	101,410
Deferred tax liabilities	33	2,228,273	1,534,228
Total non-current liabilities		7,852,270	6,825,761
Capital	24		
Ordinary share capital		18,223	18,223
Share premium		2,518,015	2,518,015
Capital funds		102,678	524,043
Retained earnings		8,394,872	8,040,660
Total capital attributed to the holders of the parent company		11,033,788	11,100,941
Non-controlling interests		430,270	423,896
Total Capital		11,464,058	11,524,837
Total Liabilities and Capital		23,179,713	21,343,378

March 21, 2012			
Date of the approval of the financial statements	**David Azrieli Chairman of the Board of Directors**	**Shlomo Sherf, CEO**	**Yuval Bronstein Chief Financial Officer**

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Comprehensive Income

	Note	Year ended December 31		
		2011	2010	2009
		(NIS in thousands)		
Revenues				
From sales, labor and services	26	6,291,304	5,238,630	4,522,395
From rental, management And maintenance fees	26	1,255,966	1,105,292	1,007,580
Net profit from the adjustment of the fair value of Investment property and investment property under construction	14	848,859	890,696	217,686
Financing income	32	101,661	151,635	67,320
Other	30	54,608	56,285	27,877
Total revenues		8,552,398	7 ,442,538	5,842,858
Costs and Expenses				
Costs of revenues from sales labor and services	27	5,205,350	4,171,617	3,501,107
Costs of revenues from rental, management and maintenance fees	27	266,842	216,684	206,206
Sales and marketing	28	764,650	742,087	701,462
Administrative and general	29	200,288	225,030	214,833
Share of results of associates, net of tax	10	17,512	21,378	5,946
Financing expenses	32	591,159	514,437	492,135
Other	31	7,504	4,042	9,483
Total costs and expenses		7,053,305	5,895,275	5,131,172
Profit before taxes on income		1,499,093	1,547,263	711,686
Taxes on income (expense) benefit	33	(876,081)	(292,159)	288,344
Net profit for the year		623,012	1,255,104	1,000,030
Other comprehensive income (loss), net of tax				
Change in fair value of financial assets available for sale, net of tax		(431,783)	81,515	479,978
Realization of financial assets available for sale, net of tax		-	(16,387)	-
Actuarial profit (loss) in respect of defined benefit plan, net of tax		(2,769)	1,292	(500)
The effective share of the change in fair value of the hedging of cash flows		(143)	-	(659)
Net change, in fair value of the hedging of cash flows, net tax		88	-	-
Translation differentials due to overseas operations		15,917	(4,540)	(1,119)
Other comprehensive income (loss) for the year, net of tax		(418,690)	61,880	477,700
Total other comprehensive income for the year		204,322	1,316,984	1,477,730

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Comprehensive income
(Continued)

	Note	For the year ended December 31		
		2011	2010	2009
		NIS in Thousands	NIS in Thousands	NIS in Thousands
Net income for the year attributed to:				
Holders of the parent company		595,854	1,224,180	956,357
Non-controlling interests		27,158	30,924	43,673
		623,012	1,255,104	1,000,030
Net comprehensive income for the year attributed to:				
Holders of the parent company		173,098	1,293,069	1,430,739
Non-controlling interests		31,224	23,915	46,991
		204,322	1,316,984	1,477,730
		NIS	NIS	NIS
Base and Diluted Profit per ordinary share (in NIS) of par value NIS 0.1 attributed to the holders of the parent company	42	4.91	11.33	10.52

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Changes in Shareholders' Capital

	For the year ended December 31, 2011									
	Share Capital	Share premium	Revaluation reserve on available for sale financial assets	Capital reserve on translation differences on foreign operations	Capital reserve on transactions with related parties	Other capital reserves	Surpluses	Total attributed to holders of the parent company	Non-controlling interests	Total
	NIS in Thousands									
Balance as of January 1, 2011	18,223	2,518,015	573,325	(16,850)	(31,000)	(1,432)	8,040,660	11,100,941	423,896	11,524,837
Net profit for year	-	-	-	-	-	-	595,854	595,854	27,158	623,012
Change in fair value of financial assets available for sale, net of tax	-	-	(434,717)	-	-	-	-	(434,717)	2,934	(431,783)
Actuarial loss in respect of defined benefit plan, net of tax	-	-	-	-	-	-	(1,642)	(1,642)	(1,127)	(2,769)
Translation differentials due to overseas operations	-	-	-	13,630	-	-	-	13,630	2,287	15,917
The effective share of the change in fair value of the hedge of cash flows	-	-	-	-	-	(72)	-	(72)	(71)	(143)
Net change in fair value of the hedge of cash flows transferred to profit and loss, net of tax	-	-	-	-	-	45	-	45	43	88
Total comprehensive income for the year	-	-	(434,717)	13,630	-	(27)	594,212	173,098	31,224	204,322
Acquisition of non-controlling interests in consolidated companies	-	-	-	-	-	(330)	-	(330)	(36,501)	(36,831)
Non-controlling interests in a consolidated company	-	-	-	-	-	-	-	-	17,628	17,628
Dividend to shareholders of the company	-	-	-	-	-	-	(240,000)	(240,000)	-	(240,000)
Dividend to holders of non-controlling interests	-	-	-	-	-	-	-	-	(5,898)	(5,898)
Capital reserve on transactions with affiliated parties	-	-	-	-	79	-	-	79	(79)	-
Total transactions with the Company's shareholders	-	-	-	-	79	(330)	(240,000)	(240,251)	(24,850)	(265,101)
Balance as of December 31, 2011	18,223	2,518,015	138,608	(3,220)	(30,921)	(1,789)	8,394,872	11,033,788	430,270	11,464,058

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Changes in Shareholders' Capital
(Continued)

	For the year ended December 31, 2010									
	Share Capital	Share premium	Revaluation reserve on available for sale financial assets	Capital reserve on translation differences on foreign operations	Capital reserve on transactions with related parties	Other capital reserves	Surpluses	Total attributed to holders of the parent company	Non-controlling interests	Total
	NIS in Thousands									
Balance as of January 1, 2010	6,300	40,351	501,027	(12,585)	(31,184)	-	6,824,775	7,328,684	374,498	7,703,182
Net profit per year	-	-	-	-	-	-	1,224,180	1,224,180	30,924	1,255,104
Realization of financial assets available for sale, net of tax	-	-	(9,856)	-	-	-	-	(9,856)	(6,531)	(16,387)
Change in fair value of financial assets available for sale, net of tax	-	-	82,135	-	-	-	-	82,135	(620)	81,515
Actuarial profit in respect of defined benefit plan, net of tax	-	-	-	-	-	-	875	875	417	1,292
Translation differentials due to overseas operations	-	-	-	(4,265)	-	-	-	(4,265)	(275)	(4,540)
Total comprehensive income for the year	-	-	72,279	(4,265)	-	-	1,225,055	1,293,069	23,915	1,316,984
Exercise of warrants for shares in a consolidated company	-	-	-	-	-	(380)	-	(380)	1,955	1,575
Acquisition of non-controlling interests in a consolidated company	-	-	-	-	-	(1,052)	-	(1,052)	1,052	-
Issue of shares of the Company (net of issue expenses in the sum of approx. NIS 44 million)	3,033	2,477,664	-	-	-	-	-	2,480,697	-	2,480,697
Change in non-controlling interests in a consolidated company due to the issue of shares in a consolidated company	-	-	19	-	195	-	(280)	(66)	66	-
Allotment of stock dividends of the Company	8,890	-	-	-	-	-	(8,890)	-	-	-
Dividend to holders of non-controlling interests	-	-	-	-	-	-	-	-	(10,248)	(10,248)
Acquisition of non-controlling interests in a business combination	-	-	-	-	-	-	-	-	32,408	32,408
Other	-	-	-	-	(11)	-	-	(11)	250	239
Total transactions with shareholders in the company	11,923	2,477,664	19	-	184	(1,432)	(9,170)	2,479,188	25,483	2,504,671
Balance as of December 31, 2010	18,223	2,518,015	573,325	(16,850)	(31,000)	(1,432)	8,040,660	11,100,941	423,896	11,524,837

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Changes in Shareholders' Capital
(Continued)

	For the year ended December 31, 2009									
	Share Capital	Share premium	Revaluation reserve on available for sale financial assets	Capital reserve on translation differences on foreign operations	Capital reserve on transactions with related parties	Capital reserve on the hedging of cash flows	Surpluses	Total attributed to holders of the parent company	Non-controlling interests	Total
	NIS Thousands									
Balance as of January 1, 2009	6,217	40,351	24,929	(11,419)	(31,051)	337	5,854,230	5,883,594	331,505	6,215,099
Net profit per year	-	-	-	-	-	-	956,357	956,357	43,673	1,000,030
Actuary loss in respect of defined benefit plan, net of tax	-	-	-	-	-	-	(213)	(213)	(287)	(500)
Change in fair value of financial assets available for sale, net of tax	-	-	476,098	-	-	-	-	476,098	3,880	479,978
Loss in respect of the hedging of cash flows, net of tax	-	-	-	-	-	(337)	-	(337)	(322)	(659)
Translation differentials due to overseas operations	-	-	-	(1,166)	-	-	-	(1,166)	47	(1,119)
Total comprehensive income for the year	-	-	476,098	(1,166)	-	(337)	956,144	1,430,739	46,991	1,477,730
Expiration of warrants in a consolidated company	-	-	-	-	-	-	-	-	(2,927)	(2,927)
Acquisition of non-controlling interests in a consolidated company	-	-	-	-	-	-	-	-	(251)	(251)
Share based payment to employees in consolidated companies	-	-	-	-	-	-	-	-	2,403	2,403
Issue of shares of the Company	83	-	-	-	-	-	(83)	-	-	-
Capital reserve on transactions with related parties	-	-	-	-	(133)	-	-	(133)	133	-
Total transactions with shareholders in the company	83	-	-	-	(133)	-	(83)	(133)	(642)	(775)
Balance as of December 31, 2009	6,300	40,351	501,027	(12,585)	(31,184)	-	6,810,291	7,314,200	377,854	7,692,054

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Cash Flows

	Year ended December 31		
	2011	2010	2009
	(in NIS thousand)		
Cash flows - operating activities			
Net profit for the year	623,012	1,255,104	1,000,030
Depreciation and amortization	134,680	145,643	136,259
Impairment of fixed assets and intangible assets	1,620	579	4,776
Reductions and reduction in value of investments and loans to associates	73	-	1,583
Loss from sale of investments in associates	-	202	1,041
Net profit from adjusting fair value of Investment property and investment property under construction	(848,859)	(890,696)	(217,686)
Financing and other expenses, net	314,290	387,457	422,214
Impairment of available for sale financial assets	1,496	-	-
Dividend received from available for sale financial assets	44,564	(*) 31,032	(*) 11,183
Interest and dividend received from financial assets held for trading	68,642	26,763	6,683
Loss from the sale of fixed assets, investment property and intangible assets, net	1,610	1,505	4,327
Share in the losses of associates treated under the equity method	17,512	21,378	5,946
Change in imputed benefit in respect of share based payment	(449)	14,606	2,403
Expenses (income) taxes that were recognized in the income statement	876,081	292,159	(288,344)
Change in financial assets held for trading	908,637	(2,239,890)	166,799
Profit from acquisition of shares in investee companies	-	(2,884)	-
Profit from realization of investments in available for sale financial assets	-	(22,265)	-
Expiration of warrants in a consolidated company	-	-	(2,927)
Income tax (paid) received, net	(103,092)	16,272	(38,624)
Revaluation of the Fuel Administration's balance	(9,151)	7,611	4,597
Revaluation of financial assets designated at fair value through profit and loss	1,443	5,454	(1,346)
Change in inventory	(93,436)	(21,489)	4,956
Change in account receivables and other receivables	(415,950)	(32,159)	(172)
Change in receivables in respect of a franchise arrangement	(8,529)	(17,143)	-
Change in account payables and other payables	179,144	(10,388)	199,846
Change in provisions and benefits to employees	(6,435)	(13,012)	5,160
Net cash - operating activities	1,686,903	(1,044,161)	1,428,704
Cash flows - investment activities			
Proceeds from fixed assets and intangible assets	4,234	25,626	10,381
Proceeds from investment property	-	9,086	85,913
Purchase and investment in investment property and investment property under construction	(1,707,785)	(474,468)	(998,108)
Purchase of fixed assets and intangible assets	(148,355)	(188,406)	(257,223)
Investment in and providing loans to associates	(20,123)	(19,094)	(70,753)
Change in long-term deposit	-	-	135
Change in short-term deposits	(35,942)	124,342	(124,607)
Change in restricted investments	(8)	(7,502)	-
Receipt (payment) for the removal of derivative financial instruments, net	18,568	(32,196)	(16,212)
Investment in financial assets available for sale	-	-	(743,150)
Recovery of Investment (Investment) in financial assets designated at fair value through profit and loss	(1,674)	185	(2,983)
Long term loans	(8,343)	(14,185)	(11,886)
Collection of long-term loans	29,836	11,761	33,908
Collection of loans from associates	-	73,861	-
Interest received	38,178	39,232	11,029
Acquisition of initially consolidated companies	-	(20,536)	-
Increase in the balance of the fuel administration	-	-	(45,863)
Proceeds from financial assets available for sale	-	35,616	2,600
Proceeds from realization of financial assets designated at fair value through profit and loss	-	211	-
Income tax paid pertaining to disposal of assets and investments	-	(10,736)	-
Net cash - investment activities	(1,831,414)	(447,203)	(2,126,819)

(*) Reclassified

The notes to the financial statements form an integral part thereof.

Azrieli Group Ltd.

Consolidated Statements of Cash Flows
(Continued)

	Year ended December 31		
	2011	2010	2009
	(in thousand NIS)		
Cash flows from financing activities			
Distribution of dividend to shareholders	(240,000)	-	-
Proceeds from issuance of bonds (less issuance expenses)	-	-	99,279
Repayment of bonds	(197,313)	(152,540)	(133,833)
Receipt of long-term loans from banks	873,198	563,838	1,097,074
Repayment of long-term loans from banks	(594,883)	(848,943)	(336,493)
Short-term credit from banks and others, net	773,333	(121,650)	282,819
Proceeds from issuance of shares (less issue expenses in the sum of approx. NIS 44 million)	-	2,480,697	-
Proceeds from the exercise of options for shares by employees in consolidated company	-	1,575	-
Repayment of deposits from customers	(2,970)	(2,021)	(1,069)
Receipt of deposits from customers	5,388	3,800	11,994
Acquisition of non-controlling interests (including loans)	(65,093)	(1,306)	(5,200)
Dividend to holders of non-controlling interests	(5,898)	(10,248)	-
Proceeds from the issue of shares in a consolidated company to holders of non-controlling interests	9,337	20	-
Interest paid	(364,085)	(330,145)	(297,487)
Net cash - financing activities	191,014	1,583,077	717,084
Increase in cash and cash equivalents	46,503	91,713	18,969
Cash and cash equivalents at the beginning of the year	177,858	92,632	75,771
Effect of fluctuations in exchange rates on balances of cash and cash equivalents	69	(6,487)	(2,108)
Cash and cash equivalents at the end of the year	224,430	177,858	92,632

The notes to the financial statements form an integral part thereof.

Note 1 General

A. General description of the Company and its operations

Azrieli Group Ltd. (the "Company" and/or the "Group") is a company domiciled in Israel, which was incorporated in Israel and whose registered address is Azrieli Center 1, Tel-Aviv. The Company has been traded on the Tel Aviv Stock Exchange since June 2010, and is included in the "Tel Aviv 25" index. The Group's consolidated financial statements as of December 31, 2011 include those of the Company and of its subsidiaries (jointly, the "Group"), as well as the Group's rights in associates and in entities under common control.

The Company is held at the rate of approx. 73.6% (until the issue of the Company, the Company was held at the rate of 100%) by the company Nadav Investments Inc. (the "Parent Company"), a private company incorporated under Canadian law, which is wholly owned and controlled by Azrieli Holdings Inc., a private company that was incorporated under Canadian law, which is wholly owned and controlled by Mr. David Azrieli, the Chairman of the Company's Board of Directors, who holds, directly and indirectly, approx. 40% of the issued and paid-up share capital, and his four children who each hold, directly and indirectly, approx. 15% of the issued and paid-up share capital.

The Company engages (both directly and through investee companies in which it invests and which it develops) in the following principal operating segments:

(1) In development, construction, acquisition, management and lease in the commercial centers and malls segment in Israel..

(2) In development, construction, acquisition, management and lease in the office and other space for lease segment in Israel.

(3) In the acquisition, management and lease in the income-producing property segment in the US.

(4) The holding of 60.68% of the shares and the voting rights in Granite Hacarmel Investments Ltd. ("Granite"). Granite is a company domiciled in Israel, which was incorporated in Israel and whose securities are listed on the TASE.

Granite and its consolidated companies engage primarily in:

- the sale of fuel in the fuelling stations and selling various consumer goods in the convenience stores and in the fuelling stations platforms.

- local purchase and import of gasoline and oils, the direct marketing and distribution thereof.

- local purchase and import of LPG, construction of an infrastructure for the distribution and marketing of natural gas, as well as development and construction of facilities for the production of solar energy.

- production and marketing of paints, coatings, powders and sealing, construction complementary products, gypsum and dry construction, etc.

- engineering planning, production and operating of facilities and systems for water desalination, water improvement and purification and sewage treatment.

B. Definitions

The Company	-	Azrieli Group Ltd. (the "Company" and/or the "Group")
The Parent Company	-	Nadav Investments Inc.
The Group	-	The Company and its consolidated companies.
Consolidated Companies	-	Companies in which the Company has control (as defined in IAS 27), either directly or indirectly, in the voting rights or in the rights to appoint members of the Board of Directors, at a rate that exceeds 50%, and whose financial statements are fully consolidated with those of the Company.
Companies under Common Control	-	Entities that are held by a number of bodies, between which there exists a contractual arrangement for the joint exercise of control over the economic activity of those entities.

Note 1 **General (contd.)**

B. Definitions (contd.)

Associates	-	Companies, including entities under common control, in which the Group has material effect and which are recorded in the financial statements under the equity method.
Investee Companies	-	Consolidated Companies, Companies under Common Control and Associates. See Note 46 for a list of the investee companies.
Joint Venture	-	A contractual arrangement, according to which two or more parties take economic activity upon themselves, which is subject to the exercise of joint control.
Other Companies	-	Companies that are held by the Group, in which there is no control, common control or material effect.
Related Parties	-	As defined in IAS 24.
Interested Parties	-	As defined in the Securities Law, 5728-1968, and regulations thereunder.
Controlling Interest	-	Within the meaning thereof in the Securities Regulations (Annual Financial Statements), 5770-2010.
Index	-	The Consumer Price Index, as published by the Israeli Central Bureau of Statistics.
Dollar	-	The US Dollar.
Euro	-	The currency of the European Union.
Canit Hashalom	-	Canit Hashalom Investments Ltd.
Granite	-	Granite Hacarmel Investments Ltd.
Sonol	-	Sonol Israel Ltd.
Tambour	-	Tambour Ltd.
G.E.S.		G.E.S. Global Environmental Solutions Ltd.
Supergas		Supergas - Israeli Gas Distribution Company Ltd.

Note 2 **Principal accounting policies**

A. Declaration in respect of the application of the International Financial Reporting Standards (IFRS):

The Group's consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (the "IFRS Standards") and the interpretations thereto, which have been published by the International Accounting Standards Board (IASB). The principal accounting policies that are detailed further on in this report have been applied in a consistent manner for all of the reporting periods that are presented in these consolidated financial statements, except for changes in the accounting policies, which derived from the application of standards, amendments to standards and interpretation, which have taken effect as of the date of the financial statements, as detailed in Note 2AO.

The consolidated financial statements were approved for publication by the Company’s Board of Directors on March 21, 2012.

Note 2 Principal accounting policies (contd.)

B. The financial statements include the disclosure requirements in accordance with the Securities Regulations (Annual Financial Statements), 5770-2010 (the "Financial Statements Regulations").

C. The operating cycle period:

The Group's operating cycle does not exceed 12 months.

D. The basis of the preparation of the financial statements:

Until December 31, 2003, Israel was considered to be a country in which hyper-inflationary conditions existed. Accordingly, non-monetary items in the balance sheets were presented on the basis of cost, as adjusted for changes in the Consumer Price Index until December 31, 2003. From that time onwards the adjusted amounts have served as a basis for the reporting for the periods following December 31, 2003 (the "Historical Cost"). The financial statements have been prepared on the historical cost basis, except for:

- The following assets and liabilities, which are presented in accordance with their fair values: available for sale financial assets, derivative financial instruments, financial instruments that are measured at fair value through profit and loss, financial instruments that are classified as available for sale, investment property and investment property under construction.
- Fixed assets and intangible assets, which are presented in accordance with the lower of cost, less accumulated depreciation and their realizable amounts.
- Inventory, which is presented at the lower of cost and net realizable value.
- Assets and liabilities in respect of employee benefits.
- Provisions, which are recognized in accordance with the best estimate of the expense that is required in order to extinguish a present commitment at the end of the reporting period. Where the impact of the time value of the money is important, the future cash flows are discounted using a pre-tax interest rate that reflects the market's current evaluations of the time value of the money and of the risks that are specific to the commitment.
- Investments in associates and in entities under common control treated under the equity method.

E. The format for the analysis of the expenses that have been recognized in the statement of comprehensive income:

The Company's expenses in the statement of comprehensive income are presented in accordance with a method of classification based on the nature of the activity to which the expense relates.

F. Foreign currency:

(1) The functional currency and the presentation currency

The financial statements of each of the companies in the Group have been prepared in the currency of the main economic environment in which they operate (the "Functional Currency"). For the purposes of the consolidation of the financial statements, the results and the financial position of each of the companies in the Group are presented in New Israeli Shekels (NIS), which is the Company's functional currency. The Company's consolidated financial statements are presented in NIS in thousands. See Note 2AN on the subject of exchange rates and the changes therein in the course of the periods that are presented.

(2) The translation of transactions other than in the functional currency

In the preparation of the financial statements of each of the companies in the Group, transactions that were executed in currencies that are different from the Company's functional currency ("Foreign Currency") have been recorded in accordance with the exchange rates that were in force at the time of the transactions. At the end of each reporting period, monetary items that are stated in foreign currency are translated in accordance with the exchange rates in force as of that time. Non-monetary items that are measured at fair value and stated in foreign currency are translated in accordance with the exchange rate at the time at which the fair value was determined; non-monetary items that are measured in historical cost terms are translated in accordance with the exchange rates that were in force at the time of the execution of the transaction in respect of the non-monetary item.

Note 2 Principal accounting policies (contd.)

F. Foreign currency: (contd.)

(3) The manner in which exchange differences are recorded

Exchange differences are recognized in the income statement in the period in which they arise, except for the following cases:

- Exchange differences that relate to assets under construction for the purposes of future use in manufacturing, are recorded under the cost of those assets, where the constitute the adjustment of interest costs on credit in foreign currency (see Note 2Q in respect of the Group's accounting policy on the subject of the capitalization of credit costs).
- Exchange differences in respect of transactions that were designated for the hedging of certain foreign currency risks (see Note 2N in respect of the Group's accounting policy on the subject of hedging transactions).
- Exchange differences in respect of financial items receivable or payable from foreign operations, whose settlement is not planned or expected to occur and accordingly they constitute part of the net investment in foreign operations, are recognized in the statement of other comprehensive income under the item "exchange differences in respect of foreign operations", and are carried to the income statement at the time of the disposal of the net investment in foreign operations.

(4) The translation of the financial statements of associates whose functional currency is different from the Shekel (the Group's functional currency)

For the purposes of the presentation of the consolidated financial statements, the assets and the liabilities of foreign operations, including goodwill and attributed surplus cost, are presented in accordance with the exchange rate in force at the end of the reporting period. Income and expense items are translated in accordance with the average exchange rate for the reporting period unless there shall have been significant fluctuations in the exchange rates in the course of the period. In such a case, the translation of these items is done using the exchange rates at the time of the execution of the transactions and the related exchange differences are recognized in the statement of comprehensive income under "translation differences in respect of foreign operations". The translation differences are classified to the income statement on the disposal of the foreign operations in respect of which they were recorded.

G. Consolidated financial statements:

The Group's consolidated financial statements include the financial statements of the Company and of entities that are directly or indirectly controlled by the Company. Control exists where the Company has the power to control the financial and operating policies of the investee company for the purpose of achieving benefits from its operations. Potential voting rights, which can be exercised or converted immediately into shares in an investee company are taken into account in the testing for the existence of control.

The operating results of subsidiaries that have been acquired or disposed of during the course of the reporting period are included in the Company's statements of comprehensive income as from the time at which the control is achieved or up to the time that control is discontinued, as the case may be.

The financial statements of the consolidated companies that were prepared other than in accordance with the Group's accounting policies were adjusted, prior to their consolidation, to the accounting policies that have been implemented by the Group.

For the purposes of the consolidation, all inter-company transactions, balances, income and expenses have been eliminated in full.

H. Non-controlling interests:

Non-controlling interests are the capital in a subsidiary which cannot be attributed, either directly or indirectly, to the parent company, and include additional components such as options for shares of subsidiaries.

Note 2 Principal accounting policies (contd.)

H. Non-controlling interests: (contd.)

Measurement of non-controlling interests on the date of the business combination
For non-controlling interests which are instruments that grant an ownership right in the present and which grant the holder thereof a net share of the assets in the event of dissolution (for example: ordinary shares) are measured on the date of the business combination at fair value or according to their proportionate share of the identified assets and liabilities of the acquiree, on the basis of each transaction separately.
Election of this accounting policy is not permitted for other instruments that meet the definition of non-controlling interests (for example: options for ordinary shares). These instruments will be measured at fair value or according to the provisions of other relevant IFRS standards.

With respect to acquisitions that occurred between January 1, 2007 and January 1, 2010, non-controlling interests were measured on the date of the business combination according to their proportionate share of the identified assets and liabilities of the acquiree.

With respect to acquisitions that occurred before the transition date, the Group adopted the relief in IFRS 1 and elected not to apply the provisions of IFRS 3 (2004) retroactively, as described above.

Allotment of the comprehensive income between the shareholders
From January 1, 2010, profit or loss and any component of other comprehensive income are attributed to the holders of the Company and to non-controlling interests. The sum total of comprehensive income is attributed to the holders of the Company and to non-controlling interests, even if as a result thereof, the balance of the non-controlling interests will be negative. To date, no profits or losses and components of other comprehensive income have been attributed to non-controlling interests if as a result thereof this balance would have been negative, except in the event that the non-controlling interests had a contractual obligation and the ability to make another investment to cover the losses.

Transactions with non-controlling interests, while retaining control
Until January 1, 2010, in respect of the acquisition of non-controlling interests, the Group implemented the acquisition method only in respect of the additional holding percentages that were acquired, while the previous holding remained unchanged and the effect in respect of the sale of non-controlling interests was carried to the income statement.
From January 1, 2010, transactions with non-controlling interests while retaining control are treated as equity transactions. Any difference between the consideration paid or received and the change in the non-controlling interests is carried to the share of the holders of the Company directly to capital funds.

In addition, upon changes at the rate of the holding in a subsidiary, while retaining control, the Company reattributes the aggregate amounts that were recognized in other comprehensive income between the holders of the Company and the non-controlling interests.

I. Business combinations:

The Group applies the acquisition method to all business combinations.

The acquisition date is the date on which the acquirer gains control of the acquiree. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Immediately-exercisable potential voting rights are taken into account in determining control. The company exercises discretion on the determination of the acquisition date and on whether control has been gained.

Treatment of business combinations after January 1, 2010
For acquisitions having occurred after January 1, 2010, the Group recognizes goodwill as of the acquisition date according to the fair value of the consideration remitted, including amounts recognized for any non-controlling rights in the acquiree, and the fair value as of the acquisition date of a capital right in the acquiree which was previously held by the acquirer, net of the amount (net) attributed in the acquisition to identifiable assets acquired and liabilities assumed.

Note 2 Principal accounting policies (contd.)

I. Business combinations: (contd.)

If the Group performs an acquisition at an opportunity price (which includes negative goodwill), it recognizes the profit resulting therefrom in the income statement on the acquisition date.

In addition, from January 1, 2010, goodwill is not updated in respect of the utilization of carried losses for tax purposes having existed on the date of the business combination, also in respect of previous business combinations having occurred before such date.

The consideration remitted includes the fair value of the assets transferred to the previous owners of the acquiree, liabilities incurred by the acquirer vis-à-vis the acquirer's previous owners and capital rights issued by the Group. In a business combination achieved in stages, the difference between the fair value as of the acquisition date of the capital rights in the acquiree having been previously held by the Group, and the book value as of such date, is carried to the income statement in the other expenses or revenues item.

In addition, the consideration remitted includes the fair value of contingent consideration. After the acquisition date, the Group recognizes changes in the fair value of the contingent consideration which is classified as a financial liability in the income statement. Changes in the liability in respect of a contingent consideration in business combinations having occurred before January 1, 2010, will continue to be recognized as goodwill and not carried to the income statement

Costs associated with the acquisition, incurred by the acquirer in respect of a business combination, such as broker fees, consultancy fees, legal fees, valuations and other fees for professional services or consulting services, other than those related to capital or debt instrument issues in connection with the business combination, are recognized as expenses in the period in which the services are received.

Business combinations having occurred between January 1, 2007 and January 1, 2010
For acquisitions having occurred between January 1, 2007 (the date of transition to IFRS) and January 1, 2010, the goodwill recognized represents the surplus cost of the acquisition over the Group's rights in the amount recognized (generally fair value) in respect of the recognized assets, the liabilities and contingent liabilities of the acquiree. When a negative surplus is created, the Group recognizes a profit from an opportunity acquisition in the income statement on the acquisition date.

Transaction costs incurred by the Group in respect of a business combination, other than those related to the issue of capital or debt instruments, have been recognized as part of the acquisition cost.

Business combinations having occurred before January 1, 2007 (the date of transition to IFRS)
On the date of transition to IFRS, the Group adopted the relief under IFRS 1 and elected not to apply the provisions of IFRS 3 (2004) retroactively to business combinations, acquisitions of associates and acquisition of minority rights having occurred before the transition date. Therefore, for acquisitions having accrued before January 1, 2007, the goodwill recognized and the cost surplus created represent the amounts recognized according to Israeli GAAP.

Business combinations under the same control
Business combination transactions in which all of the combined entities are controlled by the same controlling shareholder, both before and after the business combination, are measured by using a method similar to the consolidation method known as "As Pooling", as follows:

- The assets and liabilities of the acquired company are recognized for the first time in the Group's consolidated financial statements according to their book value in the financial statements of the controlling shareholder on the eve of the business combination transaction.

- The difference between the consideration determined in the transaction and the book value of the net assets of the acquired company is carried directly to equity.

Note 2 Principal accounting policies (contd.)

I. Business combinations: (contd.)

- The consolidated financial statements reflect the condition of the business and the results of operations of the Company and the acquired company, as if the business combination was performed on the day on which the Company and the acquired company were under the same control.

J. Associates and entities under common control (that are treated under the equity method):

Associates are entities in which the Group has material effect over the financial and operational policies, but where control has not been achieved. There is an assumption whereby the holding of 20% through 50% in the investee confers a material effect. In reviewing the existence of material effect, potential voting rights that are exercisable or convertible immediately to the shares of the investee company are taken into consideration. Entities under common control are entities where the Group has joint control over their activities, which has been achieved by means of a contractual agreement that requires joint agreement in respect of financial and operational decisions that relate to strategic activity.

Investment in associates and entities under common control is treated under the equity method and is initially recognized at cost. The cost of the investment includes transaction costs.

The consolidated financial statements include the Group's share of the incomes and the expenses, the profit or loss and in other comprehensive income of investee entities that are treated under the equity method, after the adjustments that are required in order to adjust the accounting policies to those of the Group, from the day on which material effect or common control arises and until the day on which material effect or common control no longer exists. Where the Group's share of the losses exceeds the value of the Group's rights in an entity that is treated under the equity method, the carrying value of those rights in the accounting records (including long-term investment that constitutes part of the investment account in the investee) is written down to zero and the Group does not recognize additional losses, unless the Group has a commitment to support the investee entity or if the Group has paid amounts on its behalf.

Profits or losses generated from transactions performed between the Company and/or a consolidated company and associates and entities under common control, are cancelled in accordance with the Group’s share in the rights of the relevant associate.

K. Change in the Holding Rates in Associates whilst Retaining Material Effect:

Upon a rise in the rate of holding in an associate which is treated under the equity method whilst retaining material effect, the Group implements the purchase method only in respect of the additional holding percentages, while the previous holding remains unchanged.

Upon a decline in the rate of holding in an associate which is treated under the equity method whilst retaining material effect, the Group writes off a proportionate share of its investment and recognizes profit or loss from the sale, in the framework of the other revenues or expenses item in the income statement.

In addition, on such date, a proportionate share of the amounts recognized in capital reserves through other comprehensive profit in relation to such associate is reclassified to the income statement or to surpluses, in such manner as would have been required had the associate itself liquidated the relevant assets or liabilities.

L. Operations under common control (joint ventures):

Operations under common control are joint ventures in which each party uses the assets that it owns for the purposes of the common operations. The consolidated financial statements include the assets of joint operations that are controlled by the Group, the commitments of the joint operations, to which it is exposed, the expenses that it bears in connection with the joint operations and its share of the income from the joint operations.

M. Goodwill:

Goodwill that derives from the acquisition of a consolidated company is measured at the level of the surplus of the cost of the acquisition over the net fair value of the identified assets, liabilities and contingent liabilities of the company, which were recognized at the time of the acquisition. Goodwill is initially recognized as an asset at cost and is measured in following periods as cost less accumulated losses from impairment in value.

Note 2 Principal accounting policies (contd.)

M. Goodwill: (contd.)

For the purposes of the testing for impairment in value, goodwill is allocated to each of the Group's cash generating units, which derive benefits from the synergies from the business combination. Cash generating units to which Goodwill has been allocated are tested for impairment in value each year or more frequently, where signs exist, which evidence a possible impairment in the value of the unit, as aforesaid. Where the recoverable amount of a cash generating unit is lower than the carrying value of that unit, the loss from impairment in value is allocated firstly to the writing down of the carrying value of any goodwill whatsoever in respect of the cash generating unit. Thereafter, the balance of the impairment loss, if any remains, is allocated to the other assets making up the cash generating unit, in proportion to their carrying values. A loss on the impairment in the value of goodwill is not cancelled in following periods.

When a consolidated company is disposed of, the amount of the goodwill that is attributed to it is included in the determination of the profit or loss on the disposal.

N. Financial instruments:

(1) Non-derivative financial instruments

The initial recognition of financial assets

The Group initially recognizes loans, receivables and deposits at the time that they are created. The other financial assets, which are purchased in the regular way (regular way purchases), are initially recognized at the time that the transaction is entered into (the trade date), on which the Group becomes a party to the contractual terms of the instrument, which means the time at which the Group has undertaken to purchase or to sell the asset. Non-derivative financial assets include investments in shares and in debt instruments, loans that have been extended, trade receivables and other receivables, receivables in respect of franchise agreements and cash and cash equivalents.

The removal of financial assets

Financial assets are removed where the Group's contractual rights to the cash flows that derive from the financial asset expire, or where the Group transfers the rights to receive the cash flows that derive from the financial assets in a transaction in which all of the risks and the benefits of the ownership of the financial asset in a transaction in which all of the risks and benefits of the ownership of the financial asset are effectively transferred from it.

Every right in financial assets that have been transferred, which has been created or retained by the Group is recognized as a separate asset or liability.

The sale of financial assets, which is effected in the regular way (a regular way sale), is recognized at the time of the entry into the transaction (trade date), which means the time at which the Group undertook to sell the asset.

See section (2) below on the subject of the setting off of financial assets and financial liabilities.

The Group classifies financial assets into the following groups:

Cash and cash equivalents

Cash and cash equivalents include cash balances that can be used immediately and demand deposits. Cash equivalents include highly liquid, short-term investments (where the time from the original deposit to the repayment date is up to 3 months), which can be easily converted into known amounts of cash and which are exposed to insignificant risks of changes in value.

Loans and receivables

Loans and receivable balances are non-derivative financial assets with fixed payments or payments that can be fixed, which are not traded in an active market. These assets are initially recognized at fair value with the addition of attributable transaction costs. Following the initial recognition, loans and receivable balances are measured at cost, which is amortized using the effective interest method and less losses from impairment in value.

Loans and receivables include deposits, trade and other receivables, receivables for work in progress as well as receivables in respect of franchise agreement.

Note 2 Principal accounting policies (contd.)

N. Financial instruments: (contd.)

(1) Non-derivative financial instruments (contd.)

Investments that are presented at fair value through profit and loss

Financial instruments are classified as "financial assets at fair value through profit and loss", where those assets are held for trade or if they are designated as financial assets at fair value through profit and loss.

A financial asset (an investment in a high-tech company in Israel and abroad), which is not a financial asset and which is held for trading purposes, is designated as a financial asset at fair value through profit and loss at the time of initial recognition, if the financial asset forms part of a group of assets or financial liabilities or both of them together, whose management and performance are evaluated on the basis of their fair value, in accordance with the Group's documented policy for the management of the risks or its investment strategy, and information in respect of the group of financial instruments is passed on within the framework of the internal reporting, in accordance with this basis, to the Group's key managerial personnel. The Company's management tests the fair value in every reporting period, on the basis of the use of up to date transactions in the market between a willing buyer and a willing seller, who are acting in an educated manner, and who are not influenced by especial relationships between the parties. For investments for which there are not quotes in an active market, the fair value is based on the price of transactions that have been executed close to the reporting period. Where no transactions have been executed in a period that exceeds one year, the fair value for those investments is adjusted using an evaluation technique that makes maximum usage of market data and reported data (such as : data from the financial statements and information for investors of companies).

A financial asset at fair value through profit and loss is presented at fair value. Any gain or loss that derives from changes in the fair value, including those that are sources in changes in exchange rates, is recognized in the income statement in the period in which the change occurs. The net gain or loss that is recognized in the income statement, also includes the dividend or interest that has been generated in respect of the financial asset.

A financial asset is classified as held for trade purposes if:

- It was purchased primarily for the purpose of sale in the near future; or
- It forms part of the portfolio of identified financial instruments, which are managed together by the Group and which has a proven actual pattern of activity for the purposes of producing gains in the short-term; or
- It is a derivative that is designated and effective as a hedging instrument.

Available for sale financial assets

Investments in marketable and non-marketable capital instruments, which are not derivative financial instruments, which have not been classified as financial assets at fair value through the profit and loss or as loans and receivables, are classified as available for sale financial instruments.

Gains or losses that derive from changes in the fair value are reflected directly in other comprehensive income under the item "profit (loss) in respect of available for sale financial assets", except for losses from impairment in value, which in certain circumstances are carried to the income statement, where the investments in those financial assets are disposed of or where an impairment has occurred in their value. The gains or losses that have accumulated up to the time of the disposal or impairment in value, as the case may be, and which have been reflected under other comprehensive income, are recorded in the income statement in the period in which the disposal was executes or in which the impairment in value occurred.

The fair value of available for sale financial assets, which are stated in foreign currency, is determined in that same currency and translated into the Group's functional currency (NIS) in accordance with the exchange rates that was in force at the end of the reporting period. Gains and losses as the result of a change in the exchange rates are carried to the income statement on the basis of the amortized cost of the financial item. Other gains and losses in respect of changes in the exchange rates are recognized in other comprehensive income.

Note 2 Principal accounting policies (contd.)

N. Financial instruments: (contd.)

(1) Non-derivative financial instruments (contd.)

Available for sale financial assets (contd.)

Income from dividends in respect of an investment in available for sale instruments are recognized in the income statement when the Group's entitlement to receive payments in respect of them is created.

(2) Non-derivative financial liabilities

The Group initially recognizes debt instruments that have been issued at the time that they are created. Other financial liabilities are initially recognized at the time of the entry into the transactions (the trade date) on which the Group becomes a party to the contractual terms of the instrument. Financial liabilities are removed when the Group's commitment, as detailed in the agreement, expires or when it is cleared or it is cancelled.

Financial liabilities are initially recognized at fair value with the addition of all of the attributable transactions costs. Following the initial recognition, the financial liabilities are measured at amortized cost in accordance with the effective interest method.

Replacement of debt instruments with materially different conditions between existing borrower and lender, is treated as repayment of the original financial liability and recognition of a new financial liability at fair value. Also, significant change in the conditions of an existing financial liability or any part thereof, is treated as the repayment of the original financial liability and recognition of a new financial liability.

The terms are materially different if the current discounted value of the cash flows according to the new terms, including any commissions paid less any commissions received and discounted through the original effective interest rate, is different by at least ten percent from the current discounted value of the remaining cash flows of the original financial liability.

In addition to the aforesaid quantitative criteria, the Group examines, *inter alia*, whether changes had occurred also to various economic and qualitative parameters entailed in the replaced debt instruments.

The non-derivative financial liabilities include: bank overdrafts, loans and credit from banking entities and other providers of credit, liabilities in respect of finance leases, deposits from customers and trade and other payables.

Financial assets and financial liabilities are set off and the amounts are presented net in the statement of financial position, where the group has a current, enforceable legal right to set-off the amounts that have been recognized and it intends to clear the asset and the liability on a net basis or to dispose of the asset and to clear the liability simultaneously.

(3) Derivative financial instruments including hedge accounting

The Group holds derivative financial instruments for the purpose of hedging foreign currency risks and interest rate risks, as well as derivatives not used for hedging, including separated embedded derivatives.

Hedge accounting

At the time of commencement of the hedge accounting, the Group formally documents the hedge relationship between the hedging instrument and the hedged item, including the risk management purpose and the Group’s strategy in performing the hedging, as well as the manner in which the Group will evaluate the effectiveness of the hedge relationship.

Note 2 Principal accounting policies (contd.)

N. Financial instruments: (contd.)

(3) Derivative financial instruments including hedge accounting (contd.)

Hedge accounting (contd.)

At the time the hedge is made and in subsequent periods, the Group evaluates whether the hedge is expected to be highly effective in the achievement of offsetting cash flow changes, which can be attributed to the hedged risk over the period for which the hedge is designated, and whether the actual results of the hedge are within the range of 80-125%.

With respect to cash flow hedging, a forecasted transaction which is a hedged item is required to be highly probable and cause an exposure to cash flows changes which could ultimately affect the profit and loss.

Measurement of derivative financial instruments

Derivatives are initially recognized at fair value. Attributable transaction costs are carried to the income statement when incurred. After the initial recognition, the derivatives are measured at fair value, whilst the changes in the fair value are treated as follows:

Cash flow hedge

Changes in the fair value of derivatives used to hedge cash flows, in respect of the effective hedging portion, are carried through other comprehensive income directly to the hedge fund. In respect of the non-effective portion, the changes in fair value are carried to the income statement. The amount accrued in the hedge fund is reclassified to the income statement in the period in which the cash flows affect the income statement and is presented in the same income statement item in which the hedged item is found. If the hedging instrument no longer meets the criteria of hedge accounting, or expires, is sold, cancelled or exercised, then hedge accounting treatment is stopped. The profit or loss previously accrued in the hedge fund through other comprehensive income, remains in the fund until the forecasted transaction is performed or until the forecasted transaction is no longer expected to take place. If the forecasted transaction is no longer expected to take place, the accrued profit or loss in respect of the hedging instrument, which accrued in the hedge fund, will be reclassified to the income statement. When the hedged item is a non-financial asset, the amount attributed to the hedge fund is carried to the asset's book value at the time of recognition thereof.

In other cases, the amount attributed to the hedge fund is carried to the income statement in the period in which the hedged item affects the profit and loss.

Economic hedge

Hedging accounting is not implemented in respect of derivative instruments that are used for the economic hedging of financial assets and liabilities that are stated in foreign currency. The changes in the fair value of these derivatives are carried to the income statement, as financing income or expenses.

Derivatives that are not used for hedge

Changes in the fair value of derivatives that are not used for hedging are reflected immediately in the income statement, as financing income or expenses. The Group applies the accounting treatment, as aforesaid, in respect of changes in the fair value of the conversion element of convertible bonds that are index linked.

Note 2 Principal accounting policies (contd.)

N. Financial instruments: (contd.)

Embedded derivatives that were separated and are not used for hedge

Embedded derivatives are separated from the host contract and treated separately if: (a) there is no close connection between the financial characteristics and the risks of the host contract and of the embedded derivative, (b) a separate instrument with the same conditions as the embedded derivative would have met the definition of a derivative and (c) the hybrid instrument is not measured according to fair value through profit and loss. Changes in the fair value of imbedded derivatives that can be separated are reflected immediately in the income statement, as financing income or expenses.

(4) Index-linked convertible bonds

Bonds that are convertible into shares in a consolidated company, which are linked to the Consumer Prices Index, are hybrid financial instruments, which include a debt component and a convertible option. At the time of the initial recognition the consideration from the issue is split between the debt component of the bond and the convertible option that it contains.

At the time of the issue, the convertible option is measured at fair value. The balance of the consideration in respect of the bond is attributed to the debt component. Recruitment costs are allocated to the debt component and to the convertible option in proportion to the relative fair value of each component at the time of the issue. The portion of the recruitment costs that are attributed to the debt component is presented as a set-off against the liability in respect of the convertible bonds. The portion of the recruitment costs that is attributed to the convertible options is reflected immediately in the income statement.

The convertible option is presented as a derivative, and is measures at fair value at the end of each reporting period with changes in the fair value being carried to the income statement.

(5) Index-linked assets and liabilities that are not measured at fair value

The effective interest rate of a group of financial assets that are linked to the Consumer Prices Index (the "Index", which are not measured at fair value through profit and loss, is determined as the real rate with the addition of linkage differences in accordance with the actual changes in the index up to the end of the reporting period.

(6) Financial guarantees

At the time of the initial recognition, a financial guarantee is recognized at its fair value. In following periods, a financial guarantee is measured in accordance with the higher of the amount that is recognized in accordance with the provisions of IAS 37 and the liability that was initially recognized, after it has been amortized in accordance with IAS 18. Any update of the amount of the liability, in accordance with the aforesaid, is carried to the income statement.

(7) Share capital

Additional costs, which relate directly to the issuance of ordinary shares and options for shares, are presented as a deduction from capital.

(8) The issuance of a parcel of securities

At the time of the issuance of a parcel of securities, the consideration from the issue is attributed firstly to the financial liabilities, which are measured each period at fair value through profit and loss, and afterwards to financial liabilities, which are measured at the time of the initial recognition alone at fair value and the value that is attributed to the capital element is calculated as the residual value.

Direct issuance expenses are attributed specifically to the securities with which they are identified. Joint issuance expenses are attributed to the securities proportionately, on the basis of the manner in which the consideration from the issuance of the parcel is attributed, as described above.

Note 2 Principal accounting policies (contd.)

N. Financial instruments: (contd.)

(9) Deposits from customers

Within the context of its operations, a consolidated company receives deposits from its customers in respect of containers and other equipment that are lent. The deposit will be returned in accordance with the prices of the deposit that the consolidated company collects from its customers, which are linked to the index from the day of the latest update. In accordance with IAS 39, the fair value of financial liabilities with a demand characteristic is not to be lower than the amount that is to be paid on demand, discounted from the first time at which it will be possible to demand the amount. Accordingly, the deposits are presented at their full value. Moreover, since the consolidated company has no irrevocable right to defer the clearance of the liabilities in respect of the deposits for a period of at least 12 months after the reporting date, the deposits are presented as current liabilities, on the basis of their full value.

O. Fixed assets:

(1) Recognition and measurement

Fixed asset items are measured at cost less accumulated depreciation and losses from impairment in value. The cost of realty assets and various additional fixed asset items was determined at their fair value as of January 1, 2007, the transition date to IFRS (calculated cost).

The cost includes the expenses that can be directly attributed to the acquisition of the asset. The cost of assets that have been self-built includes the cost of the materials and the direct labor, as well as any additional cost that can be directly related to bringing the asset to the location and the state that are required in order for it to operate in the manner intended by management, as well as the costs of the dismantling and removal of the item and the rehabilitation of the site at which the item is located. The cost of software that has been acquired, which constitutes an integral part of the relevant plant and equipment, is recognized as part of the cost of that equipment.

Where significant components of the fixed assets (including significant periodic checking costs) have a different lifetime, they are treated a separate items (significant components) of the fixed assets.

A profit or loss on the disposal of a fixed asset item is determined in accordance with the comparison of the consideration from the disposal of the asset to the carrying value in the accounting records, and is recognized under other income or other expenses in the income statement, as the case may be.

(2) Further costs

The cost of the replacement of a part of a fixed asset item is recognized as part of the carrying value in the accounting records of that item if it is expected that the future economic benefit that is inherent in the item will flow to the Group and that its cost can be measured in a reliable manner. The carrying value in the accounting records of the part that has been replaced is removed. Routine maintenance costs in respect of fixed asset items are carried to the income statement as incurred.

(3) Depreciation

Depreciation is the systematic allocation of the depreciable amount of an asset over the length of its useful lifetime. The depreciable amount is the cost of the asset, or some other amount that replaces the cost, net of the residual value of the asset.

Depreciation is carried to the income statement in accordance with the straight line method in accordance with an estimate of the useful lifetime of each of the fixed asset items, since this method reflects the manner of the forecast consumption of the future economic benefits that are inherent in an asset in the best way. Leased assets, including lands, are amortized over the shorter of the lease period and the period in which the assets are used, unless it is reasonably expected that the Group shall acquire ownership over the asset at the end of the lease period. Lands are not amortized.

Note 2 Principal accounting policies (contd.)

O. Fixed assets: (contd.)

(3) Depreciation (contd.)

The estimated useful lifetimes for the current period and for the comparative periods are as follows:

	Useful lifetime in years	Depreciation rate %
Buildings (including temporary buildings)	10–50	2–10
Plant and equipment	3–30 (primarily 6-10)	3–33 (primarily 10–15)
Office furniture and equipment	3–17	6–33
Motor vehicles	5–6	15–20
Computers	3–5	20-33
Leasehold improvements	Throughout the lease period, which does not exceed the economic lifetime of the asset.	

The depreciation method, the residual value and the useful lifetimes of the assets are reviewed by the Company's management at the end of each financial year. Changes are treated as a change in an estimate by way of "prospective application".

P. Investment property:

Investment property is property (land or a building – or part of them - or both of them), which are held by the Group for the purpose of the production of rental income or for the purposes of a capital gain or both of them, and not for the purposes of use in the production or supply of goods or services or for administrative purposes or for sale in the ordinary course of business.

Investment property, as aforesaid, also includes investment property that is under construction or development.

The Group's investment property includes building and land that is owned or held under finance leasing, as well as rights in real estate that are held by the Group under operating leasing where otherwise the definition of investment property would be complied with. Investment property is initially measured at cost, which includes transaction costs. In periods following the initial recognition, investment property is measured at fair value. Gains or losses deriving from changes in the fair value of investment property, including those that are sources in changes in exchange rates, are recorded in the income statement in the period in which they were generated, under the item "net gain on the adjustment of the fair value of investment property and investment property under construction".

The direct costs of the disposal of investment property are carried to the income statement at the time at which the asset is sold and are set-off against the gain on disposal. The difference between the consideration that is received on the disposal of investment property and the fair value, is the capital gain (loss) on disposal, which is carried to the income statement at the time of the completion of the disposal transaction under "net gain on the adjustment of the fair value of investment property and investment property under construction".

Q. Credit costs:

Specific credit costs and non-specific credit costs are capitalized to qualifying assets in the course of the period that is required for the completion and for the construction up to the time at which they are ready for their designated use. Non-specific credit costs are capitalized in the same manner for the same investment in qualifying assets or to the part of it that is not financed by specific credit, using a rate which is a weighted average of the rates of the cost in respect of the sources of credit whose cost has not been capitalized in a specific manner. Other credit costs are carried to the income statement as incurred.

Income deriving from the temporary investment of specific credit that was received for the purpose of investment in qualifying assets is deducted from the credit costs that qualify for capitalization.

All other credit costs are carried to the income statement as incurred.

Note 2 Principal accounting policies (contd.)

R. Intangible assets, except for goodwill:

Intangible assets are assets that are not identifiable and which lack a physical presence. Intangible assets having an indefinite useful lifetime are not amortized and are tested for impairment in value once a year, or at any time at which a sign exists, which indicates the possibility that an impairment in value has occurred in accordance with the provisions of IAS 36. The estimate of the useful lifetimes of intangible assets having an indefinite lifetime is tested at the end of each reporting year. A change in the estimated useful lifetime of an intangible asset, which turns from being indefinite to being defined is treated by way of "prospective application".

Intangible assets having a defined useful lifetime are amortized on a straight line over the length of their estimated useful lives, subject to testing for impairment in value. A change in an estimate of the useful lifetime of an intangible asset with a defined lifetime is treated by way of "prospective application".

See Note 2M on the subject of the accounting treatment of goodwill.

The useful lifetimes that have been used in the amortization of intangible assets having a defined lifetime are as follows:

Distribution rights	-	20 years or in accordance with the period of the agreement.
Supply rights	-	20 years or in accordance with the period of the agreement.
Software	-	3 – 6 years
Customer relations	-	7 – 14 years
Franchise arrangement		Over the period of the franchise.
Brand name	-	7 – 12 years
Others	-	Over the period of the benefit

Following costs

Following costs are recognized as an intangible asset solely and exclusively where they increase the future economic benefit that is inherent in an asset, in respect of which they were expended. All of the other costs, including costs that are connected to goodwill and to brands that have been developed independently, are carried to the income statement as incurred.

Intangible assets that were acquired within the context of business combinations

Intangible assets that were acquired within the framework of business combinations are identified and recognized separately from goodwill, where they meet the definition of an intangible asset and their fair value can be reliably measured. The cost of such intangible assets is their fair value at the time of the business combination.

In the periods following the initial recognition, intangible assets that have been acquired within the framework of business combinations are presented in accordance with their cost, less accumulated amortization and losses from impairment in value. The amortization of intangible assets, having a defined lifetime, is calculated on the straight line basis over the length of their estimated useful lifetimes. The estimate of the useful lifetime and the method of amortization are tested at the end of each reporting year, where the effect of a change in them is treated by way of "prospective application".

S. Leased assets:

Leases, including leases of land from the Israel Land Administration or from other third parties where the Group bears significantly all of the risks and the yields that derive from the asset, are classified as finance leasing. On initial recognition, the leased assets are measured at an amount that is equivalent to the lower of the fair value and the present value of the minimum future lease payments. Future payments for exercise of the option to extend the lease period vis-à-vis the Israel Land Administration are not recognized as part of the relevant asset and liability, since they constitute contingent rent, which derives from the fair value of the land on the future dates of renewal of the lease agreement. Following the initial recognition, the asset is treated in accordance with the accounting policy that is customary in respect of that asset.

Note 2 Principal accounting policies (contd.)

S. Leased assets: (contd.)

The other leased assets are classified as operating leasing, except for leases of property that is classified as investment property, where the leased assets are not recognized in the Group's statement of financial position. Real estate assets under operating leasing, which have been classified by the Group as investment property, are recognized in the Group's statement of financial position at their fair value, and the leasing is treated as finance leasing.

Rental fees that have been paid in advance to the Israel Land Administration in respect of leases of land which are classified as operating leases are presented in the statement of financial position as prepaid expenses and are carried to the income statement over the length of the leasing period. The leasing period and the amounts of the amortization take into account any option to extend the leasing period, in the event that at the time of the commitment under the lease it is reasonably certain that the option will be exercised.

In a lease of land and buildings the components of the land and the buildings are examined separately for lease classification purposes, with a significant consideration in the classification of the components of the land being the fact that land usually has an indefinite lifetime.

T. Construction work in progress:

Construction work in progress reflect the gross amount, against which accounts have not yet been issued, which is expected to be collected from customers in respect of work that has been executed up to that time. This amount is measured in accordance with the costs that have been incurred with the addition of the profit that has been recognized as of that time, less charges that have been issued to customers during the course of the construction period and losses that have been recognized. The cost includes all of the costs that relate directly to the relevant projects with the addition of the allocation of fixed and variable overhead expenses that the Group bears in the course of the execution of the works in accordance with the contract, based on the normative capacity of the operations.

Construction work in progress are presented in the statement of financial position as a separate item – receivables in respect of works in progress. In cases where the payments that have been received from customers exceed the amount of the costs that have been incurred with the addition of the profits that have been recognized, then the difference is recognized in the statement of financial position as deferred income.

U. Inventory:

(1) Inventory of oil distillates

The inventory is presented in accordance with the lower of the cost or the net realizable value. The cost of the inventory is determined on the basis of "first in first out" (FIFO), and it includes the costs of the purchase of the inventory and of bringing it to its current location and condition. The net realizable value is an estimate of the selling price in the ordinary course of business less an estimate of the costs that are required in order to carry out the sale.

(2) Other inventory

The Inventory of oils, spare parts and other items is presented at the lower of cost and net realizable value. The cost of the inventory is determined on the moving average basis.

The inventory of paints is presented at the lower of cost and net realizable value. The cost of the inventory is primarily determined as follows:

Raw materials and packing material	-	In accordance with the moving average method.
Finished goods	-	In accordance with a standard price based on raw materials, packaging materials, plus calculated production cost.
Work in progress	-	In accordance with a standard price based on raw materials plus calculated production costs.
Purchased goods	-	In accordance with the moving average method.

V. Impairment of financial assets:

Impairment in the value of a financial asset that is not presented at fair value through profit and loss is tested where there is objective evidence that a loss event has occurred after the time of the initial recognition of the asset and that this loss event has had a negative impact on the estimated future cash flows from the asset, which can be measured in a reliable manner.

Note 2 Principal accounting policies (contd.)

V. Impairment of financial assets: (contd.)

Objective evidence that an impairment in the value of an asset has occurred may include the breach of a contract by a debtor, the re-organization of an amount that is due to the Group based on terms that the group would not have considered in other cases, negative changes in the status of the payments of borrowers, changes in the economic environment which attest to insolvency of debt issuers or the absence of an active market for a security.

In the testing for impairment in the value of available for sale financial assets, which are capital instruments, the Group also tests the degree of the difference between the fair value of the asset and its original cost, whilst relating to changes in the fair value of the asset, for the length of time in which the fair value of the asset is lower than its original cost and for changes in the technological, economic or legal environment or in the environment in the market in which the company that issued the instruments operates. In general, an impairment in value of 30% of the original cost will be considered to be material, where the impairment is over the face of a year. This policy was determined in according to the nature of two of the company's most significant investments, See Note 12(a)(1)-(2).

The Group examines evidence of impairment in value in respect of receivables both at the level of the individual asset and also on a Group-wide level. The balances of trade receivables, loans and other receivables that are significant individually are tested specifically for impairment in value. The balances of trade receivables, loans and other receivables, in respect of which no specific impairment in value has been identified, are grouped together and are tested on a Group-wide basis for impairment in value, with the objective of identifying any impairment in value that has occurred and has not yet been identified. In respect of the trade receivables, loans and other receivables that are not individually significant, the Group-wide testing for impairment in value is carried out by grouping them together on the basis of similar risk characteristics.

In the Group-wide testing for impairment in value the Group makes use of historical trends of the probability of a breach, the timing of the receipt of the repayment and the total actual loss, in accordance with management's judgment in respect of the question of whether the actual losses are expected to be larger or smaller by comparison with the losses that arise from the historical trends, in the light of the economic situation and the existing credit terms.

A loss from the impairment in the value of a financial asset, which is measured at amortized cost, is calculated as the difference between the carrying value of the asset in the accounting records and the present value of the estimated future cash flows, discounted at the asset's original effective interest rate. Losses are carried to the income statement and are presented as a provision for a loss against the balances of the trade receivables, the other receivables and the loans. Interest income in respect of assets whose value has been impaired is recognized by means of the use of the interest rate used to discount the future cash flows for the purposes of measuring the loss from impairment in value.

Losses from impairment in value in respect of available for sale financial assets, are recognized by transferring the cumulative loss that has been reflected in a capital reserve in respect of available for sale assets to the income statement. The cumulative loss that is classified from other comprehensive income to the income statement is the difference between the acquisition cost and the current fair value less impairments in value that were recognized in the past through the income statement.

A loss from impairment in value is cancelled where it can be objectively attributed to an event that has occurred after the recognition of the loss from the impairment in value. The cancellation of a loss from impairment in value in respect of financial assets, which are measured at depreciated cost, is carried to the income statement. The cancellation of a loss from impairment in value in respect of financial assets that are classified as available for sale, which are capital instruments, is reflected directly under other comprehensive income.

Note 2 Principal accounting policies (contd.)

W. Impairment of non-financial assets:

At the end of each reporting period, the Group tests the carrying value in the accounting records of its non-financial assets, except for inventory, investment property and deferred tax assets with the objective of determining whether any signs whatsoever exist, which evidence an impairment in the value of those assets. In the event that signs exist, as aforesaid, an estimate is made of the recoverable amount of the asset, with the objective of determining the amount of the loss from impairment in value that has arisen, if any. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash generating unit to which the asset belongs. Common assets are also allocated to the individual cash generating units in the event that it is possible to identify a reasonable and consistent basis for such an allocation.. In the event that it is not possible to allocate the common assets to the individual cash generating units on the said basis, the common assets are allocated to the smallest cash generating units in respect of which it is possible to identify a reasonable and consistent basis for the allocation.

The recoverable amount is the higher of the fair value of an asset less selling costs and its value in use. In the evaluation of the value in use, estimated future cash flows are discounted to their present value, using a pre-tax discount rate, which reflects the market's present evaluation in respect of the time value of the money, and the specific risks that relate to the asset, in respect of which the estimated future cash flows have not been adjusted.

Where the recoverable amount of an asset (or of a cash generating unit) is estimated to be lower that the carrying value, the carrying value of the asset (or of the cash generating unit) is written down to its recoverable amount. A loss from impairment in value is recognized immediately as an expense in the income statement, unless the relevant asset is measured in accordance with the revaluation model. In that case, the loss from impairment in value is treated as a reduction of the revaluation reserve, until it is reduced to zero, and the balance of the reduction, if there is one, is recognized in the income statement.

Where a loss from impairment that has been recognized in previous periods is cancelled, the carrying value of the asset (or of the cash generating unit) is increased back to the updated estimated recoverable amount, but not more than the carrying value of the asset (or of the cash generating unit) that would have been set if it were not for the recognition of a loss from impairment in value in respect of its in previous periods. The cancellation of a loss from impairment in value is recognized immediately in the income statement, unless the relevant asset is asset is measured in accordance with the revaluation model. In that case, the cancellation of the loss from is recognized directly in the income statement up to the amount at which the impairment in value that was recognized in the income statement in previous periods is cancelled, and the balance of the increase, if there is one, is reflected under the other comprehensive income.

X. Impairment of Investments in Associates and in Entities under Common Control Treated under the Equity Method

An investment in an associate or in an entity under common control is examined for impairment when there is objective evidence which indicates impairment (as specified in Section V above).

Goodwill which constitutes a part of the account of the investment in the associate is not recognized as a separate asset and therefore is not examined separately for impairment.

In the event that there is objective evidence which indicates that the value of the investment may have been impaired, the Group performs an estimate of the recoverable amount of the investment which is the higher of the usage value and the net sale price thereof.

Upon determining the usage value of an investment in an associate, the Group estimates its share in the present value of the estimated future cash flows which are projected to be generated by the associated company, including the cash flows from the associated company's operations and the proceeds from the ultimate liquidation of the investment, or the present value of the estimated future cash flows which are projected to derive from dividends to be received and from the ultimate liquidation.

Loss from impairment is recognized when the book value of the investment, after application of the equity method, exceeds the recoverable amount and is carried to the income statement.

Loss from impairment is not allocated to any asset, including to goodwill which constitutes part of the account of the investment in an associate or in an entity under common control.

Note 2 Principal accounting policies (contd.)

Loss from impairment is recovered if and only if changes shall have occurred in estimates which were used in the determination of the recoverable amount of the investment from the date on which the loss from impairment was last recognized. The book value of the investment, after recovery of the loss from impairment, will not exceed the book value of the investment which would have been determined according to the equity method, had the loss from impairment not been recognized.

Y. Employee benefits:

(1) Post-employment benefits

The Group maintains a number of post-employment benefit plans. The plans are generally financed by the making of deposits in insurance companies or central severance pay funds and they are classified as defined deposit plans and also as defined benefit plans.

Defined deposit plans

A defined deposit plan is a post-termination plan whereby the Group makes fixed payments to a separate entity without having a legal or implied obligation to make additional payments. The Group's commitment to make deposits in a defined deposit plan is recognized as an expense in the income statement during the periods in which the employees provided related services.

Defined benefit plans

A defined benefit plan is a post-employment benefit plan which is not a defined deposit plan.The Group's net commitment, which relates to a defined benefits plan in respect of post-employment benefits, is calculated separately for each plan by means of an estimate of the future amount of the benefit that will be due to an employee in consideration for their services, in the current period and in previous periods. This benefit is presented in accordance with the present value less the fair value of the plan assets. The discount rate is determined in accordance with the yield on government bonds, whose currency and repayment terms are similar to the terms of the Group's commitment. The calculations are prepared by a qualified actuary in accordance with the unit of contractual entitlement method.

Where, in accordance with the results of the calculation, a net asset is created for the Group, an asset is recognized up to the net amount of the present value of the economic benefits, which are available by way of a refund from the plan or by the reduction of future deposits in the plan. An economic benefit in the form of refunds or the reduction of future deposits will be calculated as available where it can be exercised within the course of the lifetime of the plan or after the commitment is cleared.

The Group immediately reflects all of the actuarial gains and losses, which derive from a defined benefit plan, through the statement of other comprehensive income.

Interest costs and projected yield on the plan assets that were carried to profit and loss are presented net in the payroll expense items.

Note 2 Principal accounting policies (contd.)

Y. Employee benefits (contd.)

(2) Other long-term benefits to employees

The Group's net commitment in respect of long-term benefits to employees, which do not relate to post-employment plans, is in respect of the future benefits that are due to employees in respect of services that have been provided in the current period and in previous periods. The amount of these benefits is discounted to their present value and the fair values of the assets that relate to this commitment are deducted from it. The discount rate for the commitment is determined in accordance with the comparison at the reporting date of government bonds whose currency and repayment terms are similar to the terms of the Group's commitment. The calculation is carried out using the unit of forecast entitlement method. Actuarial gains and losses are reflected directly in the income statement in the period in which they are created.

(3) Benefits in respect of termination of employment

Benefits in respect of termination of employment are recognized as an expense where the Group has clearly undertaken, without a real possibility of cancellation, to dismiss employees before they reach the customary retirement age in accordance with a formal, detailed program or to provide benefits in respect of termination as the result of an offer that has been made to encourage voluntary termination of employment. The benefits that are extended to employees on voluntary termination of employment are reflected as an expense where the Group has made a proposal to employees of a program that encourages voluntary termination, it is expected that the proposal will be accepted and it is possible to make a reliable estimate of the number of employees who will respond to the proposal.

If the benefits are to be paid more than 12 months after the end of the reporting period, there are discounted to their present value. The discount rate is determined in accordance with the yield on government bonds whose currency and repayment terms are similar to the terms of the Group's commitment.

(4) Short-term benefits

Commitments in respect of short-term benefits to employees include the Group's liability in respect of holiday pay, recuperation pay, bonuses and salaries. These benefits are measured on a non-discounted basis, and the expense is reflected at the time that the relevant service is provided, or in the event of non-accrued absences (such as maternity leave), at the actual time of the absences.

A provision in respect of short-term benefits to employees in respect of a cash bonus or a profit participation scheme, is recognized in the amount that is expected to be paid where the Group has a current legal or implicit commitment to pay the said amount in respect of service that has been provided by the employee in the past and the amount of the commitment can be reliably estimated.

Classification of employee benefits as short-time benefits or as other long-term employee benefits is performed in accordance with the date on which the liability is due to be settled.

(5) Share based payments paid in cash

In share based payment transactions which are paid in cash (phantom shares for officers and employees) the Group measures the goods or services purchased and the liability incurred due to share based payments paid in cash, according to the fair value of the liability. Until the repayment of the liability, the Group revaluates the fair value of the liability on every report date and on the repayment date, while any changes in the fair value are recognized in the income statement for the period.

Note 2 Principal accounting policies (contd.)

Z. Provisions:

A provision is recognized where the Group has a current commitment, whether legal or implicit, as the result of an event that has taken place in the past, which can be reliably measured, and where it is expected that economic resources will be required in order to clear the commitment. The provisions are determined by discounting the future cash flows at a pre-tax interest rate, which reflects the market's current evaluations of the time value of money and the risks that are specific to the commitment. The carrying value of the provision in the accounting records is adjusted in each period in order to reflect the passage of time and is recognized in a financing expense.

(1) Provision for warranties

A provision for warranty is recognized where the products or the service, in respect of which a warranty is provided, are sold. The provision is based on historical data, as well as on management's evaluations, and taking into account all of the possible results and their probabilities.

(2) Legal claims

A provision for claims is recognized where the Group has a present legal commitment or an implicit commitment as the result of an event that has taken place in the past, it being more likely than not that the Group will be required to use economic resources to settle the commitment and it may be reliably estimated. Where the impact of the time value is material, the provision is measured in accordance with its present value.

AA. Revenues:

(1) The sale of products

Income from the sale of products in the ordinary course of business is measured at the fair value of the consideration that is received or which is to be received, less returns, commercial discounts and quantity discounts. In cases in which the credit period is short and reflects the credit that is customary in the sector, the future consideration is not discounted.

The Group recognizes income where there is convincing evidence (usually performance of a sale agreement) that the significant risks and benefits of the ownership of the product are transferred to the purchaser, the receipt of the consideration is expected, the possibility exists of reliably estimating the possibility that the goods will be returned, the costs that have been incurred, or which will be incurred in respect of the transaction may be reliably estimated, where the management has no continuing involvement with the goods, and also where the income can be reliably estimated. If it is expected that a discount will be provided and its amount can be reliably measured, the discount is deducted from the revenues from the sale of the products.

The timing of the transfer of the risks and the yields varies in accordance with the specific terms of the sales contract. In respect of the sale of products in Israel, the transfer of the risks and the yields generally takes place when the products reach the customer's warehouse, however for certain international shipments transfer occurs when the goods are loaded on the transporter's means of transportation.

(2) Construction contracts

Income and expenses from construction contracts are carried to the income statement, on a pro rata basis based on the percentage of the completion of the contract, where it is possible to reliably estimate its results. Income from construction contracts includes the original amount that was included in the contract with the addition of amounts in respect of changes in the work, claims and incentives, in the event that income is expected and that it is possible to measure it in a reliable manner.

The evaluation of the percentage completion is based on the review of the works that have been performed. Where it is not possible to reliable evaluate the results of the construction contract, income is recognized from the contract only up to the level of the costs that it is reasonable to assume that will be recovered. A forecast loss on a construction contract is recognized immediately in the income statement.

Note 2 Principal accounting policies (contd.)

AA. Revenues:

(3) Rental income

Rental income in respect of investment property is recognized on the straight line basis over the length of the relevant rental period.

(4) Services

Income from services provided is carried to profit and loss proportionately to the stage of completion of the transaction on the date of the report. An estimate of the completion stage is calculated in reference to a review of the work performed.

(5) Income from management and maintenance fees and net income from the use of electricity

Income from management and maintenance fees and net income from the use of electricity is reflected pro-rata over the length of the period in which the relevant services are provided.

(6) Dividend income

Dividend income in respect of investments is recognized at the time at which the shareholders' entitlement to receive the income is created.

AB. Government grants:

Unconditional Government grants are initially recognized at fair value, where there is a reasonable degree of confidence that they will be received and that the Group will meet the conditions that entitle it to receive them. Grants that are received as compensation for expenses that the Group has borne are presented as a deduction from the relevant expense. Government grants that are received for the purpose of the purchase of an asset are presented as a deduction from the relevant asset and are carried to the income statement on a systematic basis, over the length of the useful lifetime of the asset.

Grants from the Chief Scientist in respect of R&D projects are treated as forgivable loans in accordance with IAS 20. Chief Scientist grants that have been received are recognized as a liability according to its fair value on the date of receipt of the grants, unless on such date it is reasonably certain that the amount received will not be returned. The sum of the liability is reexamined in each period and the changes, if any, in the present value of the cash flows that are discounted at the original interest of the grant, are carried to the income statement. The difference between the consideration and the fair value of the liability on the date of receipt of the grant is recognized in reduction of cost of sale.

AC. Discounts from suppliers:

Discounts that are received from suppliers in respect of which the Company is not committed to meet certain targets are recorded in the financial statements as they occur, on the execution of the purchases to which they relate, which entitle the Company to the said discounts.

Discounts from suppliers, where the right to receive them is conditional upon the Company's meeting certain targets, such as compliance with a minimal annual volume of purchases (quantitative or in financial terms), an increase in the volume of purchases by comparison with previous periods and so on, are recorded in the financial statements *pari passu*, in accordance with the volume of purchases that has been made from the suppliers by the Company in the reporting period, which progress the Company towards the meeting of the targets, and this where it is expected that the targets will be achieved and it is possible to make a reasonable estimate of the amount of the discounts. The estimate in respect of the compliance with targets is based, inter alia, on past experience and the Company's relationship with the suppliers, as well as the volume of purchases that will be made in the rest of the period, as forecasted.

Note 2 Principal accounting policies (contd.)

AD. Payment of lease fees:

Payments under an operating lease are carried to the income statement under the straight line method, over the length of the period of the lease.

Minimal leasing payments, which are paid within the framework of finance leasing, are divided between the financing expense and the reduction of the balance of the liability. The financing expenses are allocated to each of the periods covered by the lease, such that a fixed periodic interest rate is receive, for the remaining balance of the liability.

Minimal leasing payments, in respect of conditional leasing charges are updated when the conditional amount is clarified.

AE. Transactions with and loan to a related party:

Assets and liabilities (including loans), in respect of which a transaction has been performed with a controlling interest, are measured in accordance with their fair value at the time of the transaction. As a result of the fact that these are transactions on the capital plain, the Company reflects the difference between the fair value and the consideration from the transaction under shareholders' equity.

AF. Non-current assets and disposal groups that are held for sale:

Non-current assets (or disposal groups that are comprised of assets and liabilities) where it is expected that the assets will be disposed of by way of a sale and not by way of disposal at a later stage, are classified as assets that are held for sale. The same is true when the company is obligated to plan a sale which involves losing control of a subsidiary, irrespective of whether the company shall retain non-controlling interests in the former subsidiary after the sale. Immediately before the classification as held for sale, the assets (or disposal groups that are designated for removal) are measured in accordance with the Group's accounting policy. Thereafter, the assets (or the components of the groups that are designated for removal|) are measured at the lower of the carrying value in the accounting records and fair value, less selling costs. In following periods, depreciable assets that are classified as held for sale are not periodically depreciated. Any loss from impairment in value of a group that is designated for removal is allocated firstly to goodwill and thereafter it is allocated proportionately to the remaining assets and liabilities, except that no loss is allocated to assets which are not included in the measurement provisions of IFRS 5 such as: inventory, financial assets, deferred tax assets, assets relating to an employee benefit plan and investment property that is measured at fair value, which continue to be measured in accordance with the Group's accounting policies. Losses from impairment in value at the time of the initial classification of an asset as held for sale, as well as profits or losses at a later stage, as the result of re-measurement, are carried to the income statement. Gains are recognized up to the cumulative amount of the loss from impairment in value that was recorded in the past.

AG. Franchise arrangements for provision of services:

Franchise arrangements for provision of services are arrangement in which the State (the franchise issuer) engages in a contract with an entity from the private sector in which such operator undertakes to plan, build and finance some property or infrastructure for service to the public and in consideration for construction of such property, the operator receives a franchise from the state to operate the property for a defined period, and also to provide other services related to the property.

Granite as an operator, through the consolidated company Via Maris, engaged in a franchise arrangement for provision of BOO (Build, Own Operate) services with the State for construction, building and operation of a water desalination facility. Since the state controls and regulates the services which the operator is required to provide through the infrastructure, the persons to whom he is required to provide them and the price in which they shall be provided, and since the franchise arrangement with the state constitutes in essence an arrangement for the whole useful lifetime of the facility, considering that the discard value of the infrastructure at the end of the arrangement period is not significant, the Group treats the said arrangement in accordance with interpretation provision number 12 (IFRIC 12).

Note 2 Principal accounting policies (contd.)

AG. Franchise arrangements for provision of services:

The said arrangement for the construction of a facility for desalination of water is treated as a combined model, which includes both a financial asset and an intangible asset. The arrangement term is divided into two periods: the construction period and the operation period which began upon the completion of construction of the infrastructure. The Group's rights pertaining to the franchise are recognized as a financial asset, receivables in respect of a franchise arrangement for water desalination, which is treated under the application of IAS 39 as loans and receivables, since the Group has an unconditional right to receive from the entity granting the franchise secured proceeds in consideration for the construction and operation services. The asset is recognized in the construction period in respect of the construction costs, with the addition of the accepted contractual margin according to the Group's estimation, and is repaid through the proceeds during the operation period. After the initial recognition, interest income is recognized along the arrangement period according to the effective interest method. Since only some of the proceeds are secured by a payment undertaking by the franchise issuer, the franchise is recognized as a financial asset, receivables in respect of a franchise arrangement for water desalination, up to the level of the secured amount, and the balance is recognized as an intangible asset.

AH. Taxes on income:

(1) General

Tax expenses (benefit) on income include the sum of the current taxation as well as the change in the deferred taxation balances, except in respect of deferred taxes that derive from transactions that are reflected directly under shareholders' equity.

(2) Current taxation

The current taxation on income expenses is calculated based on the Company and the consolidated companies' chargeable income for tax purposes, during the course of the reporting period. The chargeable income is different from the income before taxes on income, as the result of the inclusion or the non-inclusion of income and expense items that are chargeable to taxation or which are allowable as a deduction in different reporting periods, or which are not chargeable to tax or allowable as a deduction. Assets and liabilities in respect of current taxation have been calculated on the basis of the tax rates and the tax laws that have been legislated or whose legislation has been effectively completed as of the date of the Statement of the Financial Position.

(3) Deferred taxation

The companies in the Group record deferred taxation in respect of timing differences between the values of assets and liabilities for tax purposes and their values in the financial statements. Deferred tax balances (assets or liabilities) are calculated in accordance with the tax rates that are expected to apply at the time that they are realized, based on the tax rates and the tax laws that have been legislated or whose legislation has been effectively completed as of the date of the Statement of the Financial Position. Deferred taxation liabilities are generally recognized in respect of all of the timing differences between the value of assets and liabilities for tax purposes and their values in the financial statements. Deferred tax assets are recognized in respect of timing differences that can be deducted up to the amount of the chargeable income against which it is expected that the deductible timing differences can be exploited.

The taxes that would apply in the event of the disposal of the investments in associates are not taken into account in the calculation of the deferred taxes, since it is the Group's intent to hold those investments and to develop them. The Group may be liable for a tax increment in the event of the distribution of dividends by the Group companies. Such tax increment was not included in the financial statements, while the policy of the Group companies is not to cause the distribution of a dividend which involves a tax increment for the recipient company in the foreseeable future.

Deferred tax assets and liabilities are presented after having been set-off, where the entity has an enforceable legal right to set off current tax assets against current tax liabilities, and where they relate to taxes on income that are levied by the same tax authority and where the Group intends to clear the current tax assets and liabilities on a net basis.

Note 2 Principal accounting policies (contd.)

AI. Share based payments:

Share based payments to employees and to others, who provide similar services, which are cleared using the Company's capital instruments are measured at fair value at the time of the grant. The Company measures the fair value of the capital instruments at the time of the grant using the Black-Scholes Model. Where the capital instruments that are granted do not vest until the employees complete a defined period of service, meet performance related terms or if a defined condition exists in the market, the Company recognizes the share based payment in the financial statements over the length of the vesting period, against an increase in capital, under the item "capital reserve on share based payments". At every balance sheet date the Company estimates the number of capital instruments that are expected to vest. A change in the estimate in relation to previous periods is recognized in the income statement over the balance of the vesting period.

AJ. Other income:

Income from dividends and gains from the sale of financial assets that are classified as available for sale are included under other income.

AK. Financing income and expenses:

Financing income includes interest income in respect of amounts that have been invested (including financial assets that are available for sale and financial assets from franchise agreements), changes in the fair value of financial assets that are presented at fair value through profit and loss, profits from exchange differences and profits from hedging instruments that are recognized in the income statement. Financing income is recognized as it arises, by means of the effective interest method.

Income from dividends in respect of marketable shares is recognized as income on the ex date. Changes in the fair value of financial assets that are presented at fair value through profit and loss also includes income from dividends and interest.

Financing expenses include interest expenses on loans that have been received, bonds that have been issued, changes in respect of the value of time in respect of provisions, changes in the fair value of financial assets that are presented at fair value through profit and loss, losses from the impairment in value of financial assets except for trade receivables (which are presented in the framework of the G&A expenses item), other receivables and hedging instruments that are recognized in the income statement. The credit costs, which are not capitalized, are carried to the income statement in accordance with the effective interest method.

Gains and losses from rate differences are reported net, as financing revenues or financing expenses, depending on exchange rate fluctuations and depending on their position (net profit or loss).

AL. Segments:

An operating segment is a component of the Group that meets the following three conditions:

(1) The engagement in business activities from which income is likely to be generated and in respect of which expenses are likely to be incurred, including income and expenses that relate to transactions between companies in the Group;

(2) The results of the operations are reviewed as a matter of routine by the Group's chief operational decision maker, in order to make decisions in respect of the resources that will be allocated to it and in order to evaluate its performance; and also

(3) Separate, readily available financial information exists in respect of it.

See Note 41 for further information on the Group's operating segments.

AM. Earnings per share:

The Company calculates the amounts of the basic earnings per share in respect of the profit or loss that is attributed to the shareholders in the Company by dividing the profit or loss that is attributed to the shareholders in the Company by the weighted average number of ordinary shares in circulation during the course of the reporting period. For the purposes of the calculation of the diluted earnings per share, the Company adjusts the profit or loss that is attributed to the regular shareholders and the weighted average number of ordinary shares in circulation in respect of the impact of all of the potential dilutionary shares.

Note 2 Principal accounting policies (contd.)

AN. Exchange rates and linkage base:

(1) Balances that are stated in foreign currency or which are linked thereto are recorded in the financial statements in accordance with the representative exchange rates that were published by the Bank of Israel and which were in force as of the date of the statement of the financial position.

(2) Balances that are linked to the Consumer Prices Index are presented in accordance with the last known index as of the date of the statement of financial position (the index for the month preceding the date of the financial statements), or in accordance with the index in respect of the last month of the reporting period (the index for the month in which the date of the financial statements lies), in accordance with the terms of the transaction.

(3) The following are details in respect of the exchange rates and Index:

	Representative exchange rate of			The Index in Israel	
	Euro	Canadian Dollar	US Dollar	Index for	Known index
	NIS to 1 Euro	NIS to 1 Dollar	NIS to 1 Dollar	Basis 1993	Basis 1993
The date of the financial statements:					
December 31, 2011	4.938	3.7395	3.821	216.27	216.27
December 31, 2010	4.738	3.555	3.549	211.67	210.89
December 31, 2009	5.442	3.603	3.775	206.19	206.19
	%	%	%	%	%
Change in the year ended on:					
December 31, 2011	4.23	5.19	7.66	2.17	2.55
December 31, 2010	(12.94)	(1.33)	(5.99)	2.66	2.28
December 31, 2009	2.73	15.74	(0.71)	3.91	3.82

AO. Effective amendments of standards which are applied in these financial statements:

(1) IAS 24 (Amended) "Related Party Disclosures"

The new standard reduces the disclosure requirements of a government-related entity, a government authority or similar entity, in respect of transactions made with entities related to that government, government authority or similar entity. The standard further revises the definition of related party. The standard is applied retrospectively. The application of the standard has had no material effect on the financial statements.

(2) Amendment of IAS 1 (Amended) "Presentation of Financial Statements" (regarding the presentation of other comprehensive income items in the statement of changes in equity)"

The amendment provides that the other comprehensive income items be presented in the Statement of Changes in Equity or in the Notes, according to the company's accounting policy. The standard is applied retrospectively. The Company does not present the comprehensive income items in the Statement of Changes in Equity. The application of the amendment has had no effect on the financial statements.

(3) Amendment of IFRS 7 "Financial Instruments: Disclosures" (nature and extent of risks arising from financial instruments)

The amendment encourages the making of qualitative disclosures in connection with quantitative disclosure, which is required to help statement readers in forming an overall picture of the nature and extent of risks arising from financial instruments.

Note 2 Principal accounting policies (contd.)

AO. Effective amendments of standards which are applied in these financial statements: (contd.)

(3) Amendment of IFRS 7 "Financial Instruments: Disclosures" (nature and extent of risks arising from financial instruments) (contd.)

The amendment further clarifies the level of disclosure required with respect to credit risk and collateral held, and further grants disclosure relief in connection with loans whose terms have been re-discussed. The amendment is applied retrospectively for annual reporting periods commencing on or after January 1, 2011.

The required disclosures have been expressed in the financial statements. For further information see Note 39 on Financial Instruments.

AP. New Standards, Amendments to Standards and Interpretations Not Yet Adopted:

- **Amendment of IAS 12 "Income Taxes"**

  The amendment introduces a presumption that the carrying amount of investment properties measured at fair value in accordance with the provisions of IAS 40, will be recovered through sale. Accordingly, deferred taxes will be calculated according to the tax rates and bases applicable at the time of sale of the property. The said presumption is rebuttable if the investment property is depreciable and is held within a business model whose objective is to consume substantially all the investment property's economic benefits over time, through use rather than through sale. The amendment is applied retrospectively in respect of annual reporting periods commencing on or after January 1, 2012. Early application is possible.

  The application of the amendment is not expected to have a material effect on the financial statements.

- **Amendment of IAS 32 "Financial Instruments: Presentation" (offsetting financial assets and financial liabilities)**

  The amendment determines that in order to meet the conditions for offsetting a financial asset and a financial liability, the set-off right cannot be contingent on a future event and must be enforceable in the ordinary course of business, in the event of bankruptcy, insolvency or credit default. The amendment further determines that some gross settlement systems would be considered equivalent to net settlement if they eliminate or result in insignificant credit and liquidity risk and process receivables and payables in a single settlement process. The amendment is applied retrospectively in respect of annual reporting periods commencing on or after January 1, 2014. Early adoption is possible.

  At this time, the Company's management is unable to assess the effect of the amendment on its financial position and results of operations.

- **IFRS 7 "Financial Instruments: Disclosures" (offsetting financial assets and financial liabilities)**

  In the context of the amendment to IAS 32 "Financial Instruments: Presentation" added disclosure requirements regarding the effect of financial asset and financial liability offsetting agreements on an entity's financial position.

  The amendment is applied retrospectively in respect of annual reporting periods commencing on or after January 1, 2013. Early adoption is possible.

Note 2 Principal accounting policies (contd.)

AP. New Standards, Amendments to Standards and Interpretations Not Yet Adopted: (contd.)

- **IFRS 7 "Financial Instruments: Disclosures" (Disclosures – Transfer of Financial Assets)**

  The amendment sets forth disclosure requirements regarding the entity's exposure to risks in respect of transactions for the transfer of financial assets, in the context of which the transferor retains a certain level of ongoing exposure to the asset ("continued involvement"), and with respect to transactions for the transfer of financial assets which were fully written-off, which were performed shortly before the end of the reporting period.

  The provisions of the amendment are applicable from the annual periods commencing on January 1, 2012; early application is possible. The new disclosures are not required in respect of reporting periods preceding the date of first application of the provisions of the amendment.

- **IFRS 9 "Financial Instruments"**

  The standard sets forth the instructions for classification and measurement of financial instruments. The standard determines that all financial assets be treated as follows:

  - Debt instruments will be classified and measured after initial recognition at depreciated cost or at fair value through profit and loss. The measurement model will be determined in consideration of the entity's business model regarding financial asset management and according to the characteristics of the contractual cash flow deriving from such financial assets.

  - A debt instrument which, according to the tests, is measured at depreciated cost, may be designated for fair value through profit and loss, only if such designation counters an inconsistency in the recognition and measurement, which would have arisen had the asset been measured at depreciated cost.

  - Capital instruments will be measured at fair value through profit and loss.

  - On the date of initial recognition, capital instruments may be designated for fair value, with profits or losses carried to other comprehensive income. Instruments so designated will no longer be subject to impairment review, and profit or loss thereon will not be carried to the income statement, including upon disposition.

  - Embedded derivatives will not be separated from a host contract falling within the standard's applicability. Instead, hybrid contracts will be measured on the whole at depreciated cost or at fair value, according to the business model tests and the contractual cash flow.

  - Debt instruments will be reclassified from depreciated cost to fair value and vice versa, only when the entity changes its business model for financial asset management.

  - Investments in capital instruments having no quoted price in an active market, including derivatives from such instruments, will always be measured at fair value. The alternative of measurement at cost in certain circumstances has been eliminated. However, the standard states that in specific circumstances, cost may be an appropriate approximation of fair value.

  The standard also sets forth the following provisions regarding financial liabilities:

  - The change in the fair value of a financial liability, which is designated at the time of initial recognition as fair value through profit and loss, which is attributed to changes in the credit risk of the liability, will be carried directly to other comprehensive income, unless an accounting mismatch is thereby created or enlarged.

Note 2 Principal accounting policies (contd.)

AP. New Standards, Amendments to Standards and Interpretations Not Yet Adopted: (contd.)

- When the financial liability is paid or settled, amounts carried to other comprehensive income will not be classified to profit and loss.

- All derivatives, whether assets or liabilities, will be measured at fair value, including a derivative financial instrument which is a liability related to an unquoted capital instrument, whose fair value cannot be reliably measured.

The provisions of the standard apply to annual reporting periods commencing on or after January 1, 2015. Early application is possible. Furthermore, subject to the standard's transitional provisions, early adoption of the standard's provisions regarding financial assets only is possible, without adopting the aforesaid provisions regarding financial liabilities.

The provisions of the standard may be initially applied either prospectively or retrospectively, at the entity's election. Entities applying the standard for the first time in 2012, which have elected not to restate the comparative figures, are required to include certain disclosure requirements as specified in IFRS 7. Entities applying the standard for the first time on or after January 1, 2013 are not required to restate comparative figures, but are required to include certain disclosure requirements as specified in IFRS 7.

At this stage, the Group's management is unable to assess the effect of application of the standard on its financial position and results of operations.

- **IFRS 10 "Consolidated Financial Statements"**

The standard sets forth the following provisions regarding consolidated financial statements:

- Control by one entity of another will be determined based on a uniform model, irrespective of the other entity's being a "special purpose entity". In this context, SIC Interpretation 12, "Consolidation – Special Purpose Entities" has been eliminated.

- An investor has control of another entity (the "Investee Entity") when the investor holds power in reference to the Investee Entity, has exposure to changing yields from its involvement in the Investee Entity and is able to exercise its power to affect the amount of the yield.

- The standard sets forth instructions for examining the existence of "de facto control", where an entity holds less than one half of the voting rights in another entity. For this purpose an examination is made, *inter alia*, of the investor's holdings rate in the Investee Entity, and the extent and dispersion of public holdings.

- Potential voting rights in the Investee Entity are taken into account to determine the existence of control, where the terms thereof provide substantial ability to direct the entity's relevant activities in the present.

- The standard does not include a change in the procedures for consolidating financial statements.

This standard is applied retrospectively, apart from certain exceptions as specified in the standard, with respect to annual reporting periods commencing on or after January 1, 2013. Early application is possible, provided that application is made concurrently with IFRS 11 "Joint Arrangements", IFRS 12 "Disclosure of Interests in Other Entities" and IAS 28 (2011) "Investments in Associates and Joint Ventures".

At this stage, the Company's management is unable to assess the effect of application of the standard on its financial position and results of operations.

Note 2 Principal accounting policies (contd.)

AP. New Standards, Amendments to Standards and Interpretations Not Yet Adopted: (contd.)

- **IFRS 11 "Joint Arrangements"**

  The standard states that a joint arrangement is an arrangement in which two parties or more hold joint control (as defined in IFRS 10) thereof. The standard further sets forth the following types of joint arrangements, and the accounting treatment thereof:

  - An arrangement under joint control is a joint arrangement between parties holding joint control, which grants them rights to the assets and obligations for the liabilities of the arrangement. An entity holding joint control of an arrangement under joint control, shall recognize its share in the assets, liabilities, revenues and expenses of the arrangement in its consolidated financial statements.

  - A joint venture is a joint arrangement between parties holding joint control of the arrangement, which hold rights to net assets of the venture. An entity holding joint control of a joint venture shall present its investment therein according to the equity method according to IAS 28 (2011) "Investments in Associates and Joint Ventures".

  This standard is applied retrospectively, apart from certain exceptions as specified in the standard, with respect to annual reporting periods commencing on or after January 1, 2013. Early application is possible, provided that application is made concurrently with IFRS 10 "Consolidated Financial Statements", IFRS 12 "Disclosure of Interests in Other Entities" and IAS 28 (2011) "Investments in Associates and Joint Ventures".

  At this time, the Company's management is unable to assess the effect of application of the standard on its financial position and results of operations.

- **IFRS 12 "Disclosure of Interests in Other Entities"**

  The standard sets forth disclosure requirements in reference to an entity's interests in consolidated companies, joint arrangements, associates and non-consolidated structured entities. The purpose of the disclosures is to assist in the evaluation of the nature and related risks in connection with the interests in the said entities and the effect of such interests on the financial statements of the reporting entity. The standard sets forth the following provisions with regard to consolidated financial statements:

  This standard is applied retrospectively with respect to annual reporting periods commencing on or after January 1, 2013. Early application is possible, provided that application is made concurrently with IFRS 10 "Consolidated Financial Statements", IFRS 11 "Joint Arrangements" and IAS 28 (2011) "Investments in Associates and Joint Ventures". However, entities may include any of the new disclosures in their financial statements prior thereto. Control by one entity of another entity will be determined based on a uniform model, irrespective of the other entity's being a "special purpose entity". In this context, SIC Interpretation 12, "Consolidation – Special Purpose Entities" has been eliminated.

- **IAS 28 (2011) "Investments in Associates and Joint Ventures"**

  The standard sets forth the following instructions regarding application of the equity method:

  - The equity method shall be applied to both associates and joint ventures.

  - When an investment in a joint venture is classified as an investment in an associate, or vice versa, no re-measurement of the entity's rights in the investee is performed.

  - Upon a decline in the holding rate in the joint venture or associate, which does not stop the application of the equity method, the investor shall reclassify to profit or loss only a relative part of the amounts previously recognized in other comprehensive income.

Note 2 Principal accounting policies (contd.)

AP. New Standards, Amendments to Standards and Interpretations Not Yet Adopted: (contd.)

- **IAS 28 (2011) "Investments in Associates and Joint Ventures" (contd.)**

  - Part of the investment according to the equity method will be classified as a non-current asset held for sale, if such part meets the conditions for classification as such.

  This standard is applied retrospectively, with respect to annual reporting periods commencing on or after January 1, 2013. Early application is possible, provided that application is made concurrently with IFRS 10 "Consolidated Financial Statements", IFRS 11 "Joint Arrangements" and IFRS 12 "Disclosure of Interests in Other Entities".

  At this time, the Company's management is unable to assess the effect of application of the standard on its financial position and results of operations.

- **IFRS 13 "Fair Value Measurement"**

  The standard replaces the specific fair value provisions in the various international financial reporting standards, providing a single source of guidance on how fair value is measured. Accordingly, instructions on fair value measurement have been set forth for all the items measured at fair value in the statement of financial position or for disclosure purposes.

  The standard defines fair value as the price that would be received to sell an asset or paid to transfer a liability in the ordinary course of business between market participants at the measurement date.

  The standard lists the various methods at which fair value may be measured, and states that use should be made of valuation techniques which make the maximum use of observable market data. The fair value measurement of a non-financial asset is based, according to the standard, on an estimation of its highest and best use.

  The standard is applied prospectively for annual periods commencing on or after January 1, 2013. Early application is possible.

  At this time, the Company's management is unable to assess the effect of application of the standard on its financial position and results of operations.

- **IAS 19 (2011) "Employee Benefits"**

  The standard changes the current provisions of IAS 19 "Employee Benefits", in the following aspects:

  - Actuarial profits or losses are carried to other comprehensive income and not classified later to profit and loss. Accordingly, the alternatives of carrying the actuarial profits or losses to profit and loss immediately, or according to the corridor method, have been eliminated.

  - Interest revenues in respect of assets of a defined benefit plan, are recognized based on the cap rate of the liability and not according to the expected yield on the assets.

  - Short-term employee benefits include benefits that are expected to be settled wholly before 12 months after the end of the year in which the employee renders the entitling service.

  - Termination benefits resulting from an offer encouraging voluntary retirement are recognized as a liability when the reporting entity is unable to withdraw the offer.

  The standard is applied retrospectively, apart from exceptions as specified in the standard, for annual periods commencing on or after January 1, 2013. Early application is possible.

Note 2 Principal accounting policies (contd.)

AP. New Standards, Amendments to Standards and Interpretations Not Yet Adopted: (contd.)

- **IAS 19 (2011) "Employee Benefits" (contd.)**

At this stage, the Company's management is unable to assess the effect of application of the standard on its financial position and results of operations.

- **Amendment of IAS 1 (amended) "Presentation of Financial Statements" (regarding presentation of other comprehensive income items in the statement of compensative income)**

The standard provides that items included in other comprehensive income be separated and presented in one of two groups:

- Items that will be classified in the future to the income statement;
- Items that will not be classified in the future to the income statement.

The standard further provides that if the other comprehensive income items are presented gross of tax, the comprehensive tax effect shall be presented for each group separately. The amendment is applied retrospectively for annual periods commencing on or after January 1, 2013. Early application is possible.

Note 3 Critical estimates and the determination of the fair value

A. General

In the implementation of the Group's accounting policy, which is described in Note 2 above, the managements of the companies in the Group are required to exercise broad accounting judgment in respect of estimates and assumptions, in connection with the carrying values of assets and liabilities, which cannot necessarily be found in other sources. The estimates and the related assumption are based on past experience and on other factors, which are considered to be relevant. The actual results may well be different from those estimates.

The estimates and assumptions that they are based on are reviewed routinely by the management of the companies in the Group. Changes in the accounting estimates are recognized only in the period in which the change is made in the estimates in the event that a change affects only one period or they are recognized in the said period and also in future periods in cases where the change affect both the current period and also the future periods.

B. Critical estimates

The following is information in respect of critical estimates, which have been prepared whilst implementing the accounting policies, and which have a significant impact on the financial statements:

(1) The revaluation of investment property and investment property under construction – in accordance with the IFRS and in accordance with the Company's selection, the Group presents investment property and investment property under construction in accordance with the fair value, based mainly on an evaluation by independent external appraisers, possessing the appropriate professional skills. The fair value is examined at least once a year and at any time at which indications exist that there has been a significant change in value. Even in the case where the indications do not exist, the Company's management may, per its discretion, choose to perform external valuations or review the fair value by itself. In each case where the Company's management decides to update the fair value of all or part of the assets, as the case may be, the BOD report for such quarter shall include the Board's explanations in respect of the valuation that it made itself, as required by law.

Note 3 **Critical estimates and the determination of the fair value (contd.)**

B. Critical estimates (contd.)

It shall be clarified that despite the aforesaid, the Company will not be obligated to commission an external valuation of an asset, which meet all of the following criteria: (1) its value does not exceed 1% of the Company's equity as of the date of the examination; (2) the sum total of the assets meeting definition (1) cumulatively for which no external valuation was commissioned, does not exceed 5% of the total real properties on a consolidated basis, and the Company will be entitled to perform the valuation by itself.

Changes in the fair value are carried to the income statement and accordingly they may have a material effect on the Company's results.

(2) Contingent liabilities – in the evaluation of chances of the legal claims that have been filed against the Company, consolidated companies and its associates, the companies have relied on the opinions of their legal advisers as well as on estimates made by their managements. These evaluations by the legal advisers and the managements are based on their best professional judgment, taking into account the stage at which the proceedings are to be found, and also on the legal experience that has accumulated on various subjects. Since the results of the claims will be determined in the courts, those results may be different from those evaluations.

(3) Provision for doubtful debts – the financial statements include provisions for doubtful debts, which, in the opinion of the managements of the companies in the Group, provide a fair reflection of the loss that is inherent in the debts whose collection lies in doubt. The provision for doubtful debts includes specific provisions and general provisions in accordance with IAS 39. In the determination of the fairness of the provisions, the managements have based themselves, inter alia, on information that is in its hands in respect of the financial position of the debtors, the extent of their activities, an assessment of the collateral received from them, a receivables aging analysis, history of bad debts, financial strength and a business analysis of the customer and industry trends. Actual collection of the debts may be different to the estimates of the managements of the Group companies.

(4) Impairment in the value of assets – at each balance sheet date the Group tests if events have occurred or if changes have taken place in the circumstances that indicate that an impairment has occurred in the value of one or more of the non-monetary assets. If signs of impairment in value exist, a test is conducted as to whether the amount at which the investment in the asset is presented can be recovered out of the discounted cash flows that are expected from that asset, and in the event that it is necessary, a provision for impairment in value is recorded up to the level of the amount that is recoverable. The discounting of the cash flows is calculated in accordance with a post-tax discount rate, which reflects the market's estimate in respect of the time value of the money and the specific risks that relate to that asset. The determination of the estimates of the cash flows is based on past experience with the asset or similar assets, and on the Company's best estimate in respect of the economic conditions that will be extant during the course of the balance of the useful life of the asset. In the determination of the net selling price of some of the assets use was made of evaluations by a valuator.

In respect of realty assets, the estimates also take into account the state of the market in the area in which the asset is located.

Changes in the Group's estimates, as aforesaid, may lead to significant changes in the carrying value of the assets and in the operating results.

(5) The fair value of derivatives, financial assets for sale and other financial instruments – the fair value of financial instruments that are not traded on an active market (for example: call options, put options, and investments in non-marketable instruments) is determined using evaluation techniques. The Group exercises judgment in the determination of the appropriate methodology and in the determination of the assumptions, based on generally accepted practice and the current conditions in the market and also based on calculations of fair value performed by appropriate independent external appraisers. Changes in the assumptions may lead to the recognition of impairment in value or losses in future periods.

Note 3 **Critical estimates and the determination of the fair value (contd.)**

B. Critical estimates (contd.)

(6) Employee benefits – the present value of post-employment employee benefits is dependent on various factors that are determined on an actuarial basis, using assumptions. The assumptions that are used in the determination of the net expense (income) in respect of these benefits include the cap rate, the future salary increase rate and pension allowance increase rate. Any change in these assumptions affects the carrying value of the liabilities in respect of the employee benefits in the accounting records.

(7) Deferred taxes – the Group companies are carrying out the attribution of taxes in respect of timing differences. Timing differences are differences between the value of tax purposes of assets and liabilities, and the value at which they are recorded in the accounting records, as well as losses and deductions that are available to be carried forward for tax purposes. Deferred tax balances (assets or liabilities) are calculated in accordance with the tax rates that will apply at the time that the deferred taxes are exploited, in accordance with the Group's forecasts, or when the tax benefit is exercised, based on the tax rates and the tax laws that have been enacted or whose enactment has been effectively completed as of the date of the statement of financial position. The amounts of the tax benefits that have been included in the financial statements accord with the Group's forecasts and its business plans, which forecast that their realization is expected. The actual results may be different from the expectations, something that will affect the realization of the tax benefits in the future and their timing.

(8) Taxes on income - the Group is subject to the tax laws. Broad judgment is required in order to determine the current tax liability for each of the companies in the Group.

The Group has many transactions, whose tax results are uncertain. The Group recognized liabilities in respect of the tax results of those transactions, based on management's estimates, which place reliance on professional advisors, in respect of the timing and the level of the tax liability that derives from those transactions. Where the tax results of those transactions is different from management's estimates, the tax expenses and the deferred tax liabilities will be reduced or increased at the time that the final assessments are determined.

C. Determination of fair value:

As part of the accounting principles and the disclosure requirements, the Group is required to determine the fair value of non-financial and financial assets and liabilities. The fair values have been determined for the purposes of measurement and/or disclosure on the basis of the methods that are described below. Additional information in respect of the assumptions that have been used in the determination of the fair value is provided in the noted that relate to this asset or liability.

(1) Investment property – As aforesaid in Note 2P, the Group's investment property is presented at fair value, where changes in the fair value are carried to the income statement as income or as expenses.

For the purpose of the determination of the fair value of investment property, the Company's management bases itself, primarily, on evaluations that are performed once a year by independent appraisers of land, having the required knowledge, experience and expertise. The Company's management is in the habit of determining the fair value in accordance with generally accepted evaluation methods of realty assets, primarily discounted cash flows and comparison with selling prices of similar assets and the Group's assets in the near environment. Where use has been made of the discounted cash flows method, the interest rate used in the discounting of the net cash flows that are expected from the asset can have a significant impact on the fair value.

In the determination of the fair value, the Company takes into account, inter alia, and so far as is relevant, the location of the asset and its physical state, the quality of the tenants and their stability, the rental period, the rental prices in similar properties, the adjustments that are required to the existing rental prices, the actual and forecast occupancy levels for the property and the costs of operating it. A change in the value of any of these components, or all of them, could have a significant impact on the fair value of the property as estimated by the Company's management.

Note 3 **Critical estimates and the determination of the fair value (contd.)**

C. Determination of fair value: (contd.)

(1) (contd.)

The Group strives to determine as objective a fair value as possible, but at the same time, the process of estimating the fair value of investment property also includes subjective elements, which are sources, inter alia, in the past experience of the Company's management and its understanding of what is expected to take place in the investment property market at the time at which the estimate of the fair value is determined. In the light of what is stated in the previous paragraph, the determination of the fair value of the Group's investment property mandates the exercise of judgment. Changes in the assumptions that were used in the determination of the fair value could have a significant effect on the Group's state of affairs and the results of its activities.

(2) Impairment in the value of goodwill – in order to determine whether an impairment has taken place in the value of goodwill, the Company's management prepares an estimate of the value in use of the cash generating units to which the goodwill has been allocated, for the purpose of the calculation of the value in use, the Group calculates an estimate of the future cash flows that are expected to derive from each of the cash generating units as well as the appropriate discount rate in order to calculate the present value.

(3) Investments in shares, capital instruments and debt instruments – for the purpose of the calculation of the fair value of financial assets that are measured at fair value through the profit and loss, and financial assets that are classified as available for sale, this is determined whilst relating to their average quoted closing bid prices at the reporting date. In the absence of quoted process, the evaluation is carried out using the discounted cash flows method under "going concern" assumption and/or the net asset value method.

(4) The conversion element of bonds of a consolidated company - the fair value of the conversion element of the bonds of a consolidated company is measured using the Black-Scholes Model. The assumptions used in the model include the price of the share on reporting date, the weighted average of the expected lifetime of the instruments, expected dividends, the standard deviation of the share price and the risk free interest rate (on the basis of government bonds).

(5) Derivatives – the fair value of derivative financial instruments is calculated using quoted prices, if any. In the absence of such quoted prices, an estimate is made of the fair value of forward contracts on foreign currency based on a capitalization of the difference between the forward price stated in the contract and the current forward price for the remaining period of the contract to maturity, while using an appropriate interest rate.

The fair value of forward contracts on the Index is estimated based on a capitalization of the future cash flow stated in the contract by interest rates matching the remaining period to maturity of the contract.

The fair value of vanilla options is based on their quoted price, if available. In the absence of such quoted price, the fair value of the vanilla options is estimated through the German Kolhagen formula, which is an expansion of the Black & Scholes formula for foreign currency options.

This formula is based on normal distribution and takes into account the following variables: the spot at the time of performance of the transaction, the option exercise price, the effective risk free interest rate in the primary currency and in the secondary currency, time to maturity and volatility deriving from the exchange rate.

The fair value of the interest swap contracts is estimated based on a capitalization of future cash flows – that are based, *inter alia*, on the inflation forecast, over the term of the contract, while using appropriate interest curves that are used to price derivatives and are based on short-term Libor interests and long-term IRS transactions.

Note 3 **Critical estimates and the determination of the fair value (contd.)**

C. Determination of fair value: (contd.)

(6) a. Share based payment transactions – the fair value of employee options is measured using the Binomial model. The assumptions used in the model include the share price at the time of the measurement, the exercise price of the instrument, expected volatility (based on a weighted average of historic volatility adjusted to expected changes following publicly available information), the weighted average of the expected lifetime of the instruments (based on similar instruments and the general behavior of the holders of the options), adjustment to dividend distribution existing in the option and the risk free interest rate (on the basis of government bonds). Service terms and performance terms that are not market terms are not taken into account when determining fair value.

b. The fair value of a share based payment repaid in cash is measured using the Black-Scholes Model. The model assumptions include the share price as of the date of the report, the instrument's disposition price, projected fluctuation, projected lifetime of the instrument and the rate of riskless interest on the basis of governmental bonds.

In subsequent periods, the fair value of the payment classified as a financial liability is measured in the same way in every reporting period.

(7) Trade and other receivables – the fair value of loans and receivables including trade and other receivables, other than in respect of construction work in progress but including receivables in respect of franchise agreements, is determined on the basis of the present value of the future cash flows, which are discounted using the market interest rate, which weight, *inter alia*, the risk of the borrower as of the reporting date. In periods that follow the initial recognition, the fair value of trade receivables and other receivables is calculated solely for the purpose of the provision of disclosure.

(8) Investment property under construction– As aforesaid in Note 2P, the Group's investment property under construction is presented at fair value at the end of the reporting period, where changes in the fair value are carried to the income statement as income or as expenses.

For the purpose of the determination of the fair value of investment property under construction, the Company's management bases itself, primarily, on evaluations that are performed at least once a year by independent appraisers of land, having the required knowledge, experience and expertise. The Company's management is in the habit of determining the fair value in accordance with generally accepted evaluation methods of realty assets, primarily discounted cash flows and comparison with selling prices of similar assets and the Group's assets in the near environment. Where use has been made of the discounted cash flows method, the interest rate used in the discounting of the net cash flows that are expected from the asset can have a significant impact on the fair value.

In the determination of the fair value, the Company takes into account, inter alia, and in so far as is relevant, the time needed for the construction of the project, the level of the rental fees that it will generate, the additional cost that is required for its construction until it is operated as well as the interest rate, the risk premium for the project, deduction of entrepreneurial profit, and the discount rate that is required. A change in the value of any of these components, or all of them, could have a significant impact on the fair value of the property as estimated by the Company's management.

The Group strives to determine as objective a fair value as is possible, however at the same time, the process of estimating the fair value of investment property under construction also includes subjective elements, which are sourced, inter alia, in the past experience of the Company's management and its understanding of what is expected to take place in the investment property market at the time at which the estimate of the fair value is determined. In the light of what is stated in the previous paragraph, the determination of the fair value of the Group's investment property under construction mandates the exercise of judgment. Changes in the assumptions that were used in the determination of the fair value could have a significant effect on the Group's state of affairs and the results of its activities.

Note 3 **Critical estimates and the determination of the fair value (contd.)**

C. Determination of fair value: (contd.)

(9) The Company reviews in its quarterly reports the need to update the value of the investment real estate properties by examining micro economic changes that may have a material effect on the fair value of the properties and/or upon the occurrence of a material event that was defined as a material or a very material asset in the Company's statements, due to populating, material change in rent, etc. Also, with regard to investment real estate properties under construction, the costs actually invested during the period, the updated forecast of costs for completion and lease agreements signed during the period are taken into account. Upon initial classification of a property that was under construction as investment property, and insofar as no valuation was received therefor in the six months preceding the classification date, an external valuation will be performed therefor, as of the end of the quarter in which it was first classified as investment property.

(10) The fair value of fixed assets recognized within the framework of business combination, is based on their value in the market. The market value of fixed assets is the assessment of the amount for which the fixed assets would have been exchanged on the date of performing the valuation. In a transaction between a buyer at will and a seller at will, acting in an educated manner, the market value of items in property, plant and equipment as well as facilities is based on assessments for quoted market prices for similar items, if available and replacement costs when such quotes are not available. An estimate of the reduced replacement costs takes into account adjustments for physical wear and tear and functional and economic obsolescence of the fixed asset items.

(11) The fair value of inventory purchased within a business combination, is determined based on an estimate of the sale price of the inventory in the ordinary course of business, less the estimate of costs for completion and sale thereof, as well as reasonable margin based on the efforts required for completion and sale of the inventory.

Note 4 **Cash and cash equivalents**

The composition:

	As of December 31	
	2011	**2010**
	NIS in Thousands	**NIS in Thousands**
Balances with banks	101,619	89, 418
Short-term deposits – unlinked	120,135	87,775
Short-term deposits – in Dollars	2,676	665
	224,430	177,858

Note 5 Financial assets held for trade

The composition:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Shares	246,914	251,342
Government bonds	487,252	1,031,013
Corporate bonds	547,058	780,501
Bonds convertible into shares	105	8,466
Participation certificates in trust funds and exchange-traded notes	117,994	168,684
Others	2,463	70,417
	1,401,786	2,310,423

Mainly investment of some of the issue proceeds in a diversified manner in shares which are traded in the TA-100 Index and in the Canadian stock exchange in bonds which are rated BB+ and higher and in deposits in financial institutions. (The total investment in shares and bonds in the Canadian stock exchange is approx. NIS 56 million).

Note 6 Deposits and short-term investments

Deposits and short-term investments as of December 31, 2011 include primarily: deposits, in the sum of approx. NIS 80,395 thousand bearing annual interest at a rate of 2.45% (as of December 31, 2010 mainly including deposits in the sum of approx. NIS 43,724 thousand, which bear annual interest at a rate of 1.7%), out of which deposits in the sum of approx. NIS 33 million that are pledged on behalf of bank tender guarantees.

Note 7 Trade and other receivables

A. Trade receivables:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Open debts	1,570,701	1,278,660
Income receivable	23,705	27,362
Checks collectable	233,022	159,596
Credit card companies	72,915	58,087
Current maturities of long-term loans extended	17,404	18,004
	1,917,747	1,541,709
Net of – provision for doubtful debts	(197,983)	(202,600)
	1,719,764	1,339,109

For details regarding balances in respect of related and interested parties – see Note 40C.

Note 7 Trade and other receivables (contd.)

B. Other receivables:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Receivables for the sale of available for sale financial asset (See Note 12A(3))	7,337	-
Employees	527	554
Income receivable	6,209	4,717
Institutions	13,062	6,334
Prepaid expenses	23,020	21,768
The Fuel Authority	1,636	1,737
Deposits in trust	37,990	9,249
Related parties	-	637
Current maturities of other long-term receivables	4,150	7,116
Advances to suppliers	11,363	9,167
Derivative instruments	5,147	375
Current maturities of receivables in respect of a franchise arrangement	20,316	19,308
Other receivables	25,065	23,266
	155,822	104,228
Net of – provision for doubtful debts	(11,138)	(8,995)
	144,684	95,233

For details regarding balances in respect of related and interested parties – see Note 40C.

Note 8 Receivables for work in progress:

The composition:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Capitalized costs	120,048	114,723
Plus profits recognized	31,505	20,133
Less losses recognized	(1,159)	(1,194)
Less charges issued to customers	(117,745)	(98,680)
Capitalized costs and profits recognized less losses recognized, that exceed charges issued to customers	32,649	34,982

Note 9 Inventory

A. The composition:

	As of December 31	
	2011	**2010**
	NIS in Thousands	**NIS in Thousands**
Raw materials	113,120	82,796
Work in progress	16,587	15,768
Finished works	285,694	231,244
Ancillary materials, spare parts and instillations	24,532	16,246
	439,933	346,054

B. See Note 35 on the subject of charges.

Note 10 Investments in and loans to associates

A. Active consolidated companies that are held directly by the Company:

Name of subsidiary	Country of incorporation	Holding rate in the rights in the capital of the consolidated company		Volume of the investment in the investee company		Amounts that the Company has made available to the consolidated company					
								Financial guarantees			
						Loans		Amount of guarantees		Amount of guaranteed at the end of the period	
		2011	2010	2011	2010	2011	2010	2011	2010	2011	2010
		%	%	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Canit Hashalom Investments Ltd.	Israel	100	100	4,193,304	3,760,175	(1)1,355,327	(1) 1,150,200				
International Consultants (E-Consult) Ltd.	Israel	100	100	44,142	42,697	(2) 26,782	(2) 27,723	In an unlimited amount as collateral for a loan from a bank		24,806	22,786
Azrieli Center Mall (Initiation and Management) Ltd.	Israel	100	100								
Hanegev Mall (Initiation and Management) Ltd.	Israel	100	100								
Ayalon Mall (Initiation and Management) Ltd.	Israel	100	100								
Jerusalem Mall (Initiation and Management) Ltd.	Israel	100	100								
Holon Mall – Management and Maintenance Ltd.	Israel	60	60			(2) 8,205	(2) 7,985				
Azrieli Center Parking Lot Ltd.	Israel	100	100	21,662	19,714						
Azrieli Center Towers (Initiation and Management) Ltd.	Israel	100	100								
Otzem Entrepreneurship and Investments Ltd.	Israel	100	100	44,927	38,065	(3) 127,472	(3) 23,272				
Givatayim Mall Initiation and Management Ltd.	Israel	100	100								
Canit USA II	USA	100	100								
Canit Northchase L.P. (4)	USA	99	99	10,963	16,232			In an unlimited amount as collateral for a loan from a bank		29,613	
AG Galleria Office Buildings LP (4)	USA	90		86,202					-		

(1) NIS 1,097 million Index- linked and bearing interest at the rate of 4.8% (in 2010 – approx. NIS 856 million) and approx. NIS 258 million (in 2010 – approx. 294 million), not Index- linked and bearing interest in accordance with the Income Tax Regulations (in 2011- 3.8%). In the matter of accounting treatment – see Note 2EE.
(2) The loan bears interest in accordance with the Income Tax Regulations (in 2011 – 3.8%).
(3) The capital note is not Index-linked and is non-interest bearing.
(4) Limited Partnership.

For details of consolidated companies that are not held directly – see Note 46 to the financial statements.

Note 10 **Investments in and loans to associates (contd.)**

B. Associates:

(1) Abbreviated information extracted from the financial statements of the Group's associates:

The following is abbreviated financial data in respect of associates treated under the equity method, without adjustment to the rates of the Group's holdings:

	Total assets	Total liabilities	Income	Loss for the year
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
2011	124,798	73,665	16,820	(27,004)
2010	123,946	208,006	17,234	(36,417)
2009	835,218	799,719	171,470	(23,240)

(2) Additional information:

In April 2010 the Group's holding rate in Via Maris increased from 50% to 72.1%, and in November 2011 a transaction for the purchase of the remaining shares in Via Maris was closed, such that the Group's holding rate in Via Maris as of December 31, 2011 is 100%.

C. Details in respect of loans and long-term receivables:

Details of the linkage bases and the interest terms

	As of December 31, 2011			
	Unlinked NIS	Dollar linked	Index-linked NIS	
Nominal interest rates:	0%-3.8%	4%	10%	Total
	NIS in Thousands			
Loans and long-term receivables	14,869	800	23,817	39,486
Capital notes	(1) 86,860	-	-	86,860
Net of the Company's share in losses of associates	(89,221)	(800)	(3,245)	(93,266)
	12,508	-	20,572	33,080

	As of December 31, 2010			
	Unlinked NIS	Dollar linked	Index-linked NIS	
Nominal interest rates:	0%-0.3%	4%	10%	Total
	NIS in Thousands			
Loans and long-term receivables	8,094	714	(1) 84,862	93,670
Capital notes	463	-	12,147	12,610
Net of the Company's share in losses of associates	(948)	(714)	(76,970)	(78,632)
	7,609	-	20,039	27,648

(1) During 2011, the Company converted loans extended thereby to a held company in the sum of NIS 74,250 thousand in a non-linked non-interest bearing capital note, which is payable upon dissolution.

Specification of Payment Due Dates - The payment due date for loans and long-term receivables which have been given to the associates has not yet been determined.

Note 11 Investments, loans and receivables

A. The composition:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Loans extended (see B(1) and C below)	92,506	99,889
Net of current maturities (see C below)	(22,159)	(25,063)
	70,347	74,826
Checks and notes collectable	9,607	12,763
Assets in respect of benefits for employees	1,420	1,081
Receivable in respect of the averaging of income from rental fees	30,091	26,445
Derivative instruments	505	-
Other receivables B(2)	10,156	4,418
	122,126	119,533

B. Additional information:

(1) The loans that were extended, mainly to lessors of fuelling stations, are presented at a discount for the difference between the interest stated in the loans and the market interest on the date of the granting of the credit, which was carried to financing expenses upon provision of the credit.

(2) In 2011, formed costs in the sum of NIS 4,806 thousand were included, in respect of expansion of the water desalination plant, which have not yet been recognized as a financial asset, see also Note 13. In addition, the balance of the other receivables includes mainly customer debts in respect of initial filling of oil distillates linked to the distillates prices.

Note 11 Investments, loans and receivables (contd.)

C. Details regarding long-term loans:

Specification of the linkage bases and the interest terms

	As of December 31, 2011 (NIS in Thousands)									
	Unlinked NIS			Index-linked NIS			NIS linked to the Dollar or stated in Dollars			
	Nominal interest rate			Nominal interest rate			Nominal interest rate			
	0%-2%	2%-10%	Total	0%-4%	4%-8%	Total	0%-3%	3%-8%	Total	Total
Long-term loans	12,591	16,175	28,766	29,213	28,055	57,268	1,254	5,218	6,472	92,506
Net of current maturities			(10,584)			(6,399)			(5,176)	(22,159)
Long-term loans, net			18,182			50,869			1,296	70,347

	As of December 31, 2010 (NIS in Thousands)									
	Unlinked NIS			Index-linked NIS			NIS linked to the Dollar or stated in Dollars			
	Nominal interest rate			Nominal interest rate			Nominal interest rate			
	0%-2%	2%-10%	Total	0%-4%	4%-8%	Total	0%-3%	3%-8%	Total	Total
Long-term loans	11,653	16,788	28,442	35,754	28,802	64,556	1,477	5,414	6,891	99,889
Net of current maturities			(10,917)			(8,108)			(6,038)	(25,063)
Long-term loans, net			17,525			56,448			853	74,826

Note 11 Investments, loans and receivables

D. **(1)** As collateral for the full and accurate payment of the debt for bond holders issued by a consolidated company of Supergas, Supergas had undertaken to provide, as collateral to the benefit of the bond trustee (the "Trustee") a deposit which will be in at the quarterly payment amount (principal and interest) which is the highest expected to be paid according to the bond's payment schedule, until the expiration of the bond period. The deposits are Index-linked and bear interest at a rate of 1%. The balance of the deposits as of December 31, 2011 is NIS 22,037 thousand (December 31, 2010 – NIS 21,276 thousand).

(2) The restricted investments are used as a collateral for the payment of the senior financing extended by a banking corporation for the construction of the desalination facility at Via Maris, and are mainly invested in governmental loans and their balance as of December 31, 2011 is NIS 28,893 thousand (December 31, 2010 - NIS 28,172 thousand).

Note 12 Available for sale financial assets and financial assets that have been designated as at fair value through profit and loss:

A. Available for sale financial assets

(1) Investment in Bank Leumi Le'Israel Ltd. ("Bank Leumi")

On April 30, 2009 the Company acquired approx. 4.8% of the shares in Bank Leumi (approx. 71 million shares) for a consideration that was equivalent to NIS 742 million.

In order to finance some of the acquisition amount, the Company issued short-term marketable securities in an amount of approx. NIS 153 million to institutional bodies and others. As of December 31, 2011, the balance of these securities amounted to approx. NIS 168 million (as of December 31, 2010 - NIS 199 million).

In November 2010 the Company received a dividend in the sum of approx. NIS 24 million from Bank Leumi.

In 2011 the Company received a dividend in the sum of approx. NIS 43 million from Bank Leumi.

As of the date of the statement of financial position, the balance of the Company's investment in Bank Leumi Le'Israel Ltd. is approx. NIS 771 million.

(2) Investment in Leumi Card Ltd.

In May 2008 the Company entered into an agreement with Leumi Card Ltd. ("Leumi Card") in which Leumi Card allocated 5 million shares, constituting 20% of its issued and paid up share capital immediately after the allocation on a fully diluted basis, to the Company. In consideration for the shares that were allocated, the Company paid an amount of NIS 360 million to Leumi Card.

In accordance with the provisions of the agreement, the Company is entitled to recommend on the appointment of 2 directors (out of a total of 13 directors) on the Board of Directors of Leumi Card (one director is to be an external director in accordance with Proper Conduct of Banking Business Directive 301) and if certain conditions are met the Company loses its entitlement to appoint the directors.

Leumi Financial Holdings Ltd. ("Leumi Holdings") has the right of first refusal on the sale of the shares that are held by the Company to a third party which is not a permitted transferee of the Company, as defined in the agreement.

Commencing from May 26, 2008, Mr. Menachem Einan – deputy chairman of the Azrieli Group, has served as the company's representative on Leumi Car's Board of Directors.

As of the date of the financial position, the Company holds 20% of the issued and paid up share capital of Leumi Card and the Company has one representative on the Board of Directors. Leumi holdings holds 80% the issued and paid up share capital of Leumi Card and has seven representatives on the Board of Directors

As of date of the statement of financial position, Leumi Card's Board of Directors is made up of 12 directors (of whom 4 are external directors).

Note 12 **Available for sale financial assets and financial assets that have been designated as at fair value through profit and loss: (contd.)**

In the light of the number of directors and the control structure in Leumi Card, the Company has reached the conclusion that it does not have material effect in Leumi Card and therefore the investment is presented as an "available for sale financial asset".

For clarification purposes, the significant effect of the Company in Leumi Card in which the Company holds on the date of the decision 20% of the issued and paid capital and voting rights has been removed. The Company's Board of Directors on May 6, 2010 approved to irrevocably waive the Company's voting rights in connection with 2% (two percent) of the issued and paid-up share capital of Leumi Card held by the Company is such a way that in view of this waiver the Company will hold 20% of the issued and paid-up share capital of Leumi Card and 18% of the voting rights in it. In addition, it was decided to irrevocably waive the right to recommend the appointment of an additional director in Leumi Card as an external director.

As of date of the statement of the financial position, the Company's investment balance in Leumi Card totaled at an amount of approx. NIS 483 million.

The fair value has been determined by an independent external appraiser, where the evaluation is based on the discounted cash flows approach (D.C.F.), based on the net profit as extrapolated from the business plan, adjustments to the profit and less investments. In the determination of the recoverable amount of the cash flows, a weighted average cost of capital (WACC) of 10. % has been taken into account and the long-term growth rate has been set at 2.5%.

In June 2010, the Company received a dividend in the sum of approx. NIS 2 million from Leumi Card.

On February 23, 2012, Leumi Card's board of directors approved dividend distribution to Leumi Card's shareholders in the total sum of NIS 40 million (the Company's share is NIS 8 million) out of Leumi Card's profits in 2011, to be distributed on March 29, 2012.

(3) Available for sale financial assets include investments in shares in companies, which do not exceed 20%.

In November 2011, the Company announced the exercise of a put option for the sale of its holdings in one of the above companies at a price equal to the sum of its investment in the company (which has not yet been recovered), plus annual interest of 5% in accordance with the terms and conditions of the investment agreement. The consideration in respect of this exercise is supposed to be received in 2012.

B. Financial assets that have been designated as at fair value through profit and loss:

The Company's investments are carried out through the business division that is engages in investments in hi-tech companies in Israel and abroad, at rates of between 0.16% and 5.0% of the issued share capital of those companies (the "Investee Companies"). The Investee Companies are engaged in research and development and have not yet reached a stable situation in their businesses. Consequently, the continuation of the activities of the Investee Companies involves certain risks, which derive from the nature of their activities, including uncertainty in respect of the success of the development and their ability to market their products. The Company's management has designated these investments as at fair value through profit and loss, in accordance with the provisions of International Accounting Standard 39, Financial instruments: "Recognition and Measurement" section 9(B)(2). See also Note 2 N in respect of investments that are presented at fair value through profit and loss.

Note 13 Long-term receivables in respect of a franchise arrangement

A. Sea water desalination project

On October 28, 2002, an agreement was signed between the consolidated company Via Maris Desalination (Holdings) Ltd. ("Via Maris") and the State of Israel (the "Franchise Agreement") for the planning, financing, construction, operation and maintenance of a facility for desalination of sea water at an annual production of 30 million cubic meters at a BOO (Build, Own, Operate) format, at the Kibbutz Palmachim area. The Franchise period is until 2029. During the franchise period Via Maris is obligated to supply to the state desalinated water at a scope which will be determined by the State and at a minimum quality specified in the Franchise Agreement. In consideration for construction of the desalination facility and operation thereof, Via Maris will be entitled to receive a fixed payment for providing an available capacity as well as a variable payment for the desalinated water which will be actually provided. On August 30, 2007, Via Maris received the operation certificate of the desalination facility from the state.

In the beginning of 2009, Via Maris signed with the State an agreement for the provision of additional amounts of desalinated water (the "Extension Agreement"). The Extension Agreement is for a period of approx. 18 years, until May 15, 2027. For that purpose, Via Maris extended the desalination facility to an annual production of 45 million cubic meters. The extension of the facility was completed an in July 2010 a permanent certificate was received from the State (PTO) for supply of water from the extended facility.

On November 24, 2011, a transaction was closed between GES and TAHAL Consulting Engineers Ltd. ("TAHAL"), whereby GES will acquire from TAHAL its rights in Via Maris corporations (27.9%), including the right to repayment of shareholder loans of TAHAL to Via Maris, in consideration for the sum of NIS 62.4 million (which was paid on the said date), thus increasing the rate of its holding from 72.1% to 100%. In addition, GES replaced the guarantees that TAHAL had provided to the State and to the financing bank. The difference between the consideration and the change in the non-controlling interests and in the shareholder loans thereof to Via Maris in the sum of NIS 2.4 million was carried to a capital fund as a credit balance.

On October 30, 2011, Via Maris signed with the State another amendment to the franchise agreement, regulating, *inter alia*, an additional expansion of the plant and increase of its annual capacity to 90 million cubic meter. The expansion agreement is for a period of approx. 18 years until April 28, 2029. The increase of production will be made in two phases – supply of 23 million cubic meters a year until the end of 2012 and supply of additional 22 million cubic meters until the end of July 2013.

The capitalization of the fixed payments in respect of the desalinated water, until the end of the franchise period which is defined under IFRIC 12 as a the financial asset of receivables for the franchise arrangement sums up as of the date of the report to an amount of NIS 553,373 thousand (including a current maturity in the sum of NIS 20,057 thousand presented as a current asset).

B. The composition:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Linked to the Consumer Price Index	473,399	477,554
Other(1)	65,898	68,829
Linked to a currency basket (2)	15,615	-
	554,912	546,383
Net of current maturities	20,316	19,308
	534,596	527,075

(1) Approx. 10% linked to the Consumer Price Index and approx. 90% not linked.

(2) Approx. 17% linked to the consumer price index, approx. 46% linked to the changes in dollar and Euro, approx. 14% linked to the Construction Inputs Index and approx. 23% not linked.

Note 13 Long-term receivables in respect of a franchise arrangement (contd.)

The collection dates of the balances for the receivables in respect of a franchise arrangement after the financial statements' date:

	First year	Second Year	Third year	Forth year	Above five year	Total
	NIS in Thousands					
Receivable in respect of a franchise arrangement	20,316	22,190	22,882	24,060	465,464	554,912

Note 14 Investment property and investment property under construction

A. Movements and composition:

	As of December 31, 2011			As of December 31, 2010		
	Land, buildings and commercial areas for lease	Investment property under construction	Total	Land, buildings and commercial areas for lease	Investment property under construction	Total
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Balance as at the beginning of the year	11,969,647	240,617	12,210,264	10,626,195	242,536	10,868,731
Additions during the course of the year:						
Investments	753,765	980,529	1,734,294	391,279	76,158	467,437
Adjustments to fair value	887,296	(38,437)	848,859	832,776	57,920	890,696
Net translations differences deriving from the translation of the financial statements of overseas operations	46,153	-	46,153	(14,742)	-	(14,742)
Transfer from investment property under construction	324,667	(324,667)	-	122,197	(122,197)	-
Total additions	2,011,881	617,425	2,629,306	1,331,510	11,881	1,343,391
Deductions in the course of the year:						
Disposals	-	-	-	1,858	-	1,858
Total deductions	-	-	-	1,858	-	1,858
Balance at the end of the year	13,981,528	858,042	14,839,570	11,969,647	240,617	12,210,264

B. The composition with a distinction between ownership rights and leasing rights:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Under capitalized leasing	10,506,309	9,258,109
Under non-capitalized leasing	35,886	37,214
Under ownership	4,297,375	2,914,941
	14,839,570	12,210,264

Note 14 **Investment property and investment property under construction (contd.)**

C. Determination of the fair value of the Group's investment property:

		As of December 31	
		2011	2010
		NIS in Thousands	NIS in Thousands
Commercial centers, malls and office and other space for lease	- See C(1) below	13,747,805	11,934,755
Communication facilities (*)	- See C(2) below	35,886	-
Office space for lease	- See C(2) below	39,032	37,947
Investment property/ under construction/ lands/ residential project	- See C(3) below	887,960	220,537
Investment property under construction	- See C(4) below	111,778	17,025
Payments on account of investment property	- See J below	17,109	-
		14,839,570	12,210,264

Investment property is presented at fair value as determined in revaluations performed by external appraisers possessing recognized professional skills and considerable experience in respect of the location and the type of the property that is being valued and also in accordance with evaluations by the Group's management. The fair value represents the amount on the day that the evaluation was made according to which assets would be exchanged between a seller and a purchaser in a transaction preformed at market terms after the parties have acted willingly, intelligently and with due care, in accordance with international evaluation standards.

(1) The fair value has been determined by external valuations and is measured based on the discounting of forecast cash flows, based on reliable estimates of future cash flows, which are supported by the terms of each lease or other existing contracts and by external evidence, such as current rental fees for similar property in the same location and in the same state, and also on the use of discount rates, which reflect the market's current evaluation in respect of the lack of certainty in respect of the amount and the timing of the cash flows see also Note 3C(1). The average cap rates of assets in Israel are in the range of 7.33%-9.06% (as of December 31, 2010 – 7.35%-9.07%). The average cap rates of assets in the USA are in the range of 7.25%-9.25% (as of December 31, 2010 – 7.75% - 8.75%).

In the valuation of the investment property under construction as of December 31, 2010, in addition to the aforesaid, the following were also taken into account: the construction period of the project, the deduction of entrepreneurial profit and the additional cost which is required until the current operation thereof see also Note 3C(8). The main cap rates which were used for the calculation of the fair value of the property under construction were 9.5%-10%.

(2) The fair value is measured by the Group's management based on the discounting of forecast cash flows, based on reliable estimates of future cash flows, which are supported by the terms of each lease or other existing contracts and by external evidence, such as current rental fees for similar property in the same location and in the same state, and also on the use of discount rates, which reflect the market's current evaluation in respect of the lack of certainty in respect of the amount and the timing of the cash flows. The cap rate that was used in the calculation of the fair value in the previous year was 7%, whereas the cap rate that was used in the calculation of the fair value is 7.3% (last year – 7%).

The cap rates that were used in the calculation of the fair value of communication facilities are 8%-15%.

As of December 31, 2010 communication facilities were determined and measured by external valuations.

(3) The fair value has been determined by external revaluations and has been measured based on current prices in an active market for similar property, in the same location and in the same state, subject to other similar leases.

(4) The costs that have been incurred in respect of investment property under construction and which cannot yet be value at fair value. See also Note 34B(3).

Note 14 Investment property and investment property under construction (contd.)

D. Additional information:

(1) Canit Hashalom has leased the land on which the "Azrieli Center" was built from the Municipality of Tel-Aviv-Jaffa under a capitalized lease for a period of 200 years. The lease period is until February 6, 2195. A mortgage has been registered in Canit Hashalom's lease rights in favor of the Mortgage Company of Bank Leumi, Bank Leumi Le'Israel Ltd. and Bank Hapoalim Ltd.

(2) As from December 24, 2003, Canit Hashalom has been leasing the land on which the "Azrieli Modi'in" mall has been built from the Israel Lands Authority under a capitalized lease for a period of 98 years in respect of residential units and for a period of 49 years in respects of units with other designations (the mall and offices) with an option for additional periods of 98 years and of 48 years, respectively. As of the date of the approval of the financial statements the lease agreement has not yet been signed.

(3) The Company has leased the land on which the "Azrieli Jerusalem (Malha)" mall has been built from the Israel Lands Authority under a capitalized lease for a period of 49 years, ending on August 15, 2039, with an option for an additional period of 49 years.

(4) The Company has leased the land on which the "Azrieli Ayalon" mall has been built from the Israel Lands Authority under a capitalized lease for a period of 49 years, ending on August 1, 2031, with an option for an additional period of 49 years.

(5) The Company is leasing the Azrieli Or Yehuda Outlet Mall from the Israel Lands Authority under a capitalized lease for a period of 49 years, ending on March 24, 2040, with an option for an additional period of 49 years.

(6) The Company is leasing the Azrieli Givatayim Mall from the Israel Lands Authority under a capitalized lease for a period of 49 years, ending on September 5, 2053 and February 9, 2051.

(7) The Company is leasing industrial buildings in Caesarea Industrial Park from the Caesarea Edmond Benjamin de Rothschild Development Corporation Ltd. under a capitalized lease for a period of 49 years, ending on July 7, 2053 and March 12, 2049, with an option for an additional period of 49 years.

(8) Some of the assets of consolidated companies are registered in their names in the Lands Registry. Another part has not yet been registered for technical reasons, the main reason for the non registration deriving from the proceedings of the land arrangements and the reparcelization arrangements of the land have not yet been settled.

(9) See Note 35 in respect of collateral and charges.

(10) The Group has several projects in the commercial centers and malls segment and in the office space for lease segment, which are under planning and construction - in Rishon LeZion with a net area of approx. 19,000 sqm, in Kiryat Ata (Stage B) with an area of approx. 3,000 sqm, and in Holon with an area of approx. 34,000 sqm. The total area for marketing, according to the planning of the said projects is approx. 48,000 sqm, approx. 4,000 sqm and approx. 120,000 sqm (stage A), respectively. See also Notes 14G and 14H below.

(11) See Note 34B(3) in respect of the Group's engagement through Canit Hashalom with the City of Holon.

(12) The amounts that have been carried to the income statement:

	For the year ended December 31		
	2011	**2010**	**2009**
	NIS in Thousands	**NIS in Thousands**	**NIS in Thousands**
Income from rental, management and maintenance	1,255,966	1,105,292	1,007,580
Direct operating expenses deriving from rent, management and maintenance	266,842	216,684	206,206

Note 14 Investment property and investment property under construction (contd.)

E. Azrieli Haifa Mall

In January 2010 the Company engaged in an agreement for the purchase of all of the rights in a land (through capitalized lease) in Haifa, on which the shopping and entertainment center known as the Haifa Mall is built, in consideration for an amount of approx. NIS 300 million. The overall cost of purchasing the mall, including transaction costs, totaled at approx. NIS 314 million.

For the financing of the purchase the Company took loans from a banking corporation in an amount of approx. NIS 225 million (the "Loans").

For securing the loans, the banking corporation was provided with the following collaterals:

(1) A Fixed charge on the Company's interests in the mall.

(2) A Fixed charge on the Company's interests according to the lease agreements with the lessees at the mall.

(3) A First ranking floating charge on all of the Company's interests in the mall.

The Company is leasing the Azrieli Haifa Mall from the Israel Lands Authority under a capitalized lease for periods of 49 years, ending on October 31, 2042 and March 2, 2035, with an option for an additional period of 49 years.

The mall has a temporary permit which is in effect until March 30, 2012. The Group is acting for fulfillment of the conditions required for receipt of a permanent business license.

F. Azrieli Givatayim Mall:

In December 2008 the Company entered into an agreement with Properties and Construction (Commercial Centers) Ltd. and Clal Insurance Company Ltd., for the purchase of their entire rights (100%) in land in Givatayim, on which a shopping center and entertainment center has been built, which is known as the "Givatayim Mall" (the "Mall") for a consideration of approx. NIS 795 million.

On March 31, 2009 the transaction was closed.

The Company has taken up loans amounting to NIS 660 million from a banking entity, in order to finance the acquisition (the "Loans").

As collateral for the Loans, the banking entity has been provided with the following collateral:

(1) A commitment to register a first ranking mortgage on the Mall.
(2) A first ranking charge on the contractual rights deriving from the Mall.
(3) A first ranking fixed charge on all of the rights deriving from the Mall.
(4) A first ranking floating charge on all of the rights in the Mall.

On October 31, 2011, the lease rights in the Givatayim Mall were registered at the ILA in the Company's name (with the exception of the Company's rights in the parking lots) as well as an undertaking to register the mortgage in favor of Bank Leumi.

G. Purchase of land in Southern Hakirya:

In May 2011, the Company won a tender on behalf of the ILA for the purchase of the lease rights in a lot in Southern Hakirya in Tel Aviv (of an area of approx. 9.4 dunams) (the "Lot").

The Lot is designated for the construction of an office and commercial project at a scope of approx. 125 thousand sqm of above-ground built-up area (gross) and approx. 61 thousand sqm of underground levels. In consideration for the lease of the Lot for a period of 49+49 years, the Company paid the ILA the sum of approx. NIS 522 million (not including V.A.T) and approx. NIS 39 million in development expenses.

In July 2011, the Company paid, in respect of the purchase, purchase tax in the sum of approx. NIS 27 million.

In the tender documents, the Company undertook to complete the construction of the project within 60 months, part of the work it undertook to complete within 36 months.

As of the date of the report, the Company has financed the purchase of the Lot with internal financing and through bank financing, and it intends to finance the construction through bank financing and/or internal financing.

Note 14 Investment property and investment property under construction (contd.)

H. Purchase of land in Ramla:

In January 2011, a consolidated company signed an agreement for the purchase of the rights in a lot of an area of approx. 31,650 sqm in Ramla, which constitutes part of the area known as the Gindi City project (the "Sale Agreement" and the "Lot") from Gindi Investments Projects 2006 Ltd. (the "Seller").

The transaction was closed in May 2011 and all of the consideration in the sum of NIS 100 million (plus V.A.T.) has been paid, with part thereof being held in a deposit in escrow to secure provision of the tax confirmations and performance of the transfer of the rights by the Seller.

In June 2011, the consolidated company paid the sum of approx. NIS 5 million in purchase tax.

The Lot is designated for the construction of a mall of a gross area of 31,500 sqm (main areas and service areas).

As of the date of the report, the consolidated company has financed the purchase of the Lot through financing from the Company and it intends to finance the construction through bank financing and/or financing from the Company.

I. Purchase of three office towers in Houston, Texas, U.S.:

In February 2011, Three Galleria Office Buildings, LLC., a U.S. company indirectly held, at the rate of 90%, by the Company (the "Buyer"), closed, with a third party (the "Seller"), the purchase of three office towers in Houston, U.S. (the "Agreement"), all as specified below:

(1) The Purchased Properties

In accordance with the Agreement, the Buyer purchased all of the rights in three towers that are used for offices, of a total area of approx. 99,000 sqm (1,065,789 sqf) (with no additional building rights), which are situated in the Galleria area in Houston, Texas, U.S., which constitute part of a complex which includes commercial areas, two luxury hotels and parking lots (in the legal structure of a condominium). Approx. 3,774 parking spaces serve the towers, according to a long-term agreement with the owners of the commercial property which constitutes part of the condominium structure, which was assigned to the Buyer.

(2) The Consideration

The consideration for the properties was in the total sum of U.S. $176 million, out of which the sum of approx. U.S. $22 million, which was deposited in escrow, was offset against existing liabilities of the Seller to existing lessees and to brokers, which the Buyer assumed.

(3) Financing of the Purchase

The purchase was financed through a non-recourse loan in the sum of approx. U.S. $130 million and the balance through equity. The interest on the loan is fixed interest at the rate of 5.998%. The loan is for a period of 10 years, while in the first year interest will be paid only, and subsequently principal + interest according to amortization of 30 years.

To secure the loan, the Buyer pledged the purchased properties and all of the related rights deriving therefrom. In addition, the Company provided a limited guarantee in the sum of approx. U.S. $5 million, which may only be forfeited in certain cases defined in the loan agreement, and the Company undertook to indemnify the financier for its damage in the event of certain breaches of the Buyer's undertakings in the loan agreement.

Note 14 Investment property and investment property under construction (contd.)

I. Purchase of three office towers in Houston, Texas, U.S.: (contd.)

(4) Brokerage Fee

For locating the property and initiating and promoting the transaction, the Company paid an initiation and brokerage fee to the owners of the management company in the sum of approx. U.S. $1.4 million.

(5) Agreement for the Management of the Purchased Properties, the Partners in the Buyer

The remaining 10% of the rights in the Buyer are indirectly held by the owners of the management company (the "Partner").

The Company provided the Partner with a loan in the sum of approx. U.S. $2.5 million to finance part of the Partner's share in the capital required for the purchase of its share in the rights (the "Partner's Loan"). The loan bears annual interest at the rate of 6.998% per annum. To secure the Partner's Loan, the Partner pledged in favor of the Company its rights in the Buyer, including its rights to receive distributions therefrom, and also provided a personal guarantee.

During Q3, the Partner paid the above loan and at the same time the pledge on its rights expired and the guarantee that it provided was cancelled.

In addition, the Buyer engaged with the management company in an agreement for the management of the purchased properties, in consideration for a management fee at the rate of 2.25% of the gross income from the purchased properties. The management agreement further determines that each party is entitled to terminate the management agreement at any time by advance notice of 30 days.

J. Properties Purchased After the Balance Sheet Date – Purchase of Office Building in Houston:

On January 10, 2012, AG Plaza at Enclave, LLC, a U.S. corporation indirectly held at the rate of 100% by the Company (the "Buyer") closed the purchase of an office building at an occupancy rate of 100% in the city of Houston, Texas, U.S. (the "Agreement") in consideration for the sum of approx. NIS 412 million (approx. U.S. $107.5 million) in addition to transaction costs estimated (including financing costs) in the sum of approx. NIS 3 million (approx. U.S. $750 thousand).

In accordance with the Agreement, the Buyer purchased all of the rights in an office building, of a total area of approx. 31,986 sqm (344,296 sqf), including approx. 1,500 parking spaces located in a separate parking building) which is situated in a central business district in the city of Houston, Texas, U.S., whose construction was completed in 2008 (the "Office Building").

There are four (4) tenants in the property as follows:

- A main tenant (87%), a world-leading agro-chemical company by the name of Dow Chemical Company, which is traded on the NYSE, which has a long-term lease agreement expiring in May 2026, with no possibility of early departure. The lease agreement includes an option to extend the agreement for additional periods.

- Three tenants (13% in total) who have lease agreements for periods ranging between 6-7 years, with some of the lessees having an option for early departure after approx. 5 years and all having an option to extend the agreements for additional periods.

The lease agreements include fixed mechanisms for rent increases throughout the terms of the agreements, such that the total average annual NOI for all of the contracts throughout the terms of the lease will be in the sum of approx. U.S. $8 million.

For the purchase of the building, the Company took a loan from an American financing institution in the sum of U.S. $70 million. A loan will be extended for a period of some five years and shall bear a fixed interest of 3.6%. In favor of the loan, the Buyer shall pledge the Office Building.

Note 15 Fixed assets

A. The movement and composition:

	Land and buildings at cost	Machines and equipment	Furniture, equipment and computers	Motor vehicles	Installations and leasehold improvements	Total
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Cost						
Balance as of January 1, 2010	1,170,751	1,332,339	202,114	57,146	21,549	2,783,899
First time recognition of land held under a finance lease	111,788	-	-	-	-	111,788
Additions	77,944	66,577	13,866	10,445	1,300	170,132
Write-offs	(21,063)	(111,751)	(4,360)	(7,318)	(4)	(144,496)
Purchases in the framework of business combinations	-	1,853	873	-	-	2,726
Effect of changes in exchange rates	-	(3)	(15)	(29)	(2)	(49)
Balance as of December 31, 2010	1,339,420	1,289,015	212,478	60,244	22,843	2,924,000
Additions	29,430	70,138	12,573	13,723	1,680	127,544
Write-offs	(8,104)	(6,899)	(544)	(6,208)	(615)	(22,370)
Effect of changes in exchange rates	-	3	19	43	3	68
Balance as of December 31, 2011	1,360,746	1,352,257	224,526	67,802	23,911	3,029,242
Accumulated depreciation and loss from impairment						
Balance as of January 1, 2010	470,589	860,533	141,274	30,115	11,606	1,514,117
Depreciation for the year	30,480	55,283	12,320	6,846	2,031	106,960
First time recognition of land leased under a finance lease	8,982	-	-	-	-	8,982
Write-offs	(7,055)	(109,591)	(4,250)	(4,888)	(4)	(125,788)
Effect of changes in exchange rate	-	(2)	(9)	(7)	(1)	(19)
Balance as of December 31, 2010	502,996	806,223	149,335	32,066	13,632	1,504,252
Depreciation for the year	31,147	57,957	12,708	7,393	2,106	111,311
Write-offs	(2,162)	(6,080)	(522)	(4,001)	(615)	(13,380)
Effect of changes in exchange rates	-	4	17	8	2	31
Balance as of December 31, 2011	531,981	858,104	161,538	35,466	15,125	1,602,214
Depreciated Cost:						
As of December 31, 2011	828,765	494,153	62,988	32,336	8,786	1,427,028
As of December 31, 2010	836,424	482,792	63,143	28,178	9,211	1,419,748

Note 15 Fixed assets

B. Loss from impairment:

During 2011 and 2010 no losses from impairment were included and there was no recovery of impairment previously recorded.

C. The purchase of fixed assets on credit:

See Note 37 on the subject of additional information for the cash flows statement.

D. See Note 35 on the subject of charges.

E. Construction of a plant for the manufacture of gypsum boards and blocks:

On March 1, 2010 the Group completed the construction of the plant for manufacturing of gypsum boards and blocks on the site owned by Tambour (the "Plant"). The plant's activity is performed through a consolidated company of Tambour. In April 2010 the plant received a standard mark for manufacturing gypsum boards, and in June 2010 a standard mark for manufacture of gypsum blocks was received.

The overall investments in the plant totaled at approx. NIS 133 million.

The scope of the aforesaid investments includes the capitalization of credit costs, net change in the fair value of hedging cash flows, ramp-up costs, building fees and other costs, net of profits from pre operation date sales in a total amount of approx. NIS 8 million. Tambour began depreciation of the plant upon operation thereof.

During 2011, Tambour Group leased, in favor of the gypsum plant, additional land adjacent to one of its sites with the aim of building thereon an additional gypsum block production line. The costs that had accrued until the date of the financial statements amounted to the sum of approx. NIS 6.5 million, including costs capitalized to plant under construction in the sum of approx. NIS 0.3 million.

F. Details in respect of interests in land used by the Group as fixed assets

(1) Buildings on land held under capitalized lease from the Israel Lands Authority with an amortized cost, including the buildings thereon and the capitalized lease fees as of December 31, 2011 in the amount of NIS 68,667 thousand (2010 - NIS 70,914 thousand). The original leasing periods are of 49-98 years, ending in the years 2023-2059. Some of the lands have renewal options of the lease period for additional 49 years.

(2) Buildings on land held under capitalized lease from the Israel Lands Authority with an amortized cost of NIS 46,702 thousand as of December 31, 2011 (2010 - NIS 48,092 thousand). The original leasing periods are 49 years, ending in the years 2014-2039; Other than one lease agreement which terminated and is in the process of renewal of the option for additional 49 years.

(3) Buildings on land that is either owned or leased from third parties, buildings on leased land, leasehold improvements with an amortized cost and land which is leased through financing lease in a sum of NIS 194,337 thousand as of December 31, 2011 (2010 - NIS 201,347 thousand).

Some of the land that is owned or that is leased in Israel has not yet been registered in the name of the consolidated companies at the Land Registry. The main reason for the absence of the registration is that the processes of the organization of the land and the organization of the reparcelization of the land have not yet been organized.

Note 16 Intangible assets

A. The movement and composition:

	Goodwill	Customer relations	Distribution rights to oil distillates and others and supply rights and operating rights of stations	Franchise Arrangements	Software	Others (*)	Others
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Cost							
Balance as of January 1, 2010	322,091	161,963	118,169	-	59,782	85,440	747,445
Acquisitions	-	-	18,937	2,409	5,085	4,224	30,655
Purchases in the framework of business combinations	-	-	-	49,852	-	965	50,817
Write-offs	-	(2,856)	-	-	(1,411)	(3,879)	(8,146)
Impact of changes on exchange rates	(56)	-	-	-	-	-	(56)
Effect of the changes in the accounting policy	-	-	32,254	-	-	-	32,254
Balance as of January 1, 2011	322,035	159,107	169,360	52,261	63,456	86,750	852,969
Purchases	-	-	4,189	1,502	4,977	5,348	16,016
Purchases in the framework of business combinations	-	-	-	-	-	-	-
Write-offs	(2,234)	-	-	-	-	(2,745)	(4,979)
Effect of the changes in the exchange rates	60	-	-	-	-	-	60
Balance as of December 31, 2011	319,861	159,107	173,549	53,763	68,433	89,353	864,066

(*) The amounts included under the heading others comprise primarily brand names, commercial marks, payments for vacating premised and haulage rights.

Note 16 **Intangible assets (contd.)**

A. The movement and composition: (contd.)

	Goodwill	Customer relations	Distribution rights to oil distillates and others and supply rights and operating rights of stations	Franchise Arrangements	Software	Others	Others
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Accumulated depreciation and losses from impairment							
Balance as of January 1, 2010	22,518	63,993	84,386	-	51,580	48,892	271,369
Amortization for the year	-	15,187	7,779	167	4,280	5,063	32,476
Write-offs	-	(2,856)	-	-	(1,411)	(3,749)	(8,016)
Loss from impairment, net	-	131	-	-	-	448	579
Effect of the changes in the accounting policy	-	-	5,044	-	-	-	5,044
Balance as of January 1, 2011	22,518	76,455	97,209	167	54,449	50,654	301,452
Depreciation for the year	-	12,433	796	306	4,824	4,926	23,285
Write-offs	(2,234)	-	-	-	-	(463)	(2,697)
Loss from impairment, net	1,620	-	-	-	-	-	1,620
Balance as of December 31, 2011	21,904	88,888	98,005	473	59,273	55,117	323,660
Book value							
As of December 31, 2011	297,957	70,219	75,544	53, 290	9,160	34,236	540,406
As of December 31, 2010	299,517	82,652	72,151	52,094	9,007	36,096	551,517

Original Amount of Goodwill

As of December 31, 2009	308,277
As of December 31, 2010	308,277
As of December 31, 2011	306,044

Note 16 Intangible assets (contd.)

B. Presentation of the amortization of intangible assets:

Routine amortization in respect of intangible assets is reflected under the cost of sales, administrative and general expenses and/or under selling and marketing expenses in the income statement, as the case may be. Losses from impairment in value are reflected under other expenses in the income statement.

C. Allocation of goodwill to cash generating units

The goodwill has been allocated to cash generating units for the purposes of the testing for impairment in value, as follows:

	For the year ended December 31		
	2011	2010	2009
	NIS in Thousands	NIS in Thousands	NIS in Thousands
Activity A- Fuels	152,361	153,981	153,982
Activity B - Gas	63,057	63,057	63,057
Activity C - Paint	24,391	24,391	24,390
Activity D - Ecology	58,148	58,088	58,144
	297,957	299,517	299,573

The testing for impairment for the units that are described above as cash generating units, is determined by the capitalization of the future cash flows, which will be generated from the continuing use of the units, based on the following assumptions:

(a) The cash flows are estimated based primarily on the actual results of activities and on the business plans for the coming five years.

(b) The forecast annual rate of growth that is included in the forecast cash flows is primarily in the range of 1.7%-2.5%, in accordance with management's evaluation. This growth rate is based on the long-term growth rate of the GDP, the rate of population growth in Israel, business trends in operations in each sector and on the expected increase in competition for the various products.

(c) For the purposes of the estimation of the cost of capital for the activities, an estimate has been made of the weighted average cost of capital (WACC), whilst using the CAPM model for the calculation of the price of the capital and additional assumptions in respect of the price of debt and its appropriate debt structure. In the determination of the recoverable amount of the unit, post-tax discount rates of primarily: 7.47% for fuel operations, 8% for gas operations, 10% for paint operations and 12.6% for ecology operations has been taken into account. The estimate of the discount rate was made in reliance, inter alia, on the price of the capital for each activity, including the taking into consideration of the risk free interest rate, the market premium and the beta, the price of debt, a tax rate of 25% and the yield for similar public companies and other competing companies, as the case may be.

The estimates and the assumptions were determined in accordance with the evaluations of the managements in the Group in respect of future trends in the sector, and they are based on both external and internal sources (historical data) and in accordance with economic evaluations by independent appraisers.

Note 17 Prepaid lease fees

Leases in which the Group is the lessee:

A consolidated company has entered into agreements for lease of buildings which are used thereby. Most of the lease agreements (without options) are for periods that do not exceed 10 years. The rent is mostly linked to the Consumer Price Index.

A consolidated company has lease agreements, which are for up to 25 years for the most part. Most of the lease agreements include additional lease payments, based on changes in the CPI or other market data.

A consolidated company has entered into a land lease agreement for an initial period of approx. 25 years, which is being used thereby as a water desalination site and for the company's offices.

A consolidated company mostly leases land for 10-year periods, with an option for renewal of the contract at the end of the period, and sub-leases it to parties making use of wireless communication, mostly to cellular companies. The rent is linked to the Consumer Price Index.

Prepaid lease fees which refer to rights in land and buildings leased by Granite for various periods, the last period ends in 2053, amounted to NIS 41,296 thousand (in 2010 - NIS 44,431 thousand) out of which the sum of NIS 4,727 thousand was included as prepaid expenses in the other receivables item, including derivative instruments. (In 2010 – NIS 5,485 thousand) depreciation of rent paid in advance that was carried to profit and loss as rent expenses in 2011 is approx. NIS 5,741 thousand (2010 – NIS 6,122 thousand).

The following are details of the lease payments and income in respect of sub-lease that have been carried to the income statement:

	For the year ended December 31		
	2011	2010	2009
	NIS in Thousands	NIS in Thousands	NIS in Thousands
Minimal lease payments recognized as an expense	176,107	170,931	158,774
Conditional lease payments recognized as an expense	9,205	9,372	12,656
Income in respect of sub-lease	(17,491)	(16,744)	(15,976)
	167,821	163,559	155,454

Note 18 Trade payables

The composition:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Open debts	828,420	661,228
Checks payable	26,304	21,555
	854,724	682,783

Note 19 Other payables

The composition:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Advance from customer and income in advance	31,008	31,301
Contingent consideration in respect of acquisition of a consolidated company (*)	-	4,795
Liabilities for the completion of work in progress	10,186	14,068
Liabilities to employees and other liabilities in respect of salaries and wages	61,205	65,922
Interest and expenses payable	100,836	86 ,761
Payables in respect of derivative financial instruments	6,374	11,826
Institutions	138,796	132,926
Deposits from customers	5,980	4,157
Others	31,464	14,414
	385,849	366,170

For further information regarding payables that constitute related and interested parties, see Note 40.

Note 20 Deposits from customers

A consolidated company charges its customers with a deposit for ensuring the recovery of the equipment provided to them at the time of the engagement therewith, which it is required to return upon the end of the engagement and the recovery of the equipment. According to law, the amount which will be recovered to its discontinuing customers shall equal the amount of the deposit in accordance with the latest update that has been approved by the Ministry of Industry and Trade, with the addition of linkage differentials from the time of the latest approval that has been received and up to the time of the actual payment.

Note 21 Provisions

A. The composition and movement:

	Warranty	Legal claims	Total
	NIS in Thousands	NIS in Thousands	NIS in Thousands
Balance as at January 1, 2011	350	32,533	32,883
Provisions created during the year	200	9,421	9,621
Provisions realized during the year	-	(10,292)	(10,292)
Provisions cancelled during the year	(350)	(2,574)	(2,924)
Balance as at December 31, 2011	200	29,088	29,288

B. See Note 36 for details in respect of legal claims.

Note 22 Loans and credit from banks and other credit providers

A. Current liabilities:

	As of December 31	
	2011	2010
	NIS in Thousands	NIS in Thousands
Credit from banks		
Overdrafts	2,846	1,117
Short-term loans	1,643,355	838,179
	1,646,201	839,296
Credit from other credit providers		
Marketable securities (*)	168,436	198,951
Short-term loans	1,400	2,529
	169,836	201,480
Current maturities of long-term liabilities		
Current maturities of loans from banks	447,853	421,188
Current maturities of loans from others	5,165	119,706
Current maturities of bonds	176,367	172,045
Current maturities of bonds convertible into shares in a consolidated company	-	18,598
	629,385	731,537
Total current liabilities	2,445,422	1,772,313

(*) As of December 21, 2011, the liability balance due to the issuance of the unrated marketable securities (the "MSs") amounted to approx. NIS 32 million (as of December 31, 2010 – approx. NIS 69 million). The MSs were issued for a period of one year, which will renew automatically for four additional periods of one year each, paying attention to daily exit points, for which seven business days' notice is to be given in advance and in writing. The MSs bear interest at an annual rate equivalent to the Bank of Israel's interest rate plus 0.8%, which is paid at the end of each year. The principal will be paid at the end of the period or at such time as the exit points are exercised.

On July 1, 2009, the Company announced the issuance of a series of marketable securities, which are rated P-1 by Midroog Ltd., with a volume of up to NIS 135 million for a period of ninety days from the time of the clearing, which will renew automatically for up to nineteen additional period of ninety days each (in accordance with notification, which will be sent to the investors), paying attention to daily exit points, for which seven business days' notice is to be given in advance and in writing, as an off the TASE transaction in accordance with the TASE Directives . The MSs bear interest at an annual rate equivalent to the Bank of Israel's interest rate plus 0.6%, which is paid at the earlier of the end of each period of ninety days or at such time as the exit points are exercised. The principal will be paid at the end of twenty periods of ninety days or on repayment if the period is not renewed, as aforesaid, or at such time as the exit points are exercised. This series has been registered in "Nesher", the TASE's trading system for classified investors (Securities not listed for trading in the TASE) type securities. As of December 31, 2011, the Company has issued the sum of approx. NIS 135 million.

In June 2011, Midroog extended the rating of the MSs which the Company had issued until June 30, 2012 at the P-1 rating, including confirmation of this rating in connection with the expansion of the marketable securities series at this rating in January 2012. For the purpose of securing sufficient liquidity for payment of the MSs, the Company undertook to keep an amount of no less than approx. NIS 135 million in a deposit which may not be offset against a bank loan, whose short-term rating is P-1 and/or in State of Israel Bonds free and clear of charges, until the date of payment of the MSs.

Note 22 Loans and credit from banks and other credit providers (contd.)

A. Current liabilities: (contd.)

After the date of the statement of financial position, in January 2012, Midroog has expanded the rating frame for this series to NIS 200 million.

B. Non-current liabilities:

	As of December 31	
	2011	**2010**
	NIS in Thousands	**NIS in Thousands**
Bonds		
Bonds (1), (2), (3), (4)	1,883,094	2,007,720
Bonds convertible into shares of a consolidated company (5)	-	18,598
	1,883,094	2,026,318
Loans from banks	4,107,782	3,634,844
Other long-term liabilities		
Long-term loans from others	101,988	205,130
Capital notes	1,084	1,057
	103,072	206,187
	6,093,948	5,867,349
Net of current maturities	629,385	731,537
Total non-current liabilities	5,464,563	5,135,812

(1) In March 2007 the Company executed a private issue of bonds (Series A), with a par value of 740 million bonds of par value NIS 1 each to institutional investors. The consideration from the issue amounted to approx. NIS 738 million (after deducting issuance expenses of approx. NIS 2 million). The bonds are linked to the Consumer Prices Index (principal and interest) and bear interest at a rate of 4.8% a year. The Company will repay an amount equivalent to 5% of the amount of the principal (NIS 37 million) in the month of March in each of the years 2008 to 2016 and in March 2017 it will repay an amount that is equivalent to 55% of the amount of the principal (NIS 407 million). The interest payments will be executed once every three months.

For the purposes of this issue, the bonds were rated Aa2 by Midroog and AA/Stable by Standard & Poors Maalot. In September 2009 Maalot announced that the rating for the bonds was being reduced to AA- with a stable ratings outlook. In December 2010, Maalot reconfirmed the rating of the bonds and updated the rating outlook to positive. In November 2011, Maalot upgraded the bond rating to AA/Stable.

Note 22 Loans and credit from banks and other credit providers (contd.)

B. Non-current liabilities: (contd.)

(1) (contd.)

The bonds (Series A) have been registered for trade on the continuous institutional Listing on the Stock Exchange, where the Company is entitled to register the bonds (Series A) for trade on the Stock Exchange, at its sole discretion. The bonds will be repayable immediately if certain conditions exist, including: on receivership, arrears in payments, a change in control, the sale of rights in at least two of the following assets: the Ayalon Mall, Hanegev Mall or the Jerusalem Mall, where as the result of the sale there is a lowering of the rating of the bonds is lowered, as it may be from time to time. The grounds for immediate repayment in respect of a change in control, the sale of at least two of the Group's assets, as aforesaid, and the lowering of the rating of the bonds below BBB+ or an equivalent rating thereof, will be cancelled when the Company's bonds are registered for trading. Within the framework of the issuance of the bonds (Series A), the Company has undertaken not to distribute a dividend to its shareholders, so long as such a distribution would cause a lowering of the rating for the bonds.

The balance the principal and linkage differentials of the bonds (Series A) (net of issuance expenses) as of December 31, 2011 is approx. NIS 694,653 thousand (December 31, 2010 – approx.NIS 719,569 thousand). As of the date of the Financial Statements the Company is in compliance with the contractual restrictions that have been set.

(2) In June 2005 the subsidiary Canit Hashalom issued bonds (Series A) with an overall par value of NIS 500 million, which is repayable (in equal payments for both principal and interest) four times a year, over a period of 10 years with the balance, in the amount of NIS 200 million to be paid in June 2015. The bonds are linked to the Consumer Prices Index (principal and interest) and bear interest at a rate of 4.95% a year. The bonds are not marketable.

The bonds (Series A) were issued in consideration for the payment of their par value. The issuance expenses amounts to NIS 2,545 thousand and their balance as of December 31, 2011 amounted to NIS 966 thousand (as of December 31, 2010 – NIS 1,231 thousand).

For the purposes of this issue, the bonds were rated Aa2 by Midroog Ltd.

As collateral for its liabilities vis-à-vis the holders of the bonds (Series A), Canit Hashalom registered first ranking fixed charges, in an unlimited amounts on various assets belonging to Group companies, whereas of the date of approval of the financial statements the charges are as follows: (a) 16,083,900 ordinary shares with no par value in Otzma & Co. Maccabim Investments Ltd. (a subsidiary; (b) 53,969,250 ordinary shares with no par value in Provident Yield Investments Ltd. (a subsidiary); (c) various bonds that had been issued by the subsidiaries, as aforesaid, which are collateralized by a charge on their rights in the following assets: the entire rights in Herzliya Business Park; 50% of the rights in the Azrieli Mall, Hod Hasharon; 40% of the rights in the Azrieli Holon Mall and 50% of the rights in K.M.T. Petach Tikvah.

The bonds are repayable immediately if certain conditions exist, including, on receivership, an arrears in payments, the sale of more than 50% of the rights in the "Azrieli Center", if an amount of NIS 50 million is not deposited on account of the amount that is to be reserved and which is to be charged in favor of the trustee for the holders of the bonds, within a period of 3 months, as from the beginning of 2013.

In July 2009 Canit Hashalom increased the series of the bonds (Series A) to institutions by approx. NIS 89.5 million par value, for a consideration of approx. NIS 103 million.

Note 22 Loans and credit from banks and other credit providers (contd.)

B. Non-current liabilities: (contd.)

(2) (contd.)

An amount of approx. NIS 44.5 million from the series that was increased will be repaid in equal payments for both principal and interest, four times a year, in accordance with the times and the terms that were set for the original series. The balance, in an amount of NIS 45 million is to be paid in June 2015. The bonds are linked to the Consumer Prices Index (principal and interest) and bear interest at a rate of 4.95% a year. The bonds are not marketable. For the purposes of the increase, the bonds were rated Aa2 by Midroog Ltd.

The balance the principal and linkage differentials of the bonds (Series A) (less issuance expenses) as of December 31, 2011 is approx. NIS 470,840 thousand (as of December 31, 2010 – approx. NIS 503,405 thousand). As of the date of the Financial Statements Canit Hashalom is in compliance with the contractual restrictions that have been set.

(3) During the course of the years 2004 and 2005, Granite issued registered bonds (Series 3 and 4)**,** which are non-marketable (except on the continuous institutional listing) to institutional investors, in an overall amount of NIS 300,000 thousand. The bonds are linked to the Consumer Prices Index, bear semi-annual interest of 5.70% - 6.35% a year and are repayable in seven consecutive equal annual installments, with the addition of linkage differences, in each of the years 2007 to 2013. The bonds (Series 3 and 4) were issued in consideration for the payment of their par value. As collateral for the bonds (Series 3), Granite recorded specific charges on some of its assets and on some of the assets of the subsidiaries. The bonds (Series 3) have been rated by S& P Maalot Ltd. ("Maalot"), such that as of the date of the financial statements the series 3 bonds are rated A+ and the series 4 bonds are rated A+. The rating prospect is stable.

The bonds (Series 3) were issued in accordance with the terms stated in the trust deed that was signed with the Mizrahi Tefahot Trust Company Ltd., which serves as the trustee for the holders of the bonds of that series. The bonds (Series 4) were issued in accordance with the terms stated in the trust deed that was signed with Poalim Trust Services Ltd. which serves as the trustee for the holders of the bonds of that series. In accordance with the trust deeds, the trustees have the right to make the unpaid balance of the bonds repayable immediately if a number of events occur, and inter alia the following events: in the event that Granite does not pay any amount whatsoever that it is required to pay in accordance with the bond, or in the event that Granite breaches the bond or the trust deed or the charge agreement (only for the Series 3 bonds), and the trustee considers this to constitute material damage to the bond holders; in the event that an order is issued for the liquidation of Granite or for the appointment of a receiver, if a receiver is appointed, if an attachment is placed on its principal assets, if Granite ceases to be a public company; if Maalot announces the lowering of the rating of the bonds because of activities carried out by Granite that constitute a significant breach of the terms of the bonds or the trust agreement, if Maalot has announced a downgrading of the bonds to BBB+ and lower, or if Maalot announces the lowering of the rating of the bonds to a rating of BBB+ or below or if the rating the bonds is discontinued because Granite has breached the agreement between Maalot and Granite.

As of the date of the financial statements, Granite is in compliance with the contractual limitations that have been set.

Note 22 Loans and credit from banks and other credit providers (contd.)

B. Non-current liabilities: (contd.)

(4) In July 2007, a consolidated company of Supergas which was established for the purpose of the issue, and to which, primarily, the domestic gas operations and some of the commercial gas operations, for the marketing of gas in moveable containers were transferred, executed an issue of bonds to institutional investors through a private issue, with an overall par value of NIS 600 million. The bonds, which are rated with a rating of Aa1 by Midroog Ltd., are for a period of 18 years, and are repaid in quarterly installments of the principal as from 2010. The bonds are linked to the Consumer Prices Index (principal and interest) and bear interest at a rate of 4.9% a year, which is paid once every calendar quarter. The balance of the bonds is presented after deducting net issuance expenses, which amount to NIS 1,504 thousand as of December 31, 2011 (December 31, 2010 – NIS 1,736 thousand). The effective rate of interest for the bonds is 4.94% a year.

The bonds are secured by a floating charge, in an unlimited amount, on all of the assets of the consolidated company of Supergas, in addition, Supergas charged by a first ranking fixed charge in an unlimited amount all of the shares of the consolidated company owned and held thereby, including the rights deriving from such shares.

According to the bond terms, the consolidated company of Supergas is required to meet financial covenants. Deviation from the financial covenants would allow the holders of the bonds to demand the acceleration of repayment or early repayment as described below.

Accelerated repayment:

a. If the ratio between the average quarterly free cash flows from the domestic gas operations (the cash flow of the receipts from the domestic operations less actual purchases of gas and expenses in respect of the services agreement in respect of the domestic gas operations), for the past year and the quarterly installment (principal and interest) which are expected to be paid to the bondholders at the time of the first expected payment (the "Debt Cover Ratio") falls below 111%.

b. If the rate of the margin on the commercial gas operations in containers falls below 12%.

Collateral acceleration and exercise:

a. If the Debt Cover Ratio falls below 103%.

b. In the event of insolvency.

c. The non payment of a payment of principal or interest.

d. A decision for dissolution or receivership of Supergas' consolidated company.

e. The imposition of an attachment or execution of the entire or material assets of Supergas' consolidated company.

f. A fundamental breach of the terms of the bonds.

g. In the event that Supergas' consolidated company loses the gas license.

h. In the event of a change in control such that Granite ceases, under certain conditions, to control Supergas.

i. The lowering of the rating of the bonds rating below Baa1 or if the rating is not monitored.

Note 22 Loans and credit from banks and other credit providers (contd.)

B. Non-current liabilities: (contd.)

(4) (contd.)

Accelerated repayment: (contd.)

b. If the rate of the margin on the commercial gas operations in containers falls below 12%. (contd.)

Collateral acceleration and exercise: (contd.)

In addition, there are grounds for the replacement of Supergas as a supplier of services in the transaction, the main ones being: if the debt cover ratio falls below 106%; events in which Supergas becomes insolvent or if it loses its gas supplier license.

As of the date of the financial statements, Super gas's consolidated company is in compliance with the covenants.

(5) In 2005 the consolidated company Via Maris signed with Bank Hapoalim an agreement for provision of the required senior financing for the construction of the desalination project, at a total amount of approx. NIS 315 million (which also includes financing for the construction of a power station adjacent to the desalination facility area – insofar as it shall be decided to construct the same) but no more than an amount equal to 78% of the comprehensive investment amount in the facility (the "Original Financing Agreement").

In August 2009, Via Maris signed, within the realization of the extension plan for the facility (see Note 13), a new financing agreement with Bank Hapoalim, incorporating also the provisions of the Original Financing Agreement (the "Incorporated Financing Agreement"), Accordingly, the bank provided financing facilities, in shekels and in foreign currency, for the financing of 90% of the extension costs. The balance of the financing was provided by the shareholders of Via Maris mainly by way of providing inferior shareholders loans.

The Incorporated Financing Agreement determines a series of provisions, representations and warranties including the compliance with several financial ratios, of which principles are: debt coverage ratio of 1.10:1, fixed payment to fixed expense ratio of 1:1, loan lifetime coverage ratio of 1.15:1. The total credit for Via Maris, included in the financial statements, as of December 31, 2011 sums up to approx. NIS 439 million.

As of the date of the financial statements Via Maris is in compliance with the required financial ratios.

After the date of the financial statements, on January 30, 2012, an agreement was signed with Bank Hapoalim to finance another expansion of the desalination plant (see also Note 13 regarding receivables in respect of a franchise agreement), which was closed on March 1, 2012. The agreement integrates the provisions of the original financing agreement, the provisions of the combined financing agreement and further provisions added or amended (the "Second Expansion Financing Agreement"). Accordingly, the bank shall provide financing facilities in NIS and in foreign currency to finance up to 80% of the cost of the second expansion. The balance of the financing shall be provided by the shareholders by way of inferior shareholder loans. The Second Expansion Financing Agreement sets forth a series of provisions, representations and undertakings, including a 5% reduction of the shareholder's financing after completion of the expansion, such that the leverage ratio in respect of the second expansion be 85:15 and the leverage ratio for the entire plant 20:80, as well as compliance with a minimal debt coverage ratio of 1:2:1.

Note 22 Loans and credit from banks and other credit providers (contd.)

B. Non-current liabilities: (contd.)

(5) (contd.)

According to the financing agreement with the bank, any purchase of Via Maris, its assets, shares, rights in respect of the bank account, its IP and all of the project agreements and insurance policies are pledged to the bank.

The Fixed Guaranteed Revenues in respect of an agreement for the desalination facility expansion, in the sum of NIS 3.45 million per month, are linked to several currencies, and the linkage mechanism varies over the term of the agreement (the "Linkage Basket"). The linkage of the Guaranteed Revenues constitutes indemnification against the construction costs in foreign currency, which the Company will be required to bear. In respect of the Linkage Basket mechanism, the Company has separated, on its books, embedded derivatives whose balance as of December 31, 2011 is NIS 1.7 million, and has treated the same at fair value through profit and loss.

Note 22 Loans and credit from banks and other credit providers (contd.)

C. Details in respect of interest and linkage:

			As of December 31			
			2011		2010	
	Linkage	Nominal interest	Par value	Carrying value	Par value	Carrying value
		%		NIS in Thousands		NIS in Thousands
Overdrafts from banks	Unlinked			2,846		1,117
Short-term loans from banks	Unlinked	3.55-5.30		1,505,769		736,700
Short-term loans from banks	Foreign currency	2.40-5.30		137,586		101,479
Short-term loans from other credit providers	Index	4.00		1,400		2,529
Marketable securities	Unlinked	Bank of Israel + 0.8		168,436		198,951
Bonds that are not convertible into shares	Index	Bank of Israel + 0.6 4.80-6.30	1,609,799	1,883,094	1,760,587	2,007,720
Bonds that are convertible into shares in a consolidated company	Index	9.50	-	-	20,420	18,598
Long-term loans from banks	Index	1.07-4.00		255,718		239,205
Long-term loans from banks	Index	4.00-7.00		2,645,505		2,796,342
Long-term loans from banks	Unlinked	4.25-7.60		612,347		524,573
Long-term loans from banks	Linked to the Dollar	4.35-6.00		594,212		74,724
Liabilities in respect of finance leasing	Index	4.50-8.00		7,625		9,301
Liabilities in respect of finance leasing	Unlinked	5.80-9.40		9,868		14,700
Liabilities in respect of finance leasing	Linked to the Dollar	8.00		40,691		38,188
Capital notes	Unlinked	-		1,084		1,057
Other long-term loans	Index	4.20-5.50		2,596		31,291
Other long-term loans	Foreign currency	5.51		90,174		173,839
Other long-term loans	Unlinked	4.75		10,000		
Other long-term payables	Index	-		1,397		38,131
Other long-term payables	unlinked	-		1,530		1,090
Total loans and credit from banks and other credit providers			1,609,799	7,971,878	1,781,007	7,009,535

See Note 35 for details in respect of loans that are secured by charges.

Note 22 Loans and credit from banks and other credit providers (contd.)

D. Contractual restrictions and financial covenants in the Company:

(1) If certain conditions exist, as detailed in the loan agreements (primarily at the time of a change in the structure and the control in the Company, arrears in payments, receivership and a worsening of the value of the collateral), the banks are entitled to make the amount of the loans repayable immediately. The total sum of credit for which the Company committed for the aforesaid terms amounted as of December 31 ,2011 to approx. NIS 1,450 million.

As of the date of the financial statements, the Company is in compliance with the contractual restrictions that have been set.

(2) See Note 14F in respect of the Company's commitment to a banking entity in connection with loans that were extended to finance the acquisition of "Azrieli Givatayim" Mall.

E. Contractual restrictions in Canit Hashalom:

If certain conditions exist as detailed in the loan agreements (primarily at the time of a change in the structure and the control in the Canit Hashalom, arrears in payments, receivership and a worsening of the value of the collateral), the banks are entitled to make the amount of the loans repayable immediately. The total sum of credit for which Canit Hashalom committed for the aforesaid terms amounted as of December 31 ,2011 to approx. NIS 1,010 million.

As of the date of the financial statements, Canit Hashalom is in compliance with the contractual restrictions that have been set.

F. Contractual restrictions and financial covenants in Granite:

(1) During December 2011, Granite signed financing agreements with banking corporations, which include various undertakings, including undertakings to meet financial covenants in the total sum of NIS 125 million for payment in December 2012 that are described in Section 2 below and additional financial covenants as follows:

[1] The amount of the equity, net of the non-controlling interest component, shall be no less than NIS 650,000 thousand, linked to the Index that was published on December 15, 2011.

[2] The rate of the equity out of the total statement of financial position of Granite (standalone) shall be no less than 50%.

[3] The total financial credit (bank credit and bonds) in Granite (standalone) shall not exceed NIS 400,000 thousand.

Granite has further undertaken, over and above the pledge of the holdings in Tambour as provided in (2) below, not to pledge or charge any asset in favor of any third party, not to give any guarantee in favor of any third party and not to undertake to give and/or create any pledge and/or charge and/or guarantee without the banking corporations' prior written consent.

As of the date of the financial statements, Granite is in compliance with the required covenants.

(2) In 2004, and as part of the outline for the reduction of the capital in Tambour, agreements were signed between Granite, Tambour, and a banking corporation (in this section: the "Bank") and an additional bank (the "Additional Bank"), which purchased 30% of the credit risk that Granite has taken up in 2001 (jointly, the "Banks"), which organize the endorsement of the credits and the terms of the remaining credit and the endorsed credit (the " Endorsement Agreements").

In 2009 and in December 2011 (see Note 22F(1) above), Granite signed agreements with the Bank, which change some of the terms of these agreements.

Note 22 Loans and credit from banks and other credit providers (contd.)

F. Contractual restrictions and financial covenants in Granite: (contd.)

(2) (contd.)

In accordance with the Endorsement Agreements (after modifications) and as collateral for the remaining credit, which sums up as of the date of the report to NIS 45 million (for payment until 2013), all of Granite's holdings in Tambour were pledged. Nowadays, Granite received the Banks' consent to release some of the pledged shares, such that the remaining of the pledged shares will constitute 51% of the interests in Tambour. Granite is acting to complete the formal proceedings that are required for the purpose of releasing some of such shares.

As collateral for the charge, Granite's shares in Tambour were transferred on behalf of the Bank's trust company (the "Trust Company"), which holds the shares in trust for the Bank as the holder of the charge and for Granite as owner of the shares.

The Trust Company has provided Granite with a power of attorney according to which Granite is entitled to participate and vote at the general meetings of Tambour and to execute Granite's rights as a shareholder (in this section: the "General Power of Attorney"). Granite is not entitled to use the General Power of Attorney, and the Trust Company is entitled to cancel it or to give the Bank itself a power of attorney to participate and to vote at the general meetings of Tambour in cases in which any events have occurred which are grounds for immediate repayment in accordance with a document that was signed with the Bank.

The General Power of Attorney does not apply to certain decisions which are not in the ordinary course of business of Tambour, in respect of the said certain decisions, Granite will be required to approach the Trust Company in order to receive a specific power of attorney. The Trust Company will be entitled to refuse to give the specific power of attorney, or to make it conditional or to give it to the Bank itself.

The current management of the holdings of the Tambour shares is performed by Granite without need for update or obtaining the banks' approval. In addition, Granite was granted a specific power of attorney for the specific decisions which were adopted, in respect of which such specific power of attorney was required, to vote according to its discretion, including regarding transactions with related parties.

In addition, any amount that will be paid to Granite by Tambour as dividends, as management fees, which exceed the existing amount upon such date, or in any other way whatsoever or on any other grounds whatsoever, will be used solely and exclusively for the purpose of the repayment of the remaining credit. This provision will not apply to certain payments, which include directors fees for directors who are appointed in Tambour on the Company's behalf, nor to payments for commercial transactions, in the ordinary course of business and at market terms, between the Group and Tambour.

The Bank will be entitled to demand the immediate repayment of the remaining credit, upon the occurrence of irregular events that were defined.

In respect of the remaining credit, whose balance as of the date of the report is approx. NIS 45 million, Granite undertook to comply with financial covenants whose principles are as follows:

[1] The amount of equity of Granite (consolidated), plus liabilities due to customer deposits, shall at all times be no less than NIS 450,000 thousand, Index-linked as from the Index published on January 15, 1999 (approx. NIS 585,190 thousand as of December 31, 2011).

Note 22 Loans and credit from banks and other credit providers (contd.)

[2] The share of the equity, plus deposits from customers, out of the total assets in the consolidated statement of financial position, net of the Fuel Administration Balance and net of receivables in respect of a franchise agreement, shall be no less than 15%, provided that for any decline below 17%, a special report shall be given by Granite's auditor, quantifying the amount of the effect of the rise in fuel prices since March 2004 on the inventory and trade receivables items, and that the ratio net of such effect is equal to or higher than 17%.

[3] The ratio of Granite's holdings value in Tambour's shares and the remaining credit balance shall be no less than 3.

As of the date of the financial statements, Granite is in compliance with the required covenants.

G. Contractual restrictions and financial covenants in Tambour:

(1) During year 2009 and 2010 the consolidated company Tambour signed on new financing agreements with banks that have made credit available to it, which include a change in the original financial stipulations, which it had signed on. The following are the main stipulations that are in effect:

a. Tambour's tangible capital is not to fall below an amount of NIS 150 million. For this matter, tangible capital is the capital as presented in the financial statements, less rights which do not confer control and net of intangible assets.

b. The ratio of the tangible equity and the total amount of the statement of financial position is not to fall below 20%.

For this matter, the total amount of the statement of financial position in accordance with the financial statements less goodwill and less intangible assets as defined in the agreement.

c. The total of Tambour's financing liabilities divided by the cumulative amount of the EBITDA for the four sequential consecutive quarterly periods ending on the date of the last financial statements, is not to exceed 7.5 up to December 31, 2011, is not to exceed 7.0 up to December 31, 2012, is not to exceed 6.5 up to December 31, 2013, is not to exceed 6.0 up to December 31, 2014 and is not to exceed 5.5 as from January 1, 2015.

Financing liabilities – liabilities to banking entities, including bonds and guarantees to third parties that have been issued at the company's request.

d. Tambour's overall financing liabilities are not to exceed NIS 500 million.

e. The cumulative amount of the operating profit, as defined in the agreements that were signed, throughout the four sequential consecutive quarterly periods ending on the date of the last financial statements, is not to be less than NIS 30 million.

f. The cumulative amount of the EBITDA, as defined in the agreements that were signed, throughout the four sequential consecutive quarterly periods ending on the date of the last financial statements, is not to be less than NIS 50 million.

g. The overall amount of Tambour's financing liabilities less 2/3 of the debts due from customers by comparison with the EBITDA is not to exceed 5.5.

The abovementioned liabilities will be reviewed each quarter on the basis of the latest quarterly financial statements. A deviation of up to 10% (the "Permitted Deviation Rate") in each of the covenants that are detailed above will not be considered to be a deviations from the said undertakings and solely that in the following quarter there was no deviation at all. A deviation of more than the permitted rate will be considered to be a breach of the covenants. The total credit on which such covenants apply sum up as of December 31, 2011 to approx. NIS 338 million.

As of the date of the financial statements, Tambour is in compliance with the financial covenants that have been set.

In addition, the aforesaid agreements include restrictions in connection with the distribution of a dividend by Tambour, as detailed below:

a. No dividend is to be distributed without the agreement of the bank in advance and in writing, before the publication of the financial statements as of December 31, 2011.

b. After December 31, 2011, Tambour shall not declare, distribute or pay a dividend in any manner whatsoever to its shareholders, unless all of the following cumulative pre-conditions are met:

[1] The distribution and/or the payment of the dividend is to be made out of Tambour's net profit for the reporting period, and solely that the dividend does not exceed fifty percent of the net profit for that period.

[2] The debt service ratio for the last four sequential consecutive quarterly periods which preceded the date of the distribution of the dividend and for the two periods of half a year that immediately follow the period in respect of which it is distributed, is not to be less than 1.1.

Debt service ratio- the ratio between the EBITDA and the total financing and current tax expenses for the same period, with the addition of the current maturities (within the meaning of that term in the financial statements).

[3] In a year in which the financial debt, as defined in the agreements that were signed is equal to or exceeds NIS 300 million, no dividend is to be distributed, except with the agreement of the bank.

[4] No distribution of a dividend that derives from the revaluation of assets is to be made.

c. After the date of the financial statements, in January 2012, Tambour received the consent of the banks with which it works to the distribution of a NIS 12 million dividend in the second quarter of 2012, insofar as such distribution is approved by Tambour's competent organs, even though Tambour is not in compliance with all of the financial covenants as described above, in connection with the dividend distribution.

(2) Within the framework of the credit endorsement documents from Granite to Tambour, certain irregular events were determined, the occurrence of which will give the Banks the right to demand the immediate repayment of the credit.

H. Contractual restrictions and financial covenants in Sonol:

During 2011, Sonol signed with a banking corporation that provided it with credit a financing agreement that includes financial covenants, the main ones being:

(1) The net financial debt to CAP ratio (net financial debt plus the equity) shall not exceed 0.9.

(2) The net financial debt to EBITDA ratio (with certain adjustments) shall not exceed 12.

The sum of the credit to which the said covenants apply amounts, as of December 31, 2011, to approx. NIS 182 million (out of which approx. NIS 140 million long-term).

As of the date of the financial statements, Sonol is in compliance the first covenant and has received a letter of waiver from the bank for the second covenant.

After the date of the report on March 12, 2012, the bank notified Sonol that the authorized organ in the bank approved an amendment to the covenants. Accordingly, the Company's management estimate, based on Sonol's management estimate, that Sonol shall be in compliance with the covenants during 2012.

I. Contractual restrictions and financial covenants in GES:

For securing GES's undertakings to banking corporations, GES had undertaken to comply with financial covenants, as specified below:

(1) Minimum equity in the sum of NIS 116 million.

(2) Minimum ratio of equity to the total assets at a minimum rate of 30%.

Inferior shareholders' loans will be added to the amount of the capital in an amount no less than NIS 90 million.

As of the date of the financial statements, GES is in compliance with the aforesaid financial covenants and other stipulations to the banking corporations. The total credit to which such stipulations apply amounts, as of December 31, 2011, to approx. NIS 24 million. For financial covenants in Via Maris see Section B(6) above.

J. In the matter of terms and conditions of the loan for the purchase of three office buildings in Texas in 2011 – see Note 14I(3).

K. Other Liabilities:

	As of December 31	
	2011	**2010**
	NIS in thousands	**NIS in thousands**
Liabilities for financing lease	58,184	62,189
Other	41,938	39 ,221
	100,122	101,410

Information pertaining to liabilities in respect of finance leasing according to segmentation of payment dates:

	As of December 31, 2011		
	Minimum future lease fees	**Interest component**	**Current value of minimum lease fees**
	NIS in thousands	**NIS in thousands**	**NIS in thousands**
Less than a year	5,763	2,043	3,720
One year to	23,026	11,868	11,158

five years			
More than five years	81,057	34,031	47,026
	109,846	47,942	61,904

	As of December 31, 2010		
	Minimum future lease fees	**Interest component**	**Current value of minimum lease fees**
	NIS in thousands	**NIS in thousands**	**NIS in thousands**
Less than a year	6,140	2,256	3,884
One year to five years	24,613	11,560	13,053
More than five years	97,525	48,389	49,136
	128,278	62,205	66,073

Note 23 Benefits for employees

Employee benefits include post-employment benefits, other long-term benefits, benefits upon the termination of employment, short-term benefits and also share-based payments.

In respect of post-employment employee benefits, the Group has defined benefits plans, in respect of which it deposits amounts in appropriate severance pay funds and insurance policies. Moreover, the Group has a defined deposit plan in respect of some of its employees, with regard to whom section 14 of the Severance Pay Law, 5723-1963 applies.

See Note 25 in respect of share-based payments.

	As of December 31	
	2011	2010
	NIS in thousands	NIS in thousands
Present value of unfunded liability (1)	14,134	16,496
Present value of funded liability (1)	32,329	28,611
Total present value of liability	46,463	45,107
Fair value of the plan assets (1)	30,289	28,400
Liability recognized in respect of defined benefit plan	16,174	16,707
Liability in respect of other short-term benefits	48,435	46,715
Liability in respect of other long-term benefits (2)	10,581	7,596
Liability in respect of termination of employment (early pensions)	23,719	27,488
Liability in respect of share-based payment	14,154	14,587
Total employee benefits	113,063	113,093
Presented under the following items:		
Investments and loans – assets in respect of employee benefits	(1,420)	(1,081)
Other payables	55,171	59,863
Long-term employee benefits	59,312	54,311
	113,063	113,093

(1) Actuarial assumptions

The main actuarial assumptions as of the reporting date (according to the weighted average):

	2011	2010	2009
	%	%	%
Cap rate as of December 31 (A)	2.81 - 5.08	3.83-5.27	3.36-5.7
Expected yield on plan assets as of January 1 (A)	4.12 - 5.03	4.5-5.5	4.70-5.5
Rate of future salary increases	1.86 - 4.00	2.78-3.81	4.0

a. The expected capitalization and yield rates on the plan assets are based on unlinked Israeli government bonds, which bear fixed interest.

b. The calculations are based on the following demographic assumptions:

[1] The mortality rate is based on published statistical data and on generally acceptable mortality tables.

[2] The rate at which employees leave is based on an analysis of past data.

(2) Liabilities for other long-term benefits

	As of December 31	
	2011	2010
	NIS thousands	NIS thousands
Liability in respect of sick leave	1,486	1,449
Liability in respect of seniority and adjustment grant	9,095	6,147
	10,581	7,596

Note 24 - Capital

A. The share capital and share rights as of December 31, 2011 and 2010:

	Registered		Issued and paid up	
	As of December 31		As of December 31	
	2011	2010	2011	2010
	NIS	NIS	NIS	NIS
Ordinary shares of par value NIS 0.1	12,750,150	12,750,150	12,127,276	12,127,276

Every ordinary share of NIS 0.1 par value fully paid grants the right to participate to vote at general meetings. Every shareholder will have one vote for every share he owns, which is fully paid up. All the shares have equal rights relating to the amounts of capital paid or credited as paid on their par value, and everything connected with distribution of dividend, bonus shares and any other distribution, repayment of capital and participation in the distribution of the Company's surplus assets upon liquidation.

B. Dividend distribution policy:

In May 2010, the Company' Board of Directors approved a policy for the distribution of dividends in the Company, subject to any law and the Company's needs, whereby each year, upon the publication of the Company's annual financial statements or thereafter, the Company will distribute to its shareholders a dividend at a rate of 35% of the Company's net income, according to these annual statements, and subject to the Company's cash flow situation, and its need for cash to finance its operations as existing at that time and/or the future expected and/or planned operations, and all as will be examined at the sole discretion of the Company's BOD.

In March 2011, the Company's BOD determined that until the receipt of another decision, in view of the Company's main operations in income-producing property, a dividend will be distributed from the Company's net profit, subject to any law and the Company's needs, net of revaluations and net of the tax effect thereon, and also taking into consideration other indexes typical to income-producing property companies such as the FFO Index.

The amount of the dividends distributed in the future is expected to be affected by the Company's profits and operation needs, including investments and business opportunities when the investment in them is likely to reduce the liquidity.

In addition, the Company's BOD decided that the Company will include in its periodic and/or quarterly statements, as the case may be, disclosure regarding any decision in connection with implementation of this decision and policy. In addition, the Company's BOD may reexamine and change, at any time, the dividend distribution policy, and all at its sole discretion.

On March 29, 2011, the Company's Board of Directors decided upon the distribution of a dividend in the sum of NIS 240 million (NIS 1.98 per share) that was paid on April 27, 2011.

Note 25 - Share-Based Payments

A. In May 2010 the Company's board of directors and the general meeting of the shareholders approved a phantom unit allotment plan ("Phantom Units") at a total value of approx. NIS 28 million to be allotted to 32 senior officers of the Company (with the exception of the chairman of the Company's board of directors and the deputy chairman of the Company's board of directors) and employees of the Company (the "Plan"). The Phantom Units that will be granted as aforesaid by virtue of the Plan will entitle the Offerees to cash monetary compensation which derives from the rise in the value of the Company's shares, based on the mechanism specified in the Plan. The Company's board of directors confirmed that the base price will be the price of the share that will be determined in a tender in which the Company's shares were offered.

The compensation in respect of the exercised Phantom Units will be the amount which derives from multiplying the number of units in respect of which an exercise notice shall have been delivered by the compensation per unit, which is the difference between the base price (which is, as aforesaid, the share price to be determined in the tender) and the average price of the Company's share, as determined upon the conclusion of the 30 trading days which preceded the exercise date. Upon the allotment of units by virtue of the Plan, the financial value of the Phantom Units shall be calculated according to the Black-Scholes formula, considering the price per share to be determined in the tender (according to which the base value will also be determined), the expected lifespan for exercise of the units (which will be determined as an average between the unit vesting period in each one of the installments and the period for expiration thereof), a standard deviation to be calculated based on historic standard deviations of share yields of the Company and similar companies as well as interest rates for capitalization to be determined according to yield figures for redemption of risk-free NIS assets with a similar lifespan, as shall be published by the Bank of Israel in proximity to the date of the allotment.

The Phantom Units will be granted in three equal installments, commencing one, two and three years after the date of allotment thereof, and the right to exercise the same will be valid for a period of two years from the date of release of each installment.

The Plan sets forth accepted instructions for adjustment of the base price of the Phantom Units, or the number of Phantom Units, in cases of the distribution of a dividend, the distribution of stock dividends, rights offerings by the Company to its shareholders, capital split or consolidation, the performance of merger or split transactions or any other restructuring, as the case may be.

On June 10, 2010 the foregoing Phantom Units were granted according to the share price which was determined in the tender and amounted to NIS 83.25 per share.

As of December 31, 2011 this cost is estimated, before tax, at approx. NIS 21 million (including options granted in 2011 to the Company's CEO, whose office commenced on April 1, 2011, see below). The parameters used for the estimate were the average closing price of Azrieli Group's stock in the 30 trading days before December 31, 2011, which was NIS 88.31 per share, the average standard deviation of the three installments is 28.30% (which constitutes a weighted average of the standard deviation of the share of the Company and of companies in an operating segment similar to that of the Company, which are traded on TASE), and an average risk-free interest rate of 2.76% (based on the yield to maturity of a government bond with a similar lifespan). The cost recognized in the Income Statement in the year ended on December 31, 2011 amounts to the sum of approx. NIS 1.5 million before tax (in 2010 - approx. NIS 9.8 million).

Similarly to the terms and conditions of the existing plan at the Company, in April 2011 the management company, which is wholly owned by the Company's CEO, was granted 284,527 Phantom Units of a total value of approx. NIS 9 million according to a base price that was determined according to an average share price, in March 2011, of NIS 98.09 (see also Note 40C(7)).

The parameters used to evaluate the cost of the phantom units granted to the CEO as of December 31, 2011 are the closing rate as aforesaid, an average standard deviation of the three installments of 26.18%, and an average risk-free interest rate of 2.88%. The cost carried to the income statement in the year ended December 31, 2011 amounts to approx. NIS 1.5 million before tax.

As of December 31, 2011, 27,485 options were exercised by officers.

B. Allocation of options to Granite's CEO:

On March 17, 2010, Granite's audit committee and board of directors approved a share-based payment transaction, payable in cash (phantom) of 2,238,677 units to Granite's CEO, which entitle him to monetary compensation which is derived from the appreciation of Granite's share value, based on the mechanism specified in the plan. The number of phantom units, had they been options exercisable for Granite's shares after allotment thereof, constitute 1.5% of Granite's issued and paid-up share capital, on a fully diluted basis, as of the date of grant thereof.

The right to exercise the phantom units is conferred in three installments on three dates as follows:

One third is exercisable from September 1, 2010;
One third are exercisable from September 1, 2011; and
One third is exercisable from September 1, 2012.

The options are exercisable, subject to the terms of the plan, from the date of vesting of each installment, and for 24 months from the date of grant of the last installment.

The compensation in respect of the Phantom Units exercised is the amount resulting from a multiplication of the number of units in respect of which an exercise notice is being given, by the compensation per unit, which is the difference between the exercise price which was originally set at NIS 8.5 per unit (subject to adjustments), and the share price on TASE on the date of the exercise notice. As of December 31, 2011, the exercise price, adjusted to dividend distributions is NIS 8.23. On the date of approval, the cost of the grant, before tax, was estimated at approx. NIS 8.2 million.

The cost of grant of the Phantom Units to the CEO is carried to the income statement over the vesting period of each installment, from January 1, 2010, the date of commencement of the benefit period. The cost is updated in each reporting period according to the relevant parameters at the end of the period. In respect of this cost, Granite will be entitled to a tax benefit.

As of December 31, 2011, this cost is estimated, before tax, at approx. NIS 0.7 million. The parameters that were used for the estimate were the closing price of Granite's share on December 31, 2011, which was NIS 4.6 (2010 – NIS 8), a standard deviation of 33% (2010 – 42%), and a risk-free interest rate of 2.9% (2010 – 3.7%) (based on yield-to-maturity of government bonds having a similar lifetime). The revenue carried to the income statement in the year ended December 31, 2011, amounts to approx. NIS 3.4 million (in the year ended on December 31, 2010 an expense of approx. NIS 4.1 million was carried).

C. Allocation of options to the Granite's Chairman of the Board:

(1) In 2007, 2,797,715 non-negotiable options were granted to Granite's Chairman of the Board (who also serves as Active Deputy to the Company's Chairman of the Board, hereinafter: the "Offeree"), on the basis of the option plan for employees and officers of Granite and/or of Granite's subsidiaries, which was adopted by Granite's Board of Directors at that time (the "Plan"). The options are exercisable into 2,797,715 ordinary shares of NIS 1 par value each in Granite (subject to adjustments), in consideration for an additional amount payable on exercise of NIS 8.366 per option, linked to the Consumer Price Index. The exercise price which is adjusted after adjustment due to dividend distribution is NIS 9.45, in practice however, the Offeree will not be allotted all of the shares deriving from each option but only shares reflecting the amount of the financial benefit incorporated (the profit to the Offeree) in the option as calculated on the exercise date.

The cost of the granting of the options to the Chairman of Granite amounted at the date of the grant to approx, NIS 8.7 million (not including change of options terms, as specified in Section 2 below).

The options were allotted on the capital gains tax track, within the meaning thereof in Section 102(b)(2) of the Income Tax Ordinance.

(2) In 2009 Granite's general meeting and board of directors approved a change in the terms of the options that were granted to the Chairman of the Board, such that the period for their exercise was extended. The right to exercise the options into ordinary shares of Granite in respect of the remaining three installments that have not expired upon such date that amounted to 2,098,286 options was extended until December 6, 2012. The economic value of the change in the terms of the option amounts to approx. NIS 1.4 million and has been credited as an expense in 2009.

As of the date of the report, no options were exercised.

D. Allocation of options in Tambour:

(1) In May 2004 Tambour's Board of Directors approved a plan for the issuance of options for the purchase of ordinary shares of par value NIS 1 each in Tambour, to employees, directors, advisors and other service providers.

In accordance with the said plan, Tambour allocated 1,610,000 options for exercise into ordinary shares of Tambour in a ratio such that each option will be exercisable into one ordinary share of NIS 1 par value, in consideration for a cash payment of NIS 4 (unlinked) for each option warrant (after an adjustment made as the result of the distribution of a dividend).The options can be exercised in three equal installments, after two, three and four years from the allocation date, subject to the crystallization of the entitlement of the employee.

Options that will not be exercised by the end of ten years from the allocation date will expire. The average fair value as determined at the time of the grant was NIS 2.21 per option warrant for the Chief Executive Officer and NIS 2.04 per option for the other senior employees.

On December 31, 2011, the balance of the options exercisable into shares of Tambour are held by Tambour's CEO and amount to 60 thousand (December 31, 2010 - 60 thousand, December 31, 2009 - 470 thousand).

(2) Number of options and the weighted average of the exercise price

	Weighted average of the exercise price (1)	Number of options (in thousands)	Weighted average of the exercise price (1)	Number of options (in thousands)
	2011	2011	2010	2010
Balance as of January 1	3.836	60	3.836	470
Exercised during the year		-		410
Balance as of December 31 (2)		60		60
Exercisable as of December 31		60		60

(1) After adjustment in respect of the distribution of a dividend.
(2) The weighted average of the remaining contractual lifetime of options in circulation on December 31, 2011 is 3 years (2010: 4 years).

E. Phantom-type share based payment to the CEO of Tambour:

In July 2010, the audit committee and board of directors of Tambour approved a designated, phantom-type (cash) compensation plan for the incumbent CEO of Tambour through a private company wholly owned by him (the "CEO"), in the context of which 810,528 phantom units were granted, to be paid in cash in the following manner and under the following conditions:

(1) The payment per unit will be made according to the excess share price on the date of exercise thereof over an exercise price of NIS 5 per share. The plan further provides for adjustments for cases such as: dividend distributions, the distribution of stock dividends, rights offerings to the shareholders, the performance of merger transactions, etc.

(2) The phantom units shall vest and be exercisable in three equal installments every year, on December 31, 2010, December 31, 2011 and December 31, 2012.

(3) The phantom units shall expire 24 months after the vesting date of each installment.

(4) The tax liability in respect of the plan shall be borne by the CEO.

The cost of the benefit, as of December 31, 2011, based on the Black-Scholes Model, is estimated at approx. NIS 0.6 million (2010 – NIS 1.7 million), based on a share price of NIS 4.66 (2010 – NIS 5.96), expected volatility of 31%-32% (2010 – 32-36%), an expected lifetime of each unit until the date of expiry thereof and a risk-free interest rate of 1.8%-3% (2010 – 2.8%-3.5%).

In March 2011, Tambour's CEO exercised 135,088 phantom units.

The liabilities in accordance with the plan as of December 31, 2011 amount to sum of NIS 444 thousand (as of December 31, 2010 – NIS 738 thousand) and the salary's revenues recorded during the year, amount to the sum of approx. NIS 70 thousand (2010 – salary expenses in the sum of NIS 738 thousand).

F. Compensation expenses (revenues) in respect of share-based payment arrangements and further details:

	For the Year ended on December 31,		
	2011	2010	2009
	NIS in Thousands	NIS in Thousands	NIS in Thousands
Compensation expenses (revenues) in respect of share-based payment bonuses which are paid in the capital instruments of the Group	-	16	2,403
Compensation expenses (revenues)in respect of share-based payment bonuses which are paid in cash	(212)	14,640	-
Total expenses (revenues) recorded as salary's expenses in respect of share-based payments	(212)	14,656	2,403

Note 26 Income

The Composition:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Income	10,678,354	9,257,828	8,142,280
Net of government levies	3,131,084	2,913,906	2,612,305
Net income	7,547,270	6,343,922	5,529,975
Composition of the income, net:			
Sales	6,100,096	5,075,358	4,418,161
Services	39,384	42,573	40,142
Rental, management and maintenance fees	1,255,966	1,105,292	1,007,580
Construction contracts	53,611	43,093	62,662
Franchise agreements (*)	98,213	77,606	-
Other activities	-	-	1,430
Total income	7,547,270	6,343,922	5,529,975

(*) Do not include income in respect of the permanent component of the water price in the sum of approx. NIS 42 million in 2011 (in 2010 – approx. NIS 36 million) which was recorded as financing income for the financial asset.

Note 27 Cost of income

The composition:

	For the year ended December 31		
	2011	2010	2009
	NIS thousands	NIS thousands	NIS thousands
A. According to the sources of income:			
Sales	5,050,992	4,025,501	3,406,196
Services	32, 770	36,953	35,238
Rental, management and maintenance fees	266, 842	216,684	206,206
Construction contracts (B)	44,016	43,495	58,364
Franchise agreements	77,572	65,668	-
Other activities	-	-	1,309
	5,472,192	4,388,301	3,707,313
B. According to its components:			
Oil distillates and other material consumed	5,052,317	3,945,977	3,285,738
Labor and external work (*)	144,150	156,943	145,721
Depreciation and amortization	36,865	42,060	46,671
Production expenses and others	294,129	250,888	237,513
	5,527,461	4,395,868	3,715,643
Less increase/plus decrease in inventory of work in progress	(819)	896	(527)
Less increase/ plus decrease in inventory of finished goods	(54,450)	(8,463)	(7,803)
	5,472,192	4,388, 301	3,707,313

(*) For 2011 – including a sum of approx. NIS 581 thousand for share based payment (for 2010 - NIS 3,217 thousand).

Note 28 Sales and marketing expenses

The composition:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Wages, salaries and related expenses	251,410	243,963	232,940
Automatic fuelling and commissions paid	25,852	23,970	21,973
Advertising	29,990	31,048	29,022
Depreciation and amortization	82,559	82,345	77,797
Maintenance of buildings, facilities and fuelling stations	44,114	45,251	43,107
Rental fees and municipal taxes	210,457	202,280	189,937
Haulage and maintenance of commercial motor vehicles	68,518	62,200	58,156
Other sales and marketing expenses	51,750	51,030	48,530
	764,650	742,087	701,462

Note 29 Administrative and general expenses

The composition:

	For the year ended December 31		
	2011	2010	2009
	NIS thousands	NIS thousands	NIS thousands
Wages, salaries and related expenses	80,626	84,341	89,699
Share based payments	(865)	11,423	2,403
Consultancy, legal and audit fees	43,085	36,043	22,285
Provision for bad and lost debts	2,715	10,727	21,000
Depreciation and amortization	14,482	13,512	14,986
Management fees to related parties	21,132	24,866	26,859
Other administrative and general expenses	39,113	44,118	37,601
	200,288	225,030	214,833

Note 30 - Other income

The composition:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Dividends received from investments in available for sale financial assets (see also Note 12)	44,564	26,133	17,026
Capital gain from the sale of fixed assets	570	777	1,303
Profit from the sale of available for sale financial assets (2)	1,702	22,265	434
Profit from the acquisition of shares in investee companies (3)	-	2,884	-
Profit from waiving conditional consideration in an acquisition of a consolidated company (1)	5,733	-	-
Miscellaneous	2,039	4,226	9,114
	54,608	56,285	27,877

(1) In October 2010, a transaction was closed between the consolidated company GES and Orlev Industries and Works 2000 Ltd. ("Orlev") whereby GES acquired the holdings (100%) of Orlev in GES Plant Operation Ltd. (formerly Nitron Chemtec Ltd.).

In March 2011, an addendum was signed to the agreement for the sale of the shares whereby the seller waived payment of the consideration. As a result of the aforesaid, the Group recorded a profit in the sum of approx. NIS 5.7 million.

(2) On March 8, 2010 Granite and Sonol sold their holdings in Haifa Basic Oils Ltd. (14%) which was presented in the Statement of Financial Position as a financial asset available for sale, to Oil Refineries Ltd. in consideration for an amount of approx. NIS 35.6 million. The capital gain from the transaction amounted to approx. NIS 22.3 million before tax, and to approx. NIS 16.4 million, after tax. In 2011 – see Note 12A(3).

(3) In 2010, a profit was recorded from the acquisition of shares in a held company and a profit from revaluation of a previous holding in an associate due to a rise to control. In 2009, a profit was recorded from negative goodwill due to the acquisition of 22.1% of the share capital of Via Maris.

Note 31 – Other Expenses

The composition:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Impairment in respect of fixed assets and intangible assets	1,620	579	1,596
Amortization of investments in associates	73	-	166
Settlement arrangement in respect of claim	1,496	-	-
Loss from realization of investment in associates	-	209	1,175
Capital loss from realization of fixed assets	2,187	2,282	1,008
Capital loss from realization of investment property	-	-	4,650
Miscellaneous	2,128	972	888
	7,504	4,042	9,483

Note 32 Financing revenues and expenses

The composition:

	For the year ended December 31		
	2011	2010	2009
	NIS thousands	NIS thousands	NIS thousands
Financing income			
Income from interest on loans and receivables	17,130	22,063	25,958
Financing income from financial asset for franchise arrangement	41,946	36,178	-
Financing income from suppliers	229	364	63
Profit from changes in exchange rates, net	-	21,069	3,656
Income from interest on deposits in banks	5,848	4,989	2,246
Income from interest from the Income Tax Authority	929	1,390	5,037
Net change in the fair value of the conversion component of bonds	42	120	-
Net change in the fair value of held for sale financial assets	764	41,199	11,210
Interest and dividend from financial assets held for trade	-	23,709	-
Change in the fair value of derivative financial instruments	33,975	-	15,964
Other financing income	798	554	3,186
Financing income credited to the profit and loss	101,661	151,635	67,320
Financing expenses			
Interest expenses on loans	510,098	453,660	467,661
Net Loss from changes in exchange rates	30,809	-	1,260
Change in the fair value of derivative financial instruments	4,494	44,505	19,922
Net change in the fair value of available for sale financial assets, designated as at fair value through profit and loss	1,374	5,288	-
Net change in the fair value of financial assets held for trade	100,193	-	-
Interest and dividend from financial assets held for trade	(66,189)	-	-
Change in fair value of embedded derivatives	1,700	-	-
Miscellaneous bank expenses and charges	11,248	9,081	7,439
Linkage on deposits from customers	3,611	3,242	5,502
Other financing expenses	4,650	4,024	7,201
Financing expenses	601,988	519,800	508,985
Less capitalized credit costs	(10,829)	(5,363)	(16,850)
Financing expenses carried to the income statement	591,159	514,437	492,135
Net financing expenses carried to the income statement	489,498	362,802	424,815

Note 33 Taxes on income

A. Details in respect of the tax environment in which the Group operates:

(1) Amendments to the Income Tax Ordinance and the Land Betterment Tax Law

a. On July 25, 2005 the Knesset passed the Law for the Amendment of the Income Tax Ordnance (No. 147), 5765-2005, which determined, inter alia, the gradual reduction of the tax rate for companies to 25% in the 2010 tax year and thereafter.

On July 14, 2009, the Knesset passed the Economic Efficiency Law (Amendments to Legislation for the Implementation of the Economic Plan for the Years 2009 and 2010), 5069-2009, which determined, inter alia an additional gradual reduction of the tax rate for companies to 18% in the tax year 2016 and thereafter. In accordance with the said amendments, the tax rates for companies that apply in the tax year 2010 and thereafter, are as follows: in the year 2010 -25%, in the 2011 tax year -24%, in the 2012 tax year – 23%, in the 2013 tax year – 22%, in the 2014 tax year – 21%, in the 2015 tax year – 20% and in the 2016 tax year and thereafter, a tax rate of 18% will apply to companies.

On September 26, 2011, the recommendations of the committee for social and Economic Change headed by Professor Manuel Trajtenberg were published, following which, on December 6, 2011, the Law for Change in the Tax Burden (Legislative Amendments), which is based on the recommendations of the taxation chapter of the Trajtenberg Committee, was published after having passed its third reading the day before at the Israeli Knesset.

Set forth below are the main changes in the new law in the field of corporate taxation:

(1) Cancellation of reductions that were planned in the coming years in income tax and in corporate tax commencing from 2012.

(2) Rise in corporate tax in 2012 to the rate of 25%.

(3) Rise in the rates of capital gains tax and appreciation tax to the rate specified in Section 2 above.

Since the legislative process was completed in the last quarter of 2011, the Group has updated, as of the date of the statement of financial position, its deferred tax balances as a result of the said changes in the tax rates in the years in which the temporary differences in respect of which the Group recognized deferred taxes are expected to invert. Accordingly, as of December 31, 2011, the Group has recognized an increase in deferred tax liabilities in the sum of NIS 608,576 thousand, out of which a sum of NIS 600,832 thousand against deferred tax expenses and a sum of NIS 7,744 thousand was carried as an expense to other comprehensive income.

b. On September 17, 2009 the Income Tax Regulations (The determination of the interest rate for the purposes of Section 3(J)) (Amendment), 5769-2009 were published, in the framework of which the provisions in the Tax Regulations (Determinations of the interest rate for the purposes of Section 3(J)), 5746-1986 were changed comprehensively.

The amendment applies to a loan that is extended as from October 1, 2009, and within the framework of the amendment transition provisions were also set in relation to loans that were extended before the amendment entered force.

Commencing on October 1, 2009, the annual interest rate for the purposes of Section 3(J) of the Ordinance, in relation to assessees that are subject to the section and which extend a loan in Shekels, is 3.3% (unlinked). This rate applies to the period from October 1, 2009, until December 31, 2009. The annual interest rate for the purposes of Section 3(J) of the Ordinance, commencing on January 1, 2010 is 3% (unlinked).

On February 23, 2012 the Minister of Finance's notice in respect of determining the interest rate for the purposes of Section 3(J) of the Tax Ordinance was published in the official gazette.

The interest rate for the purposes of Section 3(J) of the Ordinance for 2011 will be 3.8%.

The interest rate for the purposes of Section 3(J) of the Ordinance for 2012 will be 4.68%.

On the other hand, where the loans are extended in foreign currency (as defined in the Regulation), the interest rate for the purposes of Section 3 (J) has been set as the rate of the change of the exchange rate for that currency plus 3%.

In addition, special provision has been set in relation to the determination of the interest rate for the matter of Shekel loans or loans in foreign currency that were extended for a period of up to 14 days before or after a loan was received under identical terms other than from a relation.

c. On February 4, 2010 Amendment No. 174 to the Income Tax Law - Emergency Provisions for the 2007, 2008 and 2009 tax years (the "Amendment to the Ordinance") was published in the official gazette. In accordance with the Amendment to the Ordinance, Israeli Accounting Standard Number 29 on the subject of the adoption of the International Financial Reporting Standards (IFRS), will not apply for the purposes of the determination of the chargeable income from the said years, even if it has been implemented for the purposes of the preparation of the financial statements. In January 2012 Amendment no. 188 to the Ordinance was published, in which framework the temporary provision was amended, such that Regulation 29 shall not apply also in determining the chargeable income in 2010 and 2011.

(2) A fully owned Israeli subsidiary belonging to the Company has a direct holding in a real estate asset in Leeds, Great Britain. The chargeable income (less the expenses that are deductible for tax purposes), which it derives from the rental of the real estate asset in Great Britain will be chargeable to taxation in Britain at a reduced tax rate of 20% (as from January 1, 2009). Any capital gain, which it derives from the sale of the real estate asset in Great Britain, will be exempt from tax in Great Britain if the said asset is held for passive investment purposes and if it does not amount to a business (the activity of renting the asset does not create for the Israeli subsidiary the status of "a permanent institution" in Great Britain).

The chargeable income, which it derives from the rental of the real estate asset in Great Britain, as well as a real capital gain that is derived from its sale, will be chargeable to taxation in Israel in accordance with the tax rate for companies. On the other hand, it will be given a credit in respect of the foreign taxation, paid in Great Britain, subject to the provisions of Sections 196 to 214 of the Ordinance.

Tax that was paid in Great Britain and for which a tax credit cannot be received in Israel in the tax year in which it was paid, inter alia, as a result of losses for tax purposes of the subsidiary, will only be available as a credit (in adjusted values, in accordance with the rise in the Consumer Prices Index) against tax that is levied on the subsidiary in respect of rental income from abroad in the following five years.

A loss, which is derived from the rental of property in Great Britain, will be considered a loss from outside of Israel, for the purposes of Section 29 of the Ordinance, and accordingly it will be a available to be offset in the tax year in which it was created against chargeable income (including a capital gain) from a business outside of Israel and also against passive income that is chargeable from outside of Israel. The balance of the loss, which remains after the offsetting, as aforesaid, can be offset against chargeable income (including capital gains) from a business outside of Israel in the following tax years. Under certain circumstances, it is possible to offset the said loss against chargeable income in Israel, with restrictions being placed on the receipt of a credit from foreign taxation.

(3) The Company and a subsidiary have a holding (90%-99%) in American partnerships, which hold real property. The profits (losses) of the American partnerships from the rental of the real properties and from the sale thereof are attributed directly to the partners, in accordance with their shares in the capital in the partnerships, because under American tax law, a partnership which has been registered in the USA is considered to be transparent for tax purposes.

Accordingly, the Group will have the profits (losses) of the American partnerships in which they serve as the general partners attributed to them and they will be chargeable with tax in the USA in respect of profits, which are attributed to them, as aforesaid, in accordance with the federal corporation tax rate (at a rate of up to 35%) and with state tax, which is customary in Texas (whose rate is 1% of the revenue taxable margin, as defined by law), which constitutes an expense for the purposes of the calculation of the federal tax. In addition, under certain circumstances, a "branch tax" at a rate of 12.5% may be levies on the profits of the partnerships (even if they have not yet actually been distributed). If the profits, as aforesaid are reinvested for the purposes of the operations in the USA and subject to compliance with additional conditions, the "branch tax" may be deferred.

In a similar manner, the general partners in the American partnerships will be liable for tax in the USA in respect of their share (1%) of the profits (losses) from the rental of the realty assets and/or from their sale, in accordance with the tax rates that are mentioned above (with the exclusion of "branch tax").

In accordance with the provisions of Section 63 of the Ordinance, the general partners (the Company and its subsidiary), will be liable for corporation tax in Israel in respect of their share of the profits from the rental of the land in the USA and in the real capital gain that is derived from their sale by the American partnerships.

See section A(2) above on the subject of the offsetting of losses and the credit in respect of foreign taxation.

(4) Taxation under conditions of inflation

The Income Tax Law (Adjustments for Inflation), 5745-1985 (the "Law") has been in force since 1985. The Law instituted a regime of the measurement of results for tax purposes on a real basis. The various adjustments that are required under the Law, are intended to result in the taxation of income on a real basis. In light of the fact that the financial statements are not adjusted for the Consumer Prices Index from the time at which the Israeli economy ceased to be considered hyper-inflationary, differences have been created between the profit as per the financial statements and the adjusted profits for tax purposes, and accordingly, there are also timing differences between the values of the assets and the liabilities as reported in the financial statements and their tax basis.

On February 26, 2008 the Knesset passed the Income Tax Law (Adjustments for Inflation) (Amendment No. 20) (Restriction of the Period of Application), 5768-2008 (the "Amendment"). According to the Amendment, the application of the Adjustments Law was terminated in the 2007 tax year and from the 2008 tax year onwards the provisions of the Law no longer apply, except for transition provisions whose objective it is to prevent distortions in the tax calculations.

In accordance with the Amendment, in the 2008 tax year and thereafter, the adjustment of the income for tax purposes will no longer be calculated on a real basis. Similarly the linkage to the index of the amount of the depreciation on fixed assets and the amounts of losses carried forward for tax purposes has been discontinued and those amounts have been adjusted up to the index for the end of the 2007 tax year, and their linkage to the index has been discontinued as from that time onwards. The impact of the Amendment to the Adjustments Law has found expression in the calculation of the current taxes and of the deferred taxes as from the year 2008.

(5) Benefits under the Encouragement of Industry (Taxes) Law

a. Tambour and some of its consolidated companies are "Industrial Companies" in accordance with the Encouragement of Industry (Taxes) Law, 5029-1969 and accordingly they are entitled to benefits, the main ones of which are:

(1) Depreciation at increased rates.

(2) The deduction of issuance expenses on shares that are registered for trade on a Stock Exchange in three equal annual installments, as from the year in which the shares are registered for trade.

(3) The possibility of presenting consolidated financial statements for companies having one production line for tax purposes. (see b below).

Certain consolidated companies in Tambour Group file since tax year 2010, a consolidated report to the tax authorities according to the Encouragement of Industry Law (Taxes), 5729-1969, since based on the opinion of Tambour's legal advisors, the companies are industrial companies with one production line as defined in the aforesaid law. Therefore, the tax payment of the Group for 2011 was reduced by an amount of approx. NIS 9 million (2010 – approx. NIS 11 million) by setting off current losses generated in the consolidated company by Tambour's revenues.

b. Via Maris Group includes several companies: Via Maris Desalination Ltd., Via Maris Operation Ltd. and Via Maris Construction Partnership. Within a restructuring which took place, a holding company was established, to which all of the interests in the aforesaid companies were transferred. According to Via Maris' approach, see water desalination is a productive activity and the company which was established and the companies being transferred are industrial companies according to the Industry Encouragement Law (Taxes) 5729-1969. Via Maris intends to file a consolidated tax report for tax purposes commencing in tax year 2011. Therefore, the tax payment for 2011 will be reduced by an amount of approx. NIS 3.6 million.

B. Tax revenues (expenses) on revenues that have been recognized in the income statement:

	For the year ended December 31		
	2011	**2010**	**2009**
	NIS thousands	**NIS thousands**	**NIS thousands**
Current tax expenses			
For the current period	(105,350)	(85,910)	(70,611)
Net adjustments in respect of previous years	7,740	1,787	4,079
	(97,610)	(84,123)	(66,532)
Deferred tax revenues (expenses)	(778,471)	(208,036)	354,876
Total revenues (expenses) of taxes on income	(876,081)	(292,159)	288,344

C. Taxes on income in respect of the components of other comprehensive income:

	2011			2010			2009		
	Amounts before tax	Tax income (expenses) (*)	Amounts withholding of taxation	Amounts before tax	Tax income (expenses) (*)	Amounts withholding of taxation	Amounts before tax	Tax income (expenses) (*)	Amounts withholding of taxation
	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands	NIS thousands
Translation differentials for overseas operations	15,917	-	15,917	(4,540)	-	(4,540)	(1,119)	-	(1,119)
Profit (loss) in respect of the hedging of cash flows	(74)	19	(55)	-	-	-	(891)	232	(659)
Change in the fair value of available for sale financial assets	(515,988)	(**)84,205	(431,783)	95,136	(13,621)	81,515	572,537	(92,559)	479,978
Realization of available for sale financial assets	-	-	-	(22,265)	5,878	(16,387)	-	-	-
Actuarial profits (losses) for defined benefit plan	(3,692)	923	(2,769)	1,533	(241)	1,292	(574)	74	(500)
Total other comprehensive income (loss)	(503,837)	85,147	(418,690)	69,864	(7,984)	61,880	569,953	(92,253)	477,700

(*) In 2011 the deferred taxes have been calculated in accordance with a tax rate of 25% (in previous years mainly in accordance with a tax rate of 18%).

(**) Including effect of the change in tax rate in the sum of approx. NIS 7.7 million.

D. Taxes on income that has been credited directly under equity:

	2 0 1 1	2010
	NIS in thousands	NIS in thousands
Discounting capital notes issued to holders of rights which do not confer control in Tambour	-	(36)
Effect of the implementation of the amendment to the IAS 17 due to finance leases.	-	(2,971)
Acquisition of loans from non-controlling interests	4,884	-
	4,884	(3,007)

E. Compatibility between the theoretical tax on the profits before taxes on income and the tax expenses:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Profits before taxes on income	1,499,093	1,547,263	711,686
The Company's principal tax rate	24%	25%	26%
Tax calculated at the Company's principal tax rate	359,782	386,816	185,039
Addition,(saving) in the tax liability in respect of:			
Different tax rates and laws in subsidiaries that operate outside of Israel	13,594	544	536
Elimination of tax calculated in respect of the Company's share of the profits of affiliated companies treated under the equity method	3,889	5,344	2,717
Exempt income	(15,410)	(8,648)	(5,071)
Income chargeable at a special tax rate	62	92	68
Disallowed expenses	1,227	1,046	2,198
Company's share in partnership	131	(495)	(217)
Permanent differences	1,177	-	(2,921)
Exploitation and creation of deferred taxes in respect of losses and benefits from previous years, in respect of which deferred taxes were not recorded	(7,084)	(9,646)	-
Change in timing differences, in respect of which deferred taxes were not recorded	-	-	(3,610)
Losses and benefits for tax purposes from periods in respect of which deferred taxes were not recorded	3,042	3,041	11,238
Taxes in respect of previous years	(7,740)	(1,787)	(4,079)
Differences in the definition of capital, assets and expenses for tax purposes and others	(19,093)	(27,756)	(16,949)
Effect of the change in the tax rates on timing differences in the reporting period	(11,786)	3,962	(67)
Effect of change in the statutory tax rate	600,832	-	(436,283)
Effect of the tax rates in respect of the net gain on the adjustment of the fair value of investment property	(49,829)	(62,692)	(16,540)
Other differences	3,287	2,338	(4,403)
Tax expenses (benefit) on income	876,081	292,159	(288,344)

F. Deferred taxes assets and liabilities:

(1) Deferred tax assets and liabilities that have been recognized:

The deferred taxes in respect of companies in Israel have been calculated in accordance with the tax rates that are expected to apply at the time of the reversal, as detailed above. Deferred taxes in respect of subsidiaries that operate outside of Israel have been calculated in accordance with the relevant tax in each country.

The deferred tax assets and liabilities are attributed to the following items:

	Realty assets and fixed assets (3)	Benefits for employees	Financial instruments (1), (3)	Deductions and losses carried forward for tax purposes (4)	Others (2)	Total
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Balance of assets (liabilities)						
Deferred Tax as of January 1, 2010	(1,237,468)	16,733	(134,946)	48,767	56,857	(1,250,057)
Changes carried to the income statement	(194,707)	476	(5,785)	(8,309)	289	(208,036)
Changes recognized as other comprehensive income	-	(232)	(7,744)	-	(8)	(7,984)
Changes recognized as equity	(13,437)	-	-	-	10,430	(3,007)
Other changes	(1,819)	227	96	(2,102)	4,050	452
Business combinations	-	108	(15,460)	10,528	(10,921)	(15,745)
Balance of assets (liabilities)						
Deferred Tax as of December 31, 2010	(1,447,431)	17,312	(163,839)	48,884	60,697	(1,484,377)
Changes carried to the income statement	(205,817)	599	19,262	7,048	1,269	(177,639)
Changes carried to other comprehensive income	-	917	91,968	-	-	92,885
Changes carried to equity	-	-	-	-	4,884	4,884
Effect of change in the tax rate carried to the income statement	(623,425)	2,924	(5,913)	13,949	11,633	(600,832)
Effect of change in the tax rate carried to the other comprehensive income	-	-	(7,744)	-	-	(7,744)
Deferred Tax as of December 31, 2011	(2,276,673)	21,752	(66,266)	69,881	78,483	(2,172,823)

(1) Primarily for available for sale financial assets and financial asset – receivables for a franchise arrangement.

(2) Primarily doubtful debts and linkage differentials on deposits from customers that have not been recognized for tax purposes and liabilities for financing lease.

(3) The deferred taxes as of December 31, 2011 have been calculated mainly at a tax rate of 25% (As of December 31, 2010 – 18%).

(4) The deferred taxes as of December 31, 2011 have been calculated at a tax rate of 25% (As of December 31, 2010 – 22%).

(2) Deferred tax assets that have not been recognized:

Deferred taxes have not been recognized in respect of the following items:

	As of December 31	
	2011	2010
	NIS thousands	NIS thousands
Losses for tax purposes	212,639	204,164
Capital losses for tax purposes	63,516	86,496
Real differences from securities	48,000	49,000
	324,155	339,660

(3) Losses and deductions for tax purposes that are available to be carried forward to the coming years

a. The current business losses for tax purposes of consolidated companies, which are carried forward to the following year amounted to approx. NIS 394,737 thousand as of December 31, 2011 (December 31, 2010: approx. NIS 398,883 thousand).

Consolidated companies have recorded a deferred tax asset in an amount of NIS 44,832 thousand in respect of the accumulated business losses (December 31, 2010 – NIS 38,762 thousand) in accordance with management's evaluation that there is a high level of confidence that these losses will be exploited in the coming years.

b. A consolidated company has a real difference on marketable securities that have not been allowed as a deduction in the reporting year and which are available to be carried forward to the coming years, whose balance is approx. NIS 48,000 thousand as of December 31, 2011 (December 31, 2010 – NIS 49,000 thousand). This difference will be allowable as a deduction in the coming years against income from marketable securities, if there is such income in those years. Deferred taxes receivable have not been reflected in respect of these accumulated losses.

c. The Company and consolidated companies have accumulated capital losses for tax purposes in an amount of approx. NIS 144,422 thousand (December 31, 2010 – approx. NIS 142,732 thousand). The Company and the consolidated companies have recorded deferred tax assets of NIS 16,414 thousand in respect of the accumulated business losses (December 31, 2010 – NIS 10,122 thousand).

d. According to the existing tax laws, there is no time restriction for the exploitation of losses for tax purposes, or on the exploitation of the deductible timing differences. Deferred tax assets have not been recognized in respect of such losses and differences , in cases where it is not expected that there will be sufficient chargeable income in the coming years against which it will be possible to exploit the tax benefits.

e. The Group did not create deferred tax in respect of its investments in consolidated companies since the decision whether to liquidate the companies is given to the Group and it intends not to dispose of them in the near future.

G. Tax assessments:

Sonol and GES have final tax assessments up to and including tax year 2006. The other companies in the Group (other than as stated below) have final tax assessments up to and including the 2007 tax year, within the context of Section 145A(2) of the Income Tax Ordinance (Obsolescence).

In December 2010 the Company and two consolidated companies thereof received assessments to the best of judgment for 2006. As of the date of the approval of the financial statements immaterial amounts were paid and final tax assessments were finalized for the Company and a consolidated company up to and including the 2007 tax year and to another consolidated company up to and including the tax year 2009.

In October 2009 the consolidated company Supergas received assessments for the years 2005 to 2007, and in March 2010 two subsidiaries of Supergas received assessments for years 2007 and 2008 after assessment negotiations which did not mature into an agreement, Supergas received, in November 2010, orders for determination of the assessment for the aforesaid years, according to which Supergas was required to pay additional tax in the sum of approx. NIS 10.5 million (in principal terms).

Supergas appealed these assessments before the District Court. In July 2011 Supergas received assessments to the best of judgment for the tax years 2008 and 2009, for the same assessment causes included in the orders for the years 2005-2007, requiring Supergas to pay additional tax of approx. NIS 7.5 million. Supergas filed objections to these assessment demands to the Income Tax Authorities, further to the appeal filed by Supergas and the subsidiaries from the orders, and its objection to assessments for later years issued thereto to the best of judgment, as aforesaid. The Company's management, based on Granite's management which is based on Supergas' professional advisors, estimate that the chances of the appeal and the objection being granted in respect of the majority of the assessment causes are higher than 50% and that the provision made in the financial statements is adequate.

Note 34 Engagements

The consolidated companies have engagements and liabilities as of the date of the statement of financial position, as follows:

A. Material engagements:

		NIS in thousands
(1)	For the purchase of fixed assets	9,083
	For the supply of fuel, oils and equipment (for supply January- December 2011)	3,417,005
	For the performance of projects	124,794
	For rentals and leases of stations, facilities and buildings (*)	2,060,948
	For the rental and maintenance of computers and ancillary equipment for a period of up to one year	4,045
	Operating leasing agreements for motor vehicles (**)	33,516
	(*) Following are the repayment times for rental and leasing undertakings:	
	2012	184,453
	2013	177,318
	2014	169,069
	2015	162,915
	2016 and thereafter	1,367,193
		2,060,948
	(**) Following are the payment times for commitments under operating leasing undertakings for motor vehicles	
	2012	17,482
	2013	12,695
	2014	3,339
		33,516

(2) In the reporting period Sonol purchased most of its oil distillates from Oil Refineries Ltd.

(3) Supergas, through a fully owned subsidiary, entered into lease agreements for the purpose of constructions of facilities for the production of solar energy. Supergas' commitment, according to the agreements, shall commence upon receiving the permanent production licenses.

(4) See Note 40 in respect of the engagements with related and interested parties.

B. Engagements for investments:

(1) In respect of the engagements of Via the Sea Desalination Ltd. with the State of Israel, see Note 13 above.

(2) SuperNG Natural Gas Distribution Company Ltd. (“SuperNG), a company jointly owned, in equal shares, by Supergas and Shapir Civil and Marine Engineering Ltd. (“Shapir”), which was founded for the construction and operation of a natural gas distribution network, won a tender for the construction and operation of a natural gas distribution network in the Central area. On November 1, 2009, an agreement was signed between the State and SuperNG, granting such license thereto. In 2010, SuperNG signed an agreement with the government company Israel Natural Gas Lines Ltd. (“INGL”), ordering four pressure-reduction and metering stations (“PRMS”) for connection of the transmission system to the distribution system. The construction of the PRMS will be performed in the coming years by INGL, or another on its behalf, and it shall also operate them. As of the date of the report, SuperNG is performing planning and construction activities. According to the license conditions, Super NG is committed to an investment in the construction of the distribution system a sum of approx. NIS 160 million according to the milestones set in the license.

(3) Holon Azrieli Center

The Group, via Canit Hashalom , is entitled to receive leasing rights in a reserve of land with an overall area of approx. 34 dunams in the East Holon Industrial Area (in this section: the "Land Reserve") under an agreement that was signed between the City of Holon and Canit Hashalom on June 5, 2008 (in this section: the "Agreement"). Within the framework of the Agreement, Canit Hashalom made guarantees available to the Economic Company for the Development of Holon Ltd., in an amount of NIS 8 million, linked to the Consumer Prices Index (which as of December 31, 2011 were at an amount of approx. NIS 8.6 million), which is intended to ensure the compliance with Canit Hashalom's commitments under the Agreement.

The entire Land Reserve is owned by the City of Holon, without any known charges or mortgages. In accordance with the Agreement the project is for the construction of a business park (with no more than four sub-stages), including buildings for hi-tech offices, display halls and commerce, service areas and parking areas as well as for additional uses ("the Project"). The Project will be built and operated as an income-producing property (for rental) by way of a joint venture, where the material terms of the transaction are as follows:

a. The City of Holon will lease parts of the Project to Canit Hashalom, in accordance with the Agreement, for a period of 99 years with an option for an additional 99 years for a payment, in accordance with the participation rate in the transaction.

b. Canit Hashalom for its part has undertaken to execute and to complete the construction of the buildings and the works in accordance with the sub-stages that have been determined between the parties, such that it can be registered as the lessee of those constructed parts in accordance with the sub-stages of the Project.

c. Canit Hashalom will be entitled to receive 83% of the floor space that will be built in the Project, as aforesaid, whereas the Municipality of Holon will be entitled to 17% of the floor space that will be built, as aforesaid ("the participation rate in the project").

d. The construction rights that are permitted under the City Zoning Plan stand at 88,348 square meters for the main areas, of which Canit Hashalom has undertaken to exploit at least 80% of the entire buildings rights that are permitted in accordance with the Urban Construction Plan. In the first stage, (within the first three years) Canit Hashalom has committed to build 42,000 square meters of the main areas as well as 81,000 square meters of underground parking, and this in up to four sub-stages, while the first stage is supposed to be completed within 3 years of the time of the issuance of the first building permit and the last stage is supposed to be completed within 9 years of the time of the issuance of the first building permit, as aforesaid.

e. Canit Hashalom will be entitled to discontinue the Project before the start of any stage (as from the second stage and thereafter, and on condition that it has fully completed the previous stage) with the requirement that it gives notice 90 days before the time that has been set for the start of that stage, in which it requests to discontinue the Project and subject to agreed-upon compensation in the amount of NIS 8 million for the City of Holon. .

f. On the receipt of the building permit for each stage of the Project, there will be a division of areas between the parties, wherein the Municipality will be entitled to be the first to select its part of that same stage and with the requirement that the areas that are selected are continuous, in so far as is possible.

g. The Project will be managed and operated as an income producing property that is held jointly by the two parties, where the areas of the Project will be rented as a common reserve for the two parties. The areas will be rented through a management company and the division of the rental fees will be carried out using a mechanism that has been agreed by the two parties. In accordance with this mechanism, the rental receipts up to a certain amount per square meter (which is linked to the base index) will be divided between the parties in accordance with their shares in the joint venture. Over and above the said amount, the rental receipts from the general area that is managed jointly, will be divided between the parties in equal shares.

h. As of the date of signing of the financial statements, the excavation and shoring work has been completed and Canit Hashalom has begun construction of the foundations of the buildings and construction of the basements and the buildings in accordance with the comprehensive building permit for Stage A of the project which was received.

i. The management of the Project will be executed by the management company that will be owned jointly by the parties in shares that are proportionate to their holdings in the joint venture. The management will be executed on a basis of cost +15%, and this will constitute the fees of the management company.

j. Any sale and/or rental of the areas belonging to the Municipality of Holon for over and above a period of five years requires the approval of the City Council and the Minister of the Interior. .

k. The Agreement sets various restrictions on the transfer of rights in areas in the Project and/or in the rights and commitments of Canit Hashalom therein. It is further determined in the Agreement that the transfer of shares, including by way of a public floatation, in shares in Canit Hashalom in an amount of up to 25% will be permitted. It is further clarified that the provisions that touch upon the transfer of rights and a change in the ownership structure will not apply to the parent company or to a subsidiary or a related company of Canit Hashalom.

(4) Azrieli Rishonim Mall

The Group, through Canit Hashalom, owns of a block of land on an area of approx. 19,000 sqm in Rishon Lezion (the "Site"). Since the Site constitutes part of a larger block of land jointly owned by Canit Hashalom and third parties, an agreement was signed between Canit Hashalom and such third parties for division of the land, and a perpetual lease was registered in favor of Canit Hashalom for those parts of the land constituting the Site. A parallel lease is due to be registered in favor of the third parties, in reference to other parts of the land not forming part of the Site.

Part of the Site is currently used as a ground-level, above-ground parking lot, which is held and operated by the City of Rishon Lezion and is used for the Rishonim train station, until a plan allowing construction on the land, as specified below, takes effect.

A plan for the Site was deposited on August 24, 2009 which, once approved, will allow the construction of approx. 48,000 sqm of commercial and office space for lease, as well as 82,095 sqm of above- and underground parking areas. In December 2010 a decision was received from the District Committee, approving the plan for deposit for validation subject to receipt of final approvals and performance of the coordination included in said decision, and the Company is acting to obtain the required approvals in order to enable the publication of the plan for validation.

Canit Hashalom has assumed an undertaking whereby, if the plan is approved, Canit Hashalom would build, at its expense, 600 parking spaces to be used as a parking lot for the benefit of train users. On January 8, 2012 an administrative petition which was filed against the District Committee, Canit Hashalom and others, for approval of the plan under such conditions, was denied for being premature, since, at the time, the Ministry of Transport has not yet provided its response in connection with the approval of the plan. To the best of the Company's knowledge, the Petitioners are entitled to petition against approval of the plan again, upon final approval thereof. As of the date of the report, the Company has begun construction of a temporary parking lot at the Site, after receiving a building permit for such temporary parking lot.

Note 35 Charges and guarantees

A. Fixed and floating charges:

	December 31, 2011	
	NIS in thousands	Secured by
Short-term credit from banks	1,125,852	A floating charge on the general assets and on the shares of some of the consolidated companies.
Long-term loans from banks (including accumulated interest that is presented as short-term)	3,301,115	A charge on the rights to receive monies in respect of investment property of the Company and of some of the investee companies. Moreover, the Company has given an undertaking to banking entities not to create floating charges on the generality of its assets. Moreover, the Company and one of its consolidated companies have made an irrevocable commitment to a banking entity that they have not and will not create a floating charge on the generality of its property and its assets, whether they are owned by it and whether they will be owned by it in the future, and including all of its goodwill and share capital and it has also undertaken not to make an undertaking in any form whatsoever to create a floating charge, as aforesaid, without the agreement of the banking entity, in advance and in writing. The Company will be entitled to create a floating charge, as aforesaid, and solely that in parallel to the creation it also creates a floating charge in favor of the banking entity. In a consolidated company, the charge of the shares of some of the investee companies. Floating charge on the entire assets and rights of some of the principal investee companies. Fixed charge on some of the fixed assets of some of the investee companies and a charge on rights for receipt of monies in respect of projects in a subsidiary of a consolidated company.
Bonds	1,177,769	A charge over some of the fixed assets of some of the companies in the Group. Canit Hashalom a first ranking fixed charge , in an unlimited amount on the share capital of Canit Hashalom's consolidated companies as well as on its rights in connection with bonds that they have issued. In a subsidiary of a consolidated company, the bonds are collateralized by a first ranking floating charge, in an unlimited amount, on all of the assets of the consolidated company. In addition, the investee company has created a first ranking fixed charge in an unlimited amount over all of the shares in the consolidated company that it owns and in its holding, including the rights that derive from those shares.

B. The Company and consolidated companies have contingent liabilities as of the date of the statement of financial position, as follows:

		NIS thousands
(1)	Financial guarantees to banks for a subsidiary	11,259
	Financial guarantees to banks for associates and third parties	9,267
(2)	Performance guarantees and others:	
	- Performance guarantees for customers and others, including tender guarantees	111,292
	- Guarantees to authorities	67,579
(3)	Guarantees extended in connection with the desalination facility.	
	- Operation and supply guarantees	201,625
	- Guarantees for the financing of energy costs in excess of the receivables from the state in respect of the energy component	Unlimited in amount
(4)	Guarantee extended by the Company to a consolidated company for its liabilities vis-à-vis a banking entity. The balance of the liability as of December 31, 2011 is in the sum of approx. NIS 24.8 million.	Unlimited in amount
(5)	A guarantee that has been provided by a consolidated company to its consolidated company in respect of its liabilities to a banking corporation. The balance of the liability as of December 31, 2011 is NIS 10.5 million.	Unlimited in amount
(6)	A guarantee that has been provided by the Company to a limited partnership thereof in respect of its liabilities to a banking corporation. The liabilities balance as of December 31, 2011 is approx. NIS 29.6 million.	Unlimited in amount
(7)	A guarantee that has been provided by the Company to a limited partnership thereof in respect of its liabilities to a financing corporation, exercisable only in several certain cases defined in the loan agreement.	496,730

Note 36 – Contingent liabilities

a. Claims against Sonol of IDF disabled veterans operating fuelling stations as part of an arrangement between the IDF disabled veterans, the Ministry of Defence, the Israel Lands Administration and the fuel companies:

The parties	Amount of claim	Nature of claim	Prospects of claim
5 claims against Sonol	The claims are for declaratory relief and a monetary claim amounting to approx. NIS 80 million.	Claims of the IDF disabled veterans (and one of the heirs of an IDF disabled veteran) who received the operating rights to filling stations as part of an arrangement between the disabled veterans and the Rehabilitation Division of the Ministry of Defence, the Israel Lands Administration, a local authority and the fuel companies, for declaratory relief for termination of the agreements between the claimants and the Company, alleging that they involve a restrictive arrangement, which is prohibited under the Antitrust Law. In addition, in some of the said claims, it is alleged that the agreement system between the parties includes discriminatory conditions in a uniform contract, lack of good faith and adverse discrimination of the claimants in relation to the other filling stations. Furthermore, monetary compensation is claimed in respect of overcharging as a result of restrictive arrangements and/or expropriation and discrimination of prices and commercial conditions.	In the Company's opinion, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the chances of all of the claims are less than 50%. In one of the claims, an additional monetary claim has been made totalling NIS 6.2 million in respect of damage incurred from the date of submission of the initial claim, and in respect of these damages, the chance that the Company will be obliged to pay the monetary claim is higher than 50%. But there is a reasonable possibility that, even if the court decides that Sonol is responsible for the damage, the court will not rule on the monetary claim demanded in full. In the opinion of the Company management, based on Granite's management, based on Sonol's management, the probability for the payment of amounts in excess of the provision included in the financial statements is low.

b. Claims submitted against Sonol (not by IDF disabled veterans) in claims of a restrictive arrangement

The parties	Amount of claim	Nature of claim	Prospects of claim
2 claims against Sonol	Claims for declaratory relief and for monetary relief totalling approx. NIS 17.5 million.	2 claims of operators of filling stations for declaratory relief, concerning the cancellation of a system of agreements between the parties by virtue of the fact that it is a prohibited restrictive arrangement and/or standard form contract containing oppressive clauses. In one claim, an additional financial remedy was claimed in respect of discrimination, apparently, of the claimants against operators of other filling stations of Sonol, and in respect of exaggerated and overstated commercial conditions in relation to the "market price" for oil products in other companies, which, the claimants allege, Sonol collected as part of a restrictive arrangement, thus having made unjust enrichment. In one of the claims, a financial remedy was claimed in respect of appropriate fees for usage of the station.	In the Company's opinion, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, for one claim (which is only for declaratory relief), the chances are estimated at greater than 50%, even though, insofar as the claim for declaratory relief is accepted, and on the basis thereof, a monetary claim is made, the chances of receiving from Sonol "significant" payments in respect of the "restrictive practice" are less than 50%. The chances of the second claim are estimated at less than 50%.

c. Class actions:

The parties	Amount of claim	Nature of claim	Prospects of claim
1. Claim against Sonol and other fuel companies	A claim for NIS 27, with the share of Sonol and its consolidated company in the claim amounting to NIS 3, together with a motion to have it certified as a class action for a total of approx. NIS 132.6 million.	A claim and a class certification motion of December 2007. The action concerns the Plaintiffs' claim whereby service fees were collected in respect of refuelling carried out during nighttime hours and on Saturdays and festivals and that this charge, until May 30, 2002, was carried out, apparently, not according to the law and contrary to the Supervisory Order for Products and Services (Maximum Prices for Oil Products), 5752-1992, and Supervisory Order for Products and Services (Maximum Prices at Filling Stations), 5756-1996.	In the Company's opinion, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the chances of the claim and the motion being accepted are less than 50%.
2. Claim against Sonol and another fuel company	The relief claimed is declaratory relief to order the fuel companies to cease raising charges for fuel not supplied, and a monetary claim totalling approx. NIS 124 million, with the proportional share of Sonol being approx. NIS 24 million.	A claim and a class certification motion from October 2009, concerning the Plaintiff's claim whereby the fuel companies require the customers when refuelling at the automatic refuelling pumps, with the meter starting to operate and charge the customers even before fuel had come out of the pumps. The claimant alleges that with this conduct, the refuelling companies breached their obligations vis-à-vis their customers and the provisions of the Competition Law, and caused a number of damaging injustices.	In the Company's opinion, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the chances of the claim being accepted are higher than 50%. After the date of the report, the parties reached a settlement whereby Sonol was supposed to pay an immaterial amount. The court dismissed the settlement arrangement. However, in the Company's opinion, based on the management of Granite, which is based on the legal advisors of Sonol, Sonol is not expected to incur a material amount over and above the provision that was recorded.
3. Claim against Sonol and other fuel companies	Claim in the total sum of approx. NIS 1.2 billion.	Claim and class certification motion of October 2010. The action concerns a claim that the fuel companies engaged with station owners in prohibited restrictive arrangements which harm competition in the fuel industry and prevent reduction of the fuel price to the end consumer and the ability of competing entities to effectively penetrate the market.	The Company estimates, based on an assessment of Granite's management, which is based on Sonol's legal advisors, that the chances of the claim and the motion being accepted are lower than 50%.
4. Claim against Sonol and other fuel companies	Claim in a total sum estimated at approx. NIS 66.7 million (Sonol's share).	Claim and class certification motion of December 2010. The subject matter of the motion is the argument whereby the fuel companies breached and are continuing to breach the provisions of Sections 2-4 of the Consumer Protection Law, 5741-1981, by misleading the consumers with regard to the nature, quantity and quality of the fuels which they sell, and by not making public the fact that the fuels which are sold thereby are sold at ambient temperature, while upon purchase thereof they are calculated according to a 15°C temperature. According thereto, the fuel companies received money without a lawful right for a product which they sold while misleading consumers and hence gained unjust enrichment, against the provisions of Section 1 of the Unjust Enrichment Law, 5739-1979.	The Company estimates, based on the estimate of Granite's management which is based on Sonol's legal advisors, that the chances of the claim and the motion being accepted are lower than 50%.

5. Claim against Sonol and other fuel companies	A claim in the total estimated sum of approx. NIS 200 million.	Claim and class certification motion of December 2010. According to the plaintiffs, the companies violated the law in all that pertains to water pollution and caused the pollution of ground water and damage. The claim was filed pursuant to an indictment which was filed against Sonol and 3 other fuel companies.	The Company estimates, based on the estimate of Granite's management which is based on Sonol's legal advisors, that the chances of the claim and the motion are estimated at less than 50%.
6. Claim against Sonol	A claim in the total sum, estimated by the Plaintiff, of approx. NIS 899 million.	A claim and a motion for class certification of February 2011. The action concerns a claim of a "Dalkan" customer whereby Sonol charged him (and all other customers using the Dalkan system) a higher price for the purchase of diesel oil than that which was customary at stations and restrained the Dalkan customers, and therefore they are entitled to restitution of money from Sonol.	The Company estimates, based on the estimate of Granite's management which is based on Sonol's legal advisors, that at the proceeding's preliminary stage, and *inter alia* due to amendment of the class certification motion by the Plaintiffs, it is impossible to estimate the chances of the claim and the class certification motion.
7. Claim against Sonol	Claim in the sum of NIS 33.6 million.	A claim and a motion for class certification of April 2011. The action concerns the petitioner's claims that Sonol collects from customers bound by a Dalkan agreement therewith a payment in respect of "night", "Sabbath" or "holiday" increments, even when these customers fuel at self-service pumps, without receiving service from the station attendants, unlike "casual" customers using self service fuelling.	The Company estimates, based on the estimate of Granite's management which is based on Sonol's legal advisors, that the chances of the claim and the motion being accepted are estimated at more than 50%, while the Company estimates, based on the estimate of Granite's management, in reliance on Sonol's legal advisors, that Sonol will not incur a material amount over and above the provision that was recorded.
8. Claim against Sonol and other fuel companies	Claim in the sum of NIS 1 billion, while Sonol's share is at the alleged rate of 21%.	A claim and a motion for class certification of August 2011 against Sonol and other fuel companies, claiming that they misled the regulator over the years, and thus loaded on the marketing margin that was collected thereby expenses that they were prohibited from loading. It was further claimed that they sold gasoline at a more expensive price than permitted.	The Company estimates, based on the estimate of Granite's management which is based on Sonol's legal advisors, that the chances of the claim and the motion are lower than 50%.

9. Claim against a subsidiary of Sonol	Claim in the sum of NIS 6 million.	A claim and a motion for class certification of September 2011. The action concerns a claim that the subsidiary of Sonol is in breach of its duty pursuant to the Consumer Protection Regulations (Price per Measurement Unit), 5768-2008 to mark the prices of the products sold at its stores per measurement unit, in addition to the price of the product. It shall be stated that the alleged breach pertains to stores whose floor area exceeds 100 sqm.	After the date of the statements, the case was closed in a settlement that was approved by the court, whereby the subsidiary was charged with an immaterial amount.
10. Claim against Sonol and a subsidiary of Sonol	Claim in the sum of approx. NIS 42.5 million	A claim and a motion for class certification of November 2011. The action concerns a claim regarding overcharging for self-service fuelling, such that when the consumer refuels at a self-service pump and pays in cash, a payment is collected from him for full service.	The Company estimates, based on the estimate of Granite's management which is based on Sonol's legal advisors, that at the proceeding's preliminary stage, it is impossible to estimate the chances of the claim and the motion.
11. Claim against Sonol	A claim in the sum of approx. NIS 1 billion.	A claim and a motion for class certification of November 2011. The action concerns a claim whereby Sonol collected from Dalkan customers, for fuels, significantly higher prices than the prices that it collects from its "casual" customers, who are not bound therewith in a Dalkan agreement, and that such collection is contrary to law.	The Company estimates, based on the estimate of Granite's management which is based on Sonol's legal advisors, that at the proceeding's preliminary stage, it is impossible to estimate the chances of the claim and the motion..
12. Claim against Supergas and other gas companies	A claim in a total estimated sum of approx. NIS 1 billion	A claim and a motion for class certification of December 2003, claiming that between 1994 and 2003 there were cartels in the field of the private gas market and the commercial gas market.	In March 2012, the court confirmed that the proceedings pertaining to the sanctioning of the settlement arrangement as a judgment would continue. The Company's financial statements included a provision which reflects the estimate of the Company’s management, based on the estimate of Granite's management, based on Supergas's management, of the projected costs in respect of the settlement arrangement, as it expects it to take shape. Insofar as there shall be additional costs, they are not expected to be material.
13. Claim against Supergas and other gas companies	Claim in the estimated sum of approx. NIS 821 million – Supergas's share, approx. NIS 193 million. In July 2009, the petitioners sought to reduce the amount of the claim to approx. NIS 709 million.	Claim and motion for class certification of March 2009, claiming failure to credit gas consumers (who are not central-gas consumers) for gas left over in the cylinder. In July 2009, the petitioners raised new arguments whereby the gas cylinders are, from the outset, were not completely filled.	The Company estimates, based on the estimate of Granite's management which is based Supergas's legal advisors, based on a judgment in a previous claim which was filed based on similar arguments and that was dismissed with prejudice, and in view of the causes of action in the motion for class certification of the claim at bar, that the chances of the claim and the motion are less than 50%.

14. Claim against Supergas and a subsidiary thereof	Claim in the sum of approx. NIS 30 million.	A claim and a motion for class certification of September 2010. The action concerns a claim of non-fulfilment of the provisions of the law pertaining to provision of a free telephone service to Supergas customers.	In August 2011, a settlement agreement was signed between the parties, and a motion for approval of the settlement agreement was filed with the court, according to which Supergas will be charged with a negligible payment to the Plaintiffs. The Company estimates, based on an estimate of Granite's management which is based on Supergas's legal advisors, that there is a higher than 50% probability that the arrangement will be approved by the court (subject to certain modifications that may be sought in the framework of the proceeding). The Company included a provision that reflects, in the estimation of Granite's management, based on Supergas's management, the projected costs in respect of the settlement arrangement.
15. Claim against Supergas and other gas companies	Claim in the sum of approx. NIS 89.5 million (the share attributed to Supergas – approx. NIS 27 million).	A claim and a motion for class certification of November 2010. The action concerns a claim that there is an "indirect" restraint between the gas companies and buyers of apartments in condominiums, as a consequence of which the apartment buyers are ostensibly harmed, while paying excess amounts over and above the amount customary in competition conditions both for the initial connection and for consumption.	The Company estimates, based on the estimate of Granite's management which is based on Supergas's legal advisors, that the chances of the claim and the motion being accepted are lower than 50%.
16. Claim against Supergas and other gas companies	Claim in an amount that has not yet been quantified.	A claim and a motion for class certification of February 2011. The action concerns a claim that the gas companies market LPG to their customers at a higher atmospheric pressure and temperature than the conditions at which, so it is alleged, the gas companies purchase the LPG and/or than the conditions at which LPG should be sold in accordance with international trade standards, and therefore, according to the Plaintiffs, the gas companies are selling an inferior product to the product that they purchase, contrary to the Consumer Protection Law, thus gaining unjust enrichment, according to the Plaintiffs.	The Company estimates, based on the estimate of Granite's management which is based on Supergas's legal advisors, that at the proceeding's preliminary stage, it is impossible to estimate the chances of the claim and the motion.

d. Other claims

	The parties	Amount of claim	Nature of claim	Prospects of claim
1.	The State of Israel – the Fuel Administration versus Sonol, and other fuel companies, ORL and PEI; ORL v. PEI, Sonol and other fuel companies. (The hearing on these claims was consolidated with a hearing on the claim of Sonol and other fuel companies versus the Fuel Administration, ORL and PEI)	The State's claim is in the sum of approx. NIS 120.7 million (Sonol's share is approx. NIS 19 million). In an additional claim, no relief was claimed from the company. In the claim of Sonol and the fuel companies, approx. NIS 25 million was claimed from the State (Sonol's share is approx. NIS 4.6 million).	A claim filed by the State of Israel in 2004 against Sonol, other fuel companies, and against ORL and PEI in respect of monies paid by the State for storage, financing and insurance of an emergency inventory that turned to sludge, and in respect of storage fees overpaid by the State, allegedly, due to the fact that the inventory was not transferred to closed storage on the date on which the State requested its transfer. In 2005, ORL filed a claim against the company, other fuel companies and PEI, in which it petitioned for declaratory relief that the balances of crude oil appearing in the records of PEI as oil without an owner belong to ORL in full (and not to the fuel companies).	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the chances of Sonol's defense in the first claim are good, and in any event, if the claim is granted, ORL or PEI will be liable for most of the amount claimed in respect of storage fees that were transferred to these two companies.
2.	The State of Israel – the Fuel Administration versus Sonol and other fuel companies	A claim amounting to approx. NIS 23.4 million. Sonol's share is approx. NIS 4 million.	A claim filed by the State of Israel against Sonol and other fuel companies, in respect of differences in value between the value of crude oil of the emergency inventory that became unusable ("sludge") and the "affixing value" of the quantity of the emergency inventory, whose writing off the State announced in 2000.	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, if the claim shall be heard, the chances that the defendant fuel companies will be required to pay the amount of the claim are lower than 50%.
3.	PEI versus Sonol and other fuel companies	A claim amounting to approx. NIS 33 million, of which approx. NIS 5.8 million is claimed from Sonol.	A claim by PEI against Sonol, other fuel companies and ORL, concerning the refrainment of the defendant fuel companies from paying PEI storage fees for such emergency inventory of crude oil that ORL alleges became unusable ("sludge") (and in respect of which the proceedings in Sections 1 and 2 above were filed).	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the chances that this claim will be accepted are slim.
4.	Claim against Sonol	A claim in the sum of approx. NIS 9 million	A financial claim of June 2010 by a former station operator. The action concerns a claim that Sonol collected from him ostensibly high prices which, according to the Plaintiff, Sonol owes him. In view of a binding judgment in Sonol's claim against the Plaintiff, which constitutes a *res judicata* requiring the dismissal of the vast majority of the Plaintiff's claims, the Plaintiff was authorized to omit from his claim causes that had already been decided in this proceeding.	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the prospects of the claim against Sonol being accepted are less than 50%.
5.	Claim against Sonol and others	Claim in the sum of approx. NIS 13 million	A claim against a third party, alleging a breach of a loan agreement, while Sonol and three of its former employees are being sued under the claim that they collaborated in the smuggling of property of the third parties in order to thwart the	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the prospects of the claim are less than 50%, both

			repayment of the debt to the claimant.	because of the chances of a prescription claim and on the merits of the claim.
6.	Claim against Sonol	Approx. NIS 18 million	A claim against Sonol in respect of its alleged breach of a lease agreement. This claim was filed as a result of a claim by Sonol against the claimants for NIS 4 million.	In July 2011, a judgment was issued in the claim whereby Sonol was charged with an immaterial amount. In October 2011, an appeal and counter-appeal were filed with the Supreme Court from the District Court's judgment. According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the Plaintiff's chances of winning in the appeal amounts exceeding the provision in the financial statements are low.
7.	Claim against Sonol	Claim in the sum of approx. NIS 10 million	A monetary claim alleging that Sonol unlawfully terminated an agreement signed with the claimant concerning the construction of a fuelling station on the land of the claimant and its operation by Sonol in consideration for payments to the claimant.	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the chances of the claim are less than 50%.
8.	Claim against Sonol and a consolidated company thereof (counter-claim in a claim proceeding of Sonol and the consolidated company against the aforesaid claimant).	A claim in the sum of approx. NIS 7 million	Within the context of a claim in an amount of approx. NIS 4.8 million filed by Sonol against the operators of a fuelling station between 1991 and 2002 and also operated as an agency for distributing fuels in the Northern region, due to a debt from the purchase of fuels and oils. The defendant filed a counter-claim, *inter alia*, due to the setoff of amounts that, according thereto, were not credited in the current settlement of accounts between Sonol and them during operation of the fuelling station, transportation of fuels to another fuelling station and loss of future profits from the operation of the fuelling station.	In August 2011, a judgment was received in the claim and the counterclaim, whereby Sonol was paid the sum of approx. NIS 5.8 million (including linkage and interest). In October 2011, the Plaintiff filed an appeal from the judgment. According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Sonol, the chances of the Plaintiffs winning the appeal are low.
9.	Claim against Sonol	A claim in the sum of approx. NIS 15 million and for declaratory relief.	A claim filed in March 2010 by a company operating a fuelling station against Sonol for monetary relief and declaratory relief, according to which the claimant is entitled to continue to lease the commercial space and operate the fuelling station located in Sonol's main rental area.	In the Company's estimate, based on an assessment of the management of Granite, which is based on Sonol's legal advisors, the prospects of the claim are estimated at this stage as lower than 50%.
10.	Local authorities' demands from Sonol	Demands in the sum of approx. NIS 36 million	Several local authorities submitted to Sonol demands for payment of additional municipal tax (retroactively and on a current basis). Sonol denied the demands and filed an appeal in respect thereof.	According to the assessment of the Company, based on an assessment of Granite's management, based on Sonol's legal advisors, the chances that the majority of the amounts of the increase will be cancelled are higher than 50%, except with respect to two claims in a negligible amount. In the Company's estimation, based on an assessment of

			Granite's management, based on Sonol's legal advisers, Sonol has performed appropriate provisions in the statements.
11. The State of Israel v. Sonol and former officers	Criminal	In December 2010, the Ministry of Environmental Protection filed an indictment against Sonol and against former officers of Sonol, in respect of a number of violations of the said water regulations: failure to perform seal tests; failure to deliver results of seal tests; failure to report fuel leak, including in aggravated circumstances; failure to repair an unsealed facility, including in aggravated circumstances; and failure to install a Piezometer. The offenses were allegedly committed between 2000-2004.	In the Company's estimation, based on an assessment of Granite's management, which is based on Sonol's legal advisors, at this stage, it is impossible to estimate the amount of Sonol's exposure, should it be convicted, *inter alia* due to the proceeding's preliminary stage.
12. Claim against Sonol	A claim in the sum of approx. NIS 18 million	In March 2011, a claim for monetary relief was filed against Sonol by a company with which an agreement for the construction and operation of a fuelling station was signed, asserting that Sonol breached the agreement therewith.	In the Company's estimation, based on an assessment of Granite's management, which is based on Sonol's legal advisors, the chances of the claim are estimated at less than 50%.
13. Various municipalities versus Supergas	Demands in the sum of approx. NIS 55 million	A demand for the payment of municipal taxes on gas accumulators located in rooms in apartment buildings. Supergas filed an administrative appeal in connection with the charge. The court accepted the appeal and dismissed the charge for municipal taxes. One of the authorities filed a motion for leave to appeal to the Supreme Court, which dismissed the motion and returned the deliberations to the appeal committee.	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Supergas, Supergas's prospects to rebuff the demands of the municipal taxes are greater than 50%.
14. A municipality versus Supergas	Approx. NIS 6 million	A demand for the amendment of a municipal tax assessment (including linkage and interest differentials) for a gas container farm from 1997. Supergas has filed an objection against the assessment and the municipal tax manager rejected the objection. In December 2004, Supergas appealed against the manager's decision.	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Supergas, the prospects for dismissal of the claim for payment in respect of the previous years and with regard to the validity of the amended assessment are higher than 50%.
15. An agency operator versus Supergas	Approx. NIS 34 million	A claim for monetary refunds in respect of investments carried out in an agency that was operated for a several years by the claimant, and thereafter was returned to Supergas. Deliberation of the claim was transferred to arbitration.	According to the Company's assessment, based on an assessment of the management of Granite, which is based on the legal advisors of Supergas, the prospects of the claim being accepted in excess of the amount paid as an interim payment are less than 50%.

16. Supergas versus the Ministry of Environmental Protection		Following a notice received by Supergas from the Ministry of Environmental Protection, regarding its decision not to renew the toxic materials permit for the filling facility for cylinders and containers in Kiryat Atta, Supergas filed, in June 2010, a counter-petition with the Supreme Court.	In January 2012, after the date of the report, the Supreme Court dismissed the petition. In the absence of a toxic materials permit, Supergas will be unable to continue to operate the gas farm in the regular format. The aforesaid notwithstanding, the Ministry of Environmental Protection authorized Supergas to continue operating the gas facility in Kiryat Ata in a limited format, according to the outline specified in the authorization. In addition, in March 2012, a toxic materials permit was granted to the facility, valid until May 1, 2012, permitting Supergas to make use of the facility, subject to the conditions specified in the permit.
17. A municipality versus Supergas	Demands of a municipality in the sum of approx. NIS 68 million of March 2011	Supergas submitted an application for a building permit by virtue of NOP 32c for the aboveground burial of gas cylinders. As a condition to the issue of the permit, the local committee and the municipality sent payment demands on three issues: usage fees in the sum of approx. NIS 4.5 million; development levies and fees in the sum of approx. NIS 4 million; betterment levies in the sum of approx. NIS 59 million.	In the Company's estimation, based on Granite's management's estimate, which is based on Supergas's legal advisors, even though Supergas rejects the demand for betterment levies, it is impossible to quantify the chances of the claim for betterment levies and the financial scope of the liability for this levy, if determined. With respect to the development levies and fees – it may be estimated that there is a higher than 50% probability that the remaining liability, if any, will be much less than the amount requested, but at this stage, it is early to estimate the financial scope thereof. In respect of the usage fee demand – at this stage it is impossible to estimate the chances of the demand and its financial scope, if liability shall be determined. It shall be stated that the demands for betterment levies and for development levies are not mandatory for Supergas, such that if it shall withdraw the permit application, it shall be subject to no financial liability on these issues.

18. Indictment against Supergas and directors thereof	Criminal	In October 2011, the City of Kiryat Ata filed two proceedings against Supergas with the Local Matters Court in Krayot – (1) an indictment pursuant to the Business Licensing Law in respect of the operation of the gas farm in Kiryat Ata without a business license. This proceeding was filed both against the company and against directors thereof. (2) Motion for a cessation of occupation in a business order, in the framework of which the granting of an order against Supergas was sought to order it to immediately halt the gas farm's activity due to the absence of a business license. This motion was filed as an interim motion in the framework of the abovementioned indictment proceeding.	With respect to the motion for a cessation of occupation order – in January 2012, the court's decision was issued, in the framework of which the City's motion was denied. With respect to the indictment proceeding, the Company estimates, based on an assessment of Granite's management, which is based on Supergas's legal advisors, that at this preliminary stage, it is impossible to estimate the chances of the said proceedings.
19. Arbitration proceeding against GES	Approx $1.5 million (and a claim on behalf of GES in the sum of approx. NIS 4 million)	An arbitration proceeding between GES and a third party with respect to a set of agreements concerning the construction of two water treatment plants in the U.S.	The Company estimates, based on an assessment of Granite's management, which is based on GES's legal advisors, that it appears that GES has meritorious claims and that it will not need to bear financial resources (insofar as any shall be awarded against it) since they (if any) are expected to be offset against the claim of GES itself.
20. Claim against GES and others	Approx NIS 10 million	A claim with respect to damage which, according to the Plaintiff, was caused to an orchard as a result of penetration of ballast water to water provided to the orchard, by causing them to flow through the agricultural sludge treatment facility in the water pipes designated for irrigation.	The Company estimates, based on an assessment of Granite's management, which is based on the legal advisors of GES and a third party, that the chances of the claim are estimated at lower than 50%.
21. Claim against GES Plant Operation (a subsidiary of GES, formerly Nitron Chemtec) and former officers	Approx NIS 6 million (in the framework of a counterclaim of April 2011 in a claim of GES Plant Operation versus the Plaintiff in the sum of NIS 4 million, for enforcement and declaratory relief and a permanent injunction).	A claim in respect of alleged damage that was caused to the counter-plaintiff due to the alleged failure of GES Plant Operation to comply with the agreement therewith.	The Company estimates, based on an assessment of Granite's management, which is based on GES Plant Operation's legal advisors, that in view of the proceeding's preliminary stage, it is difficult to currently estimate the chances and risks of the case. However, subject to a professional opinion supporting the claims of GES Plant Operation, the chances of the claims of GES Plant Operation being accepted are greater than 50%.

e. In 2008, a claim for bodily injury totalling NIS 10 million was submitted against two of the Company's subsidiaries. The subject matter of the Complaint is a claim for alleged liability of the Companies in relation to the acts of suicide of two youths of whose heirs are the plaintiffs in the statement of claim. The claim has been recognized as an insurance event and is being conducted through attorneys on behalf of the defendants' insurance company. The case is at the stage of written summations for examination of the mere question of liability pertaining to the suicide events subject matter of the complaint. In the estimation of the Company's management, based on the managements of the companies, the amount of the claim is included within the framework of the insurance cover per insurance event.

f. Additional claims (mostly legal and in insignificant amounts) arising from the ordinary course of business have been submitted against Group companies.

g. In the opinion of the Company management, the provisions made to settle the outcome of the claims outlined above are fair.

h. See also Note 33G.

Note 37 Additional information for the cash flow statement

The following is additional information for the cash flow statement in respect of non-cash activities and the acquisition of initially consolidated companies:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
A. Non-cash activities:			
Payables in respect of the purchase of non-current assets on credit	72,293	53,585	35,476
Receivables in respect of the sale of fixed assets and investment property on credit	850	-	7,228
Receivables in respect of the sale of a financial asset	7,337	-	-
Payables in respect of purchase of shares in a consolidated company	-	4,795	-
Payables in respect of the purchase of non-controlling minority interests	100	-	1,306
B. The acquisition of initially consolidated companies:			
Working capital (except for cash and cash equivalents)	-	(20,431)	-
Investments in associates (including loans to an associate)	-	113,860	-
Fixed assets, net (including investment property)	-	(53,543)	-
Long-term liabilities	-	440,483	-
Non-controlling interests at the time of the acquisition	-	32,408	-
Surplus cost and goodwill created on the acquisition	-	-	-
Restricted investments	-	(20,325)	-
Investments and loans	-	(4,361)	-
Receivables in respect of a franchise arrangement	-	(527,256)	-
Deferred tax liabilities, net	-	15,745	-
Profit from the purchase of shares in investee companies	-	2,884	-
	-	(20,536)	-

Note 38 The management of financial risks

A. General:

The Group is exposed to the following risks, which derive from the use of financial instruments:

- Credit risk.
- Liquidity risk.
- Market risk (including currency risk, interest risk and other price risks).

Information is provided in this Note in respect of the Group's exposure to each of the abovementioned risks, the Group's objectives, its policy and its processes in respect of the measurement and management of the risk. Additional, quantitative disclosure is provided throughout these consolidated financial statements.

The comprehensive responsibility for the institution of the framework for the management of the Company's risks and those of its consolidated companies (except for the management of the risks of Granite and of its subsidiaries, which is executed by them) (the “Company”) and for the supervision over it lies in the hands of the Company’s management.

The Company's finance committee is responsible, *inter alia*, for supervision and monitoring of the Company's risk management policy, and supervises the management's monitoring of compliance with the risk management policy.

The person who has the responsibility in the Company for the management of the market risks is the Company's chief financial officer, Mr. Yuval Bronstein.

The Company's managers routinely examine the market risks in the fields of interest, the index and the exchange rates and act to reduce the economic exposure that is inherent in those risks, whilst taking cost-benefit considerations, such as changes in the composition of the long-term and short-term bank credit, into account.

The risks management policy was crystallized in order to identify and to analyze the risks that the Company is facing, to determine suitable restrictions for the risks and controls and to supervise the risks and the compliance with the restrictions.

The policies and the methods employed for the management of the risks are reviewed on a routine basis in order to reflect changes in the conditions in the market and in the Company's activities. The Company, by means of training and procedures, acts to develop an efficient control environment in which all of the employees understand their roles and their commitments.

B. Credit risk:

Credit risk is the risk of a financial loss that would be caused to the Group if a customer or a counter party to a financial instrument does not meet its contractual commitments, and it derives primarily from the debts of customers and other receivables, from the long-term loans that have been extended and from investments in securities.

The Group does not have significant credit risk that derives from its customers in the main segment, of commercial centers and in malls, and in the rental of floor space for offices and other purposes and this is since the Group is in the custom of collecting its income in respect of rental fees and management fees in advance. Moreover, in most cases, as collateral for the rental fees, the tenants are required to proved personal guarantees from third parties and/or bank guarantees and/or deposits, to the Company's satisfaction.

The Group has a credit risk deriving from the Granite sector. Granite's income derives primarily from sales in Israel to customers in the oil distillates sectors in the direct marketing market and in the fuelling stations and commercial sectors as well as from sales to customers in the paint and finishing of construction industry, and from sales to customers in the water and wastewater segment.

Granite has a procedure for the extension of credit to a customer, which includes guidelines in respect of what is to be done when a new customer is opened, the procedure includes, inter alia, a check on its financial position, a check on stability and control over the credit extended to the customer, which relies on past experience and external raisings, as well as, where possible, the receipt of collateral, such as: bank guarantees, personal guarantees, charges on land, motor vehicles, and debt notes.

Moreover, the procedure includes a hierarchy of authority for the approval of the maximum amount of a customer's credit, which starts with the credit manager and going up to the credit committee, which is headed by the Chief Executive Officer of each subsidiary. The procedure on authorities for the approval of credit is presented to the credit committees of the board of directors of each of the subsidiaries for approval. The procedure determines and defines a framework of responsibility for the collection of the payment from customers and also the ways in which customers' balances that are in arrears are to be dealt with. The routine monitoring of the receipts from customers is conducted by the credit and collection departments and by the credit committee in each subsidiary.

Granite recognizes provisions for doubtful debts, which reflect the evaluation made in respect of the loss that is contained in the debts whose collection is in doubt. This provision is made up of specific balances as well as a general component of the loss, which is determined for

certain groups of similar customers, in respect of losses that have occurred, but which have not yet been identified.

The abovementioned general provision for a loss is determined on the basis of historical information in respect of the payments statistics in respect of similar financial assets.

C. Liquidity risk:

Liquidity risk finds expression in the non-ability to meet the Group's financial commitments when they are due for payment. The Group's approach to the management of its liquidity risk is to ensure, in so far as it is possible, that there is a sufficient level of liquidity to meet its commitments on time. The Group verifies the existence of sufficient levels of cash and/or credit lines in accordance with the expected needs for the payment of the operating expenses, including the amounts that are required to meet the financial liabilities; the aforesaid does not take into account the potential impact of extreme occurrences, which it is not reasonably possible to forecast.

The Group is of the opinion that at the time of need, the banks will grant it the credits required therefor for the purposes of its business.

D. Market risks:

Market risk is the risk that changes in market prices, such as the exchange rates of foreign currencies, the Consumer Prices Index, interest rates, the prices of capital instruments and risks associated with the prices of goods, will have an impact on the Group's income or on the value of its holdings in financial instruments and on inventory balances.

The objective of the management of the market risks is to manage and to supervise the exposure to market risk within the framework of generally accepted parameters.

During the ordinary course of business, Granite buys and sells derivatives and it also takes financial commitments upon itself in order to manage the market risks. The said transactions are carried out in accordance with guidelines that have been set by Granite's balance sheet committee and its Board of Directors.

Currency risk

The Company's functional currency is the New Israeli Shekel (NIS).

Granite is exposed to currency risk in respect of the purchase of raw materials, fixed assets and export sales, which are stated in currencies that are different from the functional currency. The currencies in which most of the transactions are stated are the Euro and the US Dollar (most of the purchases of oil distillates are linked to the US Dollar).

The companies in the Granite Group take action in order to reduce the currency exposure by means of the systematic execution of futures transactions in foreign currencies, in accordance with an outline that has been approved by Granite's Board of Directors. As of the date of the report, the Group had foreign currency futures contracts in an amount of $161.5 million for payment until April 2012, which were intended to hedge the cash flows exposure mainly in respect of the purchase of oil distillates and approx. €2.25 million for reducing the currency exposure in respect of the purchase of raw materials, fixed assets and sales for export in Tambour.

The Group has loans in U.S. dollars, therefore its financial results are exposed to the risk of a change in the dollar exchange rate. Most of the Group's income in the U.S. income-producing property segment is stated in U.S. dollars, such that a rise in the exchange rate as aforesaid leads to an increase in income from rent and reduces this risk.

Interest rates risk

The Group has short-term and long-term credit at variable interest rates as well as a portfolio of securities that includes an investment in bonds that are presented at fair value. Accordingly, its financial results (financing income/expenses) are exposed to the risk of a change in the interest rates. Some of the deposits, loans extended, receivables in respect of a franchise arrangement and some of the long-term credit are at fixed interest and therefore they are exposed to risk in respect of a change in the fair value as the result of changes in the interest rate in the market.

Index risks

The Group has loans and bonds that are Index-linked, and therefore its financial results (financing income/expenses) are exposed to the risk of a change in the Index.

Most of the Group's income in the commercial centers and malls segment and in the office and other space for lease segment are linked to the Consumer Price Index, such that an increase in the Index, as aforesaid, will lead to an increase in the rental income and a reduction in this risk.

The companies in the Granite sector are in the habit of purchasing forward transactions on the Consumer Prices Index from time to time, in accordance with an outline that has been approved by the Granite's Board of Directors or by the board of its consolidated company. As of the date of the Financial Statements, the Group was engaged in forward contracts on the Consumer Prices Index in an amount of NIS 460 million.

In addition, companies in the Group from the Granite sector occasionally acquire interest on CPI rate swap contracts. As of the date of the financial statements, such companies have interest swap contracts whose payment date matches the payment date of certain loans. These contracts are designated as defined items in cash flow hedge.

Securities price risk

Upon completion of the IPO pursuant to the Prospectus and the private placement of the Company's shares, during the June 2010, the Company began managing the IPO proceeds in accordance with the policy and limitations according to which the monies will be managed in a diversified manner, in order to disperse the risks, so that a rate of up to 30% will be managed through investment in shares which are traded in the Tel Aviv 100 index or in shares of Canadian companies which are traded in the S&P TSX Composite Index in Toronto, Canada, and the balance shall be managed through investment in bonds which are rated BB+ or higher and/or in deposits in financial institutions. As of December 31, 2011, part of the IPO proceeds were invested in negotiable securities, and therefore the Company may be exposed to fluctuations in the securities' prices and the market value of its investments therein, which may affect the value of the managed portfolio, the cash flow and the liquid means of the Company. A small part of the funds are also managed overseas in the Canadian dollar currency, and therefore the Company may be exposed to fluctuations in the currency exchange rates. In general, and other than as specified by the Company in the Prospectus, the Company takes no protective measures against such exposures.

In the course of 2011, the Company has exercised most of the securities which are traded in Canada.

In addition, the Company has a material holding in Bank Leumi's shares that are traded in TASE. Changes in the rate of Bank Leumi's share may affect the equity. The Company does hedge against such exposures (see also Note 2V).

Risks associated with the prices of goods

The Group's inventory is comprised primarily of oil distillates and accordingly the Group has an exposure to changes in the prices of oil distillates. It arises from checks that have been conducted by the Company, using external consultants, that the financial instruments market does not offer appropriate hedging tools for the mechanism under which the prices of oil distillates are fixed in Israel (which are determined on the basis of the CIF prices at Lavera port in Italy). Accordingly, the Group has no effective possibility of hedging this risk. Therefore, the Group does not carry out hedging activity in respect of this risk, however it does act to reduce the quantity of inventory that is exposed and it adjusts the quantities of the inventory of distillates in accordance with the sales forecasts. It should be emphasized that this exposure primarily affects the quantities of the inventory of distillates. Distillates that are purchased and sold during the course of the month are not exposed to this risk.

Note 39 - Financial instruments

A. Credit risk:

(1) Exposure to credit risk

The carrying values of the financial assets represent the maximum credit exposure. The maximum exposure to credit risk, as of the date of the statement of financial position, was as follows:

	As of December 31	
	2011	2010
	NIS in thousands	NIS in thousands
Financial assets at fair value through profit and loss:		
Financial assets that are held for trade	1,401,786	2,310,423
Derivative financial instruments	5,147	375
Financial assets at amortized cost:		
Short-term deposits and investments	84,271	48,274
Trade receivables	1,719,764	1,339,109
Other receivables	71,778	38,283
Receivables for works in progress	32,649	34,982
Non-current investments and loans	90,615	92,007
Restricted investments	50,930	49,448
The Fuel Authority	132,720	123,569
Loans to associates	33,080	27,648
Long-term receivables in respect of a franchise arrangement	554,912	546,383
	4,177,652	4, 610,501

The maximum exposure to credit risk in respect of trade receivables, other receivables, including derivative financial instruments, receivables for works in progress, investments and long-term loans , as of the date hereof, by geographical region, is mainly local and the exposure overseas is negligible.

As of the date hereof, by counter party, the exposure was:

	As of December 31	
	2011	**2010**
	NIS in thousands	**NIS in thousands**
Institutional customers	97,586	71,084
Business customers	1,488,907	1, 110,996
Private customers	133,271	157,059
Receivables for works in progress	32,649	34,982
Other receivables, including derivative instruments	76,925	38,658
Non-current investments and loans	90,615	92,007
	1,919,953	1,504,756

See Note 5 in respect of the credit risk on financial assets that are held for trade (other than shares).

(2) The aging of debts and losses from impairment in value

The following is the aging of the trade receivables, other receivables, including derivative financial instruments, receivables for works in progress, investments and long-term loans:

	As of December 31 2011		As of December 31 2010	
	Gross	Impairment	Gross	Impairment
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Not in arrears	1,797,803	9,565	1,383,164	8,633
0–30 days in arrears	43,986	1,420	46,041	1,448
31-120 days in arrears	31,349	4,710	28,076	15,189
121 days to one year in arrears	39,211	20,433	38,642	9,784
More than one year in arrears	218,479	174,747	221,502	177,615
	2,130,828	210,875	1,717,425	212,669

The movements in the provision for impairment in value in respect of trade receivables, other receivables and non-current loans during the year were as follows:

	As of December 31	
	2011	2010
	NIS in thousands	NIS in thousands
Balance as of January 1	212,669	207,981
Impairment loss recognized	2,924	10,751
Doubtful debts that became bad debts	(4,718)	(6,063)
Balance as of December 31	210,875	212,669

The Group reviews the impairment in value in each reporting period and takes into account the period of the debt, the collateral that is available to it, the financial state of the debtors and the chances of legal proceedings against them.

As of December 31, 2011, credit of NIS 302,571 thousand to customers is secured by credit insurance (including the self deductible), (December 31, 2010 – NIS 248,224 thousand).

Based on past experience, the Group has a general provision for impairment due to losses that occurred but have not yet been recognized that amount to NIS 5,662 thousand as of December 31, 2011 (December 31, 2010 - NIS 5,077 thousand).

B. Liquidity risk

Following are details of the forecast repayment dates of the financial assets:

	As of December 31, 2011						
	Book value	Forecasted cash flow	2012	2013	2014	2015	2016 onwards
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Cash and cash equivalent	224,430	224,430	224,430	-	-	-	-
Financial assets held for trade	1,401,786	1,401,786	1,401,786	-	-	-	-
Short-term deposits and investments	84,271	84,271	84,271	-	-	-	-
Trade receivables	1,719,764	1,719,764	1,719,764	-	-	-	-
Other receivables	80,341	80,341	80,341	-	-	-	-
Receivables for work in progress	32,649	32,649	32,649	-	-	-	-
Financial assets available for sale	1,305,184	1,305,184	-	-	-	-	1,305,184
Financial assets designated at fair value through profit and loss	16,737	16,737	16,737	-	-	-	-
Loans to associates	33,080	33,080	-	-	-	-	33,080
The Fuel Administration	132,720	132,720	-	-	-	-	132,720
Long-term receivables in respect of a franchise arrangement	534,596	534,596	-	22,190	22,882	24,060	465,464
Loans to customers	69,903	69,903	-	11,372	10,946	9,974	37,611
Loans to others	444	444	-	86	86	86	186
Collectible checks and notes	9,607	9,607	-	1,834	651	332	6,790
Long-term trade and other receivables	10,660	10,660	-	562	(252)	418	9,932
Restricted investments	50,930	50,930	-	-	-	-	50,930
	5,707,102	5,707,102	3,559,978	36,044	34,313	34,870	2,041,897

	As of December 31, 2010						
	Book value	**Forecasted cash flow**	**2011**	**2012**	**2013**	**2014**	**2015 onwards**
	NIS in thousands	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**
Cash and cash equivalent	177,858	177,858	177,858	-	-	-	-
Financial assets held for trade	2,310,423	2,310,423	2,310,423	-	-	-	-
Short-term deposits and investments	48,274	48,274	48,274	-	-	-	-
Trade receivables	1,339,109	1,339,109	1,339,109	-	-	-	-
Other receivables	57,966	57,966	57,966	-	-	-	-
Receivables for work in progress	34,982	34,982	34,982	-	-	-	-
Financial assets available for sale	1,828,302	1,828,302	-	-	-	-	1,828,302
Financial assets designated at fair value through profit and loss	17,408	17,408	-	-	-	-	17,408
Loans to associates	27,648	27,648	-	-	-	-	27,648
The Fuel Administration	123,569	123,569	-	-	-	-	123,569
Long-term receivables in respect of a franchise arrangement	527,075	527,075	-	20,316	21,406	21,700	463,653
Loans to customers	62 ,225	62,225	-	8,024	6,769	6,517	40,915
Loans to others	12,601	12,601	-	1,107	1,039	1,413	9,042
Collectible checks and notes	12,763	12,763	-	4,568	985	376	6, 834
Long-term trade and other receivables	4,418	4,418	-	308	43	7	4,060
Long-term deposit	49,448	49,448	-	-	21,276	-	28,172
	6,634,069	6,634,069	3,968,612	34,323	51 ,518	30,013	2,549,603

Following are details of the forecast repayment dates of the financial assets, including estimate of interest payment:

	As of December 31, 2011						
	Book Value	**Forecasted Cash Flow**	**2012**	**2013**	**2014**	**2015**	**2016 onwards**
	NIS in thousands	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**
Non-derivative financial liabilities							
Overdraft	2,846	2,846	2,846	-	-	-	-
Short-term credit from banks and other credit providers (1)	1,815,360	1,822,314	1,822,314	-	-	-	-
Deposits from customers (3)	105,995	105,995	105,995	-	-	-	-
Loans from banks and other credit providers (2)	4,241,418	5,522,972	697,614	1,568,067	388,349	439,402	2,429,540
Bonds	1,891,768	2,334,039	269,478	262,581	213,954	139,370	1,448,656
Liabilities for finance leasing	61,904	109,843	5,763	5,766	5,769	5,773	86,772
Long-term deposits from customers	37,760	37,760	-	-	-	37,760	-
Other long-term liabilities	2,907	2,960	905	677	1,109	-	269
Capital notes	1,084	1,195	-	98	98	98	901
Derivative financial instrument liabilities							
Forward contracts on exchange rates that are not used for hedge accounting - payments	37	37	37	-	-	-	-
Forward contracts on the Consumer Price Index and payments	5,650	5,650	5,650	-	-	-	-
Embedded derivatives	1,700	1,700	-	-	-	1,700	-
	8,168,429	9,947,311	2,910,602	1,837,189	609,279	624,103	3,966,138

	As of December 31, 2010						
	Book Value	**Forecasted Cash Flow**	**2011**	**2012**	**2013**	**2014**	**2015 onwards**
	NIS in thousands	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**	**NIS in thousands**
Non-derivative financial liabilities							
Overdraft	1,117	1,117	1,117	-	-	-	-
Short-term credit from banks and other credit providers (1)	1,041,827	1,044,328	1,044,328		-	-	-
Deposits from customers (3)	103,366	103,366	103,366	-	-	-	-
Loans from banks and other credit providers (2)	3,858,582	4,986,323	742,544	589,619	1,425,611	277,414	1,951,135
Bonds	2,018,771	2,545,298	269,488	262,752	256,026	208,609	1,548,423
Bonds convertible into shares in a consolidated company (2)	21,359	21,553	21,553	-	-	-	-
Liabilities for finance leasing	66,073	128,047	6,140	6,144	6,145	6,148	103,470
Long-term deposits from customers	34,529	34,529	-	-	-	34,529	-
Other long-term liabilities	5,064	5,169	662	2,813	631	-	1,063
Capital notes	1,057	1,195	-	98	98	98	901
Derivative financial instrument liabilities							
Forward contracts on exchange rates that are not used for hedge accounting -	10,387	10,387	10,387	-	-	-	-
Forward contracts on the Consumer Price Index and payments	1,439	1,439	1,439	-	-	-	-
	7,163,571	8,882,751	2,201,024	861,426	1,688,511	526,798	3,604,992

(1) The carrying value includes the accumulated interest as of December 31, 2011 and 2010.

(2) The carrying value includes current maturities and accumulated interest as of December 31, 2011 and 2010.

(3) The deposits are presented as current liabilities since the law enables the customer to leave at any time that they choose and to receive the deposits back immediately together with this, it should be noted that Supergas's past experience is that the rate at which customers leave is immaterial and therefore the amounts of the deposits that are returned to customers each year is also immaterial.

(4) See Note 35B in respect of guarantees.

C. Index and foreign currency risks:

(1) Exposure to Index and foreign currency risk

The Group's exposure to Index and foreign currency risk, based on nominal values, is as follows:

	As of December 31, 2011					
	Israeli currency		Foreign currency			
	Non-linked	Index-linked	Dollar	Other(*)	Other	Total
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Current assets						
Cash and cash equivalent	203,643	-	16,854	3,933	-	224,430
Financial assets held for trade	797,506	501,411	11,048	91,821	-	1,401,786
Short-term deposits and investments	84,271	-	-	-	-	84,271
Trade receivables	1,644,962	3,084	66,692	5,026	-	1,719,764
Other receivables	32,794	19,552	43,881	1,011	47,446	144,684
Receivables for work in progress	20,179	943	10,588	939	-	32,649
Inventory	-	-	-	-	439,933	439,933
Current tax assets	-	-	-	-	24,626	24,626
Total current assets	2,783,355	524, 990	149,063	102,730	512,005	4,072,143
Non-current assets						
Investments in associates	-	-	-	-	13,140	13,140
Loans to associates	12,508	20,572	-	-	-	33,080
Investments, loans and receivables	37,370	52,611	5,591	-	26,554	122,126
Restricted investments	28,893	22,037	-	-	-	50,930
Financial assets available for sale	1,302,371	-	-	2,813	-	1,305,184
Financial assets designated at fair value through profit and loss	1,364	-	15,373	-	-	16,737
Long-term receivables in respect of a franchise arrangement	60,013	465,214	2,186	4,997	2,186	534,596
The Fuel Administration	-	-	132,720	-	-	132,720
Investment property and investment property under construction	-	-	-	-	14,839,570	14,839,570
Fixed assets	-	-	-	-	1,427,028	1,427,028
Intangible assets	-	-	-	-	540,406	540,406
Rent paid in advance	-	-	-	-	36,603	36,603
Deferred tax assets	-	-	-	-	55,450	55,450
Total non-current assets	1,442,519	560,434	155,870	7,810	16,940,937	19,107,570
Total assets	4,225,874	1,085,424	304,933	110,540	17,452,942	23,179,713

(*) Mainly CAD and Euro.

The Group's exposure to index and foreign currency risk, based on nominal values, is as follows:

	As of December 31, 2011					
	Israeli currency		foreign currency			
	Non-linked	Index-linked	Dollar	Other (*)	Other	Total
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Current liabilities						
Credit from banks and other credit providers	1,834,651	470,785	115,240	24,746	-	2,445,422
Trade payables	337,180	18,238	463,187	36,119	-	854,724
Other payables	81,267	41,044	37,933	513	225,092	385,849
Deposits from customers	-	105,995	-	-	-	105,995
Provisions	-	-	-	-	29,288	29,288
Current tax liabilities	-	-	-	-	42,107	42,107
Total current liabilities	2,253,098	636,062	616,360	61,378	296,487	3,863,385
Non-current liabilities						
Loans from banks and other credit providers	466,129	2,610,504	681,204	-	-	3,757,837
Bonds	-	1,706,726	-	-	-	1,706,726
Employee benefits	-	-	-	-	59,312	59,312
Other liabilities	11,685	44,486	43,225	544	182	100,122
Deferred tax liabilities	-	-	-	-	2,228,273	2,228,273
Total non-current liabilities	477,814	4,361,716	724,429	544	2,287,767	7,852,270
Total liabilities	2,730,912	4,997,778	1,340,789	61,922	2,584,254	11,715,655
Total net balance sheet balance	1,494,962	(3,912,354)	(1,035,856)	48,618	14,868,688	11,464,058

(*) Mainly Euro and GBP.

The Group's exposure to Index and foreign currency risk, based on nominal values, is as follows:

	As of December 31, 2010					
	Israeli currency		Foreign currency			
				Other*		
	Non-linked	Index-linked	Dollar		Other	Total
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Current assets						
Cash and cash equivalent	152,345	-	16,262	9,251	-	177,858
Financial assets held for trade	1,365,526	672,522	9,402	262,973	-	2,310,423
Short-term deposits and investments	48,274	-	-	-	-	48,274
Trade receivables	1,265,360	3,762	64,908	5,079	-	1,339,109
Other receivables	29,224	21,485	6,396	1,000	37,128	95,233
Receivables for work in progress	20,004	5,668	7,733	1,577	-	34,982
Inventory	-	-	-	-	346,054	346,054
Current tax assets	-	-	-	-	12,319	12,319
Total current assets	2,880,733	703,437	104,701	279,880	395,501	4,364,252
Non-current assets						
Investments in associates	-	-	-	-	15,309	15,309
Loans to associates	7,609	20,039	-	-	-	27,648
Investments and loans	34,601	56,412	994	-	27,526	119,533
Restricted investments	28,172	21,276	-	-	-	49,448
Financial assets available for sale	1,819,854	-	-	8,448	-	1,828,302
Financial assets designated at fair value through profit and loss	2,278	-	15,130	-	-	17,408
Long-term receivables in respect of a franchise arrangement	58,814	468,261	-	-	-	527,075
The Fuel Administration(**)	-	-	123,569	-	-	123,569
Investment property and investment property under construction	-	-			12,210,264	12,210,264
Fixed assets	-	-	-	-	1,419,748	1,419,748
Intangible assets	-	-	-	-	551,517	551,517
Rent paid in advance	-	-	-	-	39,454	39,454
Deferred tax assets	-	-	-	-	49,851	49,851
Total non-current assets	1,951,328	565,988	139,693	8,448	14,313,669	16,979,126
Total assets	4,832,061	1,269,425	244,394	288,328	14,709,170	21,343,378

(*) Mainly in CAD and Euro.

(**) The balance bears variable interest which is collected each month.

The Group's exposure to Index and foreign currency risk, based on nominal values, is as follows:

	As of December 31, 2010					
	Israeli currency		foreign currency			
	Non-linked	Index linked	Dollar	Other (*)	Other	Total
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Current liabilities						
Credit from banks and other credit providers	1,044,913	475,692	229,006	22,702	-	1,772,313
Trade payables	310, 651	10,880	332,247	29,005	-	682, 783
Other payables	92,646	23,085	25,075	682	224,682	366,170
Deposits from customers	-	103,366	-	-	-	103,366
Provisions	-	-	-	-	32,883	32,883
Current tax liabilities	-	-	-	-	35,265	35,265
Total current liabilities	1,448,210	613,023	586,328	52,389	292,830	2,992,780
Non-current liabilities						
Loans from banks and other credit providers	417,488	2,784,274	98,333	-	42	3,300,137
Bonds	-	1,835,675	-	-	-	1,835,675
Employee benefits	-	-	-	-	54,311	54,311
Other liabilities	15,893	46,131	39,199	-	187	101,410
Deferred tax liabilities	-	-	-	-	1,534,228	1,534,228
Total non-current liabilities	433,381	4,666,080	137,532	-	1,588,768	6 ,825,761
Total liabilities	1,881,591	5,279,103	723,860	52,389	1,881,598	9,818,541
Total net balance sheet balance	2,950,470	(4,009,678)	(479,466)	235,939	12,827,572	11,524,837

(*) Mainly Euro and GBP.

(2) Sensitivity analysis

The strengthening of the New Israeli Shekel against the following currencies as of December 31, 2011 and an increase in the Consumer Prices Index would increase (decrease) the capital and the profit or loss, net of tax, by the amounts that are presented below. This analysis has been made on the assumption that the other variables, and especially the interest rates, remain fixed. The analysis in respect of the year 2010 was made on the same basis.

	As of December 31 2011	
	Capital	Profit (loss)
	NIS in Thousands	NIS in Thousands
1% rise in the Consumer Price Index	(24,826)	(24,826)
1% rise in the exchange rate of the US Dollar	(2,673)	(2,673)

	As of December 31 2010	
	Capital	Profit (loss)
	NIS in Thousands	NIS in Thousands
1% rise in the Consumer Price Index	(25,379)	(25,379)
1% rise in the exchange rate of the US Dollar	(13)	(13)

A decrease in the exchange rate of the US Dollar by a similar rate and a decrease in the CPI by a similar rate as of December 31 would have had an identical effect, but in the opposite direction, in the same amount, on the assumption that all of the other variables remained constant.

(3) Derivative instruments

a. Following are details of the Group's derivative financial instruments:

	As of December 31, 2011				
	Par value	**Currency receivable**	**Currency payable**	**Expiry/ repayment/ exercise date**	**Fair value**
	Thousands				**NIS in Thousands**
Instruments that are not used for hedge accounting:					
Forward transactions on the CPI	459,795	NIS(*)	NIS	January-October 2012	(5,650)
Forward transactions on exchange rates	161,500	Dollar	NIS	January-April 2012	5,136
Forward transactions on exchange rates	1,000	EURO	NIS	January-April 2012	11
Sale options with foreign exchange	1,250	EURO	NIS	January-February 2012	(37)
					(540)
Instruments that are used for hedge:					
Interest rate SWAP contracts	31,298	Index	NIS	January 2012-July 2016	(182)

(*) Index-linked.

	As of December 31, 2010				
	Par value	**Currency receivable**	**Currency payable**	**Expiry/ repayment/ exercise date**	**Fair value**
	Thousands				**NIS Thousands**
Instruments that are not used for hedge accounting:					
Forward transactions on the CPI	625,000	Shekel (*)	Shekel	January – December 2011	(1,064)
Forward transactions on exchange rates	131,900	Dollar	Shekel	January- May 2011	(10,235)
Forward transactions on exchange rates	2,600	Euro	Shekel	January-April 2011	(152)
					(11,451)

(*) Index-linked.

b. The following is a sensitivity analysis in respect of the Group's derivative instruments. A change in the Consumer Prices Index or the exchange rate of the Dollar and the Euro, would increase (decrease) the profit and the loss, net of tax and the equity by the amounts that are presented below. This analysis is made on the assumption that all of the other variables will remain constant.

	December 31, 2011								
	An increase of 10%%		An increase of 5%			A decrease of 5%		A decrease of 10%	
	Capital	Profit (loss)	Capital	Profit (loss)	Fair value	Capital	Profit (loss)	Capital	Profit (loss)
	NIS in Thousands								
Instruments that are not used for hedge accounting:									
Change in the CPI									
Forward transactions	34,485	34,485	17,242	17,242	(5,650)	(17,242)	(17,242)	(34,485)	(34,485)
Change in the Dollar exchange rate									
Forward transactions	46,311	46,311	23,156	23,156	5,136	(23,156)	(23,156)	(46,311)	(46,311)
Change in the Euro exchange rate									
Forward transactions	371	371	185	185	11	(185)	(185)	(371)	(371)
Sale option	(28)	(28)	(28)	(28)	(37)	(205)	(205)	(473)	(473)
Instruments that are used for hedge:									
Interest rate SWAP contracts	2,490	2,490	1,245	1,245	(182)	(1,245)	(1,245)	(2,490)	(2,490)
Other derivative instruments									
Change in the CPI									
Embedded financial asset	7,737	7,737	3,869	3,869	(289)	(3,869)	(3,869)	(7,737)	(7,737)
Change in the Dollar exchange rate									
Embedded financial asset	5,020	5,020	2,510	2,510	(238)	(2,510)	(2,510)	(5,020)	(5,020)
Change in the Euro exchange rate									
Embedded financial asset	4,523	4,523	2,261	2,261	(544)	(2,261)	(2,261)	(4,523)	(4,523)

	As of December 31, 2010								
	An increase of 10%%		An increase of 5%			A decrease of 5%		A decrease of 10%	
	Capital	Profit (Loss)	Capital	Profit (Loss)	Fair value	Capital	Profit (Loss)	Capital	Profit (Loss)
	NIS in Thousands								
Instruments that are not used for hedge accounting:									
Change in the CPI									
Forward transactions	46,875	46,875	23,438	23,438	(1,064)	(23,438)	(23,438)	(46,875)	(46,875)
Change in the Dollar exchange rate									
Forward transactions	35,064	35,064	17,532	17,532	(10,235)	(17,532)	(17,532)	(35.064)	(35,064)
Change in the Euro exchange rate									
Forward transactions	924	924	462	462	(152)	(462)	(462)	(924)	(924)

D. Interest rate risk

(1) Type of interest

The following are details in respect of the types of interest in the Group's interest bearing financial instruments

	Carrying value	
	As of December 31	
	2011	2010
	NIS Thousands	NIS Thousands
Fixed interest instruments		
Financial assets (*)	2,007,413	2,123,456
Financial liabilities	5,595,605	5,590,253
Variable interest instruments		
Financial liabilities	1,127,815	1,386,446

(*) In the report period includes financial assets held for trade in the sum of approx. NIS 1,322 million.

(2) Sensitivity analysis for the fair value in respect of fixed interest instruments

The Group's assets and liabilities at fixed interest are not measured at fair value through profit and loss, with the exception of investment in negotiable bonds. Therefore, a change in the interest rates as of the date of this report is not expected to have any impact on the profit or loss in respect of changes in the value of assets and liabilities with fixed interest rates, other than the investment in marketable bonds with fixed interest rates.

A rise in the rate of the fixed interest as of December 31, 2011 would increase (reduce) the profit or loss, and the capital, net of tax, in the amounts presented below. This analysis was made assuming that all of the other variables remained fixed. In addition, the sensitivity analysis was made assuming that the sum of the assets as of the end of the report period, as of December 31, 2011, was applicable throughout the report year.

	Capital	Profit (Loss)
	NIS in Thousands	NIS in Thousands
A rise of 2% in the NIS interest rate	(19,880)	(19,880)
A rise of 2% in the real interest rate	(26,675)	(26,675)
A rise of 2% in the interest rate on the CAD	(3,359)	(3,359)

(3) Sensitivity analysis for variable interest instruments

A change of 1% in the interest rates on the date of the report would increase or reduce the capital and the profit or loss, net of tax, by the sum of NIS 15,462 thousand. This analysis was made assuming that the other variables remained fixed.

E. Other price risk:

Sensitivity analysis of the security price

If the prices of the held securities (other than bonds with fixed interest rates) were higher/lower by 1%, the effect after tax would be as follows:

Financial assets held for trade in the sum of approx. NIS 429 million –

The net profit for the year ended December 31, 2011 would increase/decrease by NIS 3,259 thousand.

Financial assets available for sale – (see Note 12A(1))

The net profit for the year ended December 31, 2011 would not be affected since these investments are treated as available for sale and they were not disposed of and their value does not decline.

The other comprehensive income would increase/decrease by NIS 5,783 thousand as of December 31, 2011 as a result of the change in the fair value of the shares.

F. Fair value:

(1) Fair value by comparison to the carrying values in the accounting records

The carrying value of certain financial assets and liabilities, including cash and cash equivalents, marketable securities, deposits and short-term deposits and investments, trade receivables, other receivables, derivatives, restricted investments, available for sale financial assets, overdrafts from banking entities, short-term loans and credit, suppliers, other payables and customer deposits, accord with or is close to their fair value.

The fair value of the other financial assets and liabilities and their book values, which are presented in the statement of financial position, are as follows:

	As of December 31			
	2011		2010	
	Carrying value	Fair value	Carrying value	Fair value
	NIS in Thousands	NIS in Thousands	NIS in Thousands	NIS in Thousands
Non-current assets:				
Loans to associates (1)	33,080	32,413	27,648	27,334
Loans to customers and others (1)	92,609	87,196	99,979	90,917
Receivables in respect of a franchise arrangement	554,912	589,329	546,383	598,407
	680,601	708,938	674,010	716,658
Non-current liabilities:				
Loans from banks and other credit providers (1)	4,266,224	4,446,763	3,881,368	4,135,217
Bonds (1)	1,891,768	2,046,020	2,018,771	2,248,463
Bonds convertible into shares in consolidated company (including the conversion component) (1)	-	-	21,401	21,543
Liabilities for finance leasing	61,904	61,915	66,073	70,645
	6,219,896	6,554,698	5,987,613	6,475,868
Surplus of liabilities over assets	5,539,295	5,845,760	5,313,603	5,759,210

(1) The carrying value in the accounting records includes current maturities and accrued interest.

(2) See Note 3C in respect of the basis of the determination of the fair value.

(2) The interest rates used in the determination of the fair value

The interest's rates used in the discounting of the expected cash flows, where relevant, are based on the government yield curve for each individual type of loan, as of the reporting date, with the addition of an appropriate fixed credit margin, as follows:

	As of December 31	
	2011	2010
	%	%
Non-current assets:		
Loans to associates	8	8.41
Loans to customers and others	4-8	5-9.16
Receivables in respect of a franchise arrangement	4.11-4.54	3.66-4.05
Non-current liabilities:		
Loans from banks and other credit providers	2.5-5.6	0.6-4.7
Bonds	2.27-3.9	1.83-2.45
Liabilities for finance leasing	4-8	3.86-6.33

(3) The hierarchy of fair value

The following table presents an analysis of the financial instruments that are measured at fair value, using an evaluation model. The various hierarchical levels have been defined as follows:

- Level 1: Quoted prices (without adjustments) in an active market for identical instruments.
- Level 2: Data which has been observed, directly or indirectly, which are not includes in level 1 above (in respect of investments in financial assets that were designated at fair value through profit and loss, use is made of up to date transactions in the market between a willing buyer and a willing seller. In respect of other financial investments, use is made of the expected interest rate and the expected change in the index.
- Level 3: Data that are not based on observed market data.

	As of December 31, 2011			
	Level 1	**Level 2**	**Level 3**	**Total**
	NIS in Thousands	**NIS in Thousands**	**NIS in Thousands**	**NIS in Thousands**
Financial assets held for trade:				
Government bonds	487,252	-	-	487,252
Marketable corporate bonds	547,058	-	-	547,058
Shares	246,914	-	-	246,914
Convertible bonds	105	-	-	105
Participation certificates in trust funds	117,994	-	-	117,994
Other	2,463	-	-	2,463
Derivative not used for hedge:				
Forward transactions	-	5,147	-	5,147
Derivative used for hedge:				
Interest rate SWAP contracts	-	505	-	505
Financial assets held for sale:				
Marketable shares	770,693	-	-	770,693
Non-marketable shares	-	-	534,491	534,491
Financial assets designated as at fair value through profit and loss				
Marketable shares	1,389	-	-	1,389
Non-marketable investments	-	15,348	-	15,348
	2,173,868	21,000	534,491	2,729,359
Financial liabilities:				
Forward transactions on CPI not used for hedge	-	5,650	-	5,650
Acquisition option on foreign currency	-	37	-	37
Interest rate SWAP contracts used for hedge	-	687	-	687
Embedded derivatives	-	-	1,700	1,700
	-	6,374	1,700	8,074

(4) Financial instruments that are measures at fair value at level 3

The following table represents the reconciliation between the opening balance and the closing balance in respect of financial instruments that are measured at fair value at level 3 in the hierarchy of fair value.

	For the year ended December 31 2011
	NIS in Thousands
Available for sale financial assets:	
Balance as of January 1, 2011	544,757
Total profits (losses) recognized:	
In other comprehensive income	(3,135)
In the income statement	206
Sales	(7,337)
Carried to level 3	-
	534,491

The following table shows the sensitivity of the fair values for alternatives that are reasonably possible in the assumptions as of December 31, 2011:

	Reflected under other comprehensive income	
	Reduction of 1% in the discount rate	Increase of 1% in the discount rate
	NIS Thousands	NIS Thousands
Non-marketable shares that are presented as available for sale financial assets, net of tax (see also Note 12A(2))	75,020	(57,340)

G. Financial guarantees

See Note 35B on the subject of financial guarantees.

Note 40 Related and interested parties

A. Parent company, controlling interest and subsidiary:

As aforesaid in Note 1A, the Company is a company that is held by Nadav Investments (a company that is resident in Canada) (the "Parent Company"), a company that is controlled by Mr. David Azrieli and his family. On the subject of the subsidiaries, see Note 46 in respect of the Group's entities.

B. Benefits for key managerial personnel (including directors who are employed by the Company):

Benefits in respect of the employment of key management personnel (including directors who are employed in the Company) include:

	For the year ended December 31					
	2011		2010		2009	
	Number of persons	Amount NIS in thousands	Number of persons	Amount NIS in thousands	Number of persons	Amount NIS in thousands
Short-term benefits (1) (3)	13	44,141	12	40,699	6	41,846
Benefits in respect of the termination of employee-employer relations					2	2,403
Other long-term benefits		(58)	1	1,512	1	3,895
Share based payments (2)	5	2,722	4	6,710	1	2,403
		46,805		48,921		50,547

(1) See also Note C(1) below

(2) See Notes 25A and 25C.

(3) In 2011 and 2010 it includes 6 directors who are not employed by the Company.

C. Transactions and balances with related and interested parties:

	For the year ended December 31				
	2011	2010	2009	2011	2010
	Amounts of transactions			Balances in balance sheet	
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Interested party and related parties owned by the interested party					
Rental income	325	46			377
Financing income net (**) (5)	10	6	369		
Donations (9)	7,685	5,186			
Other receivables				3	637
Other payables				15,470	10,180
Associates					
Financing income	7,624	10,444	16,123		
Income from management services		242	199		
Income from services		5,796	9,007		
Loans and capital notes to associates				126,346	106,280
Trade receivables	31			21	

	For the year ended December 31		
	2011	2010	2009
	Amounts of Transactions		
	NIS in thousands		
Key management personnel (including directors) in the Company (*)			
Interested parties who are employed by the Company	30,432	38,229	45,592
Number of persons to whom the benefit relates	3	3	4
Director remuneration for interested parties who are not employed by the Company	177	100	
Number of persons to whom the benefit relates	2	2	
Remuneration for directors who are not employed by the Company	717	261	
Number of persons to whom the benefit relates	4	4	

(*) This information is included in Section B above.

(**) As of December 31, 2010 approx. NIS 377 thousand Index-linked and bear annual interest of 4%.

(1) In January 2001 the Company entered into agreements with related companies, that are registered in Canada and which are controlled by the Chairman of the Board of Directors, according to which they are entitled to annual management fees and consultancy fees at the level of 0.5% of the annual turnover of its stores. The agreements are for a period of 5 years, as from January 1, 2001. At the end of the period, the agreement will be extended for two additional periods. Each of the parties is entitled to discontinue the commitment and this is to be done by giving written notice 30 days in advance to the other party.

In January 2001 a consolidated company entered into a commitment under agreements with related companies that are registered in Canada and which are controlled by the Chairman of the Board of Directors, according to which they are entitled to annual management fees and consultancy fees at the level of the higher of 3 million Dollars or alternatively an amount that is equivalent to 5% of their income that is derived from the rental fees for its office space and also 0.5% of the annual turnover of its stores**.** The agreements are for a period of 5 years, as from January 1, 2001. At the end of the period, the agreement will be extended for two additional periods. Each of the parties in entitled to discontinue the commitment and this is to be done by giving written notice 30 days in advance to the other party.

In January 2001 another consolidated company entered into a commitment under agreements with related companies that are registered in Canada and which are controlled by the Chairman of the Board of Directors, according to which they are entitled to annual management fees and consultancy fees at the level of 5% of their rental income. The agreements are for a period of 5 years, as from January 1, 2001. At the end of the period, the agreement will be extended for two additional periods. Each of the parties in entitled to discontinue the commitment and this is to be done by giving written notice 30 days in advance to the other party.

On May 5, 2010 the Company's board of directors and the Company's general meeting approved the replacement of the foregoing management agreement with a new agreement for provision of management services between the Company and Canadian companies wholly owned and controlled by Mr. David Azrieli (the "Management Company"), whereby the Management Company will provide the Company with management services through Mr. David Azrieli for a period of five years commencing from April 1, 2010 (the "Management Agreement").

In view of Amendment 16 to the Companies Law, the agreement will expire in May 2013.

The Management Company will grant the Company consulting, assistance, supervision and control services which include supporting the Group in its main fields of business, whilst making a significant contribution from the experience and expertise of Mr. David Azrieli or any person on behalf of the Management Company in the future, in development and architectural planning, consulting in the management and construction of commercial centers and malls and office towers and the creation of a composition of diverse, high-quality and financially strong lessees, provision of professional and business support, including supporting various processes of the Company and the Group, assistance in identifying acquisition transactions for the Company and for the Group, assistance in the conduct of negotiations for acquisitions and mergers in the fields of business of the Company and the Group and supervision of management of market research and business development, all as the Company shall require for the purpose of promoting and supervising its business and as shall be required of the Management Company by the Company's board of directors from time to time (the "Services").

In the framework of the Services, if requested to do so by the Company, the Management Company shall provide the said services, either by way of membership on boards of directors or otherwise, also to the Group companies, in Israel and overseas, without any additional consideration.

In addition, and so long as the Company's board of directors shall not have decided otherwise, Mr. David Azrieli shall serve, for no additional consideration, as active chairman of the Company's board of directors other than in the framework of the Services, unless he shall have notified the Company a reasonable period of time in advance and no less than three months in advance that he shall cease to provide services as active chairman or until such date as the board of directors shall elect another suitable candidate or a temporary candidate, so long as no other candidate shall have been elected, whichever is earlier.

The Management Company has undertaken that the Services will be provided personally and exclusively by Mr. David Azrieli, who will be entitled to enlist the assistance of other employees or managers at the Management Company in a manner which will not derogate from the duties of the Management Company according to the agreement, so long as Mr. David Azrieli serves as chairman of the board of directors of the Management Company and/or as CEO of the Management Company, and the Management Company is wholly owned and controlled by him. Insofar as the Management Company shall provide Services in the future other than personally and exclusively by Mr. David Azrieli, the audit committee will be entitled to check their suitability for providing the Services, and insofar as the audit committee shall determine that they should be replaced by others, Mr. David Azrieli shall act to replace them by others within a reasonable period of time.

In consideration for the Services, the Company shall pay the Management Company an annual management fee in the sum of NIS 8 million for each calendar year, linked to the consumer price index known on April 15, 2010 in respect of the month of March of that year (the "Management Fee"). In addition to the Management Fee, the Management Company will be entitled to receive an annual bonus in an amount equal to the rate of 1% of the EBITDA of the Company (earnings before interest, taxes, depreciation and amortization) in accordance with the annual consolidated and audited financial statement of the Company, provided that the EBITDA is not negative (the "Annual Bonus"). In the framework of the Management Agreement, it was agreed that the sum of the Management Fee plus the Annual Bonus would not exceed the sum of NIS 24 million in any calendar year, linked to the consumer price index known on April 15, 2010 in respect of the month of March of that year.

In addition to the Management Fee and the Annual Bonus, the Company will bear costs whose scope will not exceed the annual sum of NIS 175,000, which amount is linked to the rise in the index, including: (1) making available to the Management Company an executive car which fits the Services and bearing any and all costs and expenses thereof, including fuel, maintenance expenses, repairs, licensing fees and insurance, mandatory payments and grossing-up of the tax liability in respect of this benefit (if any), or alternatively, at the Management Company's choice, the Company will bear any and all costs and expenses in respect of a car purchased by the Management Company or any person on its behalf, and (2) in addition, the Company will bear the costs of usage of a landline at the residence of any person on behalf of the Management Company who provides the Services, as well as a mobile telephone which shall be in his possession, including payment of the tax deriving from the foregoing benefits. In addition, and without derogating from the aforesaid, the Company will bear all of the expenses of the Management Company, in the framework of provision of the Services to the Company, including entertainment expenses, travel expenses and *per diems* in Israel and overseas, all in accordance with the Company's procedures and against presentation of appropriate evidence. Reimbursement of the expenses will not exceed maximum amounts, as will be discussed from time to time at the audit committee and will be determined thereby as appropriate, considering the Company's business and the scope thereof.

In accordance with the aforesaid, the audit committee, on March 27, 2011, approved a framework for repayment of expenses to the Management Company for the purpose of provision of the services, which will not exceed the annual sum of NIS 2 million, including in connection with repayment of flight expenses in first class or on a private plane as necessary, *per diems*, hospitality etc., which will be paid against presentation of appropriate evidence, as stated in the Management Agreement. The said expense cap does not include expenses in respect of car and telephones, in respect of which a separate cap was determined in the framework of the Management Agreement. The audit committee stated that the annual amount was determined in accordance with the scope of the Company's business and the scope of the services which the Management Company provides to the Company and their great importance and contribution to the Company. The expenses of the chairman of the board in connection with provision of the said services, considering his circumstances are required for the business needs of the Company and as part of the ordinary course of business. Considering the aforesaid, the audit committee believes that the annual expense cap and the procedure determined for approval and examination thereof, are in the best interests of the Company and are reasonable and fair under the circumstances. The audit committee further decided that it will examine, at the end of each calendar year, the expense cap determined above and its commensurability with the Company's business and the scope thereof, with the needs of the Company and the scope of the management services. In 2011 the sum of the expenses as aforesaid amounted to the aggregate amount of approx. NIS 0.5 million (2010 – NIS 1.5 million).

In the framework of the Management Agreement the parties agreed that the Management Company would be entitled to borrow from the Company up to the sum of NIS million per year. The Management Company will be obligated to repay all of the amounts of the loans taken thereby as aforesaid, plus linkage differentials and annual interest at the rate of 4% (from the date of the taking of each and every loan), by and no later than sixty days after approval of the date of payment of the Annual Bonus to the Management Company.

The Management Agreement is for a period of 5 years whilst the parties may decide, in advance and in writing, upon the extension of the agreement, subject to receipt of all of the approvals required pursuant to any law.

The Management Agreement may not be terminated other than in the following events:

a. The Company, through the adoption of a resolution at the Company's board of directors, will be entitled to terminate the agreement immediately, without giving prior notice, in any case in which the Management Company or any person on behalf thereof shall have been convicted of embezzlement or another criminal offense involving moral turpitude.

b. In the event that during the term of the agreement, a change shall occur in the control (as defined in the Securities Law) of the Company, each one of the parties (and the Company through a resolution of the board of directors) will be entitled to give written notice to the other party, by prior notice of three (3) months in advance, of termination of the agreement before expiration thereof, and the same will not constitute a breach of the agreement.

c. Each one of the parties (and the Company through a resolution of the board of directors) will be entitled to terminate the agreement before the expiration thereof only due to special circumstances, heaven forbid, which are beyond the control of Mr. David Azrieli, due to which he may not be expected to continue to fulfill his duties for a period exceeding nine (9) consecutive months.

In any case of termination of the agreement or expiration thereof as aforesaid, insofar as on such date there shall be guarantees or commitments that Mr. David Azrieli shall have provided for the liabilities of the Company and/or the Group vis-à-vis banking corporations in Israel and overseas, the Company has undertaken to ensure that Mr. David Azrieli will be released from such guarantees or commitments prior to expiration of the agreement.

The audit committee will examine, from time to time, and at least once a year, the Services provided in such year by the Management Company, and shall report to the Company's board of directors, before approval of the annual financial statements, on the results of its examination. The Company's board of directors will examine, pursuant to the applicable law, whether the consideration is fair and reasonable, and for such purpose, will receive from the audit committee its opinion and a specification of the relevant data, including a specification of the Services provided as aforesaid.

(2) Granite's general meeting has approved:

a. The provision of an indemnification in advance to all of the officers who are so entitled in Granite and in its consolidated companies, including officers who are considered to be controlling interests, in the past, present and future. The commitment to indemnification is limited to certain types of events and to amounts as detailed in the decision that was passed.

The cumulative maximum amount of the indemnification, for all of the officers, may not exceed 20% of Granite's equity in accordance with the last financial statements that are known at the time of the passing of the decision in respect of the indemnification, with the addition of amounts that will be received from the insurance companies

b. The granting of an exemption in advance to all of the officers who are so entitled in Granite and in its consolidated companies, including officers who are considered to be controlling interests, from liability in respect of damage caused as the result of a breach of the duty of due care vis-à-vis the Company.

c. Liability insurance of the officers in Granite and in its consolidated companies, for a period of 18 months as from November 30, 2010 and within a limit of overall responsibility per case and for a period of U.S. $40 million, with the addition of legal expenses in Israel in an amount of U.S. $8 million per case and cumulatively for the period. In addition, Granite has purchased a liability insurance policy for its officers alone, with an additional cover of U.S. $10 million.

(3) On November 10, 2011, Granite's audit committee approved, and on November 15, 2011, Granite's BOD approved, the expansion of the indemnification granted to Granite's officers and directors to apply also to events arising from the Improvement of Enforcement Law, within the limits of the law. Granite further limited the retroactive indemnification amount to 20% of its equity according to the financial statements, as being on the date of actual granting of the indemnification. On the same date the audit committee and BOD approved the granting of indemnification also to Ms. Danna Azrieli, who is deemed a controlling shareholder of the Company. The said changes were approved by the general meeting of Granite's shareholders held on March 13, 2012.

(4) See Note 35 in respect of the guarantees that the Group has made available to companies in the Group.

(5) See Note 10C in respect of loans that have been extended to associates.

(6) On January 16, 2011, the Company's board of directors confirmed, after the approval and recommendation of the Company's audit committee, that Mr. Menachem Einan, the Company's former CEO ("Mr. Einan") would be promoted and appointed as Active Deputy Chairman of the Company's board of directors, in lieu of his position as CEO of the Company. In his said position, Mr. Einan shall be deemed as one of two deputy chairmen of the board who the board of directors may choose, as stated in the Company's articles of associations, in addition to Ms. Danna Azrieli, who has served, as of the date of this report, as active vice chairman of the board since June 2010. Mr. Einan will be responsible, in his new position, for the strategic fields relating to the continued business development of the Group, and realization of its long-term vision. The appointment took effect on April 1, 2011. In accordance with a management agreement that was signed between the Company and Mr. Einan dated March 1, 2010, the terms and conditions of the management agreement with Mr. Einan shall remain in effect.

Mr. Menachem Einan has served as CEO of the Azrieli Group and as director of the Company. As aforesaid, as from April 1, 2011 Mr. Menachem Einan serves as Active Deputy Chairman of the Board. Mr. Menachem Einan has been providing management services to the Group as from January 1, 2004 (from November 1992 until January 1, 2004, Mr. Menachem Einan was employed as a salaried employee by the Company and served as the President of the Azrieli Group and as the chief executive office of the subsidiary), within the framework of the employment agreement and the management agreements that have been signed between the Company,. Menachem Einan Ltd., a company that is wholly owned and controlled by Mr. Menachem Einan (hereinafter – "the management company" and the company, Canit Hashalom and International Consultants (E-Consult) Ltd.. On November 24, 2009 and on March 1, 2010, management agreements were signed between the management company and the company (the "Management Agreement"). The Management Agreement was not changed due to the change in Mr. Menachem Einan's position. Set forth below is a summary of the main provisions of the Management Agreement.

The management company will be entitled to a fixed monthly payment of NIS 300,000, linked to the Consumer Prices Index, which was published on June 15, 2009 and it is entitled to ancillary benefits, including the making available of a motor vehicle (up to Group 7), cellular telephones (including the expenses in respect thereof).

In addition, the management company will be entitled once a year to annual remuneration in an amount of NIS 1,000,000, which will be paid no later than the month of April in the following year. The said amount will be linked to the Consumer Prices Index, where the bases index will be the Index for May 2009.

The management agreement is for a period of three years, from the time that it enters force (the "First Period"). If neither of the parties has given notice of the termination of the agreement, at least 6 months prior to the end of the First Period, the agreement will be extended for an additional two years from the end of the First Period (the "Second Period"). The aforesaid notwithstanding, during the course of the Second Period, each for the parties to the agreement can bring the agreement to an end, at their own judgment, by given written notice in advance, which is to be presented to the other party 6 months in advance. Without derogating from the generality of the aforesaid, it is hereby clarified that as from the time of the end of the making available of the management services by the management company to the Company, and this for any reason whatsoever, including the end of the validity of the Management Agreement, the management company will be entitled to full payment of the consideration for an additional period of 12 months.

On May 5, 2010 the Company's Board of Directors and General Meeting approved the agreement of March 1, 2010.

In addition, Mr. Menachem Einan also holds office as the Chairman of Granite Hacarmel.

In April 2010 the general meeting of shareholders of Granite approved, by a special majority, after receiving the approval of the audit committee and board of directors of Granite, the payment of annual remuneration to Granite chairman of the Board, Mr. Einan and/or a company controlled by him, in the amount of NIS 384,000 a year, commencing on January 1, 2010 and for so long as he serves as an active chairman of the board in Granite and until otherwise decided (the "Annual Remuneration"). The Annual Remuneration is linked to the increase in the Consumer Price Index. The Annual Remuneration is paid to the chairman of Granite Board of Directors in 12 equal monthly payments and the update of the linkage to the Consumer Price Index is done on a monthly basis. It is a re-approval of the agreement signed with the chairman of Granite's board of directors in 2007 which was approved at the time, and

which no change was made to the terms and conditions thereof. The payment of the Annual Remuneration does not derogate from the payment of fees for participation in the board meetings to which the chairman of Granite's board is entitled to according to the resolution of the general meeting of Granite dated March 29, 2007 and the options granted to the chairman of Granite's board according to the resolution of Granite's general meeting dated May 8, 2007 and the update of their terms on August 17, 2009.

(7) Appointment of the Company's CEO and approval of the terms of his office:

On January 16, 2011, the Company's board of directors approved the appointment of Mr. Shlomo Sherf ("Mr. Sherf") to the position of CEO, from April 1, 2011, as well as the terms and conditions of the Company's engagement in an agreement for provision of management services with a company wholly owned by Mr. Sherf (the "Management Company").

The Management Company is entitled to a fixed monthly payment of NIS 250,000, linked to the consumer price index for the month of January 2011 that was published on February 15, 2011, and is entitled to related benefits, including provision of cars (group 7), or alternatively the Company shall bear any and all expense costs of the car purchased by Mr. Sherf or by the Management Company (including depreciation) and telephones.

In addition, the Management Company is entitled, once a year, to annual compensation in the sum of NIS 1,000,000, to be paid in two semi-annual installments. The amount as aforesaid shall be linked to the consumer price index.

Similarly to the terms and conditions of the existing phantom unit allotment plan at the Company, in April 2011 the Management Company was granted 284,527 phantom units at a total value of NIS 9 million according to a base price determined according to an average share price in March 2011, which was NIS 98.

The management agreement is for a period of three years from the date of the agreement's taking effect (the "First Period") and shall automatically be renewed each time for one year.

Each one of the parties to the agreement will be able to terminate the agreement, at its discretion, by prior written notice, to be delivered to the other party 6 months in advance.

In addition, the Management Company will be entitled to adjustment compensation in an amount equal to 3 monthly payments.

In the event that termination of Mr. Sherf's term of office shall be at the Company's initiative, Mr. Sherf will be entitled to adjustment compensation as follows:

(1) If the notice was given during the First Period – an amount equal to 6 monthly payments.

(2) If the notice was given after the First Period – an amount equal to 12 monthly payments.

The aforesaid notwithstanding, Azrieli Group will be entitled to terminate the agreement immediately, without prior notice and without payment of the consideration in respect of prior notice or adjustment compensation, upon fulfillment of one of the following:

(1) The company and/or the manager shall have been convicted of an offence involving moral turpitude.

(2) The company and/or the manager shall have committed a fundamental breach of the fiduciary duty vis-à-vis Azrieli Group.

(8) In December 2009 the Company entered into an agreement in respect of the terms of employment of an interested party in the Company, who serves in various managerial positions in the Company. in accordance with an agreement that was signed between the Company and Candan Management Services Ltd., a company that is wholly owned and controlled by the interested party (the "Management Agreement"). The Management Agreement determines that the management company will be entitled to a fixed monthly payment of NIS 164,711, linked to the Consumer Prices Index in respect of September 2009, and to ancillary benefits, including the making available of a motor vehicle, cellular telephones (including the expenses in respect thereof) and the reimbursement of expenses. The Management Agreement is for an indeterminate period of time, where each of the parties to the Management Agreement is entitled to terminate it at any time by giving notice 6 months in advance. The agreement is in force as from November 1, 2009.

On May 1, 2010, the Company engaged in a new agreement with the interested party in the Company, whose main provisions are as follows:

The management services that will include, in accordance with the agreements between the parties, as they may be from time, the services of the active Deputy Chairman of the Board of Directors and/or the Replacement Chairman of the Board of Directors and/or the Chairman of the Board of Directors and/or a Director and/or a managerial position in the Company. On June 1, 2010 the interested party was appointed as a director at the Company and on June 8, 2010 the board of directors ratified her appointment as an active deputy chairman of the board at the Company, pursuant to the agreement, as aforesaid.

The management services will be extended at a capacity of 80% of a position. The management company will be entitled to notify the Company, at any time, by giving written notice 7 days in advance, of the need for a change in the scale of the management services, by reducing the scope of the management services and the monthly consideration, which is due to the management company, will be reduced accordingly.

The management company will be entitled to a fixed monthly payment in an amount of NIS 164,711 (the "Monthly Consideration"), linked to the rate of increase in the Consumer Prices Index, as from the known index in respect of September 2009. The management company will be entitled to ancillary benefits, including the making available of a group 7 motor vehicle or higher, a mobile telephone and a land line telephone (including the expenses in respect thereof) as well as the reimbursement of expenses.

The Management Agreement will be in force as from May 1 2010 ("the determining date", and it will be in force for a period of 5 years from the determining date (the "First Period"). The parties are entitled to extend the period of the Management Agreement at their own prerogative and subject to any legal provisions, and in such a case the validity of the agreement will be extended for additional periods of 5 years each.

Each of the parties to the Management Agreement can bring it to a conclusion by giving 90 days written notice in advance to the other party.

The Company will be entitled to waive the actual receipt of the management services by giving prior notice, in whole or in part, against the payment of the Monthly Consideration and the additional components of the consideration for the management company, as of it has continued to extend the management services up to the end of the period of the advance notice.

In addition to the period of advance notice, the management company will be entitled to a period of adaptation of 270 days, and in any event where the engagement is terminated, the management company will be paid the full consideration in respect of the period of adaptation with the addition of all of the components of the consideration, as aforesaid.

On May 5, 2010 the Company's Board of Directors and the Company's general meeting approved the agreement dated May 1, 2010.

In addition, the abovementioned interested party is awarded remuneration in respect of its holding office as a director in Granite Hacarmel and in GES.

(9) On May 5, 2010, the Company's general meeting, after the approval of the Company's Board of Directors had been received on May 5, 2010, gave its approval that within the framework of the annual contributions which are given to charities by the Company, whose scope shall be determined by the Company's board of directors from time to time, the Company shall remit, inter alia, through contributions to the Azrieli Foundation (Israel) (Registered Charity), (the "Foundation")The resolution was adopted based on an examination of the main objectives of the Foundation which are to act to promote education and culture in Israel, through projects in the field of education, culture, welfare and science, the execution of project and the conducting of research alone and/or in conjunction with other organizations, including by means of awarding grants to organizations and/or individuals for the purpose of the performance of projects and/or research work that accords with the objectives of the Foundation, which have been examined and found to accord with the Company's policy on contributions. There is nothing in the said decision that prevents the Company's Board of Directors from resolving to make contributions to other charitable entities, whose objectives accord with the Company's policy on contributions, as they may be from time to time.

Within the framework of the said decision by the general meeting, it was determined that during the period until May 2015, the company will donate to the Foundation, in each calendar year, by itself or by means of companies that it controls (except for Granite), an amount that constitutes 1.5% of the Company's annual profit and in any event not more than an amount of NIS 14 million.

The contributions remitted by the Company to the Foundation shall be used for the making of contributions and for the current needs of the Foundation. This contribution will be considered as a contribution that comes out of the Company's annual budget for contributions, as it may be determined by the Company's Board of Directors from time to time.

The Company's internal auditor and/or another officer who has been appointed by the Company's Board of Directors, will execute a check in each calendar year and prior to the time of the signing of the financial statements for that year, the total scope of the contributions that the Foundation has contributed in that year, and the correlation between the contribution that stood at the basis of the decision by the general meeting that approved the annual contribution, as aforesaid.

(10) In May 2010, Provident Yield for Investments Ltd. ("Provident Yield") entered into an agreement with the Foundation (see Section 9 above), according to which Provident Yield will lease an area of approx. 242 sqm out of the office space in the Herzliya Business Park project, which is owned by the Group, and will also provide to the Foundation management and maintenance services as it provides to the other tenants in the project, which include, *inter alia*, cleaning, maintenance, building insurance and third party insurance for the public areas, payments of municipal taxes in respect of the public areas and gardening for a period of five years, with an option to extend the period for an additional five years, in consideration for a quarterly payment of approx. NIS 81 thousand. In addition, Provident Yield approved a sub-lease of a negligible area out of the said office space to an NPO related to the spouse of the Company's controlling shareholder.

On March 27 and 29, 2011, respectively, the audit committee and the board of directors confirmed that the transaction whereby the Foundation will pay a debt to Provident Yield in respect of the costs of the adjustments to the leased premises, in the total sum of NIS 782,735 plus V.A.T, in 39 quarterly installments together with the rent, plus annual interest at the rate of 7% and linkage differentials, as accepted with other tenants, is a transaction which is neither irregular nor negligible.

As of the time of the approval of the financial statements, the Foundation has undertaken to make a bank guarantee or a deposit available for the length of the rental period, and has also undertaken to insure the property.

(11) Remuneration of the directors - in accordance with the decision of the Company's BOD and the Company's general meeting, as from May 10, 2010 and August 24, 2010, the remuneration of the external directors, who are appointed in the Company, to be in accordance with the Companies Regulations (Principles for the remuneration and expenses for an external director) – 2000 (the "Remuneration"). The annual remuneration and the remuneration for participation (including remuneration as an expert outside director) will be paid in accordance with the maximum amount that is set in the remuneration regulation, in accordance with the Company's capital grade, as it may be from time to time.

In accordance with the decision of theCompany's Board of Director and general meeting as of May 6, 2010, the payment to the Company's directors, except for the external directors and except for directors who receive fees from the Company (whether themselves or by means of management companies that they control), in an amount of NIS 65 thousand and remuneration for participation in meetings in an amount of NIS 2,300. The amounts of the Remuneration will be Index-linked in accordance with the provisions of the Remuneration Regulations, In addition, the provisions of Sections 5 (B) and 6 (A) of the Remuneration Regulations will apply to the Remuneration paid to the directors, *mutatis mutandis*.

(12) In respect of the plan for the allocation of phantom units to the Active Deputy Chairman of the Company's Board, to the Company's CEO and to senior officers and employees in the Group, which was approved by the Company's BOD and by the general meeting of the shareholders on May 5, 2010, see Note 25A.

(13) According to the estimate of Granite's management, all of the transactions with interested parties and affiliated parties are made under market conditions and under customary credit conditions while obtaining the approvals required according to any law.

Granite reviewed the transactions vis-à-vis interested parties and related parties in order to examine the materiality and/or negligibility of these transactions. In this review, a transaction was deemed "negligible" if it met the following conditions: (a) the transaction itself, as a single transaction, is "negligible". (b) all of the transactions of the same kind with the same interested party are immaterial. (c) there is no connection between the various transactions of the same kind. (d) Granite does not have available information according to which the said transactions are classified as transactions with an interested party

It arises from Granite's review that transactions vis-à-vis interested parties and related parties were made in the ordinary course of business and include, *inter alia*, transactions of sale of oil distillates in fuelling stations and receipt of services in the course of current operations. It transpired from the review that transactions performed during 2009-2011 are in compliance with the terms of "negligible" transaction, as aforesaid.

D. Exemption, insurance and indemnification for officers and directors:

In accordance with the decision passed by the Board of Directors and the general meeting of the Company's shareholders on May 6, 2010. the Company has granted officers and the directors, as they may be from time to time, an exemption in advance and retrospectively from their responsibility, in whole or in part, as a result of any damage that may be caused to it and/or that has been caused to it, whether directly or indirectly, as a result of a breach of a duty of care of the Board of Directors and the officers to it and to its subsidiaries, and as officers and/or as directors in the Company or officers and/or directors acting on the Company's behalf in the subsidiaries. In accordance with the provisions of the Companies Law and in accordance with the wording of the letter of undertaking for the indemnification, the undertaking for the indemnification will apply in respect of: (a) a financial indebtedness that is placed on an officer and/or director in favor of another person under a judgment, including a judgment that is handed down as a compromise or a judgment of an arbitrator that is approved by a court and solely that those actions relate to one or more of the events that are detailed in the letter of indemnification; (b) reasonable expenses of hearings, including lawyers' fees, which are expended by an officer and/or a director or that they were charged to pay by a court, in proceedings that were presented against them by the Company or in its name or in the name of another person, or on a criminal indictment that they are acquitted of, or on a criminal indictment on which they are found guilty and which does not require proof of criminal intent; (c) reasonable expenses of hearings, including lawyers' fees that have been expended by an officer and/or a director, as the result of an investigation or proceedings that are conducted against them by an authority that is authorized to conduct the investigation or proceedings, and which ended without the presentation of an indictment against them and without any financial liability being placed upon them as an alternative to criminal proceedings, or which ended without the presentation of an indictment against them but with the placement of a financial liability as an alternative to criminal proceedings in a transgression which does not require proof of criminal intent.

The amount of the indemnification that the Company will pay to each officer (including directors), cumulatively in accordance with each letter of indemnification that is issued to them by the Company in accordance with the indemnification decision, in respect of one or more of the events that are detailed in the letter of indemnification, may not exceed 20% of the capital that is attributed to the shareholders in the Company in accordance with the last financial statements of the Company (audited or reviewed), which were published before the date of the indemnification.

After receipt of the approval of the Company's board of directors and the audit committee dated June 28, 2011, the general meeting approved the amendment to the language of the letters of exemption and indemnification which the Company granted and grants to the Company's officers and directors, including officers and directors of the Company who are deemed controlling shareholders and/or in the granting of which the controlling shareholders of the Company have a personal interest, as shall hold office from time to time, in order to adjust the same to the provisions of Section 56H of the Securities Law, such that they shall include an indemnification undertaking with respect to payments to persons injured by a breach and expenses in connection with administrative enforcement proceedings, including reasonable litigation expenses.

In addition, at the same time the Board of Directors and the general meeting of the Company's shareholders gave their approval for the Company being entitled to purchase directors and officers insurance policies, as detailed below:

Claims Made type policy – On June 3, 2010, the Company purchased a D&O insurance policy, which is on the basis of the day on which the claim is presented (claims made) for a period of up to 12 months. The said insurance policy covers all of the directors and officers in the Company and in the subsidiaries, as they may be from time to time, including under the force of their roles as directors and officers in the Company's subsidiaries, except in relation to the Granite Hacarmel Group, which holds an independent D&O insurance policy, in accordance with which all of the directors and officers of the Company who hold office in the Granite Hacarmel Group will be covered within the framework of the policy over and above the coverage that exists in the Granite Hacarmel Group's D&O policy. The limit of responsibility of the insurer is up to an amount of U.S. $100 million per event and for an insurance period with the addition of expenses relating to the legal defense at a rate of up to 20% of the limit of liability that is purchased (in Israel alone) and the annual premium is in the sum of U.S. $125 thousand and the self deductible for a claim for the Company alone in respect of claims against directors and officers may not exceed U.S. $50 thousand, in accordance with the grounds for the claim and the place where it is presented.

The insurance policy has been expanded in order to cover claims that are filed against the Company (to differentiate from claims against directors and/or officers in it), the subject matter of which is a breach of the Securities Law, at least in Israel (entity coverage for securities claims), however, the right of the directors and/or the officers to receive indemnification from the insurer in accordance with the policy has preference over the right of the company.

In the same decision it was approved that the Company will be entitled, without any additional approval being required from the general meeting for this, at any time in the course of the period and up to five cumulative insurance periods (including the first insurance period, which is described above) and with the approval of the Audit Committee and the Board of Directors of the Company, to purchase future policies to insure the responsibility of directors and officers as may hold office in the Company from time to time, to extend and/or to renew the insurance policy and/or to enter into a new policy at the time of the renewal or during the course of the insurance period, with the same insurer or with another insurer, in Israel or abroad, under similar terms to the policy that is described above, to insure the responsibility of directors and/or officers, and solely that the said commitments are to be on the basis of the main terms that have been detailed above. The Company's commitments, as aforesaid, will not be brought up for additional approval by the general meeting and they will be approved by the Company's audit committee and its BOD, including in connection with directors who act on behalf of the controlling interest, who will confirm that the new policies comply with terms of the policy that has been described above.

In June 2011 the above policy was renewed.

POSI type policy – On June 3, 2010 the Company purchased a POSI (Public Offering of Securities Insurance) type insurance policy, which covers the responsibility of the Company, the directors and the officers in it, the controlling interests and additional parties, who have taken part in the issue to the public of shares in the Company in accordance with the prospectus that was issued in May 2010 (hereinafter: "The issue"), against claims that may be filed against them in connection with the issue and this for a period of 7 years from the time of the issue. The maximum limit of responsibility of the insurer in accordance with this policy may not exceed U.S. $100 million per event and per insurance period, with the addition of expenses relating to the legal defense at a rate of up to 20% of the limit of liability that is purchased (in Israel alone), the annual premium is in the sum of U.S. $250 thousand, and the self deductible for a claim for the Company in respect of claims under this policy shall not exceed U.S. $35 thousand.

E. On November 24, 2010, the Company's BOD decided to adopt guidelines and rules regarding the classification of transactions which are not exceptional transactions, of the Company or of a consolidated company thereof with interested parties therein or controlling shareholders, as a negligible transactions. Such guidelines were prescribed, *inter alia*, considering the scope of the Company's assets, the diversity of its businesses, the nature of the transactions performed thereby and the level of effect thereof on the Company's business and results.

Such rules and guidelines will serve on the one hand for examining the need to approve the transaction at the relevant institutions in the Company, and on the other hand, for examining the duty and/or scope of disclosure in the periodic report and the prospectus (including in shelf offer reports), and/or the provision of an immediate report in respect of such a transaction. It shall be clarified, that such procedure does not address transactions of public companies held by the Company, *inter alia*, due to their being reporting companies on their own merit, and the Company shall report according to the reports thereof, if and to the extent such will be required according to law.

The Company's BOD determined that a negligible transaction at the Company is a transaction which is not exceptional (i.e. – it is done within the ordinary course of business, to the benefit of the Company and under market conditions) with controlling shareholders or another person in which the controlling shareholder has personal interest, if it complies with the following criteria:

(1) In respect of the duty to provide and immediate report – a single negligible transaction in a company or a subsidiary controlled thereby, does not exceed the rate of 0.1% of the Company's consolidated equity according to the last financial statements; in case of ongoing transactions (including rent, leases and so forth), according to the monthly transaction amount, or the total sum of the transaction for the whole duration of the engagement, according to the shorter/lower between them. For the purpose of immediate report, the negligibility of a transaction will be examined on the basis of the specific single transaction, and to the extent such will pass the negligibility threshold, the Company will report such transaction through an immediate report.

(2) In respect of providing specification in the annual report – the total sum of all of the transactions of a certain type in the Company or a subsidiary controlled thereby, in a calendar year has not exceeded a rate of 0.5% of the Company's consolidated equity according to the last annual reports. The Company will include the types of transactions and aggregate amount thereof within its annual report only if the total amount exceeds the rate stated above. For the purpose of reporting within a periodic report, financial statements and a prospectus (including a shelf proposition report), the negligibility of the aggregate of all of the transactions of the same type of the Company with the interested party or with corporations controlled by the interested party, will be examined on an annual basis.

Upon the classification of transactions as negligible, each transaction will be examined in itself, however, the negligibility of integrated transactions, or such that are contingent upon each other or transactions of the same type, will be examined in the aggregate as one transaction. In respect of multiannual transactions (agreements for a period of several years), the scope of transaction will be calculated for examination of the negligibility threshold on an annual basis (i.e. – the total monetary amount deriving from the transaction exceeding the negligibility threshold as aforesaid). In insurance transactions, the premium will be examined as the transaction amount. Regardless of the insurance coverage provided, multiannual insurance transactions will be measured on the basis of the annual insurance fees paid or collected.

The transactions classified as negligible by the Company's investees will be deemed as negligible at the Company level too, while those classified by them as non-negligible, will be examined on the Company level. In case that the Company does not have available information allowing the examination of the classification of transactions classified as non-negligible, as negligible transactions, then the aggregate of all of the transactions of the same type will be deemed as a negligible transaction, except if in light of the figures known to the Company one of the two conditions has been fulfilled: (1) According to the quantitative parameters above, the transaction in itself as a single transaction is not negligible; (2) the aggregate of the transactions is material to the Company.

Notwithstanding the aforesaid, the examination of the qualitative considerations of a negligible transaction from the quantitative aspect, may lead to the classification thereof as a transaction which is not negligible, if due to its nature, materiality and effect on the Company it is perceived as a significant event by the Company's management and serves as a basis for adoption of important managerial decisions or if within the context of the interested parties transaction, the interested parties are expected to receive benefits with regard to which there is significance in the reporting thereof to the investors' public. It is clarified that even if an interested party's transaction complied with the quantitative test below, it will not be deemed negligible if such qualitative considerations indicate a material aspect thereof.

The Approving Entity

Pursuant to Section 22.3 of the Company's articles of association, the board of directors determined that the examination of the classification of an interested parties' transaction as a negligible transaction will be done by the CFO and the Company's secretary in cooperation with legal consultation to the extent required, and in any approval of a transaction as negligible the examination and classification proceeding will be documented.

The BOD further authorizes the Company's CEO or the CFO to approve the performance of non-irregular transactions, including transactions which comply with the negligibility definition pursuant to this procedure (for so long as both of the do not have any personal interest in such transactions, as in such case, the transaction will be approved by the chairman of the audit committee, and for so long as the subject matter is not a transaction pertaining to the terms of office and employment of an officer).

Supervision and Audit

The audit committee shall review on an annual basis the manner of implementation of the provisions of this procedure by the Company and will also perform a sample examination of transactions classified as negligible transactions according to the provisions of the procedure. Within the context of the sample examination, the audit committee will examine, *inter alia*, the manners of determination of prices and the remaining terms of the transaction, according to the circumstances of the matter, and will examine the effect of the transaction on the business status of the Company and the results of the business thereof. Within the periodic report, the Company shall include disclosure regarding the performance of the review, manner of performance of the examination, results and conclusions thereof.

The Company's board of directors will examine the need for the update of this procedure from time to time, considering interested parties transactions in which the Company engages, material changes in the scope of business of the Company and the relevant financial figures and changes in the relevant provisions of law.

After discussing the implementation of the provisions of the negligible transactions procedure and reviewing the consideration for the negligible transactions signed in 2011 and their other characteristics vis-à-vis the market conditions, that was held on March 19 and 21, 2012, respectively, the audit committee and the board of directors determined that they were all made under accepted market conditions and they have no material effect on the Company's business position and results of operations. They further determined that all of the transactions examined as aforesaid were found to be transactions that meet the definition of "negligible transaction" in accordance with the Company's procedure in respect of negligible transactions, and that this procedure was adequately implemented by the Company.

Note 41 Segmental reporting

A. General:

The Company applies IFRS 8, "Operating Segments" ("IFRS 8"). In accordance with the provisions of the standard, operating segments are identified on the basis of the internal reporting in respect of the components of the Group, which are reviewed on a regular basis by the Group's chief operational decision maker for the purpose of the allocation of resources and the evaluation of the performance of the operating segments.

Following the expansion of the Company's business in the U.S., which is expressed in the acquisition of several office buildings in the U.S., the internal reporting format has been updated, per the request of the main operating decision-maker, such that the results of operations of the properties in the U.S. shall be presented thereto separately. In view of the aforesaid, from the annual financial statements for 2011, the disclosure made in connection with the results of the Group's operating segments has been updated.

The above change is expressed in the fact that the income-producing property business in the U.S., which was previously included in the framework of the commercial centers and malls and office and other rental space segments, is presented in these statements as a separate reportable segment.

The Company's business activities focus primarily on the income-producing property segment, where most of the Group's business activity is in the commercial centers and malls segment, primarily in Israel and in the office and other space for lease segment, primarily in Israel. Furthermore, the Company has an income-producing property in the USA as aforesaid (primarily office space for lease). In addition, the Company is engaged, through its holding in Granite Hacarmel, in an additional operating segment, which covers the paints, energy, water and the environment segments.

The following are the Company's operating segments:

Segment A – Commercial centers and malls in Israel.
Segment B – The office and other space for lease in Israel.
Segment C – Income-producing property in the USA.
Segment D - Granite Hacarmel.

B. Operating segments:

	For the year ended in December 31, 2011					
	Commercial centers and malls in Israel	Office and other space for lease Israel	Income-producing property USA	Granite Hacarmel	Adjust-ments	Con-solidated
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Income:						
Total external income	813,847	325,382	102,244	6,304,842	955	7,547,270
Total segmental expenses	152,389	53,513	53,859	6,104,112	72	6,363,945
Segmental profit (NOI)	661,458	271,869	48,385	200, 730	883	1,183,325
Profit, net of adjustments of the fair value of investment property and investment property under construction	554,600	217,987	76,051	221	-	848,859
Un-attributed expenses						(73,185)
Financing expenses, net						(489,498)
Other income, net						47,104
The Company's share of the results of associates, net of tax						(17,512)
Income before taxes on income						1,499,093
Additional information:						
Segmental assets	9,424,443	4,279,980	1,091,725	5,497,368	-	20,293,516
Unallocated assets						2,886,197
Total consolidated assets						23,179,713
Capital investments	323,786	727,402	682,641	-	-	1,733,829

(*) Mainly financial assets held for trade in the sum of NIS 1,322 million and available for sale financial assets in the sum of approx. NIS 1,256 million.

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	For the year ended in December 31, 2010					
	Commercial centers and malls in Israel	Office and other space for lease Israel	Income-producc-property USA	Granite Hacarmel	Adjust-ments	Con-solidated
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Income:						
Total external income	754,137	301,641	35,032	5,252,470	642	6,343,922
Total segmental expenses	139,823	54,870	14,399	5,074,980	49	5,284,121
Segmental profit (NOI)	614,314	246,771	20,633	177,490	593	1,059,801
Profit (loss), net of adjustments of the fair value of investment property and investment property under construction	775,704	109,096	6,977	(1,080)	-	890,696
Un-attributed expenses						(71,297)
Financing expenses, net						(362,802)
Other income, net						52,243
The Company's share of the results of associates, net of tax						(21,378)
Income before taxes on income						1,547,263
Additional information:						
Segmental assets	8,445,171	3,437,387	281,321	4,921,319	-	17,085,198
Unallocated assets (*)						4,258,180
Total consolidated assets						21,343,378
Capital investments	420,290	42,618	4,441	-	-	467,349

(*) Mainly financial assets which are held for trade in a sum of approx. NIS 2,235 million and available for sale financial assets in a sum of approx. NIS 1,790 million.

	For the year ended in December 31, 2009					
	Commercial centers and malls in Israel	Office and other space for lease Israel	Income-producing property USA	Granite Hacarmel	Adjust-ments	Con-solidated
	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands	NIS in thousands
Income:						
Total external income	659,019	286,152	38,130	4,546,674	-	5,529,975
Total segmental expenses	128,289	53,777	15,810	4,364,729	-	4,562,605
Segmental profit (NOI)	530,730	232,375	22,320	181,945	-	967,370
Profit (loss), net of adjustments of the fair value of investment property and investment property under construction	172,676	95,582	(46,173)	(4,399)	-	217,686
Un-attributed expenses						(61,003)
Financing expenses, net						(424,815)
Other income, net						18,394
The Company's share of the results of associates, net of tax						(5,946)
Income before taxes on income						711,686
Additional information:						
Segmental assets	7,266,457	3,268,305	284,498	4,356,715	-	15,175,975
Unallocated assets (**)						2,007,765
Total consolidated assets						17,183,740
Capital investments	887,887	137,843	4,639	-	-	1,030,369

(*) Mainly available for sale financial assets in a sum of approx. NIS 1,694 million.

Note 42 Earnings per share

Basic earnings per share:

	For the year ended December 31		
	2011	2010	2009
	NIS in thousands	NIS in thousands	NIS in thousands
Income attributed to the holders of the ordinary shares:			
Income for the year attributed to the shareholders of the parent company	595,854	1,224,180	956,357
Weighted average number of ordinary shares:			
Weighted number of ordinary shares used to calculate basic earnings per share	121,272,760	108,074,258	90,942,000
Basic earnings per share:	4.91	11.33	10.52

Note 43 Events in the Report Period

A.

(1) On August 31, 2011, Sonol received an amendment to the Supervision of Maximum Prices at Fuelling Stations Order, whereby, commencing from September 1, 2011, the marketing margin for self-service 95 octane gas was reduced by 18.5 Agorot per liter (inclusive of V.A.T) and full service by 11.5 Agorot per liter (inclusive of V.A.T).

Sonol, as well as the other fuel marketing companies, filed a petition with the HCJ against this decision. On September 19, 2011, the court decided to return the issue of examination of the marketing margin for another hearing vis-à-vis the Ministry of Infrastructures, and the price committee, on the basis of an updated database, determined timetables for completion of the proceeding and decided that until completion of the proceeding, the supervision of prices order would remain in effect.

Sonol performs various actions to minimize the said effect, including reducing car fleet and customer club discount, reducing discounts given to private customers at fuelling stations and changing commercial conditions. Sonol is also acting to reduce its expenses, mainly reducing rent paid to fuelling stations owners, manpower cutbacks and reducing payroll related costs and maintenance costs as well as taking other internal streamiling measures. The management of Granite and Sonol believes that when the steps described above are completed and their results are expressed, no material reduction of Sonol's profitability is expected.

(2) On December 21, 2011, Sonol received a letter from the joint price committee of Ministry of Energy of Water and the Ministry of Finance, whereby the committee intends to examine imposing supervision on the marketing margin for diesel oil for transportation at the fuelling stations. The letter specified the reasons for imposing supervision. Sonol has delivered its comments on the issue. As of the date of the report no hearing as yet been held for the fuel companies on the matter.

B. In September 2011, the Committee for Socioeconomic Change, headed by Prof. Trajtenberg, submitted its recommendations, whose main effect on the Group is as described below:

(1) Fuelling stations

a. Recommendation to initiate a legislative proceeding that will immediately release several fuelling stations from commitment to the fuel companies, including Sonol.

b. Giving preference in planning proceedings to sole proprietors, bodies which are not one of the four largest fuel companies, and instructing the ILA and the planning institutions to plan land for 40 new fuelling stations within two years and to market the same to sole proprietors immediately upon completion of the planning.

c. Acceleration of the implementation of regulations for a universal automated fuelling and billing system (*Dalkan*) that will allow fuelling at all of the fuelling stations.

d. To apply immediate supervision to the prices of diesel oil for transportation, at the refineries' gates and at the fuelling stations.

e. To require the Ministry of Energy and Water Resources to map geographic regions in which the four largest companies are present, with emphasis on city centers and, in view of the level of competition, determine a mechanism which requires the sale of stations to small companies with a smaller market share in order to encourage competition.

(2) LPG

a. Imposition of supervision on the price of LPG at the refinery's gates and for the consumer, which will lead to a reduction in its price.

b. Establishment of a government team to propose additional reform in the LPG industry, based on the assurance of free access to containers to increase competition.

(3) For further details regarding the recommendations of the Trajtenberg Committee and the implications thereof, see Note 33 regarding taxes on income.

Note 44 Material Events after the Date of the Financial Statements

A. With respect to the acquisition of an office building – see Note 14J.

B. On March 21, 2012 the Company's Board of Directors decided on dividend distribution in the sum of NIS 240 million.

C. On August 10, 2010 a team of the Antitrust Authority arrived at the offices of Supergas for performance of a search in respect of Afikei Gas Ltd., in which Supergas holds 50%. Supergas is cooperating, insofar as required. In addition, several officers were investigated on the matter. On March 19, 2012, Supergas' counsel received a notice (the "Notice") that the Antitrust Authority decided to file an indictment against Supergas and three officers thereof, for reason of non-provision of information, documents, books or certificates that were required by the person authorized by the Antitrust Authority. It shall be clarified that the Company intends to present its claims in writing against the filing of the indictment in accordance with the right granted thereto in the Notice. It shall be clarified that there is no certainty that the Antitrust Authority shall accept all or any of Supergas' contestations and that indeed no indictment be filed against Supergas and three officers thereof.

Note 45 Entities in the Group

The following is a list of main investee companies:

	Holding and control rates of the holding company as at December 31, 2011
	%
Consolidated companies:	
Canit Hashalom Investments Ltd.	99.12
Gemel Tesua for Investments Ltd.	100.00
Herzliya Business Park Operations Ltd.	100.00
Margalit Hasharon – Operations Ltd.	100.00
Azrieli Mall Kiryat Atta (Development and Management) Ltd.	100.00
Otzma & Partners Maccabim Investments Ltd.	100.00
Modi'in Mall (Initiation and Management) Ltd.	100.00
Azrieli Mall Modi'in (Offices) Initiation and Management Ltd.	100.00
Azrieli Mall Modi'in (Residential) Initiation and Management Ltd.	100.00
Otzem Entrepreneurship and Investments (1991) Ltd.	100.00
Azrieli Mall Akko (Development and Management) Ltd.	100.00
Azrieli Insurance Corporation	100.00
Azrieli Mall Ramla (Initiation and Management) Ltd.	100.00
Holon Mall – Management and Maintenance Ltd.	100.00
Azrieli Center Parking Lot Ltd.	99.90
Azrieli Center Towers (Initiation and Management) Ltd.	99.00
Ayalon Mall (Initiation and Management) Ltd.	100.00
Hanegev Mall (Initiation and Management) Ltd.	100.00
Jerusalem Mall (Initiation and Management) Ltd.	100.00
Azrieli Center Mall (Initiation and Management) Ltd.	100.00
Givatayim Mall Initiation and Management Ltd.	100.00
Azrieli Haifa Mall (Initiation and Management) Ltd.	100.00
International Consultants (E-Consult) Ltd.	100.00
Orban A.A.R. Ltd.	100.00
Granite Hacarmel Investments Ltd.	60.68
Sonol Israel Ltd.	100.00
Sprint Motors Ltd.	100.00
Milchen Sonol Agency Ltd.	100.00
Sonol Jerusalem Ltd.	100.00
Sonol Dan (1992) Ltd.	100.00

	Holding and control rates of the holding company as at December 31, 2011
Sonol Darom Ltd.	100.00
Sonol Canaan Ltd.	100.00
Sonol Tzafon Ltd.	100.00
Sprint Motors Transport (1999) Ltd.	100.00
Kleeson Holdings (1999) Ltd.	100.00
Sonol Kat Ltd.	100.00
So Good Ltd.	100.00
Tambour Ltd.	84.01
Tambourechev Paints (1997) Ltd.	100.00
Tzach - Serafon Ltd.	100.00
Serafon Trading (1997) Ltd.	100.00
Tambour Distribution Ltd.	100.00
Gesher Gypsum 2006 Ltd.	51.00
Tzomet Paints and More Ltd.	100.00
Tamboard Gypsum Products Ltd.	95.00
Tamboard Trade Limited	100.00
Tambor Building Keshet – Building Power Plant Ltd.	51.00
G.E.S. Global Environmental Solutions Ltd.	100.00
Saiclean Ltd.	100.00
Texma Chemicals Ltd.	100.00
Argad Technologies for Water Enhancement Ltd.	100.00
Uniclean Waste Purification Ltd.	76.00
Puritech G.E.S.	100.00
Via Maris Desalination (Holdings) Ltd.	100.00
Via Maris Operation Ltd.	100.00
Via Maris Construction Partnership	100.00
Via Maris Desalination Ltd.	100.00
Dan Viro Ltd.	87.50
GSM Facility Operation Ltd. (formerly Nirton Chimtech Ltd.)	100.00
Supergas – The Israeli Gas Distribution Company Ltd.	100.00
Supergas Eshkolot Ltd.	100.00
Rav - Gas Ltd.	100.00
Supergas for the Home Ltd.	100.00
M. Solomon & Assoc. – Gas Agency Ashkelon Ltd.	51.00
Supergas Hanegev (1990) Ltd.	65.00
S. Super Solar Ltd.	100.00
Natural Supergas Holdings Ltd.	100.00
Allied Oils and Chemicals Ltd.	100.00
Sonapco Bank Street Corporation	100.00
Granite Hacarmel Holdings (1993) Ltd.	100.00
Granite Hacarmel Properties (1993) Ltd.	100.00
Granite Hacarmel Holdings and Development Ltd	100.00
Granite Hacarmel Industries Ltd.	100.00
Granite Hacarmel Y.A. Holdings Ltd.	100.00
Granite Hacarmel NZV Holdings Ltd.	100.00

	Holding and control rates of the holding company as at December 31, 2011
Granite Hacarmel Energy (1997) Ltd.	100.00
Granite Hacarmel Tourism (1995) Ltd.	100.00
Green Anchors Ltd.	60.00
Partnerships (held by Canit Hashalom)	
South Post Oak Holdings LP	100.00
RiverCan LP	100.00
Partnership (held by the Company)	
Canit Northchase LP	100.00
AG Galleria Office Buildings, LP	100.00
Three Galleria Office Buildings member, LP	90.00
Three Galleria Office Buildings, LLC	100.00
Associates and Associated Partnerships (held by Granite)	
Park Mini Israel – Limited Partnership	50.00
Park Mini Israel Ltd.	50.00
M.I.D. Municipal Investments and Development Ltd.	37.50
Dimona WPI– Joint Venture	50.00
Triad Fuel Engineering Pvt. Ltd.	33.10
Focal Energy Holdings Ltd.	18.00
Super N.G. Company for Distribution of Natural Gas Ltd.	50.00

CHAPTER D

Further Details About the Corporation

December 31, 2011

Chapter D: Additional Details on the Corporation

Company Name: Azrieli Group Ltd.

Company Number in the Registrar of Companies: 51-096071-9

Address: 1 Azrieli Center, Tel Aviv, 67021

Facsimile: 03-6081380

Telephone: 03-6081400

Date of Report: March 21, 2012

Date of the Financial Position Statement: December 31, 2011

Regulation 8A - Description of the Corporation's Businesses

The description of the Company's businesses and the development of its businesses as occurred in the last year, in accordance with the details and principals of the Supplement of the Securities Regulations (Details, Structure and Form of Prospectus), 5730-1970, appears in Chapter A of this Report.

Regulation 8B - Valuation

A very material valuation in connection with Azrieli Center in Tel Aviv is attached as Appendix C of the Board of Directors' Report in Chapter B of this Report. For details regarding the valuations of the Company's material assets, see Section 8.2 of Chapter A of this Report.

Regulation 9 - Financial Statements

In accordance with Regulation 9 of the Securities Regulations (Periodic and Immediate Statements), 5730 – 1970 (the "Statements Regulations"), attached to this Report in Chapter C are audited financial statements of the Company for the year ended December 31, 2011, together with an opinion of the Company's auditors.

Regulation 9B - Report on the Effectiveness of the Internal Control over the Financial Reporting and the Disclosure

In accordance with Regulation 9B of the Statements Regulations, attached to this periodic Report in Chapter E are reports pertaining to the effectiveness of the internal control over the financial reporting and the disclosure of the Company for the year ended December 31, 2011, together with an opinion of the Company's auditors.

Regulation 9C - Separate Financial Statement of the Corporation

In accordance with Regulation 9C of the Statements Regulations, attached as Appendix D of the Board of Directors' Report in Chapter B of this Report is a separate financial statement of the Company for the year ended December 31, 2011, that includes financial data from the consolidated financial statements of the Company which are attributed to the Company itself as a parent company, together with an opinion of the Company's auditors.

Regulation 9D - Statement of Liabilities by Maturity Date

In accordance with Regulation 9D of the Statements Regulations, the Company is issuing, concurrently with the issuance of this periodic Report, an immediate report dated March 22, 2012, regarding the liabilities of the Company and the companies which are consolidated or proportionately consolidated in its financial statements, by maturity date.

Regulation 10 - Report of the Board of Directors on the State of the Corporation' Affairs

In accordance with Regulation 10 of the Statements Regulations, attached to this periodic Report in Chapter B is the report of the Board of Directors of the Company for the year ended December 31, 2011.

Regulation 10A - Summary of the Reports on Outcomes of the Company's Operations for Each Quarter of 2011 (in NIS thousands)

	1-3/2011	4-6/2011	7-9/2011	10-12/2011	1-12/2011
Income					
From sales, work and services	1,487,839	1,526,848	1,608,347	1,668,270	6,291,304
From rent, management and maintenance fees	295,657	301,664	322,904	335,741	1,255,966
Profit, net of fair value adjustment of investment properties and properties under construction	17,592	338,549	106,223	386,495	848,859
Financing income	36,124	14,455	21,756	29,326	101,661
Other	30,877	21,504	1,513	714	54,608
Total Income	1,868,089	2,203,020	2,060,743	2,420,546	8,552,398
Costs and Expenses					
Cost of income from sales, work and services	1,197,538	1,256,923	1,333,889	1,417,000	5,205,350
Cost of income from rent, management and maintenance fees	58,021	61,318	71,195	76,308	266,842
Sale and marketing	182,821	189,278	201,720	190,831	764,650
General and administrative	54,181	49,172	40,656	56,279	200,288
Portion of results of included companies, net of tax	4,849	4,877	3,443	4,343	17,512
Financing expenses	158,989	184,662	156,578	90,930	591,159
Other	1,456	780	964	4,304	7,504
Total Costs and Expenses	1,657,855	1,747,010	1,808,445	1,839,995	7,053,305
Profit before tax on income	210,234	456,010	252,298	580,551	1,499,093
Income (expenses) from tax on income	(29,137)	(67,810)	(63,938)	(715,196)	(876,081)
Net profit (loss) per period	181,097	388,200	188,360	(134,645)	623,012
Attributed to owners of the parent company	162,349	382,959	179,464	(128,918)	595,854
Non-controlling interests	18,748	5,241	8,896	(5,727)	27,158
	181,097	388,200	188,360	(134,645)	623,012

Regulation 10C - Use of Proceeds from Securities

Issue according to a prospectus and private placement: in June 2010 the Company issued 24,161,440 shares to the public, according to the Company's prospectus dated May 12, 2010 (reference 2010-01-477963), as amended on May 25, 2010 (reference 2010-01-494514) (the "**Prospectus**"). The total (gross) proceeds from the share issue amounted to the sum total of NIS 2,011,400 thousands. On June 14, 2010, the Company completed a private placement of 6,169,320 ordinary shares to accredited investors. The total gross proceeds from the private placement amounted to the sum total of NIS 513,595,890. The total consideration for the issue according to the Prospectus and the private placement was app. NIS 2.5 billion.

The purpose of the proceeds according to the Prospectus: As the Company specified in the Prospectus and in Section 1.1.10 of the board report in Chapter B of this Report, the net IPO proceeds were intended, in part, according to the resolutions of the Company's board of directors, as adopted from time to time, for financing the implementation of a number of projects such as shopping malls, commercial centers and areas for rent, whereas the remainder of the IPO proceeds were intended, *inter alia*, subject to the resolutions of the Board of Directors of the Company, from time to time, for expanding and intensifying its activity in the areas of its activity, financing the expenses of the Company's ongoing activity, investments in the areas of its

activity and in other areas, and upgrading its existing assets. During the period between the date of the Prospectus and the raising of the funds pursuant thereto, and until the investment of the IPO proceeds, the Board of Directors of the Company was entrusted with determining the policy for the management of the proceeds from the issue, as set forth in the Prospectus, in the immediate report of the Company dated August 29, 2010 (reference 2010-01-601578) and in Section 1.1.10 of the board report in Chapter B of this Report.

Uses of the IPO proceeds: Since the IPO, and during the Report period, the Company used the IPO proceeds (together with the Company's other financial means) in the sum total of approx. NIS 2.7 billion, *inter alia*, for payment of loans and for investments made thereby, including the development and construction of the properties under construction[1] (including properties whose construction ended during the Report period); purchase of the office towers in Houston, USA[2]; long-term lease of the plot for the purpose of construction of the Azrieli Sarona Project and development expenses to the ILA[3], and for the acquisition of land for the construction of a shopping mall in Ramla[4]. On January 10, 2012, after the date of the statement of financial position, the Company closed the acquisition of an additional office building in Houston, U.S.A.[5] To the best of the Company's knowledge, the aforesaid investments were made in accordance with the policy set forth in the Prospectus and in the Immediate Report as aforesaid, in connection with the IPO proceeds.

Regulation 11 - List of Investments in Subsidiaries and Related Companies as of the Statement of the Financial Position Date

See **Appendix A** of this Chapter.

Regulation 12 - Changes in Investments in Subsidiaries and Related Companies, Directly and Indirectly, in the Period of the Report

Date of change	Nature of change	Company name	Holder name	Security type	Total par value
January 2011	Founding a new company	Azrieli Akko Mall (Development and Management) Ltd.	Otzem Initiation and Investments (1991) Ltd.	Shares	100
January 2011	Founding a new company	Azrieli Kiryat Ata Mall (Development and Management) Ltd.	Gemel Tesua Investments Ltd.	Shares	100
January 2011	Founding a new partnership for the purpose of purchasing a property	AG Galleria Office Buildings, LP	Azrieli Group Ltd.	--- (Partnership)	
January 2011	Founding a new partnership for the purpose of purchasing a	Three Galleria Office Buildings Member, LP	Azrieli Group Ltd.	--- (Partnership)	

[1] As specified in Section 7.8 in Chapter A of this Report and in Section 1.1.3 of the Report of the Board of Directors in Chapter B of this Report;
[2] As specified in Section 10.9 in Chapter A of this Report;
[3] As specified in Section 7.8 in Chapter A of this Report.
[4] As specified in Section 7.8 in Chapter A of this Report;
[5] As specified in Section 10.10 in Chapter A of this Report;

	property				
January 2011	Founding a new partnership for the purpose of purchasing a property	Three Galleria Office Buildings, LLC.	Azrieli Group Ltd.	Units (LLC)	
November 2011	Founding a new company	Azrieli Ramla Mall (Development and Management) Ltd.	Otzem Initiation and Investments (1991) Ltd.	Shares	100

*On January 10, 2012, following the statement of the financial position date, the Company closed the purchase of the office building in Houston, USA, as specified in Section 10.1.10 of Chapter A of this Report, in consideration of an amount of approximately USD 107.5 million.

Regulation 13 - Total Profit of Subsidiaries and Related Companies and the Company's Income therefrom as of the Statement of the Financial Position Date (NIS in Thousands)*

The held company	Profit (loss) NIS in thousands		The Company's income from the subsidiary/ related company (NIS in thousands)		
	Before reserve for tax	After reserve for tax**	Dividend	Management fee	Interest and linkage differentials
Canit Hashalom Investments Ltd.	977,274	485,934	---	---	**89,785*** **
International Consultants (Iconsult) Ltd.	7,600	2,414	---	---	**1,345**
Azrieli Mall Center (Initiation and Management) Ltd.	101	16	---	---	**43**
The Negev Mall (Initiation and Management) Ltd.	(36)	(9)	---	2,191	**---**
Ayalon Mall (Initiation and Management) Ltd.	(61)	(16)	---	2,273	**---**
Jerusalem Mall (Initiation and Management) Ltd.	(25)	1	---	3,304	**---**
Canyon Holon - Management & Maintenance Ltd.	4	(3)	---	1,105	**---**
Azrieli Center Parking Lot Ltd.	2,671	1,947	---	---	**25**
Azrieli Mall Haifa (Initiation and Management) Ltd.	(13)	(1)	---	2,359	**49**
Azrieli Center Towers	(21)	(21)	---	---	**75**

The held company	Profit (loss) NIS in thousands		The Company's income from the subsidiary/ related company (NIS in thousands)		
	Before reserve for tax	After reserve for tax**	Dividend	Management fee	Interest and linkage differentials
(Initiation and Management) Ltd.					
Otzem Initiation & Investments 1991 Ltd.	1,061	1,056	---	---	---
Givatayim Mall Initiation and Management Ltd.	1	6	---	2,102	---
Canit Northchase L.P	(3,560)	(5,017)	---	---	---
AG Galleria Office Buildings, LP	39,049	11,377	---	4,932	---
Canit USA II Inc.	(1)	(1)	---	---	---
Canit Regency L.P	---	---	---	---	---
San Felipe Voss GP Inc.	---	---	---	---	---
San Felipe Voss Investments	---	---	---	---	---
Gemel Tesua Investments Ltd.	230,011	153,010	---	420	**123**
Otzma & Co. Investments Maccabim Ltd.	5,912	7,041	---	180	---
Margalit Hasharon Operations Ltd.	15	15	---	---	**34**
Herzliya Business Park Operations Ltd.	(7)	(7)	---	---	**62**
Modi'in Mall (Initiation and Management) Ltd.	(31)	---	---	---	**8**
Azrieli Kiryat Ata Mall (Initiation and Management) Ltd.	---	---	---	---	**3**

* The table does not include profits or losses of corporations which are not held directly by the Company, unless such corporations paid to the Company dividend, interest or management fees in the period of the Report.

** Before results on the basis of the balance sheet value.

*** Including capital fund

Regulation 20 - Trading on the Stock Exchange - Securities Registered for Trading/ Suspension of Trading - Dates and Reasons

a. Securities / Shares
No securities issued by the Company were listed for trade on TASE in the period of the Report

b. Suspension of Trading
During the period of the Report, there were no suspensions of trading in the securities issued by the Company, other than suspensions of trading customary at the time of issuance of financial statements.

Regulation 21 - Compensation of Senior Officers

Below is the specification of the compensation granted in the year of the Report, as specified in the sixth supplement of the Repots Regulations.

Compensation to the five most highly compensated persons:

The compensation granted during the year preceding the date of the Report to the five most highly compensated senior officers in the Company, or a corporation controlled by the Company, which were granted to them in connection with their office in the Company or a corporation controlled by the Company, are as follows (in terms of the annual cost to the Corporation, NIS in thousands, for the 12 months ended December 31, 2011):

Name of recipient of compensation				**Compensation**				
Name	**Position**	**Scope of position**	**% holding in Corp. capital**	**Management fees***	**Bonus**	**Share-based payment****	**Other**	**Total**
David Azrieli (1)	Chairperson of the Board of Directors of the Company	100%	73.66%	8,509	12,652	---	---	21,161
Menachem Einan (2)	Active Deputy Chairman of the Board	100%	0.01%	3,937	1,078***	797	1,245(a)	7,057
Shlomo Sherf (****) (3)	CEO of the Company	100%	---	2,485	765***	1,465	1,051(b)	5,766
Yuval Bronstein (4)	CFO	100%	---	2,530	---	166	859(c)	3,555
Peer Nadir (5)	CEO of Azrieli Malls	100%	---	2,722	225	127	142(d)	3,216

* The management fee component includes the following components: cost of monthly management fee, standard social and related rights and benefits, car maintenance and communication and other expense reimbursement.
** Reflects the expense which was recorded by the relevant company in 2011due to the grant of phantom units.
*** Pre-determined grant in accordance with the management services agreement.
**** For a 9 month period.
(a) Reflects compensation due to his office as the chairperson of Granite Hacarmel and a director of subsidiaries thereof, and an update of a capitalization of a component which was recorded as an expense due to adjustment months at the time of retirement.
(b) Reflects a component which was recorded as an expense due to adjustment months at the time of retirement.
(c) Reflects compensation due to office as a director of Granite Hacarmel and the subsidiaries thereof, and an update of an expense in 2011 due to updated adjustment months at the time of retirement.
(d) Reflects compensation due to office as a director of Granite Hacarmel and the subsidiaries thereof.

(1) Mr. David Azrieli serves as Executive Chairperson of the Board of Directors of the Company. For details pertaining to the management agreement with Mr. David Azrieli, which was executed prior to the Company's IPO in May 2010, see Note 43 of the financial statements and Regulation 22 below. For a specification pertaining to expense reimbursement in accordance with the resolution of the Company's audit committee dated March 27, 2011, see Regulation 22 below. In view of Amendment 16 of the Companies Law, the management agreement shall be effective until May 2013.

(2) Mr. Menachem Einan served as CEO of the Group since 1993, and provided management services to the Company as CEO until March 31, 2011. Commencing from April 1, 2011, holds office as Active Deputy Chairman of the Board. The management agreement with Mr. Einan, which was not modified pursuant to the change in his position, sets forth monthly consideration in the amount of NIS 300,000, linked to the consumer price index which was published on June 15, 2009 (which amounted to approx. NIS 323,000 as of December 31, 2011), together with a fixed annual grant in the amount of NIS 1 million (linked to the consumer price index as aforesaid). The office of Mr. Einan as Active Deputy Chairman of the Board is under the same terms and without any modification compared with the management agreement which was executed vis-à-vis him in respect of the terms which he had as the Company's CEO. Mr. Einan is further entitled to customary related benefits, including being provided with a vehicle in a suitable grade (up to vehicle of Grade 7), cellular telephones and reimbursement of actual expenses. The Company bears the full cost of all the benefits (including the cost of use and gross-up of the tax value). Mr. Einan is entitled to 12 months' adjustment pay, starting upon the actual conclusion of his employment for any reason whatsoever. On June 10, 2010, 395,778 phantom units were allocated to Mr. Einan, as part of the phantom unit allocation plan in the Company, which, as of the date of the Report, have not yet been exercised. For details see Note 25 of the financial statements in Chapter C of this Report.

With respect to his term in office as Executive Chairperson of the Board of Directors of Granite Hacarmel, Mr. Einan is entitled to annual compensation in the amount of NIS 384,000, linked to the consumer price index (of February 2008) (which amounted to approx. NIS 435,000 per year as of December 31, 2011). In addition, Mr. Einan is paid participation in meetings compensation as Chairperson of the Board of Directors of Granite and as a Director of Tambour, in accordance with the maximum amounts which were established in this matter in the Companies Regulations (Guidelines for Compensation and Expenses of Outside Directors) 5760-2000 ("**Compensation Regulations**"), according to the ranking of Granite Hacarmel or Tambour, as the case may be, pursuant to the Compensation Regulations, prior to the amendment thereof in March 2008. With respect to his term in office as director of GES, Mr. Einan is paid participation compensation in the amount of NIS 1300 per meeting. As of the date of the Report, Mr. Einan holds 2,098,286 options for Granite Hacarmel's shares, which, as of the date of the Report, have not yet been exercised, against the exercise price in the amount of NIS 8.366 per share, linked to the consumer price index of October, 2006. As of the date of the Report, the options have not been exercised. The expiration date of the aforesaid options is November 30, 2012.

(3) Shlomo Sherf - Mr. Sherf holds office as the Company's CEO since April 1, 2011, in accordance with an agreement between the Company and a company which is owned by him, in consideration for monthly management fees of NIS 250,000, together with a fixed annual grant in the amount of NIS 1 million, linked to the consumer price index of January, 2011 (the monthly management fees amounted to NIS 254,902 as of December 31, 2011). In addition, Mr. Sherf is entitled, to the customary related benefits, including being provided with a vehicle (Grade 7), or alternatively, the bearing by the Company of all of the costs of the expenses of the vehicle which was purchased by Mr. Sherf or the management company (including depreciation), telephones and reimbursement of expenses. In April 2011, 284,527 phantom units were allocated to Mr. Sherf (according to a new plan), according to a base price which was determined according to an average price of the Company's share in March 2011 (which was NIS 98), and which have not yet been exercised, as of the date of the Report. Mr. Sherf is entitled to 6 month early notice and, in the event of termination of the agreement at Mr. Sherf's initiative, to adjustment pay in the amount which is equal to 3 monthly payments. In the event of the termination of the engagement at the Company's initiative, Mr. Sherf shall be entitled to adjustment pay in the amount which is equal to 6 monthly payments, insofar as the engagement shall have been terminated during the first 3 years of employment, and

to 12 months of adjustment pay, insofar as the engagement shall have been terminated thereafter. For further details see Note 40C(9) of the Company's financial statements for 2011 and the immediate report of the Company dated January 16, 2011 (reference: 2011-01-018405), the content of which is hereby brought by way of reference. For his office as director of Granite Hacarmel and subsidiaries thereof Mr. Sherf is entitled to no further compensation The expense which the Company would have recorded due to the compensation to Mr. Sherf had he held office with the Company over a period of 12 months in 2011, would have amounted to approx. NIS 6,829 thousand.

(4) Mr. Yuval Bronstein serves as CFO of the Company, through a company owned by him, in consideration of monthly management fees, linked to the index, which on December 31, 2011, amounted to NIS 212,219, and customary related benefits, including the provision of a (Grade 6) vehicle, cellular telephones, expense reimbursement, advance notice of 3 months and a 6 month adjustment period for any reason whatsoever (after an update which was approved by the Company's board of directors on March 29, 2011). The Company bears the full cost of all the benefits (including the cost of use and gross-up of the tax value).

With respect to his term in office as a Director of Granite Hacarmel, Mr. Bronstein is entitled to annual compensation and participation compensation as well as to reimbursement of expenses, in accordance with the maximum amounts which were established in the Compensation Regulations [כבר הוגדר לעיל], prior to the amendment thereof in March 2008, according to the ranking of Granite Hacarmel, In addition, Mr. Bronstein is entitled solely to participation compensation for his service as a director of the subsidiaries of Granite Hacarmel, in the amount of NIS 1300 per meeting with respect to his term in office with Sonol Israel and GES and in accordance with the maximum amounts which were determined in this regard in the Compensation Regulations in respect of Tambour.

On June 10, 2010, 82,454 phantom units were allocated to Mr. Bronstein, as part of the phantom unit allocation plan in the Company, as specified in Note 25 of the financial statements, which have not yet been exercised, as of the date of the Report.

(5) Mr. Peer Nadir – holds office as CEO of Azrieli malls through a company held by him, in consideration for index linked, fixed, monthly management fees which, as of December 31, 2011, amounted to NIS 220,757, and standard related benefits, including the provision of a (Grade 6) vehicle, cellular telephones, expense reimbursements and advance notice of 6 months. The Company bears the full cost of all the benefits (including the cost of use and gross-up of the tax value). On February 22, 2012, the Company's board of directors and audit committee approved and ratified, for Mr. Pe'er Nadir, a one-time grant in the amount of NIS 225,000 for his contribution to the establishment, opening and marketing of the Company's malls in Akko and Kiryat Ata in the months August-September 2011 in a period which is significantly shorter than expected. For the board of directors' and audit committee's reasons for the granting of the compensation as aforesaid, see the Company's immediate report dated February 23, 2012 (reference: 2012-01-049929). For his office as a director with Granite Hacarmel, Mr. Nadir is entitled to annual compensation, and participation compensation, and expense reimbursement, in accordance with the maximum amounts which were set forth in the Compensation Regulations prior to the amendment of such regulations in March 2008, according to Granite Hacarmel's ranking. In addition, Mr. Nadir is entitled to participation compensation only, in the amount of NIS 1,300 per meeting, in respect of his office as director with the subsidiaries of Granite Hacarmel, Supergas and Sonol Israel. On June 10, 2010, 82,454 phantom units were allotted to Mr. Nadir in the context of the Company's phantom unit allotment plan as specified in Note 25 of the financial statements, one third of which have been exercised as of the date of the Report.

Compensation for Ms. Danna Azrieli, Active Vice Chairman of the Board (not included in the five most highly compensated persons):

Ms. Danna Azrieli served in the Company in various managerial positions, in accordance with management agreements between the Company and a management company owned by Ms. Azrieli. On June 1, 2010, Ms. Azrieli began serving as a Director of the Company and on June 8, 2008, she began serving as Active Vice Chairman of the Board of the Company. Ms. Danna Azrieli is entitled to monthly management fees, the cost of vehicle maintenance, the maintenance of a mobile telephone and reimbursement of expenses in accordance with the terms of the Company's engagement with a management company which is owned by her, whereby management services are provided to the Company exclusively by Ms. Danna Azrieli. In addition, compensation was paid to Ms. Danna Azrieli with respect to her term in office as a Director of Granite Hacarmel and GES, all as specified in Note 43 of the financial statements.

Name of recipient of compensation				**Compensation**				
Name	**Position**	**Scope of position**	**% holding[6]**	**Bonus**	**Share-based payment****	**Management fees(*)**	**Other**	**Total**
Danna Azrieli	Active Vice Chairman of the Board of Directors	80%	73.66%	---	---	2,186	28	2,214

* The management fee component includes the following components: cost of monthly management fee, standard social and related rights and benefits, car maintenance and communication and other expense reimbursement.

** For her office as director with granite Hacarmel and GES and less an expense which was recorded in 2011 for adjustment months at the time of retirement.

[6] Together with her father, Mr. David Azrieli, and her brother, as specified in the Company's immediate report on interested party holdings of October 6, 2011, Ref. 2011-01-295410.

Compensation of Company Directors

a. Compensation for the outside directors: Pursuant to resolutions of the Board of Directors and the General Meeting of May 10, 2010, and on August 24, 2010, the compensation of Outside Directors is in accordance with the maximum amount pursuant to the Compensation Regulations, in correspondence to the Company's capital rating, as determined periodically. In 2011, the compensation which the Company paid to the Outside Directors amounted to NIS 413,437.

b. Compensation for Mr. Joseph Ciechanover, independent director: On May 25, 2011, the audit committee and board of directors of the Company approved the classification of Mr. Joseph Ciechanover, who is a director with accounting and financial expertise, as an independent director, and approved, pursuant to the provisions of Section 1A(2) of the Companies Regulations (Relief for Transactions with Interested Parties), 5760-2000 (the "**Relief Regulations**"), the update of the compensation terms for Mr. Ciechanover and determined that pursuant to the provisions of Sections 244 and 249C of the Companies Law, 5759-1999 (the "**Companies Law**") and the Compensation Regulations, the compensation to Mr. Joseph Ciechanover as an independent director shall be identical to the compensation which is paid to an expert outside director who holds office with the Company in accordance with the approval of the general meeting of the shareholders of the Company dated August 24, 2010. In other words - the annual compensation and the participation compensation shall be paid in accordance with the maximum amount determined in the Compensation Regulations in respect of an expert outside director, in accordance with the Company's capital rating, as being from time to time. As of the date of this Report, the Company's capital rating is E. Such compensation amounts shall be linked to the consumer price index in accordance with the provisions of the Compensation Regulations. In addition, pursuant to the approval of the general meeting of the shareholders of the Company dated May 10, 2010, Mr. Ciechanover is entitled to an expense reimbursement which is identical to the expense reimbursement of all of the directors who are holding office with the Company (including Outside Directors), and in accordance with the Compensation Regulations. For details see an immediate report which was released by the Company on May 26, 2011, reference no: 2011-01-162051, which is included in this Report by way of reference.

c. Compensation for additional directors of the Company (including directors who are controlling shareholders): Pursuant to the resolution of the board of directors and general meeting of May 6, 2010, the payment to the other directors of the Company[7], shall be annual compensation in the amount of NIS 65,000 and meeting participation compensation in the amount of NIS 2,300. Such compensation amounts are linked to the consumer price index in accordance with the provisions of the Compensation Regulations. In addition, the provisions of Sections 5(b) and 6(a) of the Compensation Regulations pertaining to reimbursement of expenses to directors, including flights, *per diems* and hospitality, shall apply also with regard to such directors, *mutatis*

[7] In other words – excluding the outside directors, Mr. Joseph Ciechanover, independent director, and active directors who receive a salary from the Company, all as specified above.

mutandis. The audit committee and board of directors approved a framework for such expenses which is examined from time to time.

Regulation 21A - The Control of the Company

As of the date of the Report, the controlling party of the Company is Azrieli Holdings Inc. ("**Azrieli Holdings**"), a private company incorporated under Canadian law, which holds all of the share capital of Nadav Investments Inc., ("**Nadav Investments**"), which is the direct controlling party of the Company. Azrieli Holdings is wholly owned and controlled by members of the Azrieli family: Mr. David Azrieli, the Chairperson of the Board of Directors of the Company, holds, directly and indirectly, approximately 40% of the issued and paid-up share capital of Azrieli Holdings, and each of his four children (Naomi Azrieli, Sharon Azrieli, Danna Azrieli, and David Azrieli in trust for Rafi Azrieli) (hereinafter jointly: the "**Children**"), holds, directly and indirectly, approximately 15% of the issued and paid-up share capital of Azrieli Holdings. According to the agreement regulating the relationship between the shareholders of Azrieli Holdings, Mr. David Azrieli was granted all of the voting rights in Azrieli Holdings, in trust also for his Children, so that his voting in Azrieli Holdings shall be made at its sole discretion, including in connection with the sale of the shares of the Company.

Restructuring

In the context of a process of restructuring of the companies in the Group and primarily, steps for the consolidation of similar activities of the Group which were performed in fellow subsidiaries, and streamlining of the Group's current operation, the Company engaged, in November 2008, in an agreement with Nadav Investments whereby Nadav Investments transferred its shares in some of the Group's companies to the Company, as is, in consideration for an allotment of shares of the Company (the "**Restructuring Agreement**"). As of the date of the Report, the restriction period by virtue of Section 104A of the Income Tax Ordinance (New Version), 5721-1961, pertaining to the sale of shares which have been transferred, has expired.

Due to it being a company which is incorporated under Canadian law, Nadav Investments is governed, *inter alia*, in connection with its operations or investments in Israel, by the rules of taxation which are set forth in the treaty between the State of Israel and Canada pertaining to the prevention of double taxation and tax evasion with regard to taxes on income and capital (the "**Treaty**"), including with regard to the sale of shares in companies whose assets are mainly real properties. For purposes of clarification and interpretation of the sections of the Treaty which contemplate this issue, various tax ramifications and provisions regarding the sale of the Company's shares were set forth in the context of an agreement between the Israel Tax Authority and the Company, Canit Hashalom and Nadav Investments, dated November 2008, in accordance with the rate of the Company's holdings in real properties in Israel. In addition, the aforesaid agreement set forth provisions whereby Nadav Investments shall not act towards receiving any tax benefits in Canada which are not in accordance with the provisions of the law in Canada or the Treaty, provisions pertaining to the possibility to terminate the agreement if in the future the provisions of the Treaty and/or Chapter E of the Ordinance will be materially modified in the manner which has an effect on the manner of taxation of the sale, and additional provisions whereby in any event where there will be a tax liability in Canada due to the sale of the shares, the same shall have no effect on the tax liability which is set forth in the agreement.

Any restructuring in accordance with the provisions of the second part of the Ordinance which addresses the Company's shares and/or the shares of Canit Hashalom shall be performed solely after the receipt of the advance consent of the Mergers and Splits Department of the Tax Authority.

Activity restriction

In the context of the management agreements with the controlling shareholders of the Company which are specified in Regulation 21 above, Messrs. David Azrieli and Danna Azrieli undertook that so long as they are providing management services to the Company and/or companies of the Group, and during an additional period of six (6) months from the date of termination of the provision of the management services, and so long as no other resolution shall have been adopted by the Company's board of directors, they shall not operate in the Company's Business Segments, as defined below, through acquisition, investment, consultation, management and/or rendering of services, either directly or indirectly.

For purposes of this section the "**Company's Business Segments**", shall mean – (1) Development, maintenance and/or management of a commercial center and/or shopping mall in Israel, the area of which exceeds 12,000 sqm of commercial space for rent; and/or (2) Development, maintenance and/or management of office space for rent in Israel, the area of which exceeds 8,000 sqm of commercial space for rent; and/or (3) Development, maintenance and/or management of income-producing property in Israel, which incorporates commercial and office space, the area of which exceeds 10,000 sqm of commercial space for rent.

The aforesaid notwithstanding, the transactions and/or properties and/or projects which are specified below shall not be deemed as the use of business opportunities of the Company by such controlling shareholders: (a) Holding of properties and/or projects which are owned and/or controlled by Messrs. David Azrieli and Danna Azrieli, directly and/or indirectly, as of the date of the Report; (b) Purchasing up to 10% of properties which are in the Company's Business Segments, as aforesaid, and/or purchasing up to 10% of a corporation which holds properties as aforesaid, provided that the controlling shareholders shall have no active involvement in the management of such property; (c) Purchasing holdings in a corporation, the scope of the properties of which in the Company's Business Segments does not exceed 10% of the total scope of the assets thereof, and the scope of its income from activity in the Company's Business Segments in the year prior to the purchase date does not exceed 10% of the total scope of the income thereof; (d) Holding a corporation as provided in Subsection (c) above, also if after the purchase, which shall have been performed in accordance with the provisions of Subsection (c) above, the scope of the properties in the Company's Business Segments and/or the scope of its income from activity in the Company's Business Segments exceed 10% of the total scope of its income; and/or (e) Performing transactions and/or purchasing properties and/or projects and/or operations in the field of residential real estate in Israel. The controlling shareholders have operations in the field of real estate overseas and their aforesaid undertaking applies only with regard to the operations in Israel.

At the same time it shall be clarified that if and insofar as Messrs. David Azrieli and Danna Azrieli will seek to act in one or more of the Company's Business Segments, which are not part of the transactions which are described above, such that a business or legal or other impediment may be created to performance of specific transactions and activities by the Company and/or companies of the Group, they undertake to

present the outline of the proposed transaction to the Company's audit committee. In such a case, in the event that the Company's audit committee will decide that the Company is not interested in the proposed transaction, then they shall be entitled to perform the proposed transaction, either by themselves or through companies which are owned by them, without the same being deemed as the use of a business opportunity of the Company.

The aforesaid does not derogate from the fiduciary duty of any director in the Company, pursuant to Section 254 of the Companies Law.

Regulation 22 - Transactions with Controlling Parties

Following are the details with regard to transactions with the controlling party or in the approval of which the controlling party has a personal interest, in which the Company or a corporation controlled by it or a company related to it engaged as of the date of the issue of the Company's share to the public, or which are still in force as of the date of the Report:

Transactions listed in Section 270(4) of the Companies Law, 5759–1999 (the "Companies Law")

Engagement in a Management Agreement with a Management Company Owned and Controlled by Mr. David Azrieli

1. Mr. David Azrieli has served as Chairperson of the Board of Directors of the Company since the founding of the Company. In addition, two Canadian companies which are wholly owned and fully controlled by Mr. David Azrieli and which he manages have provided management services to the Group in accordance with a management agreement signed between them and the Company in May 2001 (in this section, the "**Management Company**)". On May 5, 2010, the General Meeting approved the replacement of the management agreement with a new agreement between the Company and the Management Company for the provision of services, pursuant to which the Management Company shall provide the Company with services, as of the date of the Report, through Mr. David Azrieli, for a period of five years, starting on April 1, 2010. For details regarding the main terms of the management agreement, see Note 43 of the financial reports. In accordance with Amendment 16 to the Companies Law, 5759-1999, the effect of the management agreement was updated until May 2013.

   Pursuant to the management agreement and following the Company's undertaking according to Section 8.1.4.4 of the Company's Prospectus dated May 12, 2010 (as amended on May 25, 2010), the audit committee approved on March 27, 2011 an expense reimbursement framework to the management company for the purpose of provision of the services, which shall not exceed an annual sum total of NIS 2 million, including in respect of reimbursement for flight expenses, first class or private airplane, as necessary, per diems, accommodation and so forth, which will be paid against provision of appropriate documentation. As stated in the management agreement, the aforesaid expense cap does not include expenses for a car and for phone communication, in respect of which a separate cap was prescribed within the framework of the management agreement in the amount of NIS 175,000. The audit committee stated that the annual amount was determined in accordance with the scope of business of the Company and the scope of services provided by the management company to the Company and the extensive

significance and contribution to the Company thereof. The expenses of the chairman of the board pertaining to the provision of the aforesaid services, considering his circumstances, are necessary for the Company's business needs and as part of the ordinary course of business. Considering the aforesaid, the audit committee believed that the annual expense cap and the procedure prescribed for approval and inspection thereof are in the benefit of the Company and are reasonable and fair in the circumstances of the matter. The audit committee further resolved that it would inspect, upon the end of each calendar year the expense cap determined above and the compatibility thereof to the Company's business and scope thereof, the Company's needs and the scope of the management services. Since the taking effect of the management agreement in April 2010 until December 31, 2011, the total amount of expenses as aforesaid was approx. NIS 1,886 thousand in the aggregate. The Company's audit committee examined on March 19, 2012, the management companies' expenses for the years 2010 and 2011, and determined that the same do not deviate from the framework which was determined therefor and that the expense cap which was determined is fits the Company's operations and the scope thereof, the Company's needs and the scope of management services which are provided by Mr. Azrieli.

2. Management Fees and Compensation for Ms. Danna Azrieli

Ms. Danna Azrieli provided the Group with various management services within the framework of an employment agreement and within the framework of management agreements between Candan Management Services Ltd. (the "**Management Company**") and the Company, starting in the year 2000. On May 1, 2010, an updated management agreement entered into force, the summary of the main provisions thereof is specified in Note 43 of the financial statements.

3. Compensation for additional directors who are controlling shareholders of the Company

Ms. Sharon Azrieli and Ms. Naomi Azrieli, daughters of Mr. David Azrieli, are entitled to directors' compensation as paid to the other directors in the Company who are not outside directors or who are not engaged in a separate management fee agreement with the Company, as specified in Regulation 21 above.

4. Insurance, Exemption and Indemnification of Controlling Shareholders

In the Company:

David Azrieli, Chairperson of the Board of Directors, Ms. Danna Azrieli, Deputy Chairperson of the Board of Directors, Ms. Naomi Azrieli, a Director, and Ms. Sharon Azrieli, a Director, have been granted exemption, insurance and indemnification in accordance with the arrangements which apply to exemption, indemnification and insurance of all of the Directors and Officers of the Company, including the Officers who are controlling parties of the Company, as they were updated at the Company's general meeting dated August 15, 2011. For details, see Regulation 29A below.

Granite Hacarmel:

Ms. Danna Azrieli, daughter of Mr. David Azrieli, the indirect controlling party of the Company and Granite Hacarmel, who is serving, as of the date of the Report,

as a Director of Granite Hacarmel, was granted a letter of indemnification under the same conditions as those granted by Granite Hacarmel to the remaining Directors and Officers of Granite Hacarmel and its subsidiaries, other than the exemption clause which shall not apply with regard to Ms. Danna Azrieli. The granting of the indemnification is pursuant to a resolution by the General Meeting of Granite Hacarmel, dated March 13, 2012.

In addition, Ms. Danna Azrieli is insured under a policy which covers the liability of Officers in the Granite Hacarmel Group, pursuant to the approval of the Audit Committee and the Board of Directors of Granite Hacarmel on May 26, 2009 and July 8, 2009, which approved the coverage of Ms. Danna Azrieli's liability under the aforesaid policy pursuant to Regulation 1B(5) of the Companies Regulations (Concessions for Transactions with Principal Shareholders), 5760-2000.

Transactions not listed in Section 270(4) of the Companies Law and which are not Negligible

1. Contributions to the Azrieli Foundation (Israel), a Registered NPO

According to the resolution of the Board of Directors and the General Meeting of the Company of May, 2010, within the framework of the annual contributions which are made by the Company to not-for-profit organizations, whose scope is determined by the Board of Directors of the Company from time to time, the Company shall transfer contributions, *inter alia*, to the Azrieli Foundation (Israel) (a Registered NPO) (the "**Foundation**"). The resolution was determined based on the examination of the principal objectives of the Foundation, which are: action toward promoting education and culture in Israel, through projects in the fields of education, culture, social welfare and science, implementation of projects and studies, alone and/or jointly with other organizations, including through the giving of grants to organizations and/or individuals for the purpose of carrying out projects and/or studies which are in line with the objectives of the Foundation – which were examined and found to be appropriate to the Company's contribution policy. The aforesaid resolution does not and shall not prevent the Board of Directors of the Company from adopting resolutions with regard to contributions to other not-for-profit organizations, the objectives of which shall be in line with the Company's contibution policy, as it shall be from time to time.

For the period ending on May 2015, the Company shall contribute to the Foundation in each calendar year, itself and/or through companies under its control (with the exception of Granite), an amount which constitutes 1.5% of the Company's annual profit and, in any event, not more than NIS 14 million. The contributions made by the Company to the Foundation will serve for donations and for the ongoing needs of the Foundation. The Company shall transfer the contributions in four (4) quarterly installments, or in accordance with the actual expenses of the Foundation, at the discretion of the CFO of the Company. This contribution shall be considered as a contribution from the total annual contribution budget of the Company, as shall be determined from time to time by the Board of Directors of the Company.

The Internal Auditor of the Company examines, each calendar year and up to the date of signature of the financial statements for that year, the overall scope of contributions in that year and their conformity to the considerations which underlay the Company's resolution as set forth above and issues a written report

to the audit committee.

On March 27 and 29, 2011, respectively, the audit committee and the board of directors approved a clarification for the aforesaid resolution, according to which the Company shall contribute to the Foundation, each calendar year, either itself and/or through companies under its control (apart from Granite)[8], the amount constituting up to 1.5% of the Company's annual profit, in accordance with the sole discretion of the Company's management, and in any event not more than the sum of NIS 14 million. The audit committee and the board of directors further approved that such clarification would only benefit the Company. For further details see an immediate report dated March 30, 2011,with regard to a transaction which would only benefit the Company pursuant to Regulation 1(2) of the Relief Regulations (in this section, the "**Immediate Report**").

It shall be stated that on February 20, 2012, the Company released an immediate report on a *lapsus calami* in the Company's Prospectus, which clarified that on page H-11 in Section 8.2.4, the title of which is Contributions to the Foundation, in the second paragraph on the third line, the number 0.15% (which refers to the total annual profit of the Company up to which the Company shall be entitled to contribute to the Foundation) shall be erased, and replaced by the number 1.5%. Accordingly - also with regard to the Immediate Report and the periodic report of the Company for 2010, it shall be deemed to read that "The Company shall contribute to the Foundation, each calendar year, either itself and/or through companies under its control (apart from Granite), the amount constituting up to 1.5% of the Company's annual profit. For details see the Company's immediate report dated February 20, 2012 (reference number 2012-01-046971).

2. Loans between the Company and/or Companies of the Group and the Controlling Parties of the Company or Companies controlled by them

For details regarding the arrangement for drawing loans up to an annual amount of NIS 1 million and the terms of repayment thereof, in the context of the management agreement of the Company with the management company owned by Mr. David Azrieli, See Note 43 of the financial statements.

3. Purchase of Shares in IC from a Company which is Wholly Owned and Controlled by the Controlling Party

On December 31, 2008, before it became a public company, the Company acquired 100% of the issued share capital of International Consultants (IConsult) Ltd. ("**IC**") from Canit Development Inc. (hereinafter: "**CDI**"), a corporation which is incorporated under Canadian law and which is wholly owned and controlled by Mr. David Azrieli and members of his family members.

In accordance with the Purchasing Agreement, the Company ensured that all of the arrangements for indemnification of Directors and Officers in IC and its subsidiaries would remain in force, as they were on the date of the purchase of the shares, including all of the Directors who were appointed by or on behalf of CDI, and insured all of the Directors and Officers of IC and its subsidiaries, including Directors and Officers who retired, for a period of seven years, starting on the date on which the Director or Office Holder ceased to serve IC or its subsidiaries as a

[8] Subject to required approvals

Director or Officer.

4. Guarantees of the Company's undertakings by the controlling party expired

In view of the Company's engagement in new financing agreements in connection with the properties Three Riverway and Northcase Plaza in Houston U.S.A. and upon the repayment of the previous loans due to such properties in March and May, 2011, Mr. David Azrieli's personal undertaking and guarantee to indemnify which were issued to the previous financers of the aforesaid properties and which were no longer required in the context of the new financing agreements, have automatically terminated.

Negligible Transactions

In the period of the Report, the Group performed negligible transactions with the controlling parties thereof, or that the controlling parties thereof had an interest in their approval, of the kinds and characteristics in accordance with a negligible transactions procedure approved by the Board of Directors of the Company, which is specified in Section 3.7 of Chapter B of this Report, and as specified in Note 43 of the financial reports, including:

1. Agreement for Rental of Offices to the Foundation: in May, 2010, Gemel Tesua Investments Ltd. ("**Gemel Tesua**") engaged in an agreement with the Foundation, pursuant to which Gemel Tesua shall rent out, at market conditions, to the Foundation, an area of approximately 242 m² in the office areas of the Herzliya Business Park Project, which is owned by the Group, and shall provide the Foundation with management and maintenance services as it provides said services to the remaining tenants of the project for a period of five (5) years, with an option for extension of the period by five additional years, in consideration of a quarterly payment of approximately NIS 81,000. In addition, Gemel Tesua approved a sub-lease of a negligible area of the space of such offices to an NPO which is affiliated with the spouse of the controlling shareholder of the Company. On March 27 and 29, 2011, respectively, the audit committee and the board of directors approved that a transaction according to which the Foundation would pay a debt to Gemel Tesua in respect of the costs of adjustments to the leased property, at a sum total of NIS 782,735 plus VAT, in 39 quarterly installments together with the rent fees, plus annual interest at a rate of 7% and linkage differentials, as customary with other lessees, is a transaction which is not irregular and is negligible.[9]

2. Rental Agreements with Related Parties: the Company, companies controlled by the Company and its related companies, have engaged in lease agreements with lessees, in the engagement with whom the controlling party and/or one or more of the senior Officers of the Company have a personal interest, pursuant to which the aforesaid companies lease out and/or leased out during 2011, in the ordinary course of business and at market conditions, areas in some of the income producing properties of the Company. The income with respect to the aforesaid rentals in the year ending on December 31, 2011, totaled approximately NIS 1.88 million (about seven lessees, including the Foundation). The Audit Committee and the Board of Directors of the Company examined in their meetings on March 19

[9] If the lease agreement will be terminated at an earlier date, the debt balance will be paid in one payment, within the framework of the settlement of accounts.

and 21, 2012, respectively , that these engagements are negligible transactions which are carried out in the ordinary course of business of the Company and at market conditions.

3. Employees of the Group who are Related to Interested Parties: the Group employs five employees who are related to controlling parties of the Company (and do not amount to the definition of "relative" in the Securities Law) in employment agreements which are not irregular and also negligible, in a total annual amount of approx. NIS 1.4 million.

4. Ties with the community – From time to time the Company makes contributions, either itself or through companies which are among the members of the Group, and to the Company's best knowledge, the Foundation donates to the community and to bodies or entities which require assistance, including bodies to which interested parties of the Company may have a link, or in which interested parties of the Company are volunteer members.

Regulation 24 - Holdings of Interested Parties and Senior Officers

Following are shares and other securities held by interested parties of the Corporation, in the Corporation or in companies held by the Corporation whose activity is material to the activity of the Corporation, as of March 21, 2012:

Name of interest holder	ID or passport no. or no. at the registrar	Company Name	Security name	Security no. in the stock exchange	Par value held and/or amount of convertible securities	Holding rate in %		Holding rate on a fully diluted basis in %(1)	
						of the capital	of voting	of the capital	of voting
Azrieli Holdings Inc.*		Azrieli Group Ltd.	Ordinary shares par value 0.1	1119478	89,336,646	73.66	73.66	73.66	73.66
Menachem Einan	008995383	Azrieli Group Ltd.	Ordinary shares par value 0.1	1119478	12,010	00.01	00.01	00.01	00.01
Yosef Chechnover	5991468	Azrieli Group Ltd.	Ordinary shares par value 0.1	1119478	790	00.00	00.00	00.00	00.00
Menachem Einan	008995383	Granite Hacarmel Investments Ltd.	Options for ordinary shares	2760080	2,098,286	--	--	--	--

* Azrieli Holdings Inc. ("Azrieli Holdings") is a private company incorporated under Canadian law. For more details, see Regulation 21A above.

* While noting the statements in Section 3.2.3 of the Company's Prospectus dated May 12, 2010, as amended on May 25, 2010 (reference: 2010-01-494514), on June 23, 2011, Nadav Investments Inc., which is the direct controlling shareholder of the Company, transferred 1,605,354 shares of the Company which are held thereby, for no consideration, to a foundation which is registered for charity purposes whose place of residence is Canada and the assets of which are intended for contributions and financing of philanthropic activity in Israel and in Canada (the "**Foundation**"). It is clarified that as has been relayed to the Company, neither Mr. David Azrieli nor any of his relatives are controlling shareholders of the Foundation and therefore, the Foundation shall not be deemed as an interested party or a controlling shareholder of the Company.

**For holdings in negligible scopes of Mr. David Azrieli and/or companies which are controlled by him in private subsidiaries of the Group, see Section 1.2 of Chapter A of this Report.

Holdings of senior officers

Name of Office Holder	ID no.	Security name	Security no. in the stock exchange	Par value held and/or amount of convertible securities	Holding rate in %		Holding rate on a fully diluted basis in %	
					of the capital	of voting	of the capital	of voting
Israel Keren	3105657	Ordinary shares par value 0.1	1119478	1,200	0	0	0	0
Avraham Yaakovi	52253747	Ordinary shares par value 0.1	1119478	1,783	0	0	0	0

Regulation 24A - Registered Capital, Issued Capital and Convertible Securities

As of December 31, 2011, the registered share capital of the Company is 127,501,500 ordinary shares par value NIS 0.1 each, and the issued share capital of the Company is 121,272,760 ordinary shares par value NIS 0.1.

Regulation 24B -The Company's Register of Shareholders

Name of shareholder	Company/ ID number	Address	Shares' type	Shares' amount	Par value
Registration Co. of Bank Hapoalim Ltd.	510356603	62 Yehuda Halevi, Tel Aviv	Ordinary shares par value NIS 0.1	121,272,760	NIS 0.1

Regulation 25A - Registered Address

The registered address of the Company is 1 Azrieli Center, Tel Aviv, 67021

Telephone: 03-6081400; Facsimile: 03-6081380

Electronic mail: michalk@azrieli.com

Regulation 26 - The Directors of the Corporation (As of the date of the Report)

Below are personal and professional details concerning the Directors of the Company:

(1)	Director Name:	David Azrieli, Chairperson of the Board
	Passport No.:	BA412456
	Date of birth:	May 10, 1922
	Address for service of process:	1 Azrieli Center, Tel Aviv
	Citizenship:	Canada
	Service on Board of Directors Committees:	Employee phantom plan management committee
	Outside Director/Independent Director:	No
	Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the Company:	Chairperson of the Board of Directors of the Company and the subsidiaries, with the exception of Granite Hacarmel Investments Ltd.
	Starting date of term in office as a Director:	August 23, 1990
	Education:	B.A. from Thomas More Institute, University of Montreal, Canada; M.Arch. from the University of Carlton, Ottawa, Canada; architectural studies at the Technion – Israel Institute of Technology.
	Occupation in the last five years and details of directorships in additional corporations:	Director of all of the companies in the Azrieli Group, with the exception of Granite Hacarmel Investments Ltd. and companies under its control. Owner and manager of a number of foreign private companies engaged in different fields.
	Family relationship to an interested party:	Yes. Mr. Azrieli's four children indirectly hold shares in the Company; for details, see Section 1.1 of Chapter A of this Report.
	Has expertise in finance and accounting or professional qualification:	Professional qualification.

(2)	Director Name:	Menachem Einan, Active Deputy Chairman of the Board
	I.D. card no.:	008995383
	Date of birth:	June 17, 1939
	Address for Service of Process:	1 Azrieli Center, Tel Aviv

Citizenship:	Israeli
Service on Board of Directors Committees:	Employee phantom plan management committee
Outside Director/Independent Director:	No
Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the Company:	Until March 31, 2011, served as CEO of the Company. As of April 1, 2011, serves as Active Deputy Chairman of the Board; Director General of Canit Hashalom Investments Ltd.; Chairman of the Board of Directors of Granite Hacarmel Investments Ltd.; Director at Tambour Ltd. and GES Global Environmental Solutions Co. Ltd.; Director at Leumi Card Ltd. [***a related company?***]
Starting date of term in office as a Director:	June 1, 2010
Education:	BA in Humanities from Bar-Ilan University; degree in Business Administration from UCLA
Occupation in the last five years and details of directorships in additional corporations:	Active Deputy Chairman of the Company's Board, previously the Company's CEO, and CEO of Canit Hashalom Investments Ld. Serves as Chairman of the Board of Directors of Granite Hacarmel Investments Ltd., Tambour Ltd. and GES Global Environmental Solutions Co. Ltd. Serves as a Director of Leumi Card Ltd.
Family relationship to an interested party:	No
Has expertise in finance and accounting or professional qualification:	Professional qualification

(3)	**Director Name:**	**Danna Azrieli, Active Vice Chairman of the Board**
	I.D. no.:	321657744
	Date of birth:	June 3, 1967
	Address for service of process:	1 Azrieli Center, Tel Aviv
	Citizenship:	Israeli
	Service on Board of Directors Committees:	No
	Outside Director/ Independent Director:	No
	Position held in the Company, a subsidiary, a related company of the Company or	Active Vice Chairman of the Board.

of an interested party of the Company:	
Starting date of term in office as a Director:	June 1, 2010
Education:	BA in Sociology and Anthropology from Swarthmore College; LLB in Law from Vermont Law School; member of the Massachusetts State Bar Association in the U.S. and the Israel Bar Association
Occupation in the last five years and details of directorships in additional corporations:	Active Vice Chairman of the Board of the Company; Chairman of the Board of Trustees of Shenkar College; serves as a Director of the following companies: Granite Hacarmel Investments Ltd., GES Global Environmental Solutions Ltd., and Candan Residences Ltd. (a company under her control). Member of the boards of directors of the University of Tel Aviv and the Herzliya Interdisciplinary Center. Chair of the Azrieli Foundation, Israel, Registered Association and director of the Azrieli Foundation, Canada.
Family relationship to an interested party:	Daughter of Mr. David Azrieli, the controlling party of the Company and Chairperson of the Board of Directors, and sister of Naomi, Sharon and Rafi Azrieli, who indirectly hold shares in the Company. For details, see Section 1.1 of Chapter A of this Report.
Has expertise in finance and accounting or professional qualification:	Professional qualification

(4)	**Director Name:**	**Sharon Azrieli**
	Passport no.:	WD011050
	Date of birth:	August 4, 1960
	Address for service of process:	1 Azrieli Center, Tel Aviv
	Citizenship:	Canadian
	Service on Board of Directors Committees:	No
	Outside Director/Independent Director:	No
	Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the Company:	None

Starting date of term in office as a Director:	June 1, 2010
Education:	PhD in Music from the University of Montreal; MA in Music from the University of Montreal; BA in Art from Vassar College; Certificate from the Juliard School of Music; degree in A.A.S. from the Parson School of Design
Occupation in the last five years and details of directorships in additional corporations:	Opera singer, cantor and artist; Conductor at several congregations Director of the Canadian body, Camp Kinneret Biluim, and of the Azrieli Foundation, Israel, Registered Association.
Family relationship to an interested party:	Daughter of Mr. David Azrieli, the controlling party of the Company and Chairperson of the Board of Directors, and sister of Danna (Deputy Chairperson of the Board of Directors), Naomi, and Rafi Azrieli, who indirectly hold shares in the Company. For details, see Section 1.1 of Chapter A of this Report.
Has expertise in finance and accounting or professional qualification:	No

(5)	**Director Name:**	**Naomi Azrieli**
	Passport no.:	WS194084
	Date of birth:	September 26, 1965
	Address for service of process:	1 Azrieli Center, Tel Aviv
	Citizenship:	Canadian
	Service on Board of Directors Committees:	No
	Outside Director/Independent Director:	No
	Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the Company:	None
	Starting date of term in office as a Director:	June 1, 2010
	Education:	PhD in International Relations and History from Oxford University, England; MA in International Economics and Public Administration from Columbia University, New York; BA from the University of Pennsylvania in Political Science and Russian Studies

Occupation in the last five years and details of directorships in additional corporations:	Director General and Director of the Azrieli Fund, a non-profit association. Owner and manager of foreign private companies.
Family relationship to an interested party:	Daughter of Mr. David Azrieli, the controlling party of the Company and Chairperson of the Board of Directors, and sister of Danna (Deputy Chairperson of the Board of Directors), Sharon, and Rafi Azrieli, who indirectly hold shares in the Company. For details, see Section 1.1 of Chapter A of this Report.
Has expertise in finance and accounting or professional qualification:	Professional qualification

(6)	Director Name:	Yosef Ciecanover
	I.D. card no.:	5991468
	Date of birth:	October 1, 1933
	Address for service of process:	1 Azrieli Center, Tel Aviv
	Citizenship:	Israeli
	Service on Board of Directors Committees:	Audit Committee, Finance Committee (serving also as the Financial Statements Review Committee)
	Outside Director/Independent Director:	Independent Director
	Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the Company:	None
	Starting date of term in office as a Director:	May 6, 2010
	Education:	PhD in Philosophy from Boston University; LLM in Law from the Hebrew University; Completed his studies towards an MBA in Business Administration at the Hebrew University (missing final paper); LLB in Law from the University of California, Berkeley.
	Occupation in the last five years and details of directorships in additional corporations:	2000 to present: Consultant for Etgar 2 Fund by way of the Atidim Funds Management Co. Ltd. Director at the Israel Discount Bank, Harel Investments, Insurance and Financial Services Ltd., the Israel Museum and a company for research and development of Bar-Ilan University. Chairman and CEO of Atidim Funds Management and I.Y.Z.
	Family relationship to an	No

interested party:	
Has expertise in finance and accounting or professional qualification:	Has expertise in finance and accounting

(7)	**Director Name:**	**Yossi Kucik**
	I.D. No.:	51008035
	Date of birth:	November 14, 1951
	Address for service of process:	1 Azrieli Center, Tel Aviv
	Citizenship:	Israeli
	Service on Board of Directors Committees:	Finance Committee (serving also as the Financial Statements Review Committee)
	Outside Director/Independent Director:	No
	Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the Company:	None
	Starting date of term in office as a Director:	June 1, 2010
	Education:	1979-1983: MA in Public Administration, the Hebrew University; 1975-1978: BA in Political Science and International Relations, the Hebrew University.
	Occupation in the last five years and details of directorships in additional corporations:	2006-2011: Vice Chairman Direct Insurance Financial Investments Ltd. As of the date of the Report: Owner of "Yossi Kucik-Merav Parsi Zadok, Strategy and Communication Ltd."; Owner of "Kucik" – Development Management and Consulting Services Ltd.; Chairman of Zur Shamir Holdings Ltd. Chairman of the board of governors – Rabin Center Director at Meitav Investment House
	Family relationship to an interested party:	None
	Has expertise in finance and accounting or professional qualification:	Professional qualification

(8)	Director Name:	Efraim Halevy, Outside Director
	I.D. No.:	49871718
	Date of birth:	December 2, 1934
	Address for service of process:	1 Azrieli Tower, Tel Aviv
	Citizenship:	Israeli
	Service on Board of Directors Committees:	Chairman of the Audit Committee, Finance Committee (which also sits as the Financial Statements Review Committee)
	Outside Director/Independent Director:	Yes
	Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the Company:	None
	Starting date of term in office as a Director:	August 24, 2010
	Education:	LL.M. - The Hebrew University in Jerusalem.
	Occupation in the last five years and details of directorships in additional corporations:	2003-2011: Head of the Shasha Center for Strategic Studies in the Hebrew University. 2004-2006: Outside Director of Makhteshim Agan Industries Ltd.
	Family relationship to an interested party:	None
	Has expertise in finance and accounting or professional qualification:	Professional qualification

(9)	Director Name:	Niv Ahituv, Outside Director
	I.D. No.:	008115693
	Date of birth:	August 16, 1943
	Address for service of process:	1 Azrieli Tower, Tel Aviv
	Citizenship:	Israeli and Canadian
	Service on Board of Directors Committees:	Audit Committee, Chairman of the Finance Committee (serving also as the Financial Statements Review Committee)
	Outside Director/Independent Director:	Expert Outside Director
	Position held in the Company, a subsidiary, a related company of the Company or of an interested party of the	None

Company:	
Starting date of term in office as a Director:	August 24, 2010
Education:	BA in Mathematics and Physics from the Hebrew University. MA in Business Administration from Tel Aviv University MA in Information Systems from Tel Aviv University. PhD in Management (specialization in Information Systems) from Tel Aviv University.
Occupation in the last five years and details of directorships in additional corporations:	2011 to date: President of the Dan Academic Center 2003-2011: Academic Director of the Institute for Internet Studies, Tel Aviv University; 2008 to date: Director of the Henry Crown Institute of Business Research in Israel, Tel Aviv University; 2010 to date: Member of the Investments Committee in Migdal Insurance; 2008 to date: Outside Director of Ace Auto Depot Ltd.; 2007 to date: Outside Director of Rapac Communication & Infrastructure Ltd. 2007 to date: Outside Director of Discount Investments; 2005-2007: Outside Director of Matrix I.T. Ltd.; 2003 and 2009: Outside Director of Harel Investments; 1981–2011- management professor at the Tel Aviv University; Since 2011 – professor emeritus at the Tel Aviv University; Member of the Management at Beit Lessin Theatre.
Family relationship to an interested party:	None
Has expertise in finance and accounting or professional qualification:	Has expertise in finance and accounting

<u>Regulation 26A - Senior Officers (as of the date of the Report)</u>

(1)	**Office Holder Name:**	**Shlomo Sherf**
	I.D. No.:	030223549
	Date of birth:	September 10, 1949
	Starting date of term in office:	**April 1, 2011**
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	No
	Education:	B.A. in Mechanical Engineering, Ben Gurion University
	Position held in the Company:	**CEO**

Position in a subsidiary, in an affiliate of the Company or of an interested party thereof:	Serves as a director of Granite Hacarmel Investments Ltd., Tambour Ltd. and GES Global Environmental Solutions Ltd. and as CEO of Canit Hashalom Investments Ltd.
Occupation in the last five years:	CEO of Electra Real Estate for 7 years. CEO and Director of Electra Ltd. and Director of subsidiaries of Electra for 15 years.

(2)	**Office Holder Name:**	**Yuval Bronstein**
	I.D. No.:	024297996
	Date of birth:	March 24, 1969
	Starting date of term in office:	March 1, 2007
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	No
	Education:	B.A. in Economics and Accounting, Hebrew University; MBA, major in Finance and Accounting, Hebrew University; Licensed as a CPA (Israel)
	Position held in the Company:	**CFO and in charge of market risk management in the Company**
	Position in a subsidiary, in an affiliate of the Company or of an interested party thereof:	Holds office as director of Granite Hacarmel Investments Ltd., Sonol Israel Ltd., Tambour Ltd. and GES Global Environmental Solutions Ltd.
	Occupation in the last five years:	2007 to date: CFO, Azrieli Group Ltd. 2005–2007: Deputy Comptroller General, Ministry of Finance

(3)	**Office Holder Name:**	**Peer Nadir**
	I.D. No.:	054097290
	Date of birth:	March 26, 1956
	Starting date of term in office:	December 1, 2009
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	No
	Education:	B.A. in Economics and Accounting, Tel Aviv University; MBA, major in Finance and Accounting, Tel Aviv University; Licensed as a CPA (Israel)
	Position held in the Company:	**CEO, Azrieli Malls**
	Position in a subsidiary, in an affiliate of the Company or of an interested party thereof:	Serves as a Director of Granite Hacarmel Investments Ltd., Supergaz–Israeli Gas Distribution Co. Ltd. and Sonol Israel Ltd.

Occupation in the last five years:	CEO of the Azrieli Malls Group. Chairman, Tel Aviv National Sports Center, Municipal Company Ltd. Member of the board of directors of the Ramat Hasharon Economic Development Company Ltd.

(4)	**Office Holder Name:**	**Arnon Toren**
	I.D. No.:	054121678
	Date of birth:	July 14, 1957
	Starting date of term in office:	January 1, 1998
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	No
	Education:	B.A. in Economics and Sociology, Hebrew University
	Position held in the Company:	**Manager of office segment and CEO, Azrieli Center Tel Aviv**
	Position in a subsidiary, in an affiliate of the Company or of an interested party thereof:	holds office as a Director of Granite Hacarmel Investments Ltd., Sonol Israel Ltd., Supergaz–Israeli Gas Distribution Co. Ltd.
	Occupation in the last five years:	Chief Marketing Officer in the Company and Manager, Azrieli Center Tel Aviv, holds office as director ofVardinon Real Estate and Investments Ltd.

(5)	**Office Holder Name:**	**Michal Kamir**
	I.D. No.:	**022802110**
	Date of birth:	**June 29, 1967**
	Starting date of term in office:	**June 20, 2010**
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	**No**
	Education:	**LLB in Law, Tel Aviv University** **MA in Business Law, Management and Marketing, Middlesex University, London**
	Position held in the Company:	**General Counsel and Company Secretary**
	Occupation in the last five years:	**2006-2010: Attorney, Herzog, Fox, Neeman, Attorneys at Law** **2000-2006: Attorney, Fischer, Behar, Chen, Well Orion & Co. Attorneys at Law** **Outside Director of Dash Ipex Holdings Ltd. until**

	2006 **Outside Director of Rimoni Industries Ltd. until November 2010**

(6)	**Office Holder Name:**	**Israel Keren**
	I.D. No.:	**003105657**
	Date of birth:	**September 17, 1947**
	Starting date of term in office:	**July 1, 2002**
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	**No**
	Education:	**B.A. in General History, Tel Aviv University**
	Position held in the Company:	**Holds office as CEO of the Group's private companies: Gemel Tesua Investments Ltd., Otzma & Co. Investments- Maccabim Ltd., Urban A.A.R. Ltd., Herzliya Business Park Operations Ltd.**
	Occupation in the last five years:	July 2007 to date: Holds office as CEO of the following companies: Gemel Tesua Investments Ltd., Urban A.A.R. Ltd. and Otzma & Co. Investments- Maccabim Ltd. In addition, manages the E Tower Construction Project in Herzliya Business Park. July 2002 to date: CEO, Herzliya Business Park Operations Management Co. Ltd. July 2002–May 2005 and November 2006–November 2007: CEO, Margalit Hasharon Operations Management Co. Ltd., simultaneously with his other positions as stated above.

(7)	**Office Holder Name:**	**Avraham Yaakovi**
	I.D. No.:	052253747
	Date of birth:	March 31, 1954
	Starting date of term in office:	July 1, 1987
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	No
	Education:	B.A. in Accounting and Economics, Bar Ilan University; Licensed as a CPA (Israel)
	Position held in the Company:	Comptroller, Azrieli Group Ltd.
	Occupation in the last five	1987 to date: Holds office as managing comptroller,

	years:	Azrieli Group Ltd.
(8)	**Office Holder Name:**	**Eyal Iohan**
	I.D. No.:	025523531
	Date of birth:	May 7, 1973
	Starting date of term in office:	June 21, 2010
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	No
	Education:	LLB in Law and BA in Business Administration, The International Disciplinary Center in Herzliya
	Position held in the Company:	**Construction Manager**
	Position in a subsidiary, in an affiliate of the Company or of an interested party thereof:	Holds office as a director of Sonol Ltd. and Via Maris Desalination Ltd.
	Occupation in the last five years:	2005-2010: Assistant to the President of the Azrieli Group, Secretary of the Company.
(9)	**Office Holder Name:**	**Rafi Wunsh**
	I.D. No.:	028145738
	Date of birth:	February 15, 1971
	Starting date of term in office:	October 15, 2010
	Interested party in the Corporation or a family member of an interested party or another senior Office Holder in the Corporation:	No
	Education:	B.A. in Economics and Accounting, Hebrew University of Jerusalem
	Position held in the Company:	**Business Development Manager**
	Occupation in the last five years:	VP Quebec region, Elad Group Canada Inc. (for three years). CFO, Elad Group Canada Inc. (for two years).
(10)	**Office Holder Name:**	**Gali Gana**
	I.D. No.:	059674770
	Date of birth:	June 2,1965
	Starting date of term in office:	September 20, 2009
	Interested party in the Corporation or a family member of an interested party or another senior Office	No

Holder in the Corporation:	
Education:	B.A. in Business Administration, Israel College of Administration; M.A. in Internal Auditing and Public Administration, Bar Ilan University; Certified Internal Auditor (CIA) since 2002; Certified Systems Auditor (SCA) since 2001, Certified in risk and information systems control (CRISC).
Position held in the Company:	**The Internal Auditor**
Occupation in the last five years:	Partner in Rosenblum Holtzman CPA Offices since 1997

Regulation 26B - Independent Authorized Signatories

As of the date of the Report, Mr. David Azrieli is an independent authorized signatory of the company and his signature alone can bind the Company.

Regulation 27 - The Company's Accountants

The Company's auditors are Brightman Almagor Zohar & Co., CPA, 1 Azrieli Center, Tel Aviv.

Regulation 28 -Amendment to the Memorandum of Association or Articles of Incorporation

On August 15, 2011, the general meeting of the shareholders of the Company approved the amendment of several sections of the Company's articles of association, with the aim of adjusting the same to Amendment Number 16 to the Companies Law, and to the Improvement of Enforcement by the ISA Law (Legislation Amendments), 5771-2011 (the "**Improvement of Enforcement Law**"), including an amendment of the sections of the articles of association pertaining to the indemnification and insurance of officers of the Company, in accordance with the Improvement of Enforcement Law, in the manner which will enable the Company to insure and indemnify the officers thereof, subject to any law, due to a monetary liability which shall have been imposed on the officer for all of the parties who are injured by the violation in an administrative proceeding as provided in Section 52-54(a)(1)(a) of the Securities Law, and due to expenses which the officer shall have expended in connection with an administrative proceeding which shall have been conducted in his regard, *inter alia*, reasonable litigations expenses, including legal fees.

In addition a provision was added to the Company's articles of association which was included in the letters of indemnification which were issued to the Company's officers, whereby the amount of the indemnification which the Company will pay to all of the officers, cumulatively, according to all of the letters of indemnification which either were and/or will be issued to them by the Company, due to one or more of the events which are, in the opinion of the directors, expected in view of the Company's actual operations at the time of the issuance of the undertaking to indemnify, and as will be specified in the Company's letters of indemnification from time to time, shall not exceed the amount which is equal to 20% of the equity which is attributed to the Company's shareholders according to the Company's, audited or reviewed, financial statements, which shall have been released close before the indemnification date.

For the full version of the amendments to the Company's articles of association see the Company's immediate report dated August 7, 2011 (reference: 2011-01-233409).

Regulation 29 - Resolutions and Recommendations of the Board of Directors

a) Resolutions of the Board of Directors regarding dividend distribution or performance of distribution, following the Company's becoming a public company:

For details regarding the resolutions of the Board of Directors with respect to dividend distribution, see Sections 4.3 and 4.4 of Chapter A of this Report.

b) Resolutions of a Special General Meeting

On August 15, 2011, a Special General Meeting of the shareholders approved the following resolutions:

1. Amendment of the Company's articles of association in accordance with the provisions of Regulation 28 above.

2. While noting the amendment of the Company's articles of association as aforesaid, and after the receipt of the approval of the audit committee and the board of directors of the Company dated June 28, 2011, the general meeting approved an amendment to the language of the letters of exemption and indemnification which the Company issued and issues to the officers and directors of the Company, including to the officers and directors of the Company who are considered controlling shareholders and/or in the issuance of which Company's controlling shareholders have a personal interest, as will hold office from time to time, in order to adjust the same to the provisions of Section 56H of the Securities Law, such that the letters of indemnification shall also include an undertaking to indemnify due to a monetary liability which shall have been imposed on the officer for all of the parties who are injured by the violation in an administrative proceeding as provided in Section 52-54(a)(1)(a) of the Securities Law, and due to expenses which the officer shall have expended in connection with an administrative proceeding which shall have been conducted in his regard, *inter alia*, reasonable litigations expenses, including legal fees.

For additional details pertaining to the general meeting, for the language of the amended articles of association and the language of the amended letters of indemnification, see immediate report of the Company dated August 7, 2011 (reference no. 2011-01-233409) and an immediate report of the Company pertaining to the results of the meeting dated August 15, 2011 (reference no. 2011-01-241173).

3. For details pertaining to the clarification of the Company's policy on contributions to the Foundation and correction of a *lapsus calami* in the Company's Prospectus in this context, see Regulation 22 above.

Regulation 29A -The Company's Resolutions

The resolutions of the Board of Directors which were not set forth in Regulation 29 above are set forth below:

Approval of actions pursuant to Section 255 of the Companies Law: None.

Actions pursuant to Section 254(a) of the Companies law: None.

Irregular transactions requiring special approvals pursuant to Section 270(1) of the Companies Law:

1. **Agreements with Officers:**

1.1. On March 29, 2011, the Board of Directors of the Company approved a plan for the allocation of phantom units, which will be allocated to the CEO of the Company, Mr. Shlomo Sherf. Pursuant to the plan for the allocation of phantom units, which were allotted to 32 senior officers of the Company (other that the Company's Chairman of the Board and Ms. Danna Azrieli, Active Vice Chairman of the Board) and the Company's employees. For details regarding the plan for the allocation of options to Mr. Sherf and the other terms of his employment, see Note 40 of the financial statements and Regulation 21 above.

1.2. For details on the amendment of the letters of indemnification for all of the Company's officers, see Regulation 29 above.

1.3. On February 22, 2012, after the date of the statement of the financial position, the audit committee and board of directors of the Company approved and ratified the granting of one-time grants to four officers of the Company. For details see the Company's immediate report dated February 23, 2012 (reference: 2012-01-049929).

1.4. For a description of the Company's engagements in agreements with Officers in the Company, who are also controlling parties thereof, or to agreements of the Company with third parties, in which the controlling parties have a personal interest, see Regulations 21 and 22 above.

2. Exemption, Indemnification and Insurance of Officers

Following is a description of the applicable arrangements with regard to exemption, indemnification and insurance for Directors and Officers in the Company:

2.1. Exemption for Directors and Officers

Pursuant to a resolution by the Board of Directors and the General Meeting dated May 6, 2010, the Company has granted its Directors and Officers, as they shall be from time to time, an exemption, in advance and retroactively, from their liability, in whole or in part, for any damage which shall be and/or has been caused to it, whether directly or indirectly, due to a breach of the duty of care by the Directors and Officers vis-à-vis the Company and vis-à-vis its subsidiaries and by virtue of their position as Officers and/or Directors in the Company or Officers and/or Directors

on behalf of the Company in subsidiaries.

2.2. Indemnification of Directors and Officers

On May 6, 2010, the Board of Directors of the Company and the General Meeting of the Company approved the granting of indemnification to all of the Officers and Directors in the Company, including controlling shareholders of the Company, all - as may be from time to time, for any liability or expense, as set forth below, which shall be imposed upon them as a result of operations which they carried out (including operations which they carried out prior to the date on which the exemption and indemnification document was issued) and/or which they shall carry out by virtue of their position as Officers and/or Directors in the Company or Officers and/or Directors on behalf of the Company in subsidiaries or related companies of the Company, or any other company in which the Company has an interest. The amount of the indemnification which the Company shall pay to all of the Officers (including the Directors), cumulatively, shall not exceed 20% of the equity capital attributed to the shareholders of the Company according to the most recent (audited or reviewed) financial statements of the Company which shall have been published prior to the date of the indemnification.

On August 15, 2011, the general meeting approved an amendment in the language of the letters of exemption and indemnification which the Company issued and issues to the officers and directors of the Company (including directors who are controlling shareholders of the Company), in order to adjust the same to the provisions of Section 56H of the Securities Law, as specified in Regulation 29 above.

2.3. Insurance policies for Officers

2.3.1. On May 6, 2010, the Company's Board of Directors and General Meeting approved a resolution whereby the Company shall be entitled, at any time during five periods of insurance, commencing from June 3, 2010, and with the approval of the Audit Committee and the Board of Directors of the Company, without requiring the additional approval of the General Meeting therefor, to purchase policies to insure the liability of the Directors and Officers as shall serve in the Company from time to time, to extend and/or to renew the existing insurance policy and/or to engage in a new policy at the time of renewal or during the period of the insurance, with the same insurer or another insurer in Israel or in another country, on terms similar to the policy which shall have been approved on such date and as specified below, to insure the liability of Directors and/or Officers, provided that such engagements in question shall be on the basis of the principal conditions set forth below. The Company's engagements as aforesaid shall not be brought before the General Meeting for additional approval, and shall be approved by the Audit Committee and the Board of Directors of the Company, including in connection with Directors on behalf of the controlling party, which shall confirm that the new policies comply with the following conditions:

a. The limit of liability within the framework of the insurance policies, as they shall be drawn up from time to time by the Company, shall not exceed USD 100 million per event and for the period of the insurance, with the addition of the costs of legal defense at a rate of up to 20% of the limit of liability to be purchased (solely in Israel).

b. The deductible per claim for the Company shall not exceed USD 150 thousands, in accordance with the cause of action and place of filing thereof.

c. The insurance annual premium shall not exceed the amount of USD 250,000.

d. The insurance policy shall be extended to cover claims to be filed against the Company (in contrast to claims against Directors and/or Officers thereof), which concern the breach of securities laws at least in Israel (Entity Coverage for securities claims), and arrangements for the payment of insurance benefits shall be determined, pursuant to which the right of the Directors and/or Officers to receive indemnification from the insurer pursuant to the policy shall have priority over the right of the Company.

e. The policy shall also cover the liability of the controlling parties, by virtue of their position as Directors and/or Officers in the Group, from time to time, provided that the terms of coverage therefor shall not exceed those of the remaining Directors and/or Officers in the Group.

2.3.2. In accordance with the aforesaid, on May 31, 2011, the audit committee and board of directors of the Company approved the extension of the Company's engagement in a director and officer liability insurance policy on a claims-made basis for a period of 12 months commencing from June 3, 2011. Such insurance policy shall cover all of the directors and officers of the Company and the subsidiaries, as being from time to time, including by virtue of their position as directors and officers of subsidiaries of the Company, other than in respect of Granite Hacarmel Group, which holds an independent officer insurance policy (all of the directors and officers of the Company who hold office with the Granite Hacarmel Group shall be covered in the context of the Company's policy in connection with their office with Granite Hacarmel only over and above the coverage which exists in Granite Hacarmel's officer and director liability insurance policy). The maximum liability cap of the insurer is U.S. $100 million per event and for the insurance period plus legal defense expenses at the rate of up to 20% of the liability cap (in Israel only), while the annual premium which the Company shall bear is in the amount of U.S. $123 thousand and the co-payment per claim for the Company only due to claims against directors and officers shall not exceed U.S. $50 thousand, according to the cause of action and place of filing thereof.

The insurance policy is extended to cover claims which will be filed against the Company (as distinguished from claims against directors and/or officers thereof) pertaining to a violation of the securities laws at least in Israel (entity coverage for securities claims), however the directors' and/or officers' right to receive indemnification from the insurer pursuant to the policy precedes the Company's right.

In addition, the audit committee and board of directors of the Company approved that the engagement in the aforesaid policy fulfills the conditions which were approved by the Company's general meeting.

2.3.3. Further to the approval of the Company's Board of Directors and General Meeting of May 6, 2010, the Company purchased a POSI (Public Offering of Securities Insurance) insurance policy that covers the liability of the Company, the Directors and Officers thereof, the controlling parties in the Company and additional entities who have taken part in the issue to the public of Company shares pursuant to the Prospectus (hereinafter: the "**Issue**"), against claims to be filed against them in connection with the Issue, for a period of 7 years from the date of the Issue. The maximum limit of liability of the insurer pursuant to this policy is USD 100 million per event and for the period of the insurance, with the addition of the costs of legal defense at a rate of 20% of the limit of liability to be purchased (solely in Israel), while the premium to be borne by the Company for this policy amounts to USD 250,000 per year. The deductible per claim to the Company in respect of claims pursuant to this policy shall not exceed US $35 thousand.

David Azrieli, Chairman of the Board of Directors	Shlomo Sherf, CEO

Date: March 21, 2012.

Appendix A – Regulation 11

List of Investments in Subsidiaries and Related Companies as of the Statement of the Financial Position Date (Not Including Inactive Companies)

				Rate in %				In NIS thousand		
Company name	**Shares' class**	**Total par value of shares in NIS**	**Total par value of held shares in NIS**	**Of the capital**	**Of voting**	**Authority to appoint Directors**	**Cost of the held shares**	**book value of investment (*)**	**Balance of loans from the Company**	
Directly held companies										
Canit Hashalom Investments Ltd.	ordinary	114	113	99.1%	99.1%	99.1%	-	4,193,304	1,355,327	1)
International Consultants (Iconsult) Ltd.	ordinary	3,900	3,900	100%	100%	100%	30,307	44,142	26,782	2)
Azrieli Mall Center (Initiation and Management) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-	
The Negev Mall (Initiation and Management) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-	
Ayalon Mall (Initiation and Management) Ltd.	ordinary	20	20	100%	100%	100%	-	-	-	
Jerusalem Mall (Initiation and Management) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-	
Canyon Holon - Management & Maintenance Ltd.	capital	100	60							
	voting	10	5							
		110	65	60%	50%		-	-	-	
Azrieli Center Parking Lot Ltd.	ordinary A	1000	999	99.9%	99.9%	99.9%	2	21,662	-	
Azrieli Center Towers (Initiation and Management) Ltd.	ordinary	100	99	99%	99%	99%	-			
Otzem Initiation & Investments (1991) Ltd.	management	80	80			100%		44,927	127,472	3)
	ordinary A	21,330,220	21,330,220							
	ordinary B	4,999	4,999							
		21,335,299	21,335,299	100%	100%	100%	-			
Givatayim Mall Initiation and Management Ltd.	ordinary	100	100	100%	100%	100%	-	-	-	

Azrieli Mall Haifa (Initiation and Management) Ltd.	ordinary	100	100		100%	100%	100%	-	-	-
Canit Northchase L.P		-	-		100%	100%	100%		86,202	-
Canit USA II Inc.	ordinary	4000	4000	4)	100%	100%	100%	4	-	29
Canit Regency L.P		-	-		100%	100%	100%	-	-	-
Canit USA Inc.	Ordinary	4000	4000	4)	100%	100%	100%	4	-	-
San Felipe Voss Investments L.P		-	-		100%	100%	100%	4	-	-
San Felipe Voss GP Inc.	Ordinary	4000	4000	4)	100%	100%	100%	-	-	-
AG Galleria Office Buildings, LP					100%	100%	---	71,604	86,202	-

					Rate in %			In NIS thousand		
Company name	**Shares' class**	**Total par value of shares in NIS**	**Total par value of held shares in NIS**		**Of the capital**	**Of voting**	**Authority to appoint Directors**	**Cost of the held shares**	**book value of investment (*)**	**Balance of loans from the Company**
Companies held by Canit Hashalom										
Granite Hacarmel Investments Ltd.	ordinary	147,146,834			60.68%	60.68%		740,836	-	-
Gemel Tesua Investments Ltd.	ordinary	53,750,000	53,696,250		99.9%	99.9%		-	-	-
Otzma & Co. Investments Maccabim Ltd.	ordinary	16,100,000	16,083,000		99.9%	99.9%		-	-	-
Modiin Mall (Initiation and Management) Ltd.	ordinary	100	100		100%	100%	100%	-	-	-
Azrieli Mall Modiin (offices) Initiation and Management Ltd.	ordinary	100	100		100%	100%	100%	-	-	-
Azrieli Mall Modiin (Residencies) Initiation and Management Ltd.	ordinary	100	100		100%	100%	100%	-	-	-
South Post Oak Holdings LP	ordinary	-	-		100%	100%		-	-	-
South Post Oak General Inc	Ordinary	4000	4000	4)	100%	100%		4	-	-
RiverCan LP	Ordinary	-	-		100%	100%		-	-	-
RiverCan GP LLC	Ordinary	4000	4000	4)	100%	100%		4	-	-

				Rate in %			In NIS thousand		
				Rate in %			In NIS thousand		
Company name	**Shares' class**	**Total par value of shares in NIS**	**Total par value of held shares in NIS**	**Of the capital**	**Of voting**	**Authority to appoint Directors**	**Cost of the held shares**	**book value of investment (*)**	**Balance of loans from the Company**
Companies held by Gemel Tesua Investments Ltd.									
Margalit Hasharon Operations Ltd.	Ordinary	100	100	100%	100%	100%	-	-	-
Herzliya Business Park Operations Ltd.	Ordinary	100	99	99.0%	99.0%		-	-	-
Canyon Holon - Management & Maintenance Ltd.	Capital	100	40						
	Voting	10	5						
	Total	110	45	40%	50%		-	-	-
Azrieli Kiryat Ata Mall (Initiation and Management) Ltd.		100	100	100%	100%		-	-	-

				Rate in %			In NIS thousand		
Company name	**Shares' class**	**Total par value of shares in NIS**	**Total par value of held shares in NIS**	**Of the capital**	**Of voting**	**Authority to appoint Directors**	**Cost of the held shares**	**book value of investment (*)**	**Balance of loans from the Company**
Companies held by International Consultants (Iconsult) Ltd.									
Urban A.A.R. Ltd.	Ordinary	4,828,637	4,828,637	100%	100%	100%	6,132	-	-
Gemel Tesua Investments Ltd.	Ordinary	53,750,000	28,350	0.051%					
Otzma & Co. Investments Maccabim Ltd.	Ordinary	16,100,000	8,236	0.051%					
Herzliya Business Park Operations Ltd.	Ordinary	100	1	1%	1%		-	-	-

Company name	Shares' class	Total par value of shares in NIS	Total par value of held shares in NIS	Rate in %			In NIS thousand		
				Of the capital	Of voting	Authority to appoint Directors	Cost of the held shares	book value of investment (*)	Balance of loans from the Company
Companies held by Otzem Initiation and Investments (1991) Ltd.									
Azrieli Akko Mall (Development and Management) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Azrieli Ramla Mall (Development and Management) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-

Company name	Shares' class	Total par value of shares in NIS	Total par value of held shares in NIS	Rate in %			In NIS thousand		
				Of the capital	Of voting	Authority to appoint Directors	Cost of the held shares	book value of investment (*)	Balance of loans from the Company
Companies held by AG Galleria Office Buildings, LP									
Three Galleria Office Buildings Member, L.P.		-	-	90%	100%	-	-	-	-
Three Galleria Office Buildings, LLC	units (LLC)		-	90%	100%(13)				

Company name	Shares' class	Total par value of shares in NIS	Total par value of held shares in NIS	Rate in %			In NIS thousand		
				Of the capital	Of voting	Authority to appoint Directors	Cost of the held shares	book value of investment (*)	Balance of loans from the Company
Companies held by Granite Hacarmel Investments Ltd.									
Sonol Israel Ltd.	ordinary	9,055	9,055	100%	100%	100%	287,730	-	-
Tambour Ltd.	ordinary	64,842,261	54,632,261	84%	84%	84%	238,978	-	-

GES Global Environmental Solutions Ltd.	ordinary	7,304,169	7,304,169	100%	100%	100%	57,078	-	-
Supergas Israel Gas Distribution Co. Ltd	ordinary	252	252	100%	100%	100%	32,289	-	-
Incorporated Company for Oils and Chemicals Ltd. (Aloc)	ordinary A	21	21	100%	100%	100%	-	-	-
	ordinary B	13,563	13,563	100%	100%	100%	-	-	-
Sonapco Bank Street Corporation 6)				100%	100%	100%	9,753	-	-
Granite Hacarmel Holdings (1993) Ltd.	ordinary	1,999	1,999	100%	100%	100%	2	-	-
Granite Hacarmel Holdings Development Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Oganim Beyarok Ltd.	ordinary	100	60	60%	60%	60%	234	-	-
Granite Hacarmel Assets (1993) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Development Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Energy Holdings Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Energy (1997) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Industries Holdings Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Industries Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Y.A. Holdings Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Tourism Holdings Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Hacarmel Tourism (1995) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Granite Automotive Agencies Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
GAA Global Automotive Ltd.	ordinary	1000	1000	100%	100%	100%	-	-	-
Super Solar Ashalim Ltd.	ordinary	100	100	100%	100%	100%	-		
Park Mini Israel Limited Partnership				49.5%	49.5%	-	-	-	-
Park Mini Israel Ltd. (1997)	ordinary			50%	50%	50%	-	-	-
Triad Fuel Engineering Pvt Ltd 7)	ordinary (8)			10.75%			-	-	-
	BCCPS			21.13%	33%	43%	12,956	-	-

	warrants			1.24%			-	-	-
Focal Energy Holdings Limited 7) 9)	preferred			17.6%	17.6%	-	14,983	-	-
Sprint Motors Ltd.	casting	1	1	100%	100%	100%	-	-	-
	ordinary A	400,000	400,000				-	-	-
	ordinary B	400,000	400,000				-	-	-
Sprint Motors Transport (1999) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Sonol Dan (1992) Ltd.	ordinary	200	200	100%	100%	100%	-	-	-
Milchen Sonol Agency Ltd.	ordinary	3000	3000	100%	100%	100%	-	-	-
Sonol Merkaz Ltd. (formerly Sonol Jerusalem Ltd.)	ordinary	3000	3000	100%	100%	100%	-	-	-
Sonol Knaan Ltd.	ordinary	2,400,000	2,400,000	100%	100%	100%	-	-	-
Sonol – Tzafon Ltd.	special	0.001	0.001	100%	100%	100%	-	-	-
	deferred	56.2	56.2						
	ordinary	300	300						
Sonol Darom Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Chem-Ami Ltd.	ordinary	62.5	62.5	100%	100%	100%	-	-	-
Chemital Industrial Chemicals to Israel Ltd.	ordinary	0.05	0.05	100%	100%	100%	-	-	-
Tzomet Plugot Ltd.	ordinary	0.0051	0.0051	100%	100%	100%	-	-	-
So Good Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Sonol Kat	ordinary	4,000	4,000	100%	100%	100%	-	-	-
Sonol Yad Mordechai Ltd	management A	0.005	0.005						
	management B	0.005	-						
	ordinary	1.70	1	58.82%	58.82%	58.82%	-	-	-
Gas Station Tzomet Raanana Ltd.	ordinary	0.102	0.051	50%	50%	50%	-	-	-
Operation Station Naaman Ltd.	ordinary	0.0101	0.0101	100%	100%	100%	-	-	-
Sonor Ltd.	ordinary	26,000	26,000	100%	100%	100%	-	-	-
Klison Holdings (1999) Ltd.	ordinary	38,000	38,000	100%	100%	100%	-	-	-
The Maccabim Station ltd.	ordinary		0.0333	33.33%	33.33%	33.33%	-	-	-
	Foundation		0.0001				-	-	-
	special		0.0001				-	-	-
Filling Station K. in Haifa Bay Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Tambourd Gypsum Products Ltd.	ordinary	1,000	1,000	95%	95%	95%	-	-	-
Tambourd Commerce Ltd. 10)	ordinary	1,000	1,000	100%	100%	100%	-	-	-

Askar Ltd.	ordinary	244	243.61	99.84%	99.84%	99.84%	-	-	-
Zeva Colour Industries Ltd.	ordinary	87.5	87.5	100%	100%	100%	-	-	-
Tzah Serafon Ltd.	ordinary	26,786,739	26,786,739	100%	100%	100%	-	-	-
Tambour Distribution Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Serafon Commerce (1997) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Askar Transport Ltd.	ordinary	0.1	0.1	100%	100%	100%	-	-	-
Tambourehev Colours (1997) Ltd.	ordinary	100	100	100%	100%	100%	-	-	-
Cotachem Farben Ltd.Co.KG 11)				100%	100%	100%	-	-	-
T.P. Developments Establishment 7)	ordinary			100%	100%	100%	-	-	-
Tambour Polymers Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Tambour Holdings (1993) Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Tzomet Zvaim Vaod Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Tamarin Marine Paints Ltd.	ordinary	0.0002	0.0002	100%	100%	100%	-	-	-
Zeva Colour Industries Ltd. ("**Zeva**")	ordinary	87.5	87.5	100%	100%	100%	-	-	-
Memberpil Ltd.	ordinary	1,000	500	50%	50%	50%	-	-	-
Ayalon Water Treatment Ltd.	ordinary	350	350	100%	100%	100%	-	-	-
	foundation	0.02	0.02						
Chematehet Chemicals for Treatment of Metal Ltd.	ordinary	40,200	40,200	100%	100%	100%	-	-	-
Gypsum-Gesher 2006 Ltd.	ordinary	100	51	51%	51%	51%	-	-	-
Nad Investmenst Ltd.	ordinary	1.96	1.96				-	-	-
	ordinary			100%	100%	100%	-	-	-
	foundation	0.02	0.02				-	-	-
C.T.Inex (1983) Ltd.	ordinary	7.968	7.968	100%	100%	100%	-	-	-
Tambour Building Keshet Powder Plant Ltd.	ordinary	40.000	20,400	51%	51%	51%	-	-	-
Supergas Eshkolot Ltd.	ordinary	1.001	1.001	100%	100%	100%	-	-	-
	repayment	0.001	0.001						
Supergas Hanegev (1990) Ltd.	ordinary	10,000	6,500	65%	65%	65%	-	-	-
Rav Gas Ltd.	special	1	1	100%	100%	100%	-	-	-
	ordinary	100	100						
Solomon M. & Co. Ashkelon Gas Agency Ltd.	ordinary	0.200	0.102	51%	51%	51%	-	-	-
Supergas for Home Ltd.	ordinary	100	100	100%	100%	100%	-	-	-

Gas Channels Ltd.	Ordinary A	5	-						
	Ordinary B	5	5	50%	50%	50%	-	-	-
GASTIV Natural Gas Distribution Company	ordinary	1,000	181.3	18.13%	18.13%	18.13%			
S. Super Solar Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Projects Ltd. 12)	ordinary	1,000	1,000	100%	100%	100%	-	-	-
P.S.I. 1Ltd.	ordinary	1,000	700	70%	70%	70%			
Super Solar Projects 1 Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Projects 2 Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Projects 4 Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Projects 9 Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Small Systems Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Natural Supergas Holdings Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Natural Supergas Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
SuperNG Natural Gas Distribution Company Ltd	ordinary	1,000	500	50%	50%	50%	-	-	-
Super CNG Ltd.	ordinary	1,000	910	91%	91%	91%	-	-	-
Super Solar Tender for Ground Mounted Systems 1 Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Tender for Ground Mounted Systems 2 Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Supergas Super Electricity Supply Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Projects 5 Small Size System Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Super Solar Projects 7 Small Size System Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Cyclean Ltd.	ordinary	8,500	8,500	100%	100%	100%	-	-	-
Texma Chemicaals Ltd.	management A	0.005	0.005	100%	100%	100%	-	-	-
	management A	1	1						
	management B	0.05	0.055						
	management B	1	1						
	ordinary	3,351,000	3,351,000						

Uniqkleen Wastewater Treatment Ltd.	ordinary	3,048	2,302	76%	76%	76%	-	-	-
Argad Water Treatment Technologies Ltd.	ordinary	1,006	1,006	100%	100%	100%	-	-	-
Via Maris Desalination (Holdings) Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Via Maris Desalination Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Via Maris Operations Ltd.	ordinary	1,000	1,000	100%	100%	100%	-	-	-
Via Maris Construction Partnership				99.99%	99.99%	99.99%	-	-	-
Activated Carbon Technologies Ltd.	ordinary	2,000	1,000	50%	50%	50%	-	-	-
M.I.D Municipal Investments & Developments Ltd.	ordinary	13,333	5,000	37.5%	37.5%	37.5%	-	-	-
Dan Viro Ltd.	ordinary	1,000	875	87.5%	87.5%	87.5%	-	-	-
Sewage Treatment Institute Dimona Partnership				50%	50%	50%	-	-	-
PURITEC GES HOLDINGS SA. 7	ordinary	10,000	5,100	100%	100%	100%	-	-	-
PURITEC GES INC. SA. 7)	ordinary			100%	100%	100%	-	-	-
PURITEC GES SA DE CV. 7)	ordinary			100%	100%	100%	-	-	-
PURITEC GES SA (NICARAGUA). 7)	ordinary			100%	100%	100%	-	-	-
PURITEC GES CORP. 7)	ordinary			100%	100%	100%	-	-	-
PURITEC GES SERVICES SA. 7)	ordinary			100%	100%	100%	-	-	-
PURITEC GES SA (PANAMA). 7)	ordinary			100%	100%	100%	-	-	-

(*) The data refers solely to the companies directly held by the Company.
(1) Deducting capital fund
(2) Deducting capital fund
(3) Capital bills
(4) In American companies, pursuant to an exchange rate of NIS 4
(5) The holding rate of the capital and of the voting reflects the holding rate of Granite Hacarmel, directly and/or indirectly, in such companies and not the holding rate of the Company.
(6) The company is registered in Delaware, USA. The company was registered as a foreign company in Israel in 1992.
(7) Foreign company
(8) Including preferred shares.
(9) Convertible into ordinary shares. The holding above assumes that the Company will perform the whole investment and in full dilution B the Company holds shares
(10) The transfer of shares to Tambourd has not yet been completed
(11) Foreign partnership
(12) Super Solar Projects Ltd. and project companies under the ownership thereof have holdings in additional companies which are designated companies for the purpose of submitting projects in the solar area.

CHAPTER E

Annual Report on the Effectiveness of Internal Control over Financial Reporting and Disclosure pursuant to Regulation 9B(a)

December 31, 2011

Attached hereto is an Annual Report on the Effectiveness of Internal Control over Financial Reporting and Disclosure pursuant to Regulation 9B(a) for year 2011:

The management, under the supervision of the board of directors of Azrieli Group Ltd. (the "Corporation"), is responsible for determining and maintaining proper internal control over the financial reporting and disclosure within the Corporation.

For this purpose, members of the management are:

1. Shlomo Sherf, CEO;
2. Yuval Bronstein, CFO;
3. Michal Kamir, General Counsel and Company Secretary;
4. Irit Sackler Philosof, Chief Comptroller for Accounting and Financial Statements.

Internal control over the financial reporting and disclosure includes controls and procedures existing within the Corporation, which were planned by or under the supervision of the CEO and the most senior financial officer, or by anyone actually performing such functions, under the supervision of the board of directors of the Corporation, which are designed to provide reasonable assurance regarding the reliability of the financial reporting and the preparation of the reports according to the provisions of the law, and to ensure that information which the Corporation is required to disclose in reports released thereby according to the law is gathered, processed, summarized and reported within the time frames and in the format set forth in the law.

Internal control includes, *inter alia*, controls and procedures which were planned to ensure that information which the Corporation is required to disclose as aforesaid, is gathered and transferred to the management of the Corporation, including the CEO and the most senior financial officer, or anyone actually performing such functions, in order to enable the timely making of decisions in reference to the disclosure requirement.

Due to its inherent limitations, internal control over financial reporting and disclosure is not designed to provide full assurance that misrepresentation or omission of information in the reports is prevented or discovered.

The management, under the supervision of the board of directors, has performed a review and assessment of the internal control over financial reporting and discourse in the Corporation and the effectiveness thereof; The assessment of the effectiveness of internal control over financial reporting and disclosure performed by the management, under the supervision of the board of directors, included:

- ✓ Mapping and documenting the controls and identifying the very material processes in the Company and in the main consolidated companies according to the reporting risks, with respect to each one of the Company or the main consolidated companies, as the case may be.

  The processes determined as very material are: <u>In the Company</u>: Rental income from investment property, investment property; <u>in Sonol</u>: The

processes of income from the sale of fuels at stations, the processes of inventory and purchase of fuels and the processes of giving credit and collection from customers; in Tambour: The income processes and customers and the processes of purchase and inventory; in Supergas: The income processes.

- ✓ Examination of the actual performance and documentation of the controls defined in the ELC processes, in the ITGC, in the process of preparation of the financial statements and in the processes identified as very material to financial reporting and disclosure.

- ✓ An overall assessment of the effectiveness of internal controls.

Based on the assessment of the effectiveness performed by the management under the supervision of the board of directors, as specified above, the board of directors and management of the Corporation have reached the conclusion that the internal control over financial reporting and disclosure in the Corporation as of December 31, 2011 is effective.

Attached hereto are statements of the CEO and the CFO, who is responsible for the financial reporting at the Company.

Date: March 21, 2012

Statement of Manager:

Statement of CEO pursuant to Regulation 9B(d)(1):

I, Shlomo Sherf, represent that:

(1) I have reviewed the periodic report of Azrieli Group Ltd. (the "Corporation") for the year 2011 (the "Reports").

(2) To my knowledge, the Reports do not contain any misrepresentation of a material fact, nor omit any representation of a material fact which are required for the representations included therein, in view of the circumstances in which such representations were included, not to be misleading in reference to the period of the Reports.

(3) To my knowledge, the Financial Statements and other financial information included in the Reports adequately reflect, from all material respects, the financial condition, results of operations and cash flows of the Corporation for the dates and periods to which the Reports relate.

(4) I have disclosed to the Corporation's auditor and to the Corporation's board of directors and the Audit and Financial Statement Committees of the Corporation, based on my most current assessment of the internal control over financial reporting and disclosure:

a. Any and all significant flaws and material weaknesses in the determination or operation of internal control over financial reporting and disclosure which may reasonably adversely affect the Corporation's ability to gather, process, summarize or report financial information in a manner which casts a doubt on the reliability of the financial reporting and preparation of the Financial Statements in accordance with the provisions of the law; and -

b. Any fraud, either material or immaterial, which involves the CEO or anyone reporting to him directly or which involves other employees who play a significant role in the internal control over the financial reporting and the disclosure;

(5) I, either alone or jointly with others in the Corporation:

a. Have determined controls and procedures, or confirmed the determination and existence of controls and procedures under my supervision, which are designed to ensure that material information in reference to the Corporation, including consolidated companies thereof as defined in the Securities Regulations (Annual Financial Statements), 5770-2010, is presented to me by others within the Corporation and the consolidated companies, particularly during the period of preparation of the Reports; and -

b. Have determined controls and procedures or confirmed the determination and existence of controls and procedures under my supervision, which are designed to provide reasonable assurance of the

reliability of the financial reporting and preparation of the Financial Statements according to the provisions of the law, including in accordance with GAAP.

c. Have assessed the effectiveness of the internal control over financial reporting and disclosure, and have presented in this Report the conclusions of the board of directors and management regarding the effectiveness of such internal control as of the date of the Reports.

The aforesaid does not derogate from my responsibility or from the responsibility of any other person, pursuant to any law.

March 21, 2012

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Shlomo Sherf, CEO

Statement of Manager:

Statement of the most senior financial officer pursuant to Regulation 9B(d)(2):

I, Yuval Bronstein, represent that:

(1) I have reviewed the Financial Statements and other financial information included in the reports of Azrieli Group Ltd. (the "Corporation") for the year 2011 (the "Reports");

(2) To my knowledge, the Financial Statements and the other financial information included in the Reports do not contain any misrepresentation of a material fact, nor omit any representation of a material fact which are required for the representations included therein, in view of the circumstances in which such representations were included, not to be misleading in reference to the period of the Reports.

(3) To my knowledge, the Financial statements and other financial information included in the Reports adequately reflect, from all material respects, the financial condition, results of operations and cash flows of the Corporation for the dates and periods to which the Reports relate;

(4) I have disclosed to the Corporation's auditor and to the Corporation's board of directors and the Audit and Financial Statement Committees of the Corporation, based on my most current assessment of the internal control over financial reporting and disclosure:

a. Any and all significant flaws and material weaknesses in the determination or operation of internal control over financial reporting and disclosure insofar as it relates to the Financial Statements and the other information included in the Reports, which may reasonably adversely affect the Corporation's ability to gather, process, summarize or report financial information in a manner which casts a doubt on the reliability of the financial reporting and preparation of the Financial Statements in accordance with the provisions of the law; and -

b. Any fraud, either material or immaterial, which involves the CEO or anyone reporting to him directly or which involves other employees who play a significant role in the internal control over the financial reporting and the disclosure;

(5) I, either alone or jointly with others in the Corporation:

a. Have determined controls and procedures, or confirmed the determination and existence of controls and procedures under my supervision, which are designed to ensure that material information in reference to the Corporation, including consolidated companies thereof as defined in the Securities Regulations (Annual Financial Statements), 5770-2010, insofar as it relates to the Financial Statements and the other information included in the Reports, is presented to me by others

within the Corporation and the consolidated companies, particularly during the period of preparation of the Reports; and -

b. Have determined controls and procedures or confirmed the determination and existence of controls and procedures under my supervision, which are designed to provide reasonable assurance of the reliability of the financial reporting and preparation of the Financial Statements according to the provisions of the law, including in accordance with GAAP;

c. Have assessed the effectiveness of the internal controls on financial reporting and disclosure, insofar as it relates to the Financial Statements and the other information included in the Reports as of the date of the Reports. My conclusions regarding my assessment as aforesaid were presented before the board of directors and the management and are integrated in this Report.

The aforesaid does not derogate from my responsibility or from the responsibility of any other person, pursuant to any law.

March 21, 2012 _____

Yuval Bronstein, CFO