

AIG Israel Insurance Company Ltd

Interim Financial Report

(Unaudited)

As of September 30, 2015

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Directors' report
AIG Israel Insurance Company Ltd ("the Company")
for the period ended September 30, 2015

The directors' report on the business of the Company as of September 30, 2015 ("**the directors' report**"), reviews the Company and developments in its business in the first three quarters of 2015 ("**the reported period**"). The information in this report are as of September 30, 2015 ("**the date of report**") unless otherwise is indicated explicitly.

The Company is an "insurer" as this term is defined in the Supervision of Financial Services Law (Insurance), 1981. Therefore, this report is prepared based on Regulations 68-69 and the Second Addendum to the Insurance Business Supervision Regulations (Report Information), 1998 ("**the Reporting Regulations**") and according to the guidance issued by the Supervisor of Capital Markets, Insurance and Savings in the Israel Ministry of Finance ("**the Supervisor of Insurance**" or "**the Supervisor**"). This directors' report was prepared assuming that the user is also holding the Company's 2014 periodic report.

The financial information in this report is in reported amounts. All financial information is in thousand NIS unless otherwise is indicated.

The business of the Company is in fields that require considerable professional knowhow that involves many professional terms that are essential for understanding the business of the Company. To present a description of the corporation that is as clear as possible, those professional terms are used along with an explanation, to the extent possible.

This directors' report is an integral part of the interim financial statements, including all its parts and should be read as one unit.

Forward looking information

This chapter in the periodic report, describing the Company, the development of its business and its fields of operations may contain forward-looking information, as this term is defined in the Israel Securities Law, 1968 ("**the Securities Law**"). Forward looking information is uncertain information about the future, based on the information available to the Company on report date and includes the subjective assessment of management based on assumptions and estimates of the Company and/or its intentions as of the date of this report. Providing such information is not a commitment for accuracy or completeness, and actual activity and/or results of the Company may be different than those presented in the forward looking information presented in this report. It is possible in certain cases to detect passages that contain forward looking information by the use of words such as: "the Company assesses", "the Company believes", "it is the intention of the Company", etc., but it is possible to see such information presented using other language or it may be specifically indicated that as a forward-looking information.



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1. Condensed description of the Company:

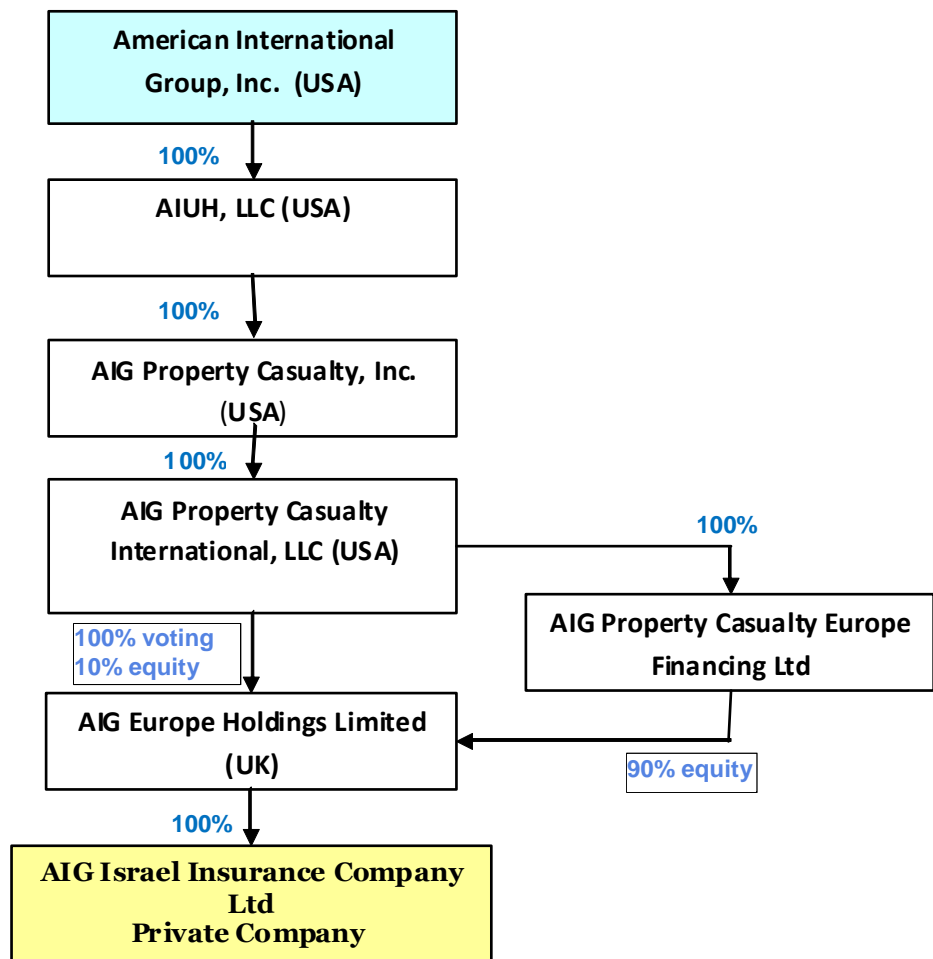
1.1 Organizational structure

AIG Israel Insurance Company Ltd ("**the Company**") was incorporated in Israel on March 27, 1996, as a private limited liability company. The Company began its insurance activity in May 1997. The company does not hold any subsidiaries or related companies. The Company has no activity outside of Israel through branches and associates.

The ultimate parent of the Company is American International Group Inc. (hereinafter: "**the global AIG corporation**"). The global AIG Corporation is a leading global insurance and financial services corporation, rated A- according to Standard & Poor's (S&P).

The shareholder of the Company is AIG Europe Holdings Limited, which holds the entire issued share capital of the Company, and is part of the global AIG corporation.

The following is the holding structure of the Company:





The Company was granted licenses by the Supervisor of Insurance to practice as an insurer in general insurance and life insurance as follows: motor vehicle insurance, compulsory motor vehicle insurance, comprehensive home insurance, health insurance (disease, hospitalization and personal injury coverage), commercial insurance (property loss, business comprehensive insurance, engineering insurance, employers' liability insurance, third-party liability insurance and product liability insurance), cargo in transit insurance, other risk insurance (limited to crime and fraud damages), comprehensive life insurance, and foreign business insurance for different insurance types.

The Company is operating in two business divisions (individual insurance and commercial insurance), headquarters, sales and customer service.

The Company is marketing and selling retail insurance policies directly to customers (without insurance agents) through call centers and online. Customers are being serviced mainly through a central service call center. Most business of the Company in commercial insurance, and some of the retail insurance business, is done through mediation of insurance agents. As a result of the above marketing methods, the organizational structure of the Company is based on activity through a head office in Petach Tikva and a small office in Haifa area.

1.2 Areas of activity

The Company mostly provides coverage to individual customers. The main business areas of the Company are as follows:

- General insurance: property vehicle insurance
- General insurance: compulsory vehicle insurance
- General insurance: home insurance
- General insurance: commercial insurance
- Health insurance: health insurance
- Life insurance: Life insurance, risk only

1.3 Dependency on customers or marketing entities

The Company has no dependency on any single customer in most business activities. For more information see Sections 2.1.3, 2.2.3, 2.3.3, 2.4.3, 2.5.3 and 2.6.3 in Chapter A (description of company's business) in the company's periodic report.

1.4 Developments or material changes in reinsurance agreements

For information about reinsurance see Section 4.5 in Chapter A (description of company's business) in the company's periodic report.

1.5 Event outside the ordinary course of company's business since last financial statements

No exceptional events have taken place since balance sheet date.



2. Description of business environment:

General

In accordance with data published by the division of Capital Market, Insurance and Savings at the Israel Ministry of Finance, there are more than 20 Israeli insurance companies currently active in Israel; most of these companies are engaged in general insurance. In accordance with these data, as of June 30, 2015, insurance fees from the general insurance business amounted to NIS 19,691 million (excluding Karnit); the share of the 5 largest insurance companies – Harel, Clal, Phoenix, Migdal and Menorah – amounted to NIS 6,533 million, which constituted 59% of the total premiums in the Israeli general insurance sectors.

For further details regarding the competition in the different lines of business of the company and regarding the measures taken by the company to face competition in this competitive market, see Sections 2.1.2, 2.2.2, 2.3.2, 2.4.2, 2.5.2 and 2.6.2 in Chapter A (description of company's business) in the company's periodic report.

Developments in the company's macro-economic environment

The company invests a considerable part of its investment portfolio in the capital market; therefore, the yields arising from different routes of investments in the capital market have a significant effect on company's profits.

The following are data on the changes in the marketable securities indexes in the stock exchange:

| | Jan-Sep 2015 | Jan-Sep 2014 | Jul-Sep 2015 | Jul-Sep 2014 | 2014 |
|---------------------------------|-----------------|-----------------|-----------------|-----------------|------|
| Government bonds indexes | | | | | |
| General government bonds | 1.4% | 6.7% | 0.9% | 2.1% | 6.6% |
| Linked government bonds | (0.2%) | 6.5% | (0.2%) | 1.6% | 5.8% |
| NIS government bonds | 2.4% | 6.8% | 1.7% | 2.4% | 7.2% |
| Corporate bonds indexes | | | | | |
| Tel Bond 60 | (0.3%) | 3.2% | (0.2%) | 1.1% | 0.9% |
| Tel Bond NIS | 2.8% | 4.8% | 2.0% | 2.0% | 4.0% |
| Shares indexes | | | | | |
| Tel-Aviv 100 | 0.9% | 8.1% | (8.3%) | 4.2% | 6.8% |

For information regarding the composition of the Company's investments see financial investment asset list in note 6 to the condensed financial statements.

For information on general trends in the insurance sector and their effect on company's business, see Section 4.3 in Chapter A (description of company's business) in the Company's 2014 periodic report.

Characteristics and developments in principal insurance lines of business

For information about characteristics and developments in principal insurance lines of business of the Company, see Sections 2.1.2, 2.2.2, 2.3.2, 2.4.2, 2.5.2, 2.6.2, 4.1, 4.5 and 4.7 in Chapter A (description of company's business) in the company's periodic report.

The impact of new laws, regulations and directives on the business of the Company in the reported period and financial statements information

The following is a summary of major regulatory changes and the key issues that are relevant to the activity of the Company, as published by the Supervisor of Insurance in circulars and drafts during the third quarter until shortly before the date of issuing this report:



Regulations

- On July 27, 2015 the Financial Services Supervision Regulations (Insurance) (Group Health Insurance), 2015 were published in the official gazette. These regulations include amendments to the Financial Services Supervision Regulations (Insurance) (Group Health Insurance), 2009, which cover, among other things the following issues: determining a maximal increase of insurance premiums in the course of the insurance period or at the time of renewal of the policy, issuance of notices to the insured person or entity in connection with renewal of the policy or change in the terms of insurance in the course of the insurance period and restricting the insurance period under a group health insurance policy to five years.
- On August 4, 2015 the Financial Services Supervision Regulations (Insurance) (Terms in Insurance Contract for Surgery and Surgery Alternative Procedures in Israel), 2015 were published in the official gazette. The regulations require that uniform insurance coverage is provided under private surgery insurance policies. The regulations will come into effect on January 1, 2016. The said regulations shall apply to new insurance policies issued as from that date or policies that will be renewed as from that date.

Circulars

- On July 15, 2015, the Supervisor issued Insurance Circular 2015-1-12 regarding "Joining an Insurance Plan". The purpose of the circular is to set principles for formalizing the practices by insurance companies and insurance agents when adding candidates to insurance policies.
- On July 29, 2015, the Supervisor issued Insurance Circular 2015-1-13 regarding "Amendments and Clarifications on General Insurance Reporting". The purpose of the circular is to add information to the mandatory reporting format set in Insurance Circular 2009-1-6 "Required Disclosure Format in Accompanying Reports of Insurance Companies" including accompanying reports to appraiser reports issued in the property home and vehicle sectors.
- On July 30, 2015, the Supervisor issued Insurance Circular 2015-1-8 titled "Independence between Individual Health Insurance Coverage". The purpose of this circular is to set provisions for marketing different insurance coverage in individual health insurance plans, and provisions about cancellation of such types of coverage that were sold together.
- On August 2, 2015, the Supervisor issued Insurance Circular 2015-1-14 regarding the "Liability Adequacy Test (LAT) in Financial Statements of Insurance Companies". The purpose of the circular is to determine the manner of calculation of the adequacy of reserves and the disclosure provided in financial statements of insurance companies, with reference to the different characteristics of the future cash flows, including non-liquidity (through the non-liquidity premium) and cost of non-hedgeable risks.
- On August 10, 2015, the Supervisor issued Circular 2015-1-15 regarding "Required Disclosure Format in (Interim) Financial Statements of Insurance Companies under International Financial Reporting Standards (IFRS)". The purpose of the circular is to set the required disclosure format in interim financial statements of insurance companies. Among other things the circular includes the following changes: requirement for issuance of an auditor's report in the case of standalone financial statements, making changes in the disclosure requirements so that they comply with the provisions of IFRS, making changes to the disclosure requirements so that comply with the provisions regarding annual financial statements and adding a requirement that a material misstatement is reported to the Supervisor.
- On August 24, 2015, the Supervisor issued Circular 2015-1-16 titled "Guidance for Drafting Insurance Plans". The circular is designed to provide a list of terms and conditions that need to be included in an insurance plan and terms and conditions that should not be included in an insurance plan, such that insurance plans will not include depriving conditions and will be simple and clear.
- On August 25, 2015, the Supervisor issued Circular 2015-9-28, titled "Principles for Medical Underwriting". The circular is designed to set guidelines for medical underwriting by financial institutions. An appendix to the circular list practices that can and cannot be used in healthcare underwriting.



- On September 6, 2015, the Supervisor issued Temporary Provision 2015-33296, titled "Provisions of Consolidated Circular on Reporting to the Supervisor of Capital Markets". The provision is designed to serve as a collection of all provisions that require reporting by financial institutions to the Supervisor of Capital Markets, either if reporting duty is directly to the Supervisor or through the institution's website.
- On September 21, 2015, the Supervisor issued Circular 2015-9-30, titled "Performance of Transactions by a financial Institution for an Employer". The purpose of the circular is to set provisions to regulate the information that a financial institution is required to provide an employer as part of general regulation to streamline work procedures, improvement of information reliability, lifting technological barriers and promoting a competitive and efficient market for pension saving. In addition, the circular sets provisions for employer-granted authorization to an operating entity on its behalf to obtain information and perform operations in insurance programs on behalf of employees.
- On October 6, 2015, the Supervisor issued Circular 2015-1-22, titled "Principles for Change of Healthcare Insurance Rates to Existing Customers". The purpose of the circular is to present the principles underlying the review of applications that insurance companies will file to the Supervisor for changing rates paid by existing customers. That circular includes, among other things, provisions that will guide the change of rate paid by existing insurance customers, claim history and calculation of damages and additional actuarial consideration in determining insurance rates.
- On October 6, 2015, the Supervisor issued Circular 2015-1-21 titled "Implementation Provisions for Supervision of Financial Services Regulations (Insurance) (Terms of Insurance Contracts for Surgery and Surgery-Replacing Treatments in Israel), 2015." The purpose of the circular is to set provisions as to approach by insurers to people who were insured under surgery policies prior to the effective date of the regulations that allow to transition to a policy that comply with new regulations, and provisions on information that needs to be reported to the Supervisor of Insurance regarding those policies.
- On October 6, 2015, the Supervisor issued Circular 2015-1-20, titled "Independence between Individual Health Insurance Coverages". The purpose of the circular is to set provisions for marketing various individual healthcare insurance coverages, and the provisions for the purpose of cancelling such insurance coverages that were sold together.
- On October 6, 2015, the Supervisor issued Circular 2015-1-19, titled "Preparing Individual Health Insurance Plan". The purpose of the circular is to set provisions for developing individual health insurance, and it includes, among other things, provisions on the following issues: the term of insurance and renewal, notifications to insurance customer about renewal of policy, change in premiums and other insurance terms and notification on the option to transition to a new policy and uniformity of changes in insurance plans.
- On October 6, 2015, the Supervisor issued Circular 2015-1-18, titled "Provisions on Insurance Coverage in Medication Insurance Plans". The purpose of the circular is to set updated provisions about insurance coverage in medication insurance plans.
- On October 6, 2015, the Supervisor issued Circular 2015-1-17 titled "Preparation of Critical Illness Insurance Plans." The purpose of the circular is to set provisions for developing insurance plans that cover critical illness and update the definition of critical illness that are covered by such policies to correspond with up-to-date medical definitions.
- On October 7, 2015, the Supervisor issued Circular 2015-9-31 titled "Employee Compensation Policy in Financial Institutions – Amendment". The amendment stated, among other things, that the compensation to a director in a financial institution, including chairman must be fixed and not conditioned on performance, and that in order to improve the oversight ability of the chairman of the board and increase its independence, and also that remuneration of chairmen of the board will be based on the remuneration mechanism of external directors. In addition, the circular provides for claw back of variable compensation paid to key officers in a financial institution in exceptional cases. In addition, the circular set rules regarding key officers in a financial institution who have additional duties in the group, and it was determined that a financial institution will not bear the costs of employing the officer with regards to its service as officer of another company in the group, and that an officer in the group of a financial institution will be prohibited from receiving compensation from another entity, including from the controlling shareholder of the financial institution or a significant shareholder that has no control over the financial institution.



- On October 8, 2015, the Supervisor issued Circular 2015-1-23, titled "Amendment of Provisions of the Consolidated Circular – Chapter 1 in Part 2 Heading 5 – Measurement". The purpose of the circular is to postpone the commencement of the application of the provision to the 2015 annual financial statements and to correct a typo found in the measurement chapter.

Drafts

- On July 7, 2015 the Supervisor issued Draft Insurance Circular 2015-95 regarding "Life Insurance Plans at Fixed Premium – Draft". The draft stipulates that companies should not market life insurance policies with a term of more than 5 years at fixed premiums, including mortgage life insurance.
- On August 5, 2015 the Supervisor issued Draft Insurance Circular 2015-85 regarding "Controls on the Monthly Report– Update". The purpose of the draft is to update circular no. 2009-9-27 of December 27, 2009 which deals with the "Controls on Monthly Report" issued to the Supervisor.
- On August 9, 2015 the Supervisor issued Draft Insurance Circular 2015-126 titled "Report to the Supervisor on Rates in Life Insurance Plans – Second Draft". The purpose of the draft is to regulate the manner in which insurance companies will disclose the insurance rates in order to present them in an online calculator for life insurance rates which will allow customers to compare premiums charged by different insurers.
- On August 31, 2015, the Supervisor issued a draft titled "Decree on Compensation to Road Accident Victims (Financing of the Fund) (Amendment), 2015". The purpose of the amendment is to revise the frequency of reporting to the Road Accident Victims Compensation Fund in relation to vehicle compulsory insurance policies issued by an insurer under the Motor Vehicle Insurance Ordinance [New Version], 1970.
- On September 2, 2015, the Supervisor issued an explanatory memorandum for a legislative amendment of the Motor Vehicle Insurance Ordinance [New Version] (Amendment), 2015". The memorandum suggests to eliminate the requirement to have one original insurance certificate and permit insurers to issue insurance certificate electronically, since existing technologies on the market can provide current and accurate referencing and validation in relation to existence of insurance under the ordinance, in place of printing and holding a physical insurance certificate.
- On September 16, 2015, the Supervisor issued Draft 2015-34838, titled "Appendix to Circular on Processing and Settlement of Claims and Handling Communications from the Public – Draft". The draft includes provisions that apply generally to all insurance sectors and provisions that apply specifically to insurance sectors. The draft is designed to establish a detailed set of rules to guide settlement of claims.
- On September 21, 2015, the Supervisor issued Draft 2015-115, titled "Update of Disclosure Format in Annual Financial Statements of Insurance Companies – Draft". The purpose of the draft is to revise Circular 2010-1-4 "Guidelines on Disclosure Format Required in Financial Statements of Insurance Companies According to International Financial Reporting Standard (IFRS)" and its appendices.
- On October 11, 2015, the Supervisor issued Draft 2015-117, titled "Management of Information Security Risks in Financial Institutions". The purpose of the draft is to ensure securing the rights of insurance and long-term saving customers by maintaining confidentiality, completeness and availability of information assets, information technology systems and business processes of a financial institution. In addition, the draft defines and increases the responsibility of financial institutions' boards and managements in the ongoing management of information security and cyber risks, to guide and oversee the implementation of information security, and continuous involvement of information security personnel in all activities of the financial institutions. In addition, the draft introduce a duty of financial institutions to manage the overall cyber and information security risks, based on information protection principles.
- On October 26, 2015, the Supervisor issued Draft 2015-38513, titled "Provisions for Correction of Irregularities – Marketing of Personal Injury Policies – Draft". The draft is designed to set provisions for correction of irregularities in marketing of personal injury policies.

Entry into and marketing of new lines of business

The Company did not enter any new lines of business during the reported period.



3. Financial information on the Company's lines of activity

The following is balance sheet highlights (in thousand NIS):

| | September 30, 2015 | September 30, 2014 | December 31, 2014 |
|-------------------------------------|-------------------------------|-------------------------------|------------------------------|
| Other assets | 335,817 | 359,311 | 349,256 |
| Deferred acquisition expenses | 153,439 | 151,867 | 148,214 |
| Financial investments and cash | 1,696,885 | 1,589,579 | 1,576,565 |
| Reinsurance assets | 665,406 | 709,349 | 718,971 |
| Total assets | 2,851,547 | 2,810,106 | 2,793,006 |
| Shareholders' equity | 739,214 | 727,692 | 690,907 |
| Liabilities in respect of insurance | 1,718,615 | 1,704,136 | 1,715,261 |
| Other liabilities | 393,718 | 378,278 | 386,838 |
| Total equity and liabilities | 2,851,547 | 2,810,106 | 2,793,006 |

The following is comprehensive income highlights (in thousands of NIS)

| | Jan-Sep 2015 | Jan-Sep 2014 | Jul-Sept 2015 | Jul-Sep 2014 | 2014 |
|--|-------------------------|-------------------------|--------------------------|-------------------------|----------------|
| Gross earned premiums | 737,020 | 685,326 | 256,184 | 233,628 | 923,251 |
| Premiums earned by reinsurers | (118,917) | (111,792) | (39,007) | (34,873) | (149,576) |
| Premiums earned in retention | 618,103 | 573,534 | 217,177 | 198,755 | 773,675 |
| Net investment revenue and financing revenue | 14,319 | 61,094 | (3,759) | 23,331 | 49,127 |
| Fee revenue | 31,495 | 29,522 | 10,138 | 8,556 | 38,427 |
| Total revenue | 663,917 | 664,150 | 223,556 | 230,642 | 861,229 |
| Payments and change in liability for insurance contracts, in retention | (348,768) | (312,588) | (108,895) | (108,034) | (428,884) |
| Total other expenses | (237,284) | (224,306) | (80,393) | (72,703) | (301,548) |
| Income before income taxes | 77,865 | 127,256 | 34,268 | 49,905 | 130,797 |
| Taxes on income | (29,558) | (42,568) | (12,990) | (13,265) | (47,894) |
| Income for the period and total comprehensive income for the period | 48,307 | 84,688 | 21,278 | 36,640 | 82,903 |

Shareholders' equity and capital requirements

As of September 30, 2015, the Company's shareholders' equity exceeds the shareholders' equity required as of that date under the Insurance Business Regulations (Minimum Capital Required from an Insurer), 1998 by NIS 185.7 million.

For details regarding the amounts of equity required from the Company and the existing amounts in accordance with the minimum equity regulations, see note 5 to the financial statements.

For information about a NIS 35 million dividend distribution after balance sheet date, see section 8 below.



4. Results of operations

The Company continued during the reported period to increase gross premiums, by 5.4% y/y. Total gross premiums in the reported period amounted to NIS 768.7 million, up from NIS 727.8 million in the corresponding period in 2014.

Premiums by key insurance business segments (NIS in thousands):

| Jan-Sep 2015 | Life insurance | Health insurance | General insurance | Total |
|---------------------|-----------------------|-------------------------|--------------------------|--------------|
| Gross | 91,681 | 162,291 | 514,750 | 768,722 |
| In retention | 74,309 | 160,662 | 409,281 | 644,252 |
| % of total gross | 11.9 | 21.1 | 67.0 | 100.0 |
| % of retention | 11.6 | 24.9 | 63.5 | 100.0 |

| Jan-Sep 2014 | Life insurance | Health insurance | General insurance | Total |
|---------------------|-----------------------|-------------------------|--------------------------|--------------|
| Gross | 86,002 | 156,069 | 485,733 | 727,804 |
| In retention | 68,398 | 151,238 | 383,678 | 603,314 |
| % of total gross | 11.8 | 21.4 | 66.8 | 100.0 |
| % of retention | 11.3 | 25.1 | 63.6 | 100.0 |

| Jan-December 2014 | Life insurance | Health insurance | General insurance | Total |
|--------------------------|-----------------------|-------------------------|--------------------------|--------------|
| Gross | 115,884 | 207,778 | 629,362 | 953,024 |
| In retention | 92,553 | 202,172 | 496,667 | 791,392 |
| % of total gross | 12.2 | 21.8 | 66.0 | 100.0 |
| % of retention | 11.7 | 25.5 | 62.8 | 100.0 |

The following is principle information on comprehensive income by key lines of business (in thousand NIS):

| | Jan-Sep 2015 | Jan-Sep 2014 | Jul-Sep 2015 | Jul-Sep 2014 | 2014 |
|---|---------------------|---------------------|---------------------|---------------------|----------------|
| Income from compulsory vehicle activity | 25,509 | 20,674 | 16,160 | 10,800 | 17,750 |
| Income from property vehicle activity | 3,182 | 24,261 | 2,463 | 7,647 | 26,643 |
| Income from home insurance activity | 7,458 | 13,337 | 2,426 | 4,396 | 14,479 |
| Income (loss) from commercial insurance activity | (103) | 2,407 | (329) | 919 | 2,159 |
| Income from health insurance activity | 36,788 | 35,507 | 20,431 | 11,857 | 38,783 |
| Income from life insurance activity | 2,375 | 2,435 | 308 | 1,075 | 4,951 |
| Other - Income (loss) not attributed to any line of business | 2,656 | 28,635 | (7,191) | 13,211 | 26,032 |
| Income before taxes | 77,865 | 127,256 | 34,268 | 49,905 | 130,797 |
| Taxes on income | (29,558) | (42,568) | (12,990) | (13,265) | (47,894) |
| Income for the year and total comprehensive income for the year | 48,307 | 84,688 | 21,278 | 36,640 | 82,903 |

Additional information on key segments – see note 4 to the condensed financial statements.

The following is explanation on the development in some items:

- Net investment income and financing income was NIS 14.3 million, compared with NIS 61.1 million in the corresponding period of 2014. The decrease in investment income resulted from lower investment returns especially in June and September 2015.



- b. The income of the Company from compulsory vehicle insurance in the reported period was NIS 25.5 million compared with NIS 20.7 million in the corresponding period in 2014. The increase in income mainly resulted from improvement in claim and expense ratio.
- c. The income of the Company from property vehicle insurance in the reported period was NIS 3.2 million, compared with NIS 24.3 million in the corresponding period of 2014. The decrease is mainly attributed to an increase in claims ratio.
- d. The income of the Company from home insurance in the reported period was NIS 7.5 million compared with NIS 13.3 million in the corresponding period in 2014. The decreased profitability is mainly a result of an increase in claim ratio.
- e. The loss of the Company from professional liability insurance in the reported period was NIS 1.3 million compared with an income of NIS 2.7 million in the corresponding period in 2014. The decrease in income is mainly a result of a lower investment income.
- f. The loss of the Company from other property liability insurance in the reported period was NIS 49 thousand compared with an income of NIS 0.7 million in the corresponding period in 2014. The decrease in income is mainly a result of a lower investment income.
- g. The income of the Company from other liability insurance in the reported period was NIS 1.3 million compared with a loss of NIS 0.9 million in the corresponding period in 2014. The increased income is a result of lower claims ratio.
- h. The income of the Company from health insurance in the reported period was NIS 36.8 million compared with NIS 35.5 million in the corresponding period in 2014. The increase in income mainly resulted from an improvement of claims ratio.
- i. The income of the Company from life insurance in the reported period was NIS 2.4 million compared with NIS 2.4 million in the corresponding period in 2014.

5. Cash flows and liquidity

Net cash provided by operating activities in the reported period was NIS 20.9 million, compared with NIS 46.4 million provided by operating activities in the corresponding period in 2014.

Net cash used in investing activities in the reported period amounted to NIS 9.8 million, compared with amount of NIS 8.5 million in the corresponding period in 2014.

As a result of the above, the balance of cash and cash equivalents in the reported period increased by NIS 11.5 million and amounted NIS 94.6 million as of September 30, 2015.

6. Sources of funding

All of the Company's operations are funded using its own resources and capital. As of the date of approving this report, the Company does not use any external funding sources.

7. The effect of external factors

For more information, see section 2 above.



8. Material subsequent events

On October 27, 2015, the Company's Board of Directors approved a NIS 35 million dividend distribution to the sole shareholder of the Company – AIG Europe Holdings Limited. The capital surplus of the Company considering the dividend distribution compared to the required capital is NIS 150.7 million, and is about 27% over the required capital.

9. CEO and CFO Disclosure regarding the effectiveness of controls and procedures applied to company's disclosures

Controls and procedures applied to disclosure

The Company's management, with the collaboration of the Company's CEO and CFO, assessed as of the end of the period covered by this report the effectiveness of the controls and procedures with respect to the Company's disclosure. Based on this assessment, the Company's CEO and CFO concluded that as of the end of this period the controls and procedures with respect to the Company's disclosure are effective in order to record, process, summarize and report the information that the Company is required to disclose in the quarterly report pursuant to the provisions of the law and the reporting provisions issued by the Commissioner of Capital Markets, Insurance and Savings, and on the date set in these provisions.

Internal controls over financial reporting

In the course of the quarter ending on September 30, 2015 no change occurred in the internal control of the Company over financial reporting, which materially affected or is reasonably expected to materially affect the Company's internal control on financial reporting.

For purposes of this paragraph, "the covered period" is the reported financial quarter.

Management's statements as to the adequacy of the financial data presented in the Company's financial statements and the existence and effectiveness of internal controls relating to the financial statements are attached hereunder.

The Board of Directors wishes to thank the Company's employees and management for their contribution to its business achievements.

Ralph Mucerino
Chairman of the Board of Directors

Shay Feldman
CEO

November 17, 2015

Declaration

I, Shay Feldman hereby declare that:

1. I reviewed the interim report of AIG Israel Insurance Company Ltd. (hereafter – "the insurance company") for the quarter ended September 30, 2015 (hereafter – "the report").
2. Based on my knowledge, the report does not include any misstatement of a material fact or omit to disclose a material fact the presentation of which in the report is necessary for the purpose of ensuring that under the circumstances in which those presentations are included, they will not be misleading regarding the period covered by the report.
3. Based on my knowledge, the quarterly financial statements and other financial information included in the report reflect fairly, in all material respects, the financial position, results of operations, changes in shareholders' equity and cash flows of the insurance company for the date and periods covered by the report.
4. The Company's other certifying officers and I are responsible for establishing and maintaining controls and procedures relating to disclosure¹ and internal controls over financial reporting of the insurance company; and -
 - (a) Accordingly, we have designed such disclosure controls and procedures, or have had such disclosure controls and procedures established under our charge, designed to ensure that material information relating to the insurance company is made known to us by others in the insurance company particularly during the period in which the reports were prepared;
 - (b) We designed internal controls over financial reporting, or supervised the design of such internal controls designed to provide a reasonable assurance regarding the reliability of the financial reporting and assurance to the effect that the financial statements are drawn up in accordance with International Financial Reporting Standards (IFRS) and in accordance with the directives of the Supervisor of Insurance.
 - (c) We assessed the effectiveness of controls and procedures regarding the disclosure of the insurance company and presented our conclusions regarding the effectiveness of disclosure controls and procedures as of the end of the period covered in the report, based on our estimate; and
 - (d) We disclosed in the report any change in the insurance company's internal controls over financial reporting which took place in this quarter and had a material effect or is expected to have a material effect on the insurance company's internal controls over financial reporting; and

¹ As defined in the provisions of the Institutional Bodies Circular regarding internal controls over financial reporting – declarations, reports and disclosures.

5. The insurance company's other certifying officers and I have disclosed to the insurance company's auditors, the insurance company's board of directors and its audit committee, based on our most recent evaluation of internal controls over financial reporting, the following:
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the insurance company's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether material or not, that involves management or other employees who have a significant role in the insurance company's internal controls over financial reporting.

There is nothing in the aforesaid to derogate from my responsibility or the responsibility of any other person, pursuant to any law.

Shay Feldman - CEO

November 17, 2015

Declaration

I, David Rothstein hereby declare that:

1. I reviewed the interim report of AIG Israel Insurance Company Ltd. (hereafter – "the insurance company") for the quarter ended September 30, 2015 (hereafter – "the report").
2. Based on my knowledge, the report does not include any misstatement of a material fact or omit to disclose a material fact the presentation of which in the report is necessary for the purpose of ensuring that under the circumstances in which those presentations are included, they will not be misleading regarding the period covered by the report.
3. Based on my knowledge, the quarterly financial statements and other financial information included in the report reflect fairly, in all material respects, the financial position, results of operations, changes in shareholders' equity and cash flows of the insurance company for the date and periods covered by the report.
4. The Company's other certifying officers and I are responsible for establishing and maintaining controls and procedures relating to disclosure¹ and internal controls over financial reporting of the insurance company; and -
 - (a) Accordingly, we have designed such disclosure controls and procedures, or have had such disclosure controls and procedures established under our charge, designed to ensure that material information relating to the insurance company is made known to us by others in the insurance company particularly during the period in which the reports were prepared;
 - (b) We designed internal controls over financial reporting, or supervised the design of such internal controls designed to provide a reasonable assurance regarding the reliability of the financial reporting and assurance to the effect that the financial statements are drawn up in accordance with International Financial Reporting Standards (IFRS) and in accordance with the directives of the Supervisor of Insurance.
 - (c) We assessed the effectiveness of controls and procedures regarding the disclosure of the insurance company and presented our conclusions regarding the effectiveness of disclosure controls and procedures as of the end of the period covered in the report, based on our estimate; and
 - (d) We disclosed in the report any change in the insurance company's internal controls over financial reporting which took place in this quarter and had a material effect or is expected to have a material effect on the insurance company's internal controls over financial reporting; and

¹ As defined in the provisions of the Institutional Bodies Circular regarding internal controls over financial reporting – declarations, reports and disclosures.

5. The insurance company's other certifying officers and I have disclosed to the insurance company's auditors, the insurance company's board of directors and its audit committee, based on our most recent evaluation of internal controls over financial reporting, the following:
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the insurance company's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether material or not, that involves management or other employees who have a significant role in the insurance company's internal controls over financial reporting.

There is nothing in the aforesaid to derogate from my responsibility or the responsibility of any other person, pursuant to any law.

David Rothstein - CFO

November 17, 2015

Directors and Management's Report Regarding Internal Controls over Financial Reporting

Management, with the supervision of the Board of Directors of AIG Insurance Company Ltd. (hereafter the "the Insurance Company") are responsible for setting and maintaining effective internal control over financial reporting. The internal controls system of the insurance company was planned in order to provide reasonable assurance to management and Board of Directors to the effect that the financial statements are prepared and presented fairly in accordance with International Financial Reporting Standards and in accordance with the directives of the Supervisor of Insurance.

All internal controls have inherent limitations regardless of the quality of planning. Therefore, even if it is determined that these controls are effective they can only provide a reasonable measure of assurance regarding the preparation and presentation of financial statements.

Management, supervised by the Board of Directors, maintains a comprehensive control system designed to ensure that transactions are carried out in accordance with management's authorization, assets are protected, and accounting records are reliable. In addition, management with the Board of Directors' supervision takes measures in order to ensure that the information and communications channels are effective and monitor implementation, including implementation of the internal control procedures.

The Insurance Company's management with the supervision of its Board of Directors evaluates the effectiveness of the internal control of the Insurance Company over financial reporting as at September 30, 2015, based on criteria set in the internal control model of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation management believes that as at September 30, 2015 the internal control of the Insurance Company over financial reporting is effective.

Mr. Ralph Mucerino
Chairman of the Board

Mr. Shay Feldman
CEO

Mr. David Rothstein
CFO

Date of approval of financial statements: November 17, 2015

AIG ISRAEL INSURANCE COMPANY LTD.
FINANCIAL INFORMATION FOR INTERIM PERIOD
(Unaudited)
SEPTEMBER 30, 2015

AIG ISRAEL INSURANCE COMPANY LTD.
FINANCIAL INFORMATION FOR INTERIM PERIOD
(Unaudited)

SEPTEMBER 30, 2015

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Auditors' review report to shareholders of AIG Israel Insurance Company Ltd.

Introduction

We have reviewed the attached financial information of AIG Israel Insurance Company Ltd ("the Company"), which is comprised of the condensed statement of financial position as of September 30, 2015 and the condensed statements of comprehensive income, changes in equity and cash flows for the nine and three-months periods ended on that date. The Board of Directors and management are responsible for the preparation and presentation of the financial information for this interim period in accordance with the provisions of International Accounting Standard No. 34, 'Interim Financial Reporting' (hereafter "IAS 34"), and they are also responsible for the preparation of the financial information for this interim period in accordance with the disclosure requirements of the Supervision of Financial Services (Insurance) Law, 1981 and the regulations promulgated thereunder. Our responsibility is to express a conclusion with respect to the financial information for this interim period, based on our review.

Scope of review

Our review was conducted in accordance with the provisions of Review Standard No. 1 of the Institute of Certified Public Accountants in Israel, 'Review of financial information for interim period undertaken by the entity's auditor.' A review of financial information for an interim period consists of the making of enquiries, in particular, of those officials responsible for financial and accounting matters, and of the application of analytical and other review procedures. A review is substantially lesser in scope than an audit conducted in accordance with auditing standards generally accepted in Israel and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, no matter has come to our attention that causes us to believe that the above financial information is not prepared, in all material respects, in accordance with IAS 34.

In addition, based on our review, no matter has come to our attention that causes us to believe that the above financial information does not comply, in all material respects, with the disclosure provisions of the Supervision of Financial Services (Insurance) Law, 1981 and the regulations promulgated thereunder.

Tel-Aviv, Israel
November 17, 2015

Kesselman & Kesselman
Certified Public Accountants (Isr.)
A member firm of PricewaterhouseCoopers International Limited

AIG ISRAEL INSURANCE COMPANY LTD.
CONDENSED STATEMENTS OF FINANCIAL POSITION
AS OF SEPTEMBER 30, 2015

| | September 30 | December 31, | |
|------------------------------------|-------------------------|---------------------|------------------|
| | 2015 | 2014 | 2014 |
| | (Unaudited) | (Audited) | |
| | NIS in thousands | | |
| Assets | | | |
| Intangible assets | 22,742 | 16,944 | 20,410 |
| Deferred acquisition costs | 153,439 | 151,867 | 148,214 |
| Fixed assets | 9,747 | 12,486 | 10,663 |
| Reinsurance assets | 665,406 | 709,349 | 718,971 |
| Premiums collectible | 202,508 | 203,548 | 193,337 |
| Current tax assets | 61,484 | 82,337 | 84,697 |
| Other receivables | 39,336 | 43,996 | 40,149 |
| | <u>1,154,662</u> | <u>1,220,527</u> | <u>1,216,441</u> |
| Financial investments: | | | |
| Marketable debt instruments | 1,233,925 | 1,200,994 | 1,183,798 |
| Non-marketable debt instruments | 204,112 | 159,313 | 164,461 |
| Marketable shares | 92,146 | 87,816 | 87,300 |
| Other | 72,129 | 36,501 | 57,919 |
| TOTAL FINANCIAL INVESTMENTS | <u>1,602,312</u> | <u>1,484,624</u> | <u>1,493,478</u> |
| Cash and cash equivalents | 94,573 | 104,955 | 83,087 |
| TOTAL ASSETS | <u>2,851,547</u> | <u>2,810,106</u> | <u>2,793,006</u> |

Ralph Mucerino
Chairman of the
Board
of Directors

Shay Feldman
C.E.O

David Rothstein
C.F.O

Date of approval of financial information for interim period by the Board of Directors of the Company –
November 17, 2015

AIG ISRAEL INSURANCE COMPANY LTD.
CONDENSED STATEMENTS OF FINANCIAL POSITION
AS OF SEPTEMBER 30, 2015

| | September 30 | | December 31, |
|---|-------------------------|------------------|---------------------|
| | 2015 | 2014 | 2014 |
| | (Unaudited) | | (Audited) |
| | NIS in thousands | | |
| EQUITY AND LIABILITIES | | | |
| EQUITY: | | | |
| Share capital | 6 | 6 | 6 |
| Share premium | 250,601 | 250,601 | 250,601 |
| Capital reserves | 11,084 | 11,084 | 11,084 |
| Retained earning | 477,523 | 466,001 | 429,216 |
| TOTAL EQUITY ATTRIBUTABLE TO COMPANY SHAREHOLDERS | 739,214 | 727,692 | 690,907 |
| LIABILITIES: | | | |
| Liabilities in respect of insurance contracts and investment contracts that are not yield dependent | 1,718,615 | 1,704,136 | 1,715,261 |
| Liabilities in respect of deferred taxes, net | 1,929 | 24,009 | 10,267 |
| Liabilities with respect to employee rights upon retirement, net | 3,001 | 1,457 | 3,069 |
| Liabilities towards reinsurers | 317,201 | 274,034 | 280,598 |
| Payables | 71,587 | 78,778 | 92,904 |
| TOTAL LIABILITIES | 2,112,333 | 2,082,414 | 2,102,099 |
| TOTAL EQUITY AND LIABILITIES | 2,851,547 | 2,810,106 | 2,793,006 |

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

AIG ISRAEL INSURANCE COMPANY LTD.

CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE NINE AND THREE MONTHS PERIODS ENDED SEPTEMBER 30, 2015

| | Nine months ended September 30 | | Three months ended September 30 | | Year ended December 31, |
|--|-----------------------------------|------------------|------------------------------------|------------------|----------------------------|
| | 2015 | 2014 | 2015 | 2014 | 2014 |
| | (Unaudited) | | (Unaudited) | | (Audited) |
| | NIS in thousands | | | | |
| Gross earned premiums | 737,020 | 685,326 | 256,184 | 233,628 | 923,251 |
| Premiums earned by reinsurers | (118,917) | (111,792) | (39,007) | (34,873) | (149,576) |
| Premiums earned on retention | 618,103 | 573,534 | 217,177 | 198,755 | 773,675 |
| Investment income, net and financing income | 14,319 | 61,094 | (3,759) | 23,331 | 49,127 |
| Commission income | 31,495 | 29,522 | 10,138 | 8,556 | 38,427 |
| TOTAL INCOME | 663,917 | 664,150 | 223,556 | 230,642 | 861,229 |
| Payments and change in liabilities with respect to insurance contracts, gross | (476,622) | (434,725) | (94,707) | (147,258) | (577,858) |
| Share of reinsurers in payments and in change in Liabilities with respect to insurance contracts | 127,854 | 122,137 | (14,188) | 39,224 | 148,974 |
| Payments and change in liabilities with respect to insurance contracts, on retention | (348,768) | (312,588) | (108,895) | (108,034) | (428,884) |
| Commission, marketing expenses and other acquisition costs | (130,069) | (122,911) | (44,927) | (38,690) | (166,902) |
| General and administrative expenses | (106,529) | (103,302) | (36,443) | (36,167) | (140,159) |
| Financing income (expenses) | (686) | 1,907 | 977 | 2,154 | 5,513 |
| TOTAL EXPENSES | (586,052) | (536,894) | (189,288) | (180,737) | (730,432) |
| INCOME BEFORE TAXES ON INCOME | 77,865 | 127,256 | 34,268 | 49,905 | 130,797 |
| Taxes on income | (29,558) | (42,568) | (12,990) | (13,265) | (47,894) |
| INCOME FOR THE PERIOD AND TOTAL COMPREHENSIVE INCOME FOR THE PERIOD | 48,307 | 84,688 | 21,278 | 36,640 | 82,903 |
| BASIC EARNINGS PER SHARE: | | | | | |
| Basic income per share (NIS in thousands) | 8.43 | 15.04 | 3.71 | 6.51 | 14.73 |

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

AIG ISRAEL INSURANCE COMPANY LTD.
CONDENSED STATEMENTS OF CHANGES IN EQUITY
FOR THE NINE AND THREE MONTHS PERIODS ENDED SEPTEMBER 30, 2015

| | <u>Share capital</u> | <u>Share premium</u> | <u>Capital reserves</u> | <u>Retained earnings</u> | <u>Total</u> |
|---|--------------------------|--------------------------|-----------------------------|------------------------------|----------------|
| | NIS in thousands | | | | |
| BALANCE AS OF JANUARY 1, 2015 (audited) | 6 | 250,601 | 11,084 | 429,216 | 690,907 |
| CHANGES DURING THE NINE MONTHS ENDED SEPTEMBER 30, 2015 (unaudited) - total income and comprehensive income for the nine months ended September 30, 2015 | | | | 48,307 | 48,307 |
| BALANCE AS OF SEPTEMBER 30, 2015 (unaudited) | <u>6</u> | <u>250,601</u> | <u>11,084</u> | <u>477,523</u> | <u>739,214</u> |
| BALANCE AS OF JANUARY 1, 2014 (audited) | 6 | 250,601 | 11,084 | 381,313 | 643,004 |
| CHANGES DURING THE NINE MONTHS ENDED SEPTEMBER 30, 2014 (unaudited) - total income and comprehensive income for nine months ended September 30, 2014 | | | | 84,688 | 84,688 |
| BALANCE AS OF SEPTEMBER 30, 2014 (unaudited) | <u>6</u> | <u>250,601</u> | <u>11,084</u> | <u>466,001</u> | <u>727,692</u> |
| BALANCE AS OF JULY 1, 2015 (unaudited) | 6 | 250,601 | 11,084 | 456,245 | 717,936 |
| CHANGES DURING THE THREE MONTHS ENDED SEPTEMBER 30, 2015 (unaudited) - Total comprehensive income for the three months ended September 30, 2015 | | | | 21,278 | 21,278 |
| BALANCE AS OF SEPTEMBER 30, 2015 (unaudited) | <u>6</u> | <u>250,601</u> | <u>11,084</u> | <u>477,523</u> | <u>739,214</u> |
| BALANCE AS OF JULY 1, 2014 (unaudited) | 6 | 250,601 | 11,084 | 429,361 | 691,052 |
| CHANGES DURING THE THREE MONTHS ENDED SEPTEMBER 30, 2014 (unaudited) - total income and comprehensive income for the three months ended September 30, 2014 | | | | 36,640 | 36,640 |
| BALANCE AS OF SEPTEMBER 30, 2014 (unaudited) | <u>6</u> | <u>250,601</u> | <u>11,084</u> | <u>466,001</u> | <u>727,692</u> |
| BALANCE AS OF JANUARY 1, 2014 (audited) | 6 | 250,601 | 11,084 | 381,313 | 643,004 |
| CHANGES DURING THE YEAR 2014 (audited) Total income and comprehensive income for year ended December 31, 2014 | | | | 82,903 | 82,903 |
| Transactions with shareholders carried directly to equity - dividend | | | | (35,000) | (35,000) |
| BALANCE AS OF DECEMBER 31, 2014 (audited) | <u>6</u> | <u>250,601</u> | <u>11,084</u> | <u>429,216</u> | <u>690,90</u> |

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

AIG ISRAEL INSURANCE COMPANY LTD.

CONDENSED STATEMENTS OF CASH FLOWS

FOR THE NINE AND THREE MONTHS PERIODS ENDED SEPTEMBER 30, 2015

| | Nine months ended September 30 | | Three months ended September 30 | | Year ended December 31, |
|---|-----------------------------------|----------------|------------------------------------|----------------|----------------------------|
| | 2015 | 2014 | 2015 | 2014 | 2014 |
| | (Unaudited) | | (Unaudited) | | (Audited) |
| | NIS in thousands | | | | |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | | | |
| Net cash provided by (used in) operations (Appendix A) | (2,373) | 64,667 | 23,273 | 56,363 | 96,078 |
| Interest received | 36,210 | 37,057 | 10,202 | 10,269 | 45,484 |
| Dividend received | 1,769 | 1,599 | 536 | 496 | 2,337 |
| Income taxes paid, net | (14,683) | (56,906) | (24,676) | (28,475) | (78,334) |
| Net cash provided by operating activities | <u>20,923</u> | <u>46,417</u> | <u>9,335</u> | <u>38,653</u> | <u>65,565</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | | | |
| Changes in assets covering equity and non-insurance liabilities: | | | | | |
| Acquisition of fixed assets | (1,463) | (1,405) | (1,573) | (842) | (1,769) |
| Acquisition of intangible assets | (8,290) | (7,048) | (2,925) | (4,747) | (12,218) |
| Net cash used in investing activities | <u>(9,753)</u> | <u>(8,453)</u> | <u>(4,498)</u> | <u>(5,589)</u> | <u>(13,987)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES - | | | | | |
| dividend paid to Company's shareholders | - | - | - | - | (35,000) |
| Net cash used in financing activities | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>(35,000)</u> |
| INCREASE IN CASH AND CASH EQUIVALENTS | 11,170 | 37,964 | 4,837 | 33,064 | 16,578 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD | 83,087 | 67,616 | 89,740 | 72,567 | 67,616 |
| INFLUENCE OF FLUCTUATION IN EXCHANGE RATE ON CASH AND CASH EQUIVALENTS | 316 | (625) | (4) | (676) | (1,107) |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | <u>94,573</u> | <u>104,955</u> | <u>94,573</u> | <u>104,955</u> | <u>83,087</u> |

AIG ISRAEL INSURANCE COMPANY LTD.

CONDENSED STATEMENTS OF CASH FLOWS

FOR THE NINE AND THREE MONTHS PERIODS ENDED SEPTEMBER 30, 2015

| | Nine months ended | | Three months ended | | Year ended |
|--|--------------------------|-----------------|---------------------------|---------------|---------------------|
| | September 30 | | September 30 | | December 31, |
| | 2015 | 2014 | 2015 | 2014 | 2014 |
| | (Unaudited) | | (Unaudited) | | (Audited) |
| | NIS in thousands | | | | |
| APPENDIX A - CASH FLOWS FROM OPERATIONS - | | | | | |
| Income before taxes on income | 77,865 | 127,256 | 34,268 | 49,905 | 130,797 |
| Adjustments for- Income and expenses not involving cash flows: | | | | | |
| Increase in liabilities with respect to insurance contracts that are not yield dependent | 56,919 | 72,730 | 7,883 | 26,546 | 74,234 |
| Decrease (increase) in deferred acquisition costs | (5,225) | (11,347) | (1,618) | (5,162) | (7,694) |
| Increase (decrease) in liabilities with respect to employee rights upon retirement, net | (68) | (988) | (146) | (300) | 624 |
| Depreciation of fixed assets | 2,853 | 4,167 | 1,192 | 1,350 | 6,354 |
| Depreciation of intangible asset | 5,485 | 4,903 | 1,946 | 1,626 | 6,607 |
| Losses (gains), net on financial investments: | | | | | |
| Marketable debt instruments | 21,306 | (14,472) | 6,196 | (6,700) | 4,057 |
| Non-marketable debt instruments | 4,984 | (2,729) | (2,281) | (2,633) | (3,525) |
| Marketable shares | 231 | (5,353) | 8,619 | (3,100) | (3,313) |
| Marketable index linked certificates | 966 | (1,423) | 1,409 | (483) | (675) |
| Influence of fluctuation in exchange rate on cash and cash equivalents | (316) | 625 | 4 | 676 | 1,107 |
| | <u>165,000</u> | <u>173,369</u> | <u>57,472</u> | <u>61,725</u> | <u>208,573</u> |
| Changes in operating assets and liabilities: | | | | | |
| Liabilities towards reinsurers | 36,603 | 17,849 | 44,970 | 6,260 | 24,413 |
| Investments in financial assets, net | (136,320) | (55,781) | (65,257) | 5,899 | (85,158) |
| Premiums collectible | (9,171) | (17,134) | (1,226) | (11,788) | (6,923) |
| Receivables | 812 | (4,953) | 801 | (2,355) | (1,106) |
| Payables | (21,318) | (10,027) | (2,749) | 7,387 | 4,100 |
| | <u>(129,394)</u> | <u>(70,046)</u> | <u>(23,461)</u> | <u>5,403</u> | <u>(64,674)</u> |
| Adjustments with respect to interest and dividend: | | | | | |
| Interest received | (36,210) | (37,057) | (10,202) | (10,269) | (45,484) |
| Dividend received | (1,769) | (1,599) | (536) | (496) | (2,337) |
| Net cash provided by (used in) operations | <u>(2,373)</u> | <u>64,667</u> | <u>23,273</u> | <u>56,363</u> | <u>96,078</u> |

Cash flows from operating activities include those stemming from financial investment purchases and sales (net) which relate to operations involving insurance contracts.

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

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS

NOTE 1 - GENERAL:

AIG Israel Insurance Company Ltd. ("the Company") was incorporated in Israel on March 27, 1996 as a private company in which the shareholders have limited responsibility. The Company commenced its insurance operations in May 1997. The Company does not hold any subsidiaries or related companies. The Company has no foreign operations through branches or investees.

The ultimate parent company is American International Group Inc. (hereafter – "AIG Global Corporation" or "AIG"), which is a leading international insurance and financial concern.

The Company's shareholder is AIG Europe Holdings Limited which holds all the issued share capital of the Company. AIG Europe Holdings Limited is a member of the AIG Global Corporation.

The registered address of the Company's office is 25 Hasivim St. Petah-Tikva.

DEFINITIONS:

- 1) The Company – AIG Israel Insurance Company Ltd.
- 2) The parent company – AIG Europe Holdings Limited
- 3) Supervisor - Supervisor of Insurance (Commissioner of the Capital Market, Insurance and Savings at the Israel Ministry of Finance).
- 4) The Supervision Law – The Supervision of Financial Services (Insurance) Law, 1981.
- 5) Investment contracts – policies which do not constitute insurance contracts.
- 6) Reinsurance assets – the reinsurer's share in the reserves for insurance contracts and in the contingent claims.
- 7) CPI - The Consumer Price Index published by the Israeli Central Bureau of Statistics.
- 8) Known CPI - The CPI known at the end of the month.
- 9) Related parties - as defined in IAS 24 "Related Party Disclosures".
- 10) Interested party - as defined in the Israeli Securities (Financial Statements) Regulations, 2010.
- 11) Life insurance fund - Actuarial fund calculated in accordance with the principles generally accepted for this purpose in Israel.
- 12) Unexpired risks fund - Funds calculated in accordance with the Regulations for Calculation of General Insurance Funds.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 1 - GENERAL (continued):

- 13) Outstanding claims - Known outstanding claims, with the addition of the expected progression of claims that have been incurred but not enough reported (I.B.N.E.R.) plus claims that have been Incurred but not reported (I.B.N.R).
- 14) Details of account regulations - Supervision of Insurance Businesses (Details of account) Regulations, 1998.
- 15) The Investment Regulations – The Supervision of Financial Services (Provident Funds) (Investment Rules Applicable to Financial Institutions) Regulations, 2012.
- 16) Shareholders' Equity Regulations - The Supervision of Insurance Business Regulations (minimum shareholders' equity required from an insurer), 1998 and amendments as amended.
- 17) Account Segregation Regulations in Life Insurance - The Supervision of Insurance Regulations (Method of Segregation of Accounts and Assets of Insurer in Life Insurance), 1984.
- 18) Regulations for Calculation of General Insurance Funds - The Supervision of Insurance Businesses Regulations (Method of Calculation of Provisions for Future Claims in General Insurance) 1984, and amendments as amended.
- 19) Exposure to reinsurers - debit balances with the company's reinsurers, including the reinsurer's share in the company's outstanding claims and unexpired risks fund, all being net of the reinsurer's deposits with the company and the amount of documentary credits granted against the debt of the reinsurer.
- 20) Insurance contract - A contract under which one party (the insurer) takes a significant insurance risk from another party (policy holder), by agreement to indemnify the policy holder if an uncertain a defined future event (insurance event) negatively affects the policy holder.
- 21) Liability for insurance contracts - Insurance reserves and outstanding claims.
- 22) Premiums - Premiums including fees and proceeds for related services
- 23) Premiums earned premiums that relate to the reporting period.

NOTE 2 - BASIS OF PREPARATION OF FINANCIAL STATEMENTS:

- a. The Company's condensed financial information as of September 30, 2015 and for the nine and three-month interim periods ended on that date ("the financial information for the interim period") has been prepared in accordance with the provisions of IAS 34 'Interim Financial Reporting' (hereafter – "IAS 34") and is in compliance with the disclosure requirements of the Supervision of Financial Services (Insurance) Law, 1981 ("the supervision law") and the regulations promulgated there under. The financial information for the interim period should be read in conjunction with the annual financial statements as of December 31, 2014 and for the year ended thereon including the accompanying notes which are in compliance with International Financial Reporting Standards, which are standards and interpretations published by the International Accounting Standards Board (hereafter – "IFRS").

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 2 - BASIS OF PREPARATION OF FINANCIAL STATEMENTS (continued):

The financial information for the interim period has been subject to review only and has not been audited.

b. Estimates

The preparation of interim financial statements requires management to exercise its judgment and also requires use of accounting estimates and assumptions that affect the application of the Company's accounting policy and the reported amounts of assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Significant judgments exercised by management in preparation of these condensed interim financial statements as well as the uncertainty involved in the key sources of those estimates were identical to the ones used in the Company's annual financial statements for the year ended December 31, 2014.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES:

The significant accounting policies and the computational methods applied in the preparation of the financial information for the interim period are consistent with the policies and methods applied in the preparation of the annual financial statements of the Company, except for the following matters:

a. Taxes on income for the reported interim period are accounted for on the basis on management's best estimate of the average tax rate applicable to the projected annual profits.

b. New accounting standards:

- 1) New IFRS and amendments to existing standards that came into effect and are mandatory for reporting periods commencing on January 1, 2015:

As specified in the Company's 2014 annual financial statements, certain amendments to IFRS came into effect for accounting periods commencing on January 1, 2015. However, the first time application of these amendments did not have a material effect on the Company's financial information for interim periods (including comparative figures).

- 2) New IFRS and amendments to existing standards, which have not yet become effective and have not been early adopted by the Company.

In its annual 2014 financial statements, the Company specified new IFRS and additional amendments to existing IFRS, which have not yet become effective and have not been early adopted by the Company. Since the date of issuance of the Company's annual financial statements through the date of approval of these interim financial statements, no new standards or amendments to existing standards were issued that are relevant to the Company's operations.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES (continued):

c. Changes in the calculation of insurance reserves in general insurance

In February 2013, The Supervision of financial Services Regulations (Insurance) (Calculation of Insurance Reserves in General Insurance), 2013 ("the New Regulations") were issued and a circular that was updated in January 2015 (jointly "the Amendment"), regarding an update of the legal provisions for calculation of insurance reserves in general insurance.

The Amendment supersedes the Control of Insurance Business Regulations (Methods of Calculating Provisions for Future Claims in General Insurance), 1984, which will be replaced by the New Regulations. The main change that will apply when the Amendment comes into force is cancellation, as from the financial statements as of December 31, 2015, of the surplus income over expenses reserve ("the Reserve"). The Reserve is currently calculated for three years, in long-tail general insurance sectors (mainly compulsory motor and liability), for which an actuarial valuation has been prepared.

In addition, as a complementary measure for the change, a position of the Supervisor was published in January 2015 regarding the best practice for actuaries when calculating general insurance reserves for the financial statements to properly and adequately reflect the insurance liabilities. The Supervisor's position includes, inter alia, the following:

- 1) "Caution" means that the reserve calculated by an actuary is an "adequate reserve to cover the insurer's obligation". This means that it is fairly likely that the reserve calculated on retention will suffice to cover the insurer's obligations. As to outstanding claims in the compulsory motor and liability sectors, the "fairly likely" test means a probability of 75% at the very least. Nevertheless, where statistical analysis is not possible, the actuary will exercise his/her judgment and may use acceptable actuarial methods.
- 2) Reference to the discounting rate of the obligations.
- 3) Grouping of sectors: to apply the Caution principle, in un-grouped sectors (as defined in the circular – statistical sectors), each sector should be considered separately; however, it is possible to group all underwriting (or damage) years in the sector. Non-statistical sectors can all be considered as a single set.
- 4) Determination of the level of reserve for policies sold shortly before the reporting date and for risks subsequent to the reporting dates.

The Company is reviewing the overall effect of the Amendment on the financial statements, together with the position of the Supervisor. At this stage, the effect cannot be assessed, since the first time application of the Supervisor's Position is to take place in December 2015 and it requires making lengthy preparations.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION

The Company's chief operational decision-maker reviews the Company's internal reports for the purposes of evaluating performance and deciding upon the allocation of resources. Management has established operating segments on the basis of these reports. Segment performance is assessed by measuring pre-tax profit and the profit before investment income and tax and by considering particular ratios, such as the claims ratio and the expenses ratio.

The Company operates in the general insurance segment, the health insurance segment and the life assurance segment, as follows:

1) Life assurance segment

The life assurance segment provides cover for life assurance risk only as well as coverage of other risks such as disability, occupational disability and other health related services

2) Health insurance segment

All the Company's health insurance operations are concentrated within this segment. The segment provides personal accident cover, severe illness cover and foreign travel cover.

3) General insurance segment

The general insurance segment encompasses the property and liability sectors. In accordance with the directives of the Supervisor of Insurance, the segment is divided into the following sectors: the compulsory motor vehicle sector, the motor vehicle property sector, the apartment's insurance sector, other property sectors, the professional liability sector and other liability sectors

- **Compulsory motor vehicle sector**

The compulsory motor vehicle sector focuses on the provision of cover, the purchase of which, by the owner or driver of a vehicle, is compulsory by law. This insurance provides cover for bodily injury occasioned to the driver of the vehicle, any passengers therein or pedestrians as a result of the use of an engine vehicle.

- **Motor vehicle property sector**

The motor vehicle property sector focuses on the provision of cover for property damage occasioned to the motor vehicle of the insured and for property damage that the motor vehicle of the insured causes to a third party.

- **Apartments insurance sector**

The apartment's insurance sector focuses in providing coverage for damages caused to apartments and includes coverage in respect of damages caused by earth quake.

- **Professional liability sector**

The professional liability sector provides cover to practitioners of the various liberal professions for any claims that may be made against them in relation to injury occasioned to a third party as a result of a mistake or professional negligence. Insurance coverage to directors and office holders in respect of an unlawful act or oversight carried out by the directors and office holders in their professional capacity.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

- **Other Property sectors**

Other property sectors provide cover with respect to those property lines which are not connected with the motor vehicle or liability sectors. Cover is principally provided with respect to property insurance, subcontractors and mechanical breakdown insurance.

- **Other liability sectors**

Other liability sectors provide cover for the liability of the insured with respect to damage that the insured causes to a third party. Amongst the liabilities covered by these sectors are third party liability, employer's liability and product liability.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

| | For the 9-month period ended September 30, 2015 (unaudited) | | | | |
|---|--|-----------------------------|------------------------------|--|--------------|
| | Life assurance | Health insurance | General insurance | Not apportionable to operating segments | Total |
| | NIS in thousands | | | | |
| Gross earned premiums | 91,571 | 161,786 | 483,663 | | 737,020 |
| Premiums earned by reinsurers | (17,372) | (1,632) | (99,913) | | (118,917) |
| Premiums earned on retention | 74,199 | 160,154 | 383,750 | | 618,103 |
| Investment income (loss), net and financing income | (1) | 1,196 | 8,391 | 4,733 | 14,319 |
| Commission income | 2,911 | 418 | 28,166 | | 31,495 |
| Total income | 77,109 | 161,768 | 420,307 | 4,733 | 663,917 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (39,622) | (63,924) | (373,076) | | (476,622) |
| Share of reinsurers in payments and change in liabilities in respect of insurance contracts | 13,057 | 2,229 | 112,568 | | 127,854 |
| Payments and change in liabilities with respect to insurance contracts, on retention | (26,565) | (61,695) | (260,508) | | (348,768) |
| Commissions and other acquisition costs | (23,177) | (30,029) | (76,863) | | (130,069) |
| General and administrative expenses | (24,992) | (33,256) | (48,281) | | (106,529) |
| Financing income (expenses) | - | - | 1,391 | (2,077) | (686) |
| Total comprehensive income before taxes on income | 2,375 | 36,788 | 36,046 | 2,656 | 77,865 |
| Liabilities with respect to insurance contracts, gross, as of September 30, 2015 | 57,823 | 133,757 | 1,527,035 | | 1,718,615 |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

| | For the 9-month period ended September 30 , 2014 (unaudited) | | | | |
|---|---|------------------|------------------|----------------------|--------------|
| | Life | Health | General | Not | |
| | assurance | insurance | insurance | apportionable | Total |
| | NIS in thousands | | | | |
| | | | | to operating | |
| | | | | segments | |
| Gross earned premiums | 85,847 | 155,897 | 443,582 | | 685,326 |
| Premiums earned by reinsurers | (17,621) | (4,838) | (89,333) | | (111,792) |
| Premiums earned on retention | 68,226 | 151,059 | 354,249 | | 573,534 |
| Investment income, net and financing income | 46 | 4,926 | 29,988 | 26,134 | 61,094 |
| Commission income | 2,637 | 1,185 | 25,700 | | 29,522 |
| Total income | 70,909 | 157,170 | 409,937 | 26,134 | 664,150 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (33,031) | (65,328) | (336,366) | | (434,725) |
| Share of reinsurers in payments and change in liabilities in respect of insurance contracts | 8,357 | 3,883 | 109,897 | | 122,137 |
| Payments and change in liabilities with respect to insurance contracts, on retention | (24,674) | (61,445) | (226,469) | | (312,588) |
| Commission and other acquisition costs | (21,761) | (29,196) | (71,954) | | (122,911) |
| General and administrative expenses | (22,039) | (31,008) | (50,255) | | (103,302) |
| Financing income (expenses) | - | (14) | (580) | 2,501 | 1,907 |
| Total comprehensive income before taxes on income | 2,435 | 35,507 | 60,679 | 28,635 | 127,256 |
| Liabilities with respect to insurance contracts, gross, as of September 30,2014 | 50,321 | 135,797 | 1,518,018 | | 1,704,136 |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

| | <u>For the 3-month period ended September 30, 2015 (unaudited)</u> | | | | |
|---|--|------------------|------------------|----------------------|--------------|
| | <u>Life</u> | <u>Health</u> | <u>General</u> | <u>Not</u> | |
| | <u>assurance</u> | <u>insurance</u> | <u>insurance</u> | <u>apportionable</u> | <u>Total</u> |
| | <u>NIS in thousands</u> | | | | |
| | | | | <u>to operating</u> | |
| | | | | <u>segments</u> | |
| Gross earned premiums | 30,977 | 57,083 | 168,124 | | 256,184 |
| Premiums earned by reinsurers | (5,713) | (327) | (32,967) | | (39,007) |
| Premiums earned on retention | 25,264 | 56,756 | 135,157 | | 217,177 |
| Investment income (loss), net and financing income | - | 525 | 3,421 | (7,705) | (3,759) |
| Commission income | 987 | 154 | 8,997 | | 10,138 |
| Total income | 26,251 | 57,435 | 147,575 | (7,705) | 223,556 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (14,057) | (15,687) | (64,963) | | (94,707) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | 3,732 | 398 | (18,318) | | (14,188) |
| Payments and change in liabilities with respect to insurance contracts on retention | (10,325) | (15,289) | (83,281) | | (108,895) |
| Commission and other acquisition costs | (8,019) | (10,861) | (26,047) | | (44,927) |
| General and administrative expenses | (7,599) | (10,854) | (17,990) | | (36,443) |
| Financing income | - | - | 463 | 514 | 977 |
| Total comprehensive income (loss) before taxes on income | 308 | 20,431 | 20,720 | (7,191) | 34,268 |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

| | For the 3-month period ended September 30, 2014 (unaudited) | | | | Total |
|---|--|-----------------------------|------------------------------|--|--------------|
| | Life assurance | Health insurance | General insurance | Not apportionable to operating segments | |
| | NIS in thousands | | | | |
| Gross earned premiums | 29,276 | 54,095 | 150,257 | | 233,628 |
| Premiums earned by reinsurers | (5,712) | (659) | (28,502) | | (34,873) |
| Premiums earned on retention | 23,564 | 53,436 | 121,755 | | 198,755 |
| Investment income, net and financing income | 6 | 1,904 | 10,355 | 11,066 | 23,331 |
| Commission income | 865 | 65 | 7,626 | | 8,556 |
| Total income | 24,435 | 55,405 | 139,736 | 11,066 | 230,642 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (11,293) | (23,513) | (112,452) | | (147,258) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | 2,507 | 543 | 36,174 | | 39,224 |
| Payments and change in liabilities with respect to insurance contracts on retention | (8,786) | (22,970) | (76,278) | | (108,034) |
| Commission and other acquisition costs | (7,122) | (10,548) | (21,020) | | (38,690) |
| General and administrative expenses | (7,452) | (10,032) | (18,683) | | (36,167) |
| Financing expenses | - | 2 | 7 | 2,145 | 2,154 |
| Total comprehensive income (loss) before taxes on income | 1,075 | 11,857 | 23,762 | 13,211 | 49,905 |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

| | For the year ended December 31, 2014 (audited) | | | | Total |
|---|---|-----------------------------|------------------------------|--|----------------|
| | Life assurance | Health insurance | General insurance | Not Apportionable to operating segments | |
| | NIS in thousands | | | | |
| Gross earned premiums | 115,500 | 208,762 | 598,989 | | 923,251 |
| Premiums earned by reinsurers | (23,354) | (5,607) | (120,615) | | (149,576) |
| Premiums earned on retention | 92,146 | 203,155 | 478,374 | | 773,675 |
| Investment income, net and financing income | 51 | 4,193 | 24,957 | 19,926 | 49,127 |
| Commission income | 3,457 | 1,278 | 33,692 | | 38,427 |
| Total income | 95,654 | 208,626 | 537,023 | 19,926 | 861,229 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (42,011) | (91,717) | (444,130) | | (577,858) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | 10,601 | 4,799 | 133,574 | | 148,974 |
| Payments and change in liabilities with respect to insurance contracts on retention | (31,410) | (86,918) | (310,556) | | (428,884) |
| Commission and other acquisition costs | (28,595) | (39,731) | (98,576) | | (166,902) |
| General and administrative expenses | (30,698) | (43,184) | (66,277) | | (140,159) |
| Financing income (expenses) | - | (10) | (583) | 6,106 | 5,513 |
| Total comprehensive income before taxes on income | 4,951 | 38,783 | 61,031 | 26,032 | 130,797 |
| Liabilities with respect to insurance contracts, gross, as of December 31, 2014 | 51,791 | 137,135 | 1,526,335 | | 1,715,261 |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

Additional information relating to general insurance segment:

| | For the 9-month period ended September 30, 2015 (unaudited) | | | | | | Total |
|---|---|------------------------------|------------|---------------------------|-------------------------------|--------------------------------|-----------|
| | Compulsory Motor vehicle | Motor vehicle property | Apartments | Professional liability | Other property Sectors* | Other liability Sectors* | |
| NIS in thousands | | | | | | | |
| Gross premiums | 113,911 | 217,501 | 79,964 | 46,917 | 27,567 | 28,890 | 514,750 |
| Reinsurance premiums | (1,592) | (87) | (14,027) | (40,246) | (26,175) | (23,342) | (105,469) |
| Premiums on retention | 112,319 | 217,414 | 65,937 | 6,671 | 1,392 | 5,548 | 409,281 |
| Change in balance of unearned premiums, on retention | (3,564) | (17,734) | (3,877) | 239 | (43) | (552) | (25,531) |
| Premiums earned on retention | 108,755 | 199,680 | 62,060 | 6,910 | 1,349 | 4,996 | 383,750 |
| Investment income, net and financing income | 4,089 | 1,239 | 474 | 1,170 | 151 | 1,268 | 8,391 |
| Commission income | - | - | 3,174 | 12,027 | 6,390 | 6,575 | 28,166 |
| Total income | 112,844 | 200,919 | 65,708 | 20,107 | 7,890 | 12,839 | 420,307 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (53,189) | (154,486) | (37,591) | (103,093) | 3,738 | (28,455) | (373,076) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | (9,597) | - | 5,253 | 97,643 | (5,357) | 24,626 | 112,568 |
| Payments and change in liabilities with respect to insurance contracts on retention | (62,786) | (154,486) | (32,338) | (5,450) | (1,619) | (3,829) | (260,508) |
| Commission, marketing expenses and other acquisition costs | (14,309) | (29,372) | (12,043) | (10,992) | (4,336) | (5,811) | (76,863) |
| General and administrative expenses | (10,240) | (14,384) | (14,754) | (4,970) | (1,984) | (1,949) | (48,281) |
| Financing income, net | - | 505 | 885 | - | - | 1 | 1,391 |
| Total expenses | (87,335) | (197,737) | (58,250) | (21,412) | (7,939) | (11,588) | (384,261) |
| Total comprehensive income (loss) before taxes on income | 25,509 | 3,182 | 7,458 | (1,305) | 1,251 | 1,251 | 36,046 |
| Liabilities with respect to insurance contracts, gross, as of September 30, 2015 | 662,800 | 198,544 | 74,483 | 236,909 | 74,241 | 280,058 | 1,527,035 |
| Net liabilities with respect to insurance contracts, retention as of September 30, 2015 | 521,537 | 198,544 | 66,259 | 47,839 | 3,561 | 42,491 | 880,231 |

* The results of other property sectors reflect mainly the results of the property insurance sectors the operations of which attract 80% of the total premiums attributable to these sectors.
The results of other liability sectors reflect mainly the results of the third party liability insurance sector, the operations of which attract 44% of the total premiums attributable to these sectors.

AIG ISRAEL INSURANCE COMPANY. LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

Additional information relating to general insurance segment:

| | For the 9-month period ended September 30, 2014 (unaudited) | | | | | | Total |
|---|---|------------------------------|------------|---------------------------|-------------------------------|--------------------------------|-----------|
| | Compulsory Motor Vehicle | Motor vehicle property | Apartments | Professional liability | Other property sectors* | Other liability sectors* | |
| | NIS in thousands | | | | | | |
| Gross premiums | 112,802 | 198,373 | 80,578 | 43,145 | 25,299 | 25,536 | 485,733 |
| Reinsurance premiums | (1,572) | (79) | (18,834) | (36,427) | (24,227) | (20,916) | (102,055) |
| Premiums on retention | 111,230 | 198,294 | 61,744 | 6,718 | 1,072 | 4,620 | 383,678 |
| Change in balance of unearned premiums on retention | (8,009) | (17,400) | (1,817) | (1,365) | (180) | (658) | (29,429) |
| Premiums earned on retention | 103,221 | 180,894 | 59,927 | 5,353 | 892 | 3,962 | 354,249 |
| Investment income, net and financing income | 13,665 | 4,762 | 2,867 | 3,937 | 610 | 4,147 | 29,988 |
| Commission income | - | - | 3,869 | 9,722 | 6,373 | 5,736 | 25,700 |
| Total income | 116,886 | 185,656 | 66,663 | 19,012 | 7,875 | 13,845 | 409,937 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (86,198) | (121,230) | (26,459) | (29,461) | (21,984) | (51,034) | (336,366) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | 17,217 | - | 3,399 | 25,433 | 20,369 | 43,479 | 109,897 |
| Payments and change in liabilities with respect to insurance contracts on retention | (68,981) | (121,230) | (23,060) | (4,028) | (1,615) | (7,555) | (226,469) |
| Commission, marketing expenses and other acquisition costs | (13,618) | (25,856) | (15,065) | (8,443) | (3,812) | (5,160) | (71,954) |
| General and administrative expenses | (13,613) | (14,309) | (15,181) | (3,608) | (1,745) | (1,799) | (50,255) |
| Financing expenses, net | - | - | (20) | (248) | (41) | (271) | (580) |
| Total expenses | (96,212) | (161,395) | (53,326) | (16,327) | (7,213) | (14,785) | (349,258) |
| Total comprehensive income (loss) before taxes on income | 20,674 | 24,261 | 13,337 | 2,685 | 662 | (940) | 60,679 |
| Liabilities with respect to insurance contracts, gross, as of September 30, 2014 | 667,722 | 171,684 | 65,196 | 265,786 | 70,549 | 277,081 | 1,518,018 |
| Net liabilities with respect to insurance contracts, retention as of September 30, 2014 | 503,181 | 171,684 | 56,171 | 49,289 | 3,645 | 43,715 | 827,865 |

* The results of other property sectors reflect mainly the results of the property insurance sectors the operations of which attract 81% of the total premiums attributable to these sectors.
The results of other liability sectors reflect mainly the results of the third party liability insurance sector, the operations of which attract 45% of the total premiums attributable to these sectors.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

Additional information relating to general insurance segment:

| | For the 3-month period ended September 30, 2015 (unaudited) | | | | | | |
|---|--|---------------------------------------|-------------------|-----------------------------------|---|--|------------------|
| | Compulsory motor vehicle | Motor vehicle property | Apartments | Professional liability | Other property sectors * | Other liability sectors * | Total |
| | NIS in thousands | | | | | | |
| Gross premiums | 37,002 | 74,705 | 28,083 | 15,822 | 11,118 | 9,068 | 175,798 |
| Reinsurance premiums | (514) | (29) | (3,986) | (13,667) | (10,636) | (7,346) | (36,178) |
| Premiums on retention | 36,488 | 74,676 | 24,097 | 2,155 | 482 | 1,722 | 139,620 |
| Change in balance of unearned premiums on retention | 2,186 | (4,089) | (2,677) | 255 | (29) | (109) | (4,463) |
| Premiums earned retention | 38,674 | 70,587 | 21,420 | 2,410 | 453 | 1,613 | 135,157 |
| Investment income, net and financing income | 1,718 | 532 | 212 | 358 | 62 | 539 | 3,421 |
| Commission income | - | - | 776 | 3,857 | 2,161 | 2,203 | 8,997 |
| Total income | 40,392 | 71,119 | 22,408 | 6,625 | 2,676 | 4,355 | 147,575 |
| Payments and change in liabilities with respect to insurance contracts (gross) | 16,080 | (53,322) | (12,572) | (7,092) | (3,967) | (4,090) | (64,963) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | (30,900) | - | 1,517 | 4,701 | 3,347 | 3,017 | (18,318) |
| Payments and change in liabilities with respect to insurance contracts on retention | (14,820) | (53,322) | (11,055) | (2,391) | (620) | (1,073) | (83,281) |
| Commissions, marketing expenses and other acquisition costs | (5,295) | (9,896) | (3,828) | (3,673) | (1,315) | (2,040) | (26,047) |
| General and administrative expenses | (4,117) | (5,616) | (5,396) | (1,616) | (634) | (611) | (17,990) |
| Financing income (expenses), net | - | 178 | 297 | (4) | - | (8) | 463 |
| Total expenses | (24,232) | (68,656) | (19,982) | (7,684) | (2,569) | (3,732) | (126,855) |
| Total comprehensive income (loss) before taxes on income | 16,160 | 2,463 | 2,426 | (1,059) | 107 | 623 | 20,720 |

* The results of other property sectors reflect mainly the results of the property insurance sector the operations of which attract 75% of the total premiums attributable to these sectors.
The results of other liability sectors reflect mainly the results of the third party liability insurance sector, the operations of which attract 39% of the total premiums attributable to these sectors.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

Additional information relating to general insurance segment:

| | For the 3-month period ended September 30, 2014 (unaudited) | | | | | | |
|---|--|---------------------------------------|-------------------|-----------------------------------|--|---|--------------|
| | Compulsory Motor Vehicle | Motor vehicle property | Apartments | Professional liability | Other property sectors* | Other liability sectors* | Total |
| | NIS in thousands | | | | | | |
| Gross premiums | 37,798 | 67,497 | 28,840 | 12,869 | 9,370 | 9,028 | 165,402 |
| Reinsurance premiums | (526) | (27) | (6,773) | (10,556) | (8,997) | (7,596) | (34,475) |
| Premiums on retention | 37,272 | 67,470 | 22,067 | 2,313 | 373 | 1,432 | 130,927 |
| Change in balance of unearned premiums relating to retention | (1,714) | (4,687) | (1,788) | (693) | (22) | (268) | (9,172) |
| Premiums earned retention | 35,558 | 62,783 | 20,279 | 1,620 | 351 | 1,164 | 121,755 |
| Investment income, net and financing income | 4,607 | 1,825 | 1,109 | 1,331 | 182 | 1,301 | 10,355 |
| Commission income | - | - | 815 | 3,138 | 1,897 | 1,776 | 7,626 |
| Total income | 40,165 | 64,608 | 22,203 | 6,089 | 2,430 | 4,241 | 139,736 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (27,154) | (43,272) | (9,527) | (13,438) | (3,867) | (15,194) | (112,452) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | 6,793 | - | 836 | 12,824 | 3,703 | 12,018 | 36,174 |
| Payments and change in liabilities with respect to insurance contracts on retention | (20,361) | (43,272) | (8,691) | (614) | (164) | (3,176) | (76,278) |
| Commissions, marketing expenses and other acquisition costs | (4,051) | (7,690) | (3,837) | (2,849) | (1,110) | (1,483) | (21,020) |
| General and administrative expenses | (4,953) | (5,999) | (5,277) | (1,239) | (663) | (552) | (18,683) |
| Financing income (expenses), net | - | - | (2) | (9) | 7 | 11 | 7 |
| Total expenses | (29,365) | (56,961) | (17,807) | (4,711) | (1,930) | (5,200) | (115,974) |
| (5,200) | 10,800 | 7,647 | 4,396 | 1,378 | 500 | (959) | 23,762 |

* The results of other property sectors reflect mainly the results of the property insurance sector the operations of which attract 81% of the total premiums attributable to these sectors.
The results of other liability sectors reflect mainly the results of the third party liability insurance sector, the operations of which attract 42% of the total premiums attributable to these sectors.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 4 - SEGMENT INFORMATION (continued):

Additional information relating to general insurance segment

| | For year ended December 31, 2014 (audited) | | | | | | Total |
|---|--|------------------------------|------------|---------------------------|-------------------------------|--------------------------------|-----------|
| | Compulsory motor vehicle | Motor vehicle property | Apartments | Professional liability | Other property sectors* | Other liability sectors* | |
| NIS in thousands | | | | | | | |
| Gross premiums | 146,272 | 256,572 | 104,123 | 56,414 | 32,036 | 33,945 | 629,362 |
| Reinsurance premiums | (2,040) | (108) | (23,970) | (47,675) | (30,777) | (28,125) | (132,695) |
| Premiums on retention | 144,232 | 256,464 | 80,153 | 8,739 | 1,259 | 5,820 | 496,667 |
| Change in balance of unearned premiums on retention | (4,733) | (11,461) | (82) | (1,364) | (136) | (517) | (18,293) |
| Premiums earned on retention | 139,499 | 245,003 | 80,071 | 7,375 | 1,123 | 5,303 | 478,374 |
| Investment income, net and financing income | 10,951 | 4,116 | 2,873 | 3,200 | 479 | 3,338 | 24,957 |
| Commission income | - | - | 4,870 | 13,233 | 8,212 | 7,377 | 33,692 |
| Total income | 150,450 | 249,119 | 87,814 | 23,808 | 9,814 | 16,018 | 537,023 |
| Payments and change in liabilities with respect to insurance contracts (gross) | (109,602) | (168,861) | (36,945) | (30,731) | (52,706) | (45,285) | (444,130) |
| Share of reinsurers in payments and change in liabilities with respect to insurance contracts | 13,460 | - | 4,592 | 25,395 | 50,327 | 39,800 | 133,574 |
| Payments and change in liabilities with respect to insurance contracts on retention | (96,142) | (168,861) | (32,353) | (5,336) | (2,379) | (5,485) | (310,556) |
| Commission, marketing expenses and other acquisition costs | (18,219) | (36,043) | (20,299) | (11,734) | (5,190) | (7,091) | (98,576) |
| General and administrative expenses | (18,339) | (17,572) | (20,663) | (5,305) | (1,974) | (2,424) | (66,277) |
| Financing expenses, net | - | - | (20) | (253) | (37) | (273) | (583) |
| Total expenses | (132,700) | (222,476) | (73,335) | (22,628) | (9,580) | (15,273) | (475,992) |
| Total comprehensive income before taxes on income | 17,750 | 26,643 | 14,479 | 1,180 | 234 | 745 | 61,031 |
| Liabilities with respect to insurance contracts, gross, as of | | | | | | | |
| December 31, 2014 | 666,500 | 168,599 | 64,517 | 262,359 | 96,557 | 267,803 | 1,526,335 |
| Net liabilities with respect to insurance contracts as of December 31, 2014 | 506,731 | 168,599 | 56,140 | 49,839 | 3,591 | 40,760 | 825,660 |

* The results of other property sectors reflect mainly the results of the property insurance sector the operations of which attract 83% of the total premiums attributable to these sectors.
The results of other liability sectors reflect mainly the results of the product liability insurance sector, the operations of which attract 44% of the total premiums attributable to these sectors.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 5 - SHAREHOLDERS' EQUITY AND CAPITAL REQUIREMENTS:

a. Dividend declared after balance sheet date

On October 27, 2015, the Company's board approved a NIS 35 million cash dividend, representing about 14% of issued capital (share capital and premium) of the Company as of September 30, 2015. The dividend per share is NIS 6,108.

b. Capital management and requirements:

1. Management pursues a policy of maintaining a sound equity base, thereby allowing the Company to continue operations in such manner that will enable it to provide a return to its shareholders and undertake future commercial operations. The Company is required to adhere to the capital requirements laid down by the Supervisor.
2. The table below provides information with respect to the capital requirements as set out in the Shareholders' Equity Regulations and the amendments thereto and in the directives of the Supervisor, together with information relating to the level of the Company's existing capital.

Company's capital in accordance with the Shareholders' Equity Regulations:

| | September 30 | | December 31, |
|--|---------------------|-------------|---------------------|
| | 2015 | 2014 | 2014 |
| | (Unaudited) | | (Audited) |
| The amount required under Shareholders' Equity Regulations and supervisor guidelines (a) | 553,523 | 529,236 | 546,550 |
| Existing amount calculated under Shareholders' Equity Regulations: | | | |
| Basic primary capital | 739,214 | 727,692 | 690,907 |
| Total existing capital calculated under Shareholders' Equity Regulations | 739,214 | 727,692 | 690,907 |
| Surplus | 185,691 | 198,456 | 144,357 |
| Subsequent events - dividend declared | (35,000) | (35,000) | - |
| Surplus after consideration of subsequent events | 150,691 | 163,456 | 144,357 |

Aside from the general requirements of the Companies' Law, the distribution of a dividend out of the equity surpluses of insurance companies is also subject to compliance with liquidity requirements and the provisions of the investment regulations. For this purpose, the investments for which it is obligatory to set against equity surplus in accordance with the Supervisors instructions constitute surplus that is not distributable.

- (a) The amount required, as it relates to the Company and in accordance with parameters defined in the amended Shareholders' Equity Regulations, including inter alia, capital requirements, with respect to:

| | September 30 | | December 31, |
|--|-------------------------|----------------|---------------------|
| | 2015 | 2014 | 2014 |
| | (Unaudited) | | (Audited) |
| | NIS in thousands | | |
| Operations related to general insurance | 126,793 | 122,223 | 123,599 |
| Exceptional life assurance risks | 35,516 | 30,503 | 31,756 |
| Deferred acquisition costs related to life assurance | 83,352 | 84,940 | 85,505 |
| Investment assets and other assets | 66,768 | 66,112 | 73,831 |
| Catastrophe risks related to general insurance | 210,112 | 194,675 | 200,903 |
| Operating risks | 30,982 | 30,783 | 30,956 |
| Total | 553,523 | 529,236 | 546,550 |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 5 - SHAREHOLDERS' EQUITY AND CAPITAL REQUIREMENTS (continued):

c. Solvency II

In November 2014, the Supervisor issued a letter addressed to insurance companies' managers (hereafter – "the letter"), which outlines the implementation of the Solvency II directive (hereafter – "the directive"). In the letter, the Supervisor notified the insurance companies that the implementation of the directive in Europe was scheduled for the beginning of 2016 and timelines were set for the implementation of the final directive. In view of the intention to issue final directives in Europe by June 2015, the Supervisor notified the insurance companies of her intention to issue in 2016 guidelines regarding the adjustment of the first tier of the directive to the local market; those guidelines shall replace the existing ones. The Supervisor noted that the insurance companies will be required to meet those guidelines commencing their 2016 annual financial statements. As part of the preparations for the implementation of the model, the Ministry of Finance requires that insurance companies carry out IQIS exercises which are designed to calibrate the model (simulations of the effect of the directive on the insurer's equity given its existing business mix and balance sheet). The Supervisor noted that several IQIS were carried out in the past and that there is an intention to carry out two additional IQIS exercises in the future in respect of the years 2014 and 2015.

It was also noted that subsequently, commencing 2016 and before the new regime comes into effect, there is an intention to require a quarterly reporting in accordance with the new layout; such quarterly reporting will be made in addition to the existing capital requirements reporting.

Changing the capital requirements is subject, among other things, to changing the Supervision of Financial Services (Insurance) (Minimum Equity Required of an Insurer) Regulations, 1998. The Supervisor also intends to issue guidelines concerning capital management and determination of new internal capital targets regarding gap analysis survey, which the companies will be required to perform with respect to the guidance relating to the risk management array, controls and corporate governance and consultation paper to advance the own risk and solvency assessment (ORSA) process.

In April 2015, the Supervisor issued an insurance circular on the requirement to perform IQIS in 2014 (hereafter – IQIS4). According to the letter attached to the circular, since it has issued the directive's layout last year, the European commission issued final solvency directives as well as technical guidelines for the implementation thereof.

In the said letter, the Supervisor notes, among other things, that the IQIS exercise reflects the Supervisor's decisions regarding the adjustments which are required for the Israeli market and will be reflected in the new instructions. It was also noted in the letter that in advance of the application of IQIS5, the Supervisor will continue monitoring the developments in European instructions, if any, and will discuss any adjustments required for the Israeli market.

The insurance companies will be required to comply with the new capital requirements commencing with the 2016 financial statements.

The guidance on performance of IQIS4 includes a number of changes and updates compared to IQIS2. The main changes relate to cancelations, longevity, interest rate, shares, spreads, risk margin and liquidity premium. The Company completed the IQIS4 exercise in June 2015 and filed the exercise results to the Supervisor by August 31, 2015, in accordance with the specified layout.

The IQIS4 exercises performed by the Company indicate that the Company's capital surplus as of December 31, 2014 increased when calculated on Solvency II-based solvency governance compared to capital surplus under the existing Israeli governance (see a. above).

It should be indicated that the model, in its current status, is highly sensitive to changes in market variables and other variables, which may result in fluctuations in the capital requirements reflected by it.

AIG ISRAEL INSURANCE COMPANY. LTD.
 NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 6 - FINANCIAL INSTRUMENTS AND FINANCIAL RISKS:

a. Fair value disclosure

Following the discussion in note 10(g) to the Company's 2014 annual financial statements, during the 9 months period ended September 30, 2015, no transfers were made between level 1 and level 2. As of balance sheet dates presented all marketable financial investments of the Company, which are measured at fair value through profit or loss, are classified as Level 1. As of balance sheet dates presented the Company has no financial liabilities that are measured at fair value.

b. The fair value of financial assets and financial liabilities:

1. The balances of cash and cash equivalents, premiums collectible, accounts receivables, liabilities to reinsurers and accounts payable in the financial statements are equal or close to their fair value.
2. For details of the fair value of financial investments, see d below.

c. No material changes have occurred in the financial risk management policy of the Company, compared to the policy it reported in its 2014 annual financial statements.

d. Composition of financial investments:

| | As of September 30, 2015 (unaudited) | | |
|------------------------------------|--|----------------------------------|------------------|
| | Measured at fair value through profit or loss | Loans and receivables | Total |
| | NIS in thousands | | |
| Marketable debt instruments(1) | 1,233,925 | - | 1,233,925 |
| Non-marketable debt instruments(2) | - | 204,112 | 204,112 |
| Marketable shares(3) | 92,146 | - | 92,146 |
| Other(4) | 72,129 | - | 72,129 |
| Total | 1,398,200 | 204,112 | 1,602,312 |

| | As of September 30, 2014 (unaudited) | | |
|------------------------------------|--|----------------------------------|------------------|
| | Measured at fair value through profit or loss | Loans and receivables | Total |
| | NIS in thousands | | |
| Marketable debt instruments(1) | 1,200,994 | - | 1,200,994 |
| Non-marketable debt instruments(2) | - | 159,313 | 159,313 |
| Marketable shares(3) | 87,816 | - | 87,816 |
| Other(4) | 36,501 | - | 36,501 |
| Total | 1,325,311 | 159,313 | 1,484,624 |

| | As of December 31, 2014 (audited) | | |
|------------------------------------|--|----------------------------------|------------------|
| | Measured at fair value through profit or loss | Loans and receivables | Total |
| | NIS in thousands | | |
| Marketable debt instruments(1) | 1,183,798 | - | 1,183,798 |
| Non-marketable debt instruments(2) | - | 164,461 | 164,461 |
| Marketable shares(3) | 87,300 | - | 87,300 |
| Other(4) | 57,919 | - | 57,919 |
| Total | 1,329,017 | 164,461 | 1,493,478 |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 6 - FINANCIAL INSTRUMENTS AND FINANCIAL RISKS (continued):

d. Composition of financial investments (continued):

- (1) **Composition of marketable debt instruments** (designated upon initial recognition to the fair value through profit or loss category):

| | As of September 30, 2015 (unaudited) | |
|--|---|---------------------------|
| | Book value | Amortized cost |
| | NIS in thousands | |
| Government debentures | 628,681 | 627,863 |
| Other debt instruments: | | |
| Other debt instruments that are not convertible | 605,244 | 614,624 |
| Other debt instruments that are convertible | - | - |
| Total marketable debt instruments | <u>1,233,925</u> | <u>1,242,487</u> |

| | As of September 30, 2014 (unaudited) | |
|--|---|---------------------------|
| | Book value | Amortized cost |
| | NIS in thousands | |
| Government debentures | 632,230 | 615,845 |
| Other debt instruments: | | |
| Other debt instruments that are not convertible | 568,702 | 558,030 |
| Other debt instruments that are convertible | 62 | 62 |
| Total marketable debt instruments | <u>1,200,994</u> | <u>1,173,937</u> |

| | As of December 31, 2014 (audited) | |
|--|--|---------------------------|
| | Book value | Amortized cost |
| | NIS in thousands | |
| Government debentures | 629,992 | 622,306 |
| Other debt instruments: | | |
| Other debt instruments that are not convertible | 553,744 | 557,229 |
| Other debt instruments that are convertible | 62 | 62 |
| Total marketable debt instruments | <u>1,183,798</u> | <u>1,179,597</u> |

AIG ISRAEL INSURANCE COMPANY. LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued):

NOTE 6 - FINANCIAL INSTRUMENTS AND FINANCIAL RISKS (continued):

d. Composition of financial investments (continued):

(2) Composition of non-marketable debt instruments

| | As of September 30, 2015 (unaudited) | |
|---|---|-------------------|
| | Book value | Fair value |
| <u>Loans and receivables:</u> | NIS in thousands | |
| Bank deposits | 98,089 | 98,186 |
| Other debt instruments that are not convertible | <u>106,023</u> | <u>107,752</u> |
| Total non-marketable debt instruments | <u>204,112</u> | <u>205,938</u> |
| | As of September 30, 2014 (unaudited) | |
| | Book value | Fair value |
| <u>Loans and receivables:</u> | NIS in thousands | |
| Bank deposits | 106,253 | 106,640 |
| Other debt instruments that are not convertible | <u>53,060</u> | <u>53,583</u> |
| Total non-marketable debt instruments | <u>159,313</u> | <u>160,223</u> |
| | As of December 31, 2014 (audited) | |
| | Book value | Fair value |
| <u>Loans and receivables:</u> | NIS in thousands | |
| Bank deposits | 103,653 | 103,559 |
| Other debt instruments that are not convertible | <u>60,808</u> | <u>60,893</u> |
| Total non-marketable debt instruments | <u>164,461</u> | <u>164,452</u> |

AIG ISRAEL INSURANCE COMPANY LTD.
 NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 6 - FINANCIAL INSTRUMENTS AND FINANCIAL RISKS (continued):

d. Composition of financial investments (continued):

(3) Shares (designated upon initial recognition to the fair value through profit or loss category):

| | As of September 30, 2015 | |
|-------------------|---------------------------------|---------------|
| | (unaudited) | |
| | <u>Book value</u> | <u>Cost</u> |
| | NIS in thousands | |
| Marketable shares | <u>92,146</u> | <u>89,358</u> |

| | As of September 30, 2014 | |
|-------------------|---------------------------------|---------------|
| | (unaudited) | |
| | <u>Book value</u> | <u>Cost</u> |
| | NIS in thousands | |
| Marketable shares | <u>87,816</u> | <u>82,139</u> |

| | As December 31, 2014 | |
|-------------------|-----------------------------|---------------|
| | (audited) | |
| | <u>Book value</u> | <u>Cost</u> |
| | NIS in thousands | |
| Marketable shares | <u>87,300</u> | <u>83,854</u> |

(4) Other financial investments (designated upon initial recognition to the fair value through profit or loss category):

| | As of September 30, 2015 | |
|----------------------------------|---------------------------------|---------------|
| | (unaudited) | |
| | <u>Book value</u> | <u>Cost</u> |
| | NIS in thousands | |
| Marketable financial investments | <u>72,129</u> | <u>73,867</u> |

| | As of September 30, 2014 | |
|----------------------------------|---------------------------------|---------------|
| | (unaudited) | |
| | <u>Book value</u> | <u>Cost</u> |
| | NIS in thousands | |
| Marketable financial investments | <u>36,501</u> | <u>35,380</u> |

| | As December 31, 2014 | |
|----------------------------------|-----------------------------|---------------|
| | (audited) | |
| | <u>Book value</u> | <u>Cost</u> |
| | NIS in thousands | |
| Marketable financial investments | <u>57,919</u> | <u>57,916</u> |

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 7 - TAXES ON INCOME

Calculating the income tax for the interim period is based on the best estimate of the weighted income tax rate (corporate tax and profit tax) expected for the full fiscal year, based on the tax laws enacted that are substantially enacted as of the statement on financial position date. The weighted average annual tax rate, as above, for the year ending December 31, 2015 is 37.71%.

The Knesset (Israeli parliament) approved in October 2015 Value Added Tax Decree (Tax Rate of Non-Profit Organizations and Financial Institutions) (Amendment), 2015 ("the Amendment") lowering, commencing October 1, 2015, the rate of payroll tax and profit tax on Israeli activity of financial institutions to 17% of payroll paid and income generated (instead of 18% until that date).

Following the amendment, the overall tax rate (corporate tax and profit tax) applicable to the Company for 2015 is 37.58%, instead of 37.71% that applied to it prior to the amendment, as above. The expected impact of the amendment on the 2015 annual financial statements of the Company is immaterial.

NOTE 8 - CONTINGENT LIABILITIES - CLASS ACTIONS:

Motions for certification of class actions

Motions for certification of class actions presented in 1-2 below, which management believes, based on the opinion it obtained from its legal advisors, that it is more likely than not that defense arguments of the Company will be accepted and the motion will be rejected, did not lead to provisions in the financial statements.

For the motion for certification of class actions in 3 below, it is not possible to estimate at this preliminary stage the likelihood of class action certification, and therefore, no provision have been recognized for this claim.

The following are motions for certification of class actions:

1. A legal claim and an application to approve the claim as a class action were filed against the Company and 7 other insurance companies in December 2012. According to the plaintiffs, in 2007 the Transportation Ordinance was changed to the effect that the classification of the plaintiffs' vehicle was changed from a commercial vehicle to a private vehicle. Despite the change in classification as above, the insurance companies allegedly continued to classify the plaintiffs' vehicles as commercial vehicles for purposes of collection of comprehensive insurance/third party insurance and compulsory vehicle insurance, thereby collecting a higher premium. The premium was only collected in respect of vehicles through 2007, whereas for vehicles from 2008 and thereafter a lower premium was collected.

According to the legal claim, the insurance companies are required to price the premium in accordance with the classification set in the Transportation Ordinance and since they have not done so they should refund the insured persons and entities with the amounts collected in excess of the lawful premiums. The group in the name of whom the legal claim was lodged is the group of insured persons and entities the classification of the vehicles of which was changed in the last seven years.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 8 - CONTINGENT LIABILITIES - CLASS ACTIONS (continued):

Total damages claimed from the Company in respect of property insurance amount to NIS 22,296,660. The legal claim does not provide an estimate of the amount collected in excess of the amount legally due for compulsory vehicle insurance.

The Company filed its reply to the application to approve the claim as a class action on June 2, 2013; the claimant filed its reply to the said application on July 7, 2013.

On July 10, 2013, a pretrial hearing was held, resulting in a court decision that the Company and all other defendants may file complementary responses to the motion for class action certification through October 6, 2013. The court also ruled that to the extent the plaintiffs are interested to file a specific discovery, they will have to do so within 30 days, with a response to the motion filed within 14 days and the counter-response within 7 days (court holiday are counted). In addition, a cross-examination of declarants was scheduled for February 24, 2014 and March 6, 2014.

The plaintiffs filed a motion for discovery and a motion to respond to a questionnaire. The Company filed its objection to the motion and the court has not given a decision.

Cross examinations of the parties' witnesses took place on February 24, 2014 March 6, 2014 and March 25, 2014. At the end of the examinations, the court recommended that the claimant considers whether to continue pursuing the case.

On June 8, 2014, the plaintiffs filed a notice to the effect that they maintain their position that the application to approve the claim as a class action shall be heard by the court. In accordance with the plaintiffs' notice, the court set a date for a summary hearing. The plaintiffs' summaries were filed recently. After a deferral, the Company is to file its summaries by September 16, 2015. Based on the opinion of its legal counsels, Company management believes that it is more likely than not that the claim will be rejected.

2. A legal claim and an application to approve the claim as a class action were filed on June 23, 2014 against the Company and 6 other insurance companies (hereafter – "the respondents") to the Jerusalem District Court (hereafter – "the court") by eight persons insured by the respondents (hereafter – "the applicants"). In the application to approve the claim as a class action it was claimed that the amount from which the mortgage life insurance premium has been derived by the respondents exceeded the actual balance of the loan with the lending bank and as a result the premiums paid the applicants were higher than the premiums they should have paid.

According to the applicants, the group of claimants in the class action includes all persons insured by the respondents under a life insurance policy for the purpose of securing a mortgage loan in the course of the seven year-period prior to filing the application and who paid to any of the respondents premiums which were higher than the premiums they should have paid since the amount from which the mortgage life insurance premium has been derived by the respondents exceeded the actual balance of the loan with the lending bank.

The causes of the claim according to the applicants are contravention of Sections 55 and 58 to the Supervision of Financial Services (Insurance) Law, 1981, breach of statutory duty, and breach of duty of good faith, negligence and unjust enrichment.

AIG ISRAEL INSURANCE COMPANY LTD.
NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 8 - CONTINGENT LIABILITIES - CLASS ACTIONS (continued):

The applicants seek to repay the persons included in the group the amount of difference between the insurance premiums which they were supposed to pay and the insurance premium they paid in practice with the addition of compensation for mental anguish. The applicants request that the court orders the respondents to update the amount of the insurance premium on a monthly or semi-annual basis based on exact mortgage loan data; they also request that the court orders the respondents to provide persons they insure an explanation regarding the option to provide the respondents with an updated balance of the loans with the lending banks (where no exact mortgage loan data is available).

The amount of the individual claim filed by the applicants against the Company is NIS 272 thousands and the amount claimed by the group of persons insured by the Company amounts to NIS 5,784,187.

On January 6, 2015 the respondents filed their reply to the application to approve the claim as a class action. In their reply the respondents claimed, among other things, that neither the law nor the insurance policy requires them to reduce the insured amount on their own accord and to adjust it to the updated balance of the loan. On the contrary, the insurance policy informs the insured individuals of the potential difference between the balance of the loan and the insured amount and in any case the updated insured amount is presented in the annual statements posted to all insured individuals; the respondents claim that without a specific request of the insured individual (to which an approval of the lending bank should be attached) they cannot reduce the insured amount since this will be considered breach of the provisions of the insurance policy; the respondents claim that they are unable to reduce the insured amount so that it corresponds to the balance of the loan since this information is subject to the bank secrecy duty; the respondents claim that the insured amount is covers not only the repayment of the principal of the loan but also the repayment of other related amounts, the existence and scope of which are not known to the insurance company in the course of the insurance period (such as payment arrears). Also, the balance of the loan is subject to changes taking place in the course of the loan period as a result of changes or revaluations carried out the borrower or the lending bank; the respondents claim that upon the occurrence of an insurance event, the respondents repay the mortgage loan and the related amounts to the lending bank and the remainder of the insured amount is paid to the other beneficiaries whose identity is determined by the insured individual; thus, according to the respondents the premiums paid the applicants are not higher than the premiums they should have paid. The respondents also claim that the underlying assumptions on which the applicants relied in their application is not shared by all applicants and that the applicants themselves acted in contradiction to those assumptions. The respondents claim that the non-disclosure claims that underlies the application to approve the claim as a class action is a specific and individual claim which should not be debated as part of a class action.

On April 19, 2015 the applicants filed their reply to the application to approve the claim as a class action. The applicants reject the claims raised in the reply to the application. A preliminary hearing to discuss the application was held on June 14, 2015. In the course of this hearing the Court informed the parties that it intends to address questions arising from the application to approve the claim as a class action to the Supervisor of Insurance; the Court asked the parties to provide it, by July 16, 2016, with questions that will be addressed to the Supervisor of Insurance. On July 16, 2015 the parties filed the Court some questions they wish to refer to the Supervisor of Insurance as above.

A further preliminary hearing was held on July 20, 2015 to discuss the application to approve the claim as a class action. In this hearing the Court ordered to refer questions to the Supervisor of Insurance by October 20, 2015. The Court also stipulated that the parties will be allowed to file their reply to the position of the Supervisor of Insurance through November 20, 2015.

AIG ISRAEL INSURANCE COMPANY LTD.
 NOTES TO CONDENSED FINANCIAL STATEMENTS (continued)

NOTE 8 - CONTINGENT LIABILITIES - CLASS ACTIONS (continued):

On October 19, 2015, a motion for extension of deadline for submitting the position of the Supervisor of Insurance was filed through the Jerusalem District Attorney's Office, asking for a new deadline on November 20, 2015, and accordingly that response of the parties to the position of the Supervisor will be filed by December 20, 2015. On October 21, 2015, the court extended the deadline as requested. A preliminary hearing to discuss the application to approve the claim as a class action was set to January 3, 2016.

Based on information and data that was received, at this preliminary stage, Company's management believes, based on the opinion of its legal advisors, that it is more likely than not that the court will not allow the application to approve the claim as a class action.

3. A legal claim and an application to approve the claim as a class action were filed in May 2015 against the Company and 5 other insurance companies. The plaintiffs claim that the insurers do not pay to insured people/entities and/or third parties the VAT component applicable to the cost of damages in cases where the alleged damages were not repaired in practice.

The plaintiffs rely in their legal claim on the Supreme Court's ruling in the Zlutzin vs. Diur La-Olle case (civil appeal 17229/99) according to which even where repairs were not carried out in practice, the defendant (who caused the damage in the said case) should bear the VAT component. The plaintiffs also rely on In-Principle Ruling 2014-46025 titled "In-Principle Ruling on Payment of VAT and Depreciation of Unrepaired Vehicle". This in-principle ruling states that even if the customer did not repair the vehicle in practice the insurer must pay the customer insurance benefits including, among other things, VAT applicable in this matter.

At this stage it is not yet clear whether the claim shall be heard in its current form since the class action plaintiff also filed an individual claim against the Company (including in connection with the VAT component) at the same time the class action motion was filed; the class action plaintiff requested the Court which hears the plaintiff's individual claim against the Company to allow him to withdraw the VAT component from this individual claim and to file an application to approve the claim as a class action in respect of this component. The relevant Court has not yet issued its decision to the said request.

The total amount claimed from the Company is NIS 40,211,388.

The Company is to file its reply within 90 days (with the addition of the 45 days of the courts recess) and a preliminary hearing was set to March 7, 2016.

At this preliminary stage Company's management and its legal advisors are still looking into the matter and it is not possible to estimate the likelihood of the claim and of the application to approve the claim as a class action.

Set forth below are the details of the applications for approval of legal claims as class actions:

| | Number of claims | The amount claimed NIS in thousands |
|---|-------------------------|--|
| Pending applications for approval of legal claims as class actions - an amount relating to the Company was specified | 3 | 68,292 |

NOTE 9 - SUBSEQUENT EVENTS

On October 27, 2015, the board of director approved a NIS 35 million dividend distribution to the Company's shareholder. See note 5a above.