The Hebrew version of the financial statements issued by the company on December 31, 2012 is the most up-to-date for all intents and purposes.

This translation is for convenience purposes only.

AIG ISRAEL INSURANCE CO. LTD.

2012 ANNUAL REPORT

AIG ISRAEL INSURANCE CO. LTD.

2012 ANNUAL REPORT

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AUDITORS' REPORT

To the shareholders of

AIG ISRAEL INSURANCE CO. LTD.

We have audited the attached statements of financial position of AIG Israel Insurance Co. Ltd. ("the Company") as of December 31, 2012 and 2011 and the statements of comprehensive income, changes in equity and cash flows for each of the three-year period ended December 31, 2012. These financial statements are the responsibility of the Board of Directors and management of the Company. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with auditing standards generally accepted in Israel, including those prescribed by the Auditors' (Mode of Performance) Regulations, 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Company's Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, formulated on the basis of our audits, the financial statements referred to above present fairly, in all material respects and in accordance with the provisions of international financial reporting standards and the disclosure requirements of the Supervision of Financial Services (Insurance) Law, 1981 and the regulations promulgated thereunder, the financial position of the Company as of December 31, 2012 and 2011 and the results of its operations, the changes in its equity and its cash flows for each of the three years in the three-year period ended December 31, 2012.

We have also audited in accordance with the standards of the Public Company Accounting Oversight Board (PCAOB) of the United States on auditing internal control over financial reporting as adopted by the Institute of Certified Public Accountants in Israel, the internal control over financial reporting of the company as of December 31, 2012, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). And our report dated March 19, 2013 expressed an unqualified opinion on the Company's effectiveness of internal control over financial reporting.

Tel-Aviv, Israel
________ 2013

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

Kesselman & Kesselman, Trade Tower, 25 Hamered Street, Tel-Aviv 68125, Israel,
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AIG ISRAEL INSURANCE CO. LTD.

STATEMENTS OF FINANCIAL POSITION

	Note	December 31 2012	December 31 2011
		ILS in thousands	
Assets			
Intangible assets	5	15,732	9,983
Deferred acquisition expenses	6	130,191	118,658
Property and equipment	7	16,885	18,743
Reinsurance assets	13,28	585,532	525,795
Premiums collectible	9	174,155	156,213
Current tax assets	18	-	10,834
Other receivables	8	33,668	30,856
		956,163	871,082
Financial investments:	10		
Marketable debt instruments		1,099,646	978,556
Non-marketable debt instruments		77,925	58,859
Marketable shares		68,284	50,934
Other		93,487	37,312
Total financial investments		1,339,342	1,125,661
Cash and cash equivalents	11	93,540	103,562
TOTAL ASSETS		2,389,045	2,100,305

Avraham Heller **Director**	**Hava Friedman-Shapira** **CEO**	**David Rothstein** **CFO**

Date of approval of financial statements by Board of Directors March, 19 2013.

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

AIG ISRAEL INSURANCE CO. LTD.

STATEMENTS OF FINANCIAL POSITION

	Note	December 31 2012	December 31 2011
		ILS in thousands	
Equity and liabilities			
EQUITY:	12		
Share capital		6	6
Share premium		250,601	250,601
Other capital reserve		11,084	11,084
Retained earnings		315,413	158,076
TOTAL EQUITY ATTRIBUTABLE TO COMPANY SHAREHOLDERS		577,104	419,767
LIABILITIES:			
Liabilities with respect to insurance contracts and non-profit participating investment contracts	13	1,409,340	1,385,290
Liabilities with respect to deferred taxes, net	18	8,877	7,376
Liabilities with respect to employee rights upon retirement, net		2,326	2,047
Liabilities towards reinsurers	28	254,484	211,410
Liabilities with respect to current taxes	18	48,549	-
Payables	19	88,365	74,415
TOTAL LIABILITIES		1,811,941	1,680,538
TOTAL EQUITY AND LIABILITIES		2,389,045	2,100,305

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

AIG ISRAEL INSURANCE CO. LTD.

STATEMENTS OF COMPREHENSIVE INCOME

	Note	2012	2011	2010
		Year ended December 31		
		ILS in thousands		
Gross premiums earned		827,158	735,053	690,304
Premiums earned by reinsurers		(185,701)	(157,712)	(142,814)
Premiums earned - retained amount	20	641,457	577,341	547,490
Investment income, net and financing income	21	97,239	** 25,333	** 65,894
Commission income	22	47,628	41,457	36,952
TOTAL INCOME		786,324	644,131	650,336
Payments and movement in liabilities with respect to insurance contracts, gross		(403,690)	(429,949)	(417,029)
Share of reinsurers in increase in insurance liabilities and payments with respect to insurance contracts		152,790	119,413	101,083
Payments and movement in liabilities with respect to insurance contracts, retained amount	23	*(250,900)	(310,536)	(315,946)
Commission, marketing expenses and other acquisition expenses	24	(147,372)	(131,406)	(126,103)
General and administrative expenses	25	(142,078)	(136,263)	(121,721)
Financing expenses	26	(2,206)	**1,380	**(866)
TOTAL EXPENSES		(542,556)	(576,825)	(564,636)
INCOME BEFORE TAXES ON INCOME		243,768	67,306	85,700
Taxes on income	18	(86,431)	(22,943)	(29,366)
INCOME FOR YEAR AND TOTAL COMPREHENSIVE INCOME FOR THE YEAR		157,337	44,363	56,334
BASIC EARNINGS PER SHARE:				
Basic earnings per share		27.95	7.88	10.01
Number of shares used in computation of basic earnings per share		5,630	5,630	5,630

* As for reducing the period of "surplus reserve" compulsory vehicle sector, see note 2.r.1.a.

** Certain amounts were reclassified, see note 2.t.

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

AIG ISRAEL INSURANCE CO. LTD.

STATEMENTS OF CHANGES IN EQUITY

	Share capital	Share premium	Other surplus	Retained earnings	Total
	ILS in thousands				
BALANCE AS OF JANUARY 1, 2012	6	250,601	11,084	158,076	419,767
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2012:					
Total comprehensive income fortheyearended December 31, 2011				157,337	157,337
Transactions with owners:					
Benefit component in respect of grant of share-based payments to employees by controlling shareholder			-		-
BALANCE AS OF DECEMBER 31, 2012	6	250,601	11,084	315,413	577,104
BALANCE AS OF JANUARY 1, 2011	6	250,601	10,898	113,713	375,218
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2011:					
Total comprehensive income for the year ended December 31, 2011				44,363	44,363
Transactions with owners:					
Benefit component in respect of grant of share-based payments to employees by controlling shareholder			186		186
BALANCE AS OF DECEMBER 31, 2011	6	250,601	11,084	158,076	419,767
BALANCE AS OF JANUARY 1, 2010	5	176,602	10,581	131,379	318,576
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2010:					
Total comprehensive income for the year ended December 31, 2010				56,334	56,334
Transactions with owners:					
Issuance of bonus shares	1	73,999		(74,000)	
Benefit component in respect of grant of share based payments to employees by controlling shareholder			317		317
Total transactions with owners	1	73,999	317	(74,000)	317
BALANCE AS OF DECEMBER 31, 2010	6	250,601	10,898	113,713	375,218

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

AIG ISRAEL INSURANCE CO. LTD.

STATEMENTS OF CASH FLOWS

	Year ended December 31		
	2012	2011	2010
	ILS in thousands		
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net cash provided by operating activities (Appendix A)	(15,557)	43,858	8,882
Interest received	40,660	36,198	36,106
Dividend received	3,680	3,488	4,343
Income taxes paid	(25,021)	(31,274)	(39,159)
Net cash provided by operating activities	3,762	52,270	10,172
CASH FLOWS FROM INVESTING ACTIVITIES:			
Changes in asset cover for equity and noninsurance liabilities:			
Acquisition of property and equipment	(2,916)	(1,524)	(7,575)
Proceeds from sale of property and equipment	-	-	110
Acquisition of intangible assets	(11,202)	(5,352)	(5,804)
Net cash used in investing activities	(14,118)	(6,876)	(13,269)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(10,356)	45,394	(3,097)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	103,562	59,879	63,078
EFFECT OF CHANGES IN EXCHANGE RATE ON CASH AND CASH EQUIVALENTS	334	(1,711)	(102)
CASH AND CASH EQUIVALENTS AT END OF PERIOD	93,540	103,562	59,879

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

AIG ISRAEL INSURANCE CO. LTD.

STATEMENTS OF CASH FLOWS

	Year ended December 31		
	2012	**2011**	**2010**
	ILS in thousands		
APPENDIX A - CASH FLOWS FROM OPERATING ACTIVITIES:			
Income before taxes on income	243,768	67,306	85,700
Adjustments with respect to:			
Income and expenses not involving cash flows:			
Loss arising on disposal of property and equipment			59
Increase in liability with respect to nonprofit participating insurance contracts	(35,688)	43,223	49,928
Increase in deferred acquisition expenses	(11,533)	(18,353)	(12,062)
Benefit component in capital instruments granted to employees and other benefits	-	186	317
Increase in liability for employee rights upon retirement, net	279	(65)	287
Depreciation of property and equipment	4,775	5,371	5,473
Depreciation of intangible assets	5,453	4,322	3,136
Losses (gains), net on realization of financial investments:			
Marketable debt instruments	(40,324)	(3,379)	(13,691)
Nonmarketable debt instruments	(1,072)	(2,606)	(2,926)
Marketable shares	(2,823)	19,966	(7,453)
Marketable basket certificates	(9,341)	160	(3,501)
Influence of fluctuation in exchange rate on cash and cash equivalents	(334)	1,711	102
	153,160	117,842	105,369
Changes in operating assets and liabilities:			
Liabilities towards reinsurers	43,074	13,920	30,635
Investments in financial assets net	(160,121)	(41,491)	(92,239)
Premiums collectible	(17,942)	(7,158)	(9,389)
Receivables	(2,813)	(1,651)	3,306
Payables	13,425	2,082	9,117
Current tax liabilities	-	-	2,532
	(124,377)	(34,298)	(56,038)
Adjustments with respect to interest and dividend received:			
Interest received	(40,660)	(36,198)	(36,106)
Dividend received	(3,680)	(3,488)	(4,343)
Net cash provided by operating activities	(15,557)	43,858	8,882

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

SUPPLEMENTARY INFORMATION ON FINANCING ACTIVITIES NOT INVOLVING CASH FLOWS -			
issuance of bonus shares	-	-	74,000

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

NOTE 1 - GENERAL

AIG Israel Insurance Company Ltd (hereinafter "the company") was incorporated in Israel on March 27, 1996 as a private, limited liability company. The company commenced its insurance activity in May 1997. The Company has no activities outside to Israel through branches and subsidiaries.

The ultimate parent company is the American International Group Inc. (hereinafter: global AIG), holding 50% of its ordinary shares and 51% of its preferred shares, and 50% of ordinary shares and 49% of preferred shares are held by Aurec group ("Aurec").

In February 2010, the company's shares, which were held through that date directly by AIG were transferred to Chartis Overseas ("CO"), which is an insurance company in the global AIG Corporation.

In January 2013, CO reached in agreement with Aurec, for CO to purchase Aurec's holdings in the company, subject to specific conditions being met. As of the date of signing this Financial Statements, these conditions have yet been met, accordingly ownership of the Company remains as described aboove.

The registered office of the company is 25 Hasivim St., Petach Tikva, Israel.

Definitions:

1) Supervisor Supervisor of Insurance (Commissioner of the Capital Market, Insurance and Savings at the Israel Ministry of Finance).

2) CPI - The consumer price index published by the Israeli Central Bureau of Statistics.

3) Known CPI - The CPI known at the end of the month.

4) Related parties - as defined in IAS 24 "Related Party Disclosures".

5) Life insurance fund - Actuarial fund calculated in accordance with the principles generally accepted for this purpose in Israel.

6) Unexpired risks fund - Funds calculated in accordance with the Regulations for Calculation of General Insurance Funds.

7) Surplus reserve* - The accumulated surplus of income over expenses (comprising premiums, acquisition costs, claims and part of the incomes from investments, all net of the reinsurers' share for the relevant underwriting year), as calculated in accordance with the Regulations for Calculation of General Insurance Funds, less a provision for unexpired risks and less outstanding claims.

   (*) The balance sheet includes the surplus reserve under the "liabilities in respect of nonyield dependent insurance contract and investments".

8) Outstanding claims - Known outstanding claims, with the addition of the expected growth 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).

9) Details of account regulations Supervision of Insurance Businesses (Details of account) Regulations, 1998.

NOTE 1 - GENERAL (continued):

10) Investment Method Regulations - The Supervision of Insurance Business Regulations (Investment Methods in Capital, Reserves and Liabilities of the Insurer), 2001 as amended.

11) Shareholders' Capital Regulations - The Supervision of Insurance Business Regulations (minimum shareholders' equity required from an insurer), 1998 and amendments as amended.

12) Account Segregation Regulations in Life Insurance - The Supervision of Insurance Regulations (Method of Segregation of Accounts and Assets of Insurer in Life Insurance), 1984.

13) 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 as amended.

14) 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.

15) 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.

16) Liability for insurance contracts - Insurance reserves and outstanding claims in general insurance.

17) Premium - Premium including fees.

18) The expression, ‘premiums earned,’ refers to premiums that relate to the period under review.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES:

a. Basis of presentation of financial statements

The Company's financial statements as of December 31, 2012 and 2011 and for each of the three years in the period ended December 31, 2012, are in compliance with International Financial Reporting Standards, which are standards and interpretations issued by the International Financial Reporting Interpretations Committee (IASB) (hereafter – IFRS) and include the disclosure requirements set in accordance with the Supervision Law and regulations promulgated thereunder.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

a. Basis of presentation of financial statements (continued):

Unless otherwise stated, the significant accounting policies described below have been applied on a consistent basis in relation to all the years presented.

The financial statements have been prepared under the historical cost convention according to International Accounting Standard No. 29, 'Financial Reporting in Hyperinflationary Economies' ("IAS 29" , subject to such adjustments as were required with respect to the revaluation of severance pay plan assets and financial assets and liabilities at fair value through profit or loss for the purpose of presenting those assets and liabilities at fair value, and subject also to the comments set out below with respect to the period during which the Israel economy was affected by hyperinflation.

The preparation of financial statements under IFRS, and especially the financial statements of an insurance company, requires management to make certain significant accounting estimates. It is also required that management exercise discretion in the process of applying the accounting policies of the Company. The principal assumptions used in the preparation of the Company's financial statements are based on actuarial estimates. Actual results could differ significantly from those derived from the use of estimates and assumptions by management. For information relating to those areas where management is required to make significant accounting estimates or exercise a significant degree of discretion in relation to accounting matters, see Note 3.

b. Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decisionmaker in the Group. The chief operating decisionmaker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the company management that makes strategic decisions.

c. Translation of balances and transactions denominated in foreign currency:

1) Functional currency and presentation currency

Items reflected in the financial statements of the Company are measured in New Israel Shekels, which is the currency of the principal economic environment in which the Company operates ("the functional currency"). The financial statements of the Company are also presented in New Israel Shekels, since this is also the presentation currency of the Company.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

c. **Translation of balances and transactions denominated in foreign currency** (continued)**:**

1) Functional currency and presentation currency (continued):

The table below sets out the changes in the exchange rate of the U.S. dollar and the Consumer Price Index during the course of the periods under review:

	Exchange rate of dollar	Consumer Price Index (last known index)	Consumer Price Index (index for particular month
		%	
Year ended December 31, 2012	(2.3)	1.4	1.6
Year ended December 31, 2011	7.7	2.5	2.2

As of December 31, 2012, the exchange rate of the U.S. dollar was $1 ILS 3.733.

2) Transactions and balances

Transactions denominated in currencies other than the functional currency (“foreign currency”) are translated into the functional currency by means of the exchange rate prevailing on the date of the transaction. The statement of income is charged or credited with exchange rate differentials stemming from the settlement of accounts relating to the above transactions and from the translation of monetary assets and liabilities denominated in a foreign currency at the rates of exchange prevailing at the end of the period.

Translation differences with respect to financial assets which are not monetary items, such as equity securities (examples of which are shares and options), and which are classified as financial instruments at fair value through profit or loss, are recognized in the statement of comprehensive income as part of the gain or loss arising on changes in their fair value under "net investment income and financing income".

Income or loss arising from change in exchange rate and related to deposits and nonmarketable securities are also recognized in comprehensive income under "net investment income and financing income".

Income or loss arising from other changes in exchange rates are presented in comprehensive income under "financing expenses".

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

d. Property and equipment

Property and equipment is initially reflected in the accounting records at the cost of acquisition. Subsequent costs incurred are either added to the carrying value of the asset in question or recognized as a separate asset, as appropriate, only if it may be expected that the future economic benefits attributable to the item will flow to the Company and that the cost of the asset may be reliably measured. If part of the item of property and equipment is replaced, the carrying value of that part is eliminated from the accounting records. All other repair costs, as well as maintenance expenses, are charged against income as incurred.

Property and equipment are presented at cost after deduction of accumulated depreciation and impairment losses. The historic cost includes costs directly attributable to the purchase of the asset.

Writedowns and impairments of value relating to property and equipment presented at cost are charged to the statement of comprehensive income.

Depreciation is computed by means of the straightline method in order to arrive at a residual value after depreciation of the cost or revalued amount of the asset over its estimated useful life, as follows:

	Annual depreciation rate
	%
Computers and communications equipment	20 - 33
Furniture and office equipment	7 - 15

Improvements to leasehold premises are amortized by means of the equal depreciation method over the shorter of the contractual period of the lease and the estimated life of the improvements.

The residual values and useful lives of assets are subject to review, and if necessary, adjustments as of each balance sheet date.

Should the carrying value of an asset be greater than its estimated recoverable value, the resultant impairment of value stemming from the reduction of the carrying value to the level of the recoverable value is recognized immediately (see paragraph (f) below).

Gains or losses on the realization of assets are determined by means of a comparison between the carrying value of the asset and the consideration received for it, and are recognized in other income in profit or loss.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

e. Intangible assets (software)

Software licenses acquired are capitalized on the basis of the actual costs incurred in the acquisition of the specific software and in the preparation of that software for use. These costs are amortized under the straightline method on the basis of the estimated useful life of the asset (from three to five years).

Costs relating to the development or maintenance of software are recognized as expenses as incurred. If costs directly related to the development of unique identifiable software products, over which products the Company exercises control, are expected to produce economic benefits during the course of a period exceeding one year in an amount that exceeds the level of the related costs, then those costs are recognized as an intangible asset.

Software development costs recognized as assets are amortized by means of the straightline method over the estimated useful life of the asset (which will not, in any event, exceed three years).

f. Impairment in value of nonmonetary assets

If an event or change in circumstances occurs that indicates that the carrying value of a depreciable asset exceeds the recoverable value of that asset, the Company undertakes a review of the decline in value of the asset in question. The amount of the recognized impairment loss is equivalent to the amount by which the carrying value of the asset exceeds the recoverable value thereof. The recoverable amount of an asset is the higher of the fair value of that asset, after deduction of selling costs, and the usage value of the asset. For the purpose of impairment reviews, assets are grouped by reference to the lowest possible level at which separate cash flows can be identified (cashgenerating units). At each balance sheet date, nonmonetary assets which have suffered impairments in value are reviewed for the purpose of determining whether or not any previouslyrecognized impairments of value can be reversed.

g. Financial assets:

1. Classification

The Company classifies its financial assets as either financial assets at fair value through profit or loss or as loans and receivables. The classification is determined by reference to the purpose for which the assets were acquired. Management determines the classification of financial assets on the date of their initial recognition.

a) Financial assets at fair value through profit or loss

This category is comprised of two subcategories - financial assets held for trading purposes and financial assets designated to be measured at fair value through profit or loss. A financial asset is placed in this category if it has been acquired principally for the purpose of sale in the short term or if management has specifically placed the asset in the category, otherwise they are classified as noncurrent assets.

Derivative financial instruments are also categorized as assets held for trading purposes, unless they are designed for hedging purposes. Assets are classified to current assets in cases where they are held for trading or expected to be disposed of within one year from the date of statement of financial position.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

b) Loans and receivables

Loans and receivables are nonderivative financial assets, marked by payments that are either fixed or capable of being fixed and which are not quoted in an active market. The loans and receivables of the Company are reflected in the balance sheet items, other receivables, premiums collectible, nonmarketable debt instruments and cash and cash equivalents.

2. Recognition and measurement

Ordinary purchases and sales of financial assets are recorded on the date of completion of the transaction, this being the date on which the asset is transferred either to or by the branch. The investment in all financial assets that are not presented at fair value through profit or loss is initially recognized in an amount equivalent to the sum of the fair value of the assets and the related transaction costs. Financial assets that are presented at fair value through profit or loss are initially recognized at fair value, with transaction costs being charged against proft or loss. Financial assets are eliminated from the balance sheet when the rights to the related cash flows have either expired or been transferred, and the Company has, in addition, transferred all the risks and rewards stemming from the ownership of those assets. Financial assets at fair value through profit or loss are presented in subsequent periods at fair value. Loans and receivables are presented at amortized cost as computed by means of the effective interest method.

Gains or losses stemming from changes in the fair value of financial assets at fair value through profit or loss are presented under investment income (loss), net in the statement of comprehensive income for the period in which the gains or losses accrued. Dividend income from financial assets at fair value through profit or loss is recognized in the statement of comprehensive income under investment income, net and financing income insofar as the Company is entitled to this income.

The fair value of financial instruments quoted in an active market is based on the current selling price of those instruments. If the financial asset is traded in a market that is not active, or if the instrument is not listed for trading, the Company uses a variety of valuation methods for determining the fair value. These methods include a reliance on recent transactions carried out under market conditions, a reliance on other instruments the principal characteristics of which are similar to those of the instrument being valued, an analysis of capitalized cash flows, and the use of option pricing models that are based primarily on market data and as little as possible on data specific to the Company itself.

As to the fair value of financial assets measured at fair value, see note 10.

3. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

4. Impairment of assets presented at amortized cost

The Company assesses at the each statement of financial position date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Company uses to determine that there is objective evidence of an impairment loss include:

- Significant financial difficulty of the issuer or obligor;
- A breach of contract, such as a default or delinquency in interest or principal payments;
- The Company, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
- It becomes probable that the borrower will enter bankruptcy or other financial reorganization;
- The disappearance of an active market for that financial asset because of financial difficulties; or

- Observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:
  (i) Adverse changes in the payment status of borrowers in the portfolio; and
  (ii) National or local economic conditions that correlate with defaults on the assets in the portfolio.

The Company first assesses whether objective evidence of impairment exists.

The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The asset's carrying amount of the asset is reduced and the amount of the loss is recognized in the consolidated income statement. If a loan or heldtomaturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the group may measure impairment on the basis of an instrument's fair value using an observable market price.
If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the debtor's credit rating), the reversal of the previously recognized impairment loss is recognized in the statement of comprehensive income.

The assessment of receivable balances for impairment is described in section h. below.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

h. Premiums collectible

Premiums collectible are initially recognized at fair value and subsequently measured at amortized cost as computed by means of the effective interest method after deduction of the provision for doubtful debts. A provision for doubtful debts is created when objective evidence exists to the effect that the Company is unable to collect all the outstanding debts receivable under the original terms. Significant financial difficulties of the debtor, a likelihood that the debtor will declare bankruptcy or undertake a restructuring exercise, and insolvency or arrears in payments are all regarded as indicators of an impairment of value of a debt. The carrying value of the debt is reduced by means of a provision account, with the amount of the loss being recognized in the statement of income. When the debt of a customer is not collectible, that debt is written off against the provision for doubtful debts. The payment in a subsequent period of a debt that was previously written off is credited to the statement of income.

i. Cash and cash equivalents

Cash and cash equivalents include cash in hand, shortterm bank deposits, and other shortterm highlyliquid investments with maturity dates not exceeding three months from the date of the investment.

j. Share capital

Ordinary shares and preferred shares of the company are classified as share capital.

k. Trade payables

Outstanding trade payables are initially recognized at fair value and subsequently measured at amortized cost as computed by means of the effective interest method.

l. Liabilities towards reinsurers and payables

Outstanding liabilities towards reinsurers and outstanding payables are initially recognized at fair value and subsequently measured at amortized cost as computed by means of the effective interest method.

m. Current and deferred taxes

The tax expense for the period is comprised of current taxes, deferred taxes and taxes relating to prior years. Taxes are recognized in the statement of comprehensive income, except for taxes related to items charged to other comprehensive income or directly to equity, which are also recognized in the statement of comprehensive income, respectively together with the item in respect of which they were created. The current income tax charge is calculated on the basis of the tax laws enacted or substantially enacted at the statement of financial position date in the counties where the company's subsidiaries and associates operate and generate taxable income. Management periodically evaluates the tax aspects applicable to its taxable income, in accordance with the relevant tax laws and establishes provisions where appropriate.

The Company recognizes deferred taxes by means of the liability method for all timing differences as between the amounts of assets and liabilities as presented in the financial statements and the equivalent amounts as computed for tax purposes. The above notwithstanding, deferred taxes are not recognized if the timing differences are created upon initial recognition of an asset or liability, if, upon the date of the transaction, the asset or liability did not affect the profit or loss, either for accounting purposes or for tax purposes.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

The deferred tax provision is computed by reference to the rates of tax expected to be in force at the time of realization of the deferred tax asset or at the time of settlement of the deferred tax liability, insofar as the legislation with respect to these tax rates and other taxing legislation has, as at the date of the balance sheet, already passed into law. The above notwithstanding, the deferred tax provision will be similarly computed if the legislative procedures in relation to proposed legislation have, as at the date of the balance sheet, been substantially completed.

Deferred tax assets are recognized for timing differences that may serve to reduce the tax expense, provided that the deferred tax assets may be expected to be capable of being utilized against future chargeable income.

Deferred income tax assets and liabilities are offset only if:

- There is a legally enforceable right to offset current tax assets against current tax liabilities; and
- When the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

n. Employee benefits:

1) Liability for severance and pension payments

Pension plans

The Company operates a number of pension schemes which are generally financed through payments transferred to insurance companies (under arrangements with respect to managers' insurance policies) or to trusteeadministered pension funds. These schemes constitute defined contribution plans, insofar as the Company makes regular deposits to a separate and independent entity. If the assets of a fund do not cover the payments due to all employees in respect of accrued benefits for the present and earlier periods, the Company is under no obligation, either implied or constructive, to make any further deposits with that fund.

Liability with respect to severance pay

In accordance with the provisions of Israel labor laws and agreements, and in accordance with the Company's prevailing practice, the Company is required to make severance payments to employees who are dismissed or who retire from their employment in certain circumstances. The Company's obligation to make severance payments is covered, for some employees, by a defined benefit plan and, for other employees, by a defined contribution plan.

In relation to the Company's obligation to those employees covered by a defined benefit plan, the benefits receivable by an employee entitled to severance pay upon retirement are based upon the number of years of service and the final salary.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

n. Employee benefits (continued):

1) Liability for severance and pension payments (continued):

The Company's obligation with respect to the remainder of its employees who are covered by a defined contribution plan is met by regular deposits with a separate and independent entity. If the assets of a fund do not cover the payments due to all employees in respect of accrued benefits for the present and earlier periods, the Company is under no obligation, either implied or constructive, to make any further deposits with that fund.

The severance pay liability presented in the balance sheet is the present value of the defined benefit liability as of the date of the balance sheet, after deducting the fair value of the plan assets. The defined benefit liability is measured on an annual basis by independent actuaries by means of the projected unit credit method.

The present value of the defined benefit liability is computed by discounting expected future cash flows, after taking into consideration the expected rate of salary increases. The computation is based on the prevailing interest rates for government debentures denominated in the currency in which the benefits are to be paid, insofar as the period prior to the date of repayment of those debentures resembles the period remaining before actual payment of the severance pay liability is due.

Under the provisions of International Accounting Standard No. 19, 'Employee Benefits' ("IAS 19"), the discount rate used in the computation of the actuarial liability is determined by reference to the market returns as of the balance sheet date of high quality corporate debentures. The above notwithstanding, IAS 19 notes that, in those countries where there is no deep market in debentures of this kind, use should be made of the market returns on government debentures as of the date of the balance sheet.

As stated above, the interest rate used by the Company for the purpose of discounting anticipated future cash flows in order to compute the actuarial liability is based on the prevailing interest rates of highlyrated government debentures, because, in the opinion of management, there is no deep market in industrial debentures in Israel.

The Company credits or charges to the statement of income in the period in which they arise, those actuarial gains or losses which stem from changes to actuarial valuations and from the difference between previous assumptions and actual results.

Costs relating to past services are recognized in the statement of income on a regular basis, unless the changes in the plan are conditional upon the employees remaining in their positions for the duration of a defined period (the training period). In this case, the costs attributable to past services are amortized by means of the straightline method over the course of the training period.

Severance pay funding is measured by reference to fair value.
The funding referred to above constitutes plan assets as that term is defined by IAS 19, and is accordingly offset against the liability for employee rights upon retirement for balance sheet presentation purposes.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

n. Employee benefits (continued):

As stated above, the Company purchases insurance policies and makes deposits with pension and severance pay funds in recognition of its liability to make pension payments to all employees and severance payments to some of its employees under the terms of its defined contribution plans. Upon making the deposits, the Company is not committed to the making of any further payments. The deposits are recognized as employee benefit expenses as incurred. Deposits made in advance are treated as an asset, provided that the deposits are refundable in cash or alternatively, that future payments are reduced accordingly

2) Vacation and rest and recreation pay

Every employee is entitled by law to paid days of vacation and rest and recreation pay, both calculated on an annual basis. The degree of entitlement is based on the length of service. The Company makes provision for vacation and rest and recreation pay on the basis of the accumulated entitlement of each employee.

3) Sharebased payment

The worldwide AIG concern operates a number of schemes for sharebased payment to Company employees, which payment is settled by means of equity instruments of the AIG worldwide concern. Under the terms of the schemes, previously awarded to employees, options and restricted stock units (“RSUs”) for the acquisition of shares of the worldwide AIG concern. The fair value of the services provided by the employees in consideration for the grant of the options and the RSUs is recognized as an expense in the statement of income over the course of the appropriate vesting period, with an equivalent amount being credited to a capital reserve presented under shareholders’ equity. The total amount recognized as an expense over the period of vesting is determined by reference to the fair value of the options and RSUs granted as of the date of the grant, excluding that part of the fair value attributable to the effect of nonmarket vesting conditions, such as, for example, compliance with profitability goals. Nonmarket vesting conditions are included amongst the factors considered when estimating the number of options and RSUs expected to vest. At each balance sheet date, the Company reviews its estimate of the number of options and RSUs expected to vest, and accordingly recognizes the effect of the change of estimate (in comparison with the original estimates, if any) in income, with a corresponding entry being made in shareholders’ equity.

4) Bonus schemes

The Company recognizes bonuses as a liability and an expense if required to do so by virtue of a contractual obligation or where previous practice with respect to the payment of bonuses has created an implied obligation to make such payments and at least one of the following conditions is met:

(a) The formal terms and conditions of the plan include a formula for determining the benefit;
(b) The company sets the amounts to be paid prior to approving the financial statements for publication;
(c) A pattern of past activity provides clear evidence for the amount of implied obligation of the company.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

o. Provisions

Provisions are made for legal claims that are not recognized insurance claims when the Company has an existing legal or constructive obligation arising out of past events, when it is expected that Company resources will be required in order to settle the obligation, and when the amount of the obligation can be reliably estimated. The Company does not recognize provisions for future operational losses.

Should a number of similar obligations exist, the likelihood that Company resources will be required in order to settle the obligations is assessed by means of a consideration of the group of obligations as a whole. A provision is recognized even if the likelihood of Company resources being required to settle each of the individual obligations in the group is low. Provisions are measured by reference to the present value of the projected cash flows required to settle the obligation. The present value is computed through the use of such pretax discount rate as reflects current market evaluations of both the time value of the money involved and the specific risks associated with the obligation. An increase in the provision that is caused by the passage of time is treated as an interest expense.

As to insurance claims, see r below.

p. Revenue recognition:

1) Premiums

   Premiums stemming from general insurance business are recorded as income as and when they appear on monthly yield reports. Premiums stemming from life assurance business are recorded as income as and when they fall due under the terms of the relevant policy. Revenues from gross premiums together with related changes in unearned premiums are recorded under premiums earned, gross.

   Premiums stemming from policies that commence after the date of the balance sheet are recorded as prepaid income.

   The income reflected in the financial statements takes account, subject to the provisions of any law, of policies that have been cancelled by policyholders and of cancellations and provisions stemming from the nonpayment of premiums. Premiums, commission and claims arising from underwriting pools and joint insurance are recorded on a proportionate basis in accordance with the rate of the Company's participation in the relevant contracts.

   Compulsory vehicle insurance premiums are recognized upon paying the premium since coverage is conditioned on paying the premium.

2) Income from investments, net and financing income:

   a. Interest received is recognized on a periodic basis in accordance with the effective interest method.
   b. Dividend income is recognized when the Company becomes entitled thereto.

q. Dividend distribution

A dividend payable to Company shareholders is recognized in the Company's financial statements as a liability in the period in which the dividend is approved by the Company in general meeting.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts

International Financial Reporting Standard No.4, 'Insurance Contracts' ("IFRS 4"), exempts an insurer from the requirement to apply the provisions of International Accounting Standard No. 8, 'Accounting Policies, Changes in Accounting Estimates and Errors' ("IAS 8"), with five exceptions, when formulating its accounting policy with respect to insurance contracts. IAS 8 determines, inter alia, the manner in which accounting policy shall be formulated in relation to transactions or events not covered by specific provisions of international financial reporting standards.The significant accounting policies and methods of computation relating to general insurance business and life assurance business used in the preparation of these financial statements were as follows:

1. General insurance:

a) Unexpired risk reserves, deferred acquisition expenses and pending claims are computed and presented in accordance with the general insurance reserve computation regulations.

In accordance with the instructions of the Supervisor of Insurance, the pending claims reflected in the financial statements in relation to particular insurance sectors (comprehensive household insurance, car damages insurance, compulsory car insurance, employer's liability insurance, third party, professional liability, product warranty, loss of property and engineering insurance) are valued by an actuary, Ms. Avital Kohler, who has reported that she has valued the pending claims in accordance with the provisions of the supervision law, the instructions of the Supervisor of Insurance, and generallyaccepted actuarial principles as of the date of the financial statements, and that, to the best of her knowledge and in accord with her best assessment, the provision for pending claims constitutes a provision that is sufficiently adequate for the purpose of covering the Company's liabilities with respect to the claims pending in the abovementioned sectors, both in total and in relation to each sector considered separately.
The actuarial valuations relate to claims in gross terms and to claims as they relate to the retained portion of the insurer's operations.

In addition, in accordance with the general insurance reserve computation regulations, in the compulsory motor vehicle and other liability sectors, the accumulation must be maintained for the period of three years commencing with the year in which the policies were issued and it must be computed in the manner prescribed by the regulations and circulars of the Supervisor of Insurance.

In accordance with a circular of the Supervisor of Insurance, as of 2007, the accumulation must incorporate investment income at a fixed annual real rate of 3%, without reference to the actual returns obtained, this being a change from the manner in which investment income was reflected in the accumulation in years prior to 2007. The above notwithstanding, the above circular also determined that the opening balance of the accumulation as of January 1, 2007, as reflected in the Company's accounting records and computed in accordance with the method prevailing prior to 2007, should not be changed.

According to an approval by the Supervisor, prior to 2012, the company has maintained in the compulsory vehicle business an surplus reserve of five years compared to three years, as is the practice in the industry. Beginning in 2012, in accordance with an agreement with the Supervisor of Insurance and in view of the company's experience with actuary computations in this sector, the company maintains a three-year surplus reserve, according to practice in the industry. This change has reduced the payment and

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts (continued):

1. General insurance (continued):

change in liabilities for gross insurance contracts, and increased the pre-tax income by ILS 79.3 million, and increased profit for the period and comprehensive income for the period by ILS 51.3 million.

In accordance with instructions received from the Supervisor of Insurance, if, in any particular sector, the balance of the accumulation before the share thereof attributable to reinsurers is lower than the above accumulation balance after adjustment with respect to the share thereof attributable to reinsurers, then the share of the above accumulation attributable to reinsurers shall be reflected in the balance sheet under 'liabilities with respect to insurance contracts and nonprofit participating investment contracts' instead of under 'reinsurance assets.'

b) Provision for indirect costs incurred in the settlement of pending claims

In accordance with the provisions of IFRS 4, the provisions for pending claims also incorporate a provision for indirect costs incurred in the settlement of claims.

c) In relation to sectors discussed in subparagraph 1a above, except for sectors with no statistical significance, IBNR and IBNER provisions have been computed on an actuarial basis. In relation to other sectors, IBNR and IBNER provisions have been computed by reference to past experience and in accordance with statistical computations prescribed by the Supervisor of Insurance.

d) The total of the subrogated claims appearing in the balance sheet does not exceed the amount which, in the opinion of management, is collectible.

e) As to revenue recognition, see p above.

f) That part of the commission and other acquisition expenses which relates to unearned premiums stemming from the retained portion of the Company's business is transferred to succeeding reporting periods as deferred acquisition expenses. These expenses are computed, for each individual sector, by reference to the lower of, on the one hand, the actual expenses incurred and, on the other hand, the percentage of the unearned premium, the percentage in question being determined by the standard rates specified by the supervision regulations.

g) The acquisition costs of policies, the underwriting periods for which have not yet commenced, are recognized in the statement of income for the year in which their underwriting period commences and not in the statement of income for the year under review.

h) The unexpired risk reserve, presented under 'liabilities with respect to insurance contracts and nonprofit participating investment contracts,' is comprised of unearned premiums which are not actuarially computed and which are not subject to any assumptions whatsoever. This reserve reflects insurance premiums relating to the period of insurance commencing after the date of the balance sheet.

i) In accordance with the instructions of the Supervisor of Insurance, the reserve shall contain, if so required, a provision for anticipated losses (premium shortfall), computed on the basis of an actuarial valuation.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts (continued):

2. Life assurance:

a) In accordance with the provisions of the life assurance segregation of accounts regulations, the Company manages its life assurance business as a separate operation and segregates the assets relating thereto.

b) As to revenue recognition, see p above.

c) Life assurance reserves, the portion of those reserves attributable to reinsurers, and deferred acquisition costs have been computed by the Company's actuary, Ms. Michal Burger, who has reported that the amounts in question ("the amounts") were based on Company data, the accuracy and completeness of which she has reviewed. Ms. Burger has also reported that the amounts were computed in accordance with accepted actuarial methods and the data utilized by the Company in connection with its insurance plans. The computational principles involved were consistent with those of the previous year.

In accordance with the provisions of the 'details of report' regulations, the deferred acquisition costs of new life assurance policies include those general and administrative expenses that relate to the acquisition of new policies. Under these provisions, the deferred acquisition costs are amortized in equal annual installments over the shorter of fifteen years and the period of the policy. In addition, a special amortization expense is recorded in order to ensure that the deferred acquisition costs do not exceed the amount that may be covered by future income. In accordance with the Company's actuarial declaration, the deferred acquisition costs for policies issued since May 1999, treated as an asset in the Company's accounting records, are expected to be covered by future income.

s. Earnings per share

As a general rule, the computation of basic earnings per share is based on the profit distributable to Ordinary shareholders. The profit is divided by the weighted average number of Ordinary shares in issue during the course of the period.

t. Reclassifications

Certain comparison figures have been reclassified in these financial statements. The said classifications do not have effect on the company's assets and liabilities as of the beginning of 2009.

u. Details of the provisions of new standards and of amendments to existing standards, which came into effect and are mandatory for reporting periods starting January 1, 2012:

Amendment to IFRS 7 – "Financial Instruments – Disclosure" (hereafter – Amendment to IFRS 7)
The amendment to IFRS 7 expands the disclosure requirements relating to financial assets transferred to another entity but which continue to be included in the company's statement of financial; the amendment also expands the disclosure requirements regarding the associated financial liabilities, including the relationship between the said assets and liabilities. In addition, the amendment to IFRS 7 expands the disclosure requirements applicable to financial assets that were derecognized but in respect of which there is an exposure to certain risks and rewards related to the transferred asset.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

v. **Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the company**

a) IFRS 9 - "Financial Instruments" (hereafter - IFRS 9).

The first part of IFRS 9, dealing with the classification and measurement of financial assets, was issued in November 2009 (hereinafter first part of IFRS 9) and the second part of IFRS 9, which includes guidance on financial liabilities and derecognition of financial instruments was issued in 2010. IFRS 9 replaces certain parts of IAS 39 "Financial Instruments: Recognition and Measurement" (hereinafter IAS 39) relating to the classification and measurement of financial instruments. IFRS 9 requires that financial assets will be classified into one of the following two categories: financial assets measured after initial recognition at fair value and financial assets measured after initial recognition at amortized cost. The decision on classification is made on the date of initial recognition, based on the entity's business model and the characteristics and the projected contractual cash flows from the asset. As to financial liabilities, IFRS 9 retains most guidance of IAS 39, with the main change being that entities with financial liabilities designated at fair value through profit or loss (FVTPL) recognize changes in the fair value due to changes in the liability's credit risk (own credit risk) directly in other comprehensive income (OCI), unless this creates an accounting mismatch. As to amounts recognized as above in other comprehensive income, the income or loss will not be recycled. However, it is possible to transfer accumulated income or loss between equity items.

In December 2011, an amendment to IFRS 9 and IFRS 7 "Financial Instruments: Disclosures" (hereinafter the amendment). The amendment deferred the mandatory effective date of the IFRS 9 and the transition provision for implementation, and added certain disclosure requirements for the transition (hereinafter the additional disclosures).

According to IFRS 9 after the amendment, both parts of IFRS 9 will apply to annual periods commencing on January 1, 2015 and thereafter. Entities can elect to early adopt IFRS 9, but it is not permitted to adopt early the second part of IFRS 9 without implementing the first part of IFRS 9 on the same date. On the other hand, it is possible to early adopt the first part of IFRS 9 without being required to implement the second part of IFRS 9 on the same date.

Under the transition provisions of IFRS 9 and since the company has not applied early adoption thereof to the annual reporting period ending December 31, 2012, upon application of IFRs 9 in the future, the company shall not be required to amend its comparative figures but shall be required to provide the additional disclosures.

b) IAS 1 (Amendment) "Financial Statements Presentation"
The amendment to IAS 1, which is part of the improvements document published in May 2012, clarifies the disclosure requirements for comparative information. According to the amendment, when an entity is required to present a third statement of financial position as required by IAS 1 (where applying accounting policy retrospectively, restating items in the financial statements or reclassifying financial statements items), the third statement of financial position should be as at the date of the beginning of the preceding period, and not the beginning of the earliest period, even if the financial statements of the entity present comparative information for earlier periods. Additionally, the third statement of financial position will be required only in cases where retrospective implementation, restatement or reclassification has material impact on the information included in the statement of financial position at the beginning of the preceding period. In such cases, an entity will not be required to present the notes relating to the statement of financial position as of the beginning of

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

u. Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the company (continued)**:**

the preceding period. However, when an entity prepares financial statements that include more than the minimum comparative information required under IFRS, it will have to present the notes relating to the additional financial statements that were included as part of the additional comparative information.

c) IFRS 13 - "Fair value measurement" (hereafter - IFRS 13).

IFRS 13, "Fair value measurement", aims to improve consistency and reduce complexity of fair value measurement by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The requirements do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs. IFRS 13 is to be applied to annual reporting period commencing on January 1, 2013 or thereafter. Early adoption is permitted, provided that the fact that the standard is early adopted is disclosed. IFRS 13 is applied prospectively commencing the beginning of the annual reporting period in which it is applied for the first time. It is not required to apply the disclosure requirements set in IFRS 13 to comparative figures relating to periods prior to first time application of the standard. The company/group is studying the expected effect of IFRS 13 on its financial statements and the timing of its application.

d) IAS 19 - "Employee Benefits" (hereafter - IAS 19 Amendment)

The amendment to IAS 19 makes changes to the recognition and measurement of defined benefit plans and termination benefit and to the disclosures for all employee benefits discussed in IAS 19. Set forth below is a summary of the key changes:

- "Actuarial gains and losses" are renamed "remeasurements" and will be recognized immediately in OCI. Actuarial gains and losses will no longer be deferred using the “corridor” approach or recognized in profit or loss.
- Pastservice costs will be recognized immediately in the period of a plan amendment; unvested benefits will no longer be spread over a futureservice period.
- Annual expense for a funded benefit plan will include net interest expense or income, calculated by applying the discount rate to the net defined benefit asset or liability. This will replace the "finance charge" and "expected return on plan assets" currently applied under IAS 19.
- The distinction between shortterm and longterm benefits for measurement purposes shall be based on when payment is expected, not when payment can be demanded.
- Any benefit that has a futureservice obligation is not a termination benefit. A liability for a termination benefit is recognized when the entity can no longer withdraw the offer of the termination benefit or recognizes any related restructuring costs.
- There are additional disclosure requirements compared with IAS 19 in its present version.

The amendment is effective for periods beginning on or after 1 January 2013. Earlier application is permitted. The amendment should be applied retrospectively, except for:

a) An entity needs not to adjust the carrying amount of assets (outside the scope of IAS 19) for changes in employee benefits costs that were included in the carrying amount before the date of initial application of the amendment.
b) Comparative information for the disclosures required in the amendment to IAS 19 about the sensitivity of the defined benefit obligation will not needed in financial statements for periods beginning before January 1, 2014.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

u. Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the company (continued)**:**

The company is studying the expected effect of IAS 19 on its financial statements and the timing of its application.

e) Amendment to IFRS 7 - "Financial Instruments: Disclosures" (hereafter - the Amendment to IFRS 7)

Amendment to IFRS 7 "Financial instruments: Disclosures". This amendment is part of the annual improvements project of the IASB published in October 2010. The amendment modifies some required quantitative and qualitative disclosures on the nature and scope of risks arising from financial instruments and clarifies the interaction between such qualitative and quantitative disclosures. The amendment will be implemented for annual periods beginning on or after January 1, 2011, and its firsttime implementation is not expected to have material impact on the financial statements of the company.

The company intends to apply the Amendment to IFRS 7 commencing January 1, 2012. The first time application is not expected to have a material effect on the company's financial statements.

f) Amendment to IAS 32 - "Offsetting of Financial Assets and Financial Liabilities" (hereafter - Amendment to IAS 32)

and Amendment to IFRS 7 - "Disclosures - Offsetting of Financial Assets and Financial Liabilities" (hereafter - Amendment to IFRS 7), which were issued in December 2011. The Amendment to IAS 32 does not change the existing model as part of IAS 32 - "Financial Instruments: Presentation" regarding offsetting of financial assets and financial liabilities (hereafter -offsetting); however, it clarifies that the right to setoff must be available today and legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy of the entity or any of the counterparties. The Amendment to IAS 32 also clarifies the cases where offsetting using gross settlement mechanisms will satisfy the criteria for offsetting by gross net settlement.

The Amendment to IFRS 7 adds disclosure requirements that focus on quantitative information about recognized financial instruments that are offset in the statement of financial position, as well as those recognized financial instruments that are subject to certain offsetting arrangements (irrespective of whether they are offset in the statement of the financial position).

The Amendment to IAS 32 will be applied retrospectively for annual reporting periods commencing on January 1, 2014 or thereafter; early adoption is permitted.

The Amendment to IFRS 7 will be applied retrospectively for annual reporting periods commencing on January 1, 2013 or thereafter and for interim reporting period within the said annual reporting periods.

NOTE 3 - SIGNIFICANT ACCOUNTING ESTIMATES AND AREAS OF DISCRETION

Estimates and areas of discretion are subject to constant reassessment on the basis of past experience and a consideration of the manner in which they are affected by the influence of other factors, these factors including expectations with regard to future events that are deemed to be reasonable in the light of existing circumstances.

Significant accounting estimates and assumptions

The Company formulates estimates and assumptions with respect to the future. By their very nature, it is rare for accounting estimates to be identical to actual results. Significant risk attaches to the implementation of material adjustments to the carrying value of assets and liabilities during the course of the coming financial year through the use of estimates and assumptions, as follows:

1) Actuarial estimates with respect to insurance liabilities

An actuarial evaluation is based on statistical estimates that contain an element of uncertainty. The statistical estimates are based on various assumptions that may not necessarily be realized. The assumptions employed for the purposes of the actuarial forecast affect the final level of the provision for insurance liabilities.

Accordingly, the actual cost of claims may be higher or lower than the statistical estimate. Previous assumptions may change in the light of new information that may be received. In cases like this, the provision will change in accordance with the change in assumptions and in the light of actual results, with the differences arising during the year under review being reflected in the statements of insurance business. Had the actuarial results been different by 10% compared with the estimates of the Company's actuary, the amount of the insurance liabilities would have been higher or lower by app. 100 million ILS.

2) Provisions for lawsuits

The Company recognizes provisions for lawsuits in its accounting records. The provisions are created at the discretion of management. In determining the amount of a provision, management considers the likelihood that cash resources will indeed be required to settle the liability in question. The level of a provision is also determined by management's estimate of the present value of the cash flows expected to be required to settle existing liabilities.

3) Testing for impairment of deferred purchase expenses in life insurance.

As discussed in note 2r, the company is testing whether the amount of DAC is more than the amount that can be covered by estimated future income from existing insurance contracts, and amortize DAC accordingly. This test requires the use of estimates on the amounts of expected revenue from existing insurance contracts, including an estimation of the useful life of the existing insurance policy portfolio.

The Company operates in a number of sectors relating to general insurance, in the health insurance sector and in the life assurance sector, as described below. A further segment covers investment operations involving the Company's equity.

NOTE 4 - OPERATING SEGMENTS

1. Life assurance sector

   The life assurance sector provides cover for life assurance risk only.

2. Health insurance sector

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

3. General insurance sector

   The general insurance sector encompasses the property and liability branches. In accordance with the directives of the Supervisor, the sector is divided into the following branches, viz. the compulsory car insurance branch, the car damages insurance branch, the apartment insurance branch, other property branches, other liability branches and the professional liability branch.

   - Compulsory car insurance branch

     The compulsory car insurance branch 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 consequence of the use of a motor vehicle.

   - Car damages insurance branch

     The car damages insurance branch 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.

   - Flats insurance sector
     The flats insurance sector focuses in providing coverage for damages caused to flats and includes coverage in respect of damages caused by earth quake.

   - Professional liability branch

     The professional liability branch 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, as well as cover to company directors and officers in relation to any unlawful act or omission committed or occurring whilst they were carrying out their duties, and Embezzlement loss coverage.

   - Property branches and miscellaneous

     Other property branches operate in sectors not connected with the motor vehicle or liability branches. Cover is principally provided with respect to property insurance, subcontractors and mechanical breakdown insurance.

   - Other liability branches

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

NOTE 4 - OPERATING SEGMENTS (continued):

	For year ended December 31, 2012				
	Life assurance	**Health insurance**	**General insurance**	**Not allocated to operating segments**	**Total**
	ILS in thousands				
Gross earned premiums	89,467	198,231	539,460		827,158
Premiums earned by reinsurers	(20,017)	(21,696)	(142,988)		(185,701)
Premiums earned retained amount	68,450	176,535	396,472		641,457
Investment income (Loss), net and financing income	165	9,806	54,425	32,843	97,239
Commission income	3,366	6,996	37,266		47,628
Total income	71,981	193,337	488,163	32,843	786,324
Increase in insurance liabilities and payments with respect to insurance contracts – gross	(30,624)	(79,215)	(293,851)		(403,690)
Share of reinsurers of increase in insurance liabilities and payments with respect to insurance contracts	10,107	6,946	135,737		152,790
Increase in insurance liabilities and payments with respect to insurance contracts relating to nonceded business	(20,517)	(72,269)	*(158,114)		(250,900)
Commissions and other acquisition expenses	(20,760)	(48,638)	(77,974)		(147,372)
General and administrative expenses	(26,780)	(32,216)	(83,082)		(142,078)
Financing income (expenses)	-	(187)	(3,255)	1,236	(2,206)
Proffit (loss) before tax	3,924	40,027	165,738	34,079	243,768

* As for reducing the period of "surplus reserve" compulsory vehicle sector, see note 2.r.1.a.

AIG ISRAEL INSURANCE CO. LTD.

NOTES TO FINANCIAL STATEMENTS (continued)

NOTE 4 - OPERATING SEGMENTS (continued):

	For year ended December 31, 2011				
	Life assurance	Health insurance	General insurance	Not allocated to operating segments	Total
	ILS in thousands				
Gross earned premiums	77,718	170,317	487,018		735,053
Premiums earned by reinsurers	(18,794)	(18,532)	(120,386)		(157,712)
Premiums earned retained amount	58,924	151,785	366,632		577,341
Investment income (Loss), net and financing income	(550)	*5,119	*31,021	*(10,257)	*25,333
Commission income	3,157	6,017	32,283		41,457
Total income	61,531	162,921	429,936	(10,257)	644,131
Increase in insurance liabilities and payments with respect to insurance contracts – gross	(14,340)	(75,842)	(339,767)		(429,949)
Share of reinsurers of increase in insurance liabilities and payments with respect to insurance contracts	5,016	5,860	108,537		119,413
Increase in insurance liabilities and payments with respect to insurance contracts relating to nonceded business	(9,324)	(69,982)	(231,230)		(310,536)
Commissions and other acquisition expenses	(13,351)	(45,137)	(72,918)		(131,406)
General and administrative expenses	(27,893)	(31,681)	(76,689)		(136,263)
Financing income (expenses)	-	*(211)	*(4,138)	*5,729	*1,380
Proffit (loss) before tax	10,963	15,910	44,961	(4,528)	67,306

* Reclassification

NOTE 4 - OPERATING SEGMENTS (continued):

	For year ended December 31, 2010				
	Life assurance	**Health insurance**	**General insurance**	**Not allocated to operating segments**	**Total**
	ILS in thousands				
Gross earned premiums	67,017	144,499	478,788		690,304
Premiums earned by reinsurers	(16,372)	(13,299)	(113,143)		(142,814)
Premiums earned retained amount	50,645	131,200	365,645		547,490
Investment income, net and financing income	(116)	*5,547	*37,793	*22,670	*65,894
Commission income	2,312	4,238	30,402		36,952
Total income	52,841	140,985	433,840	22,670	650,336
Increase in insurance liabilities and payments with respect to insurance contracts – gross	(19,264)	(58,887)	(338,878)		(417,029)
Share of reinsurers of increase in insurance liabilities and payments with respect to insurance contracts	5,868	2,637	92,578		101,083
Increase in insurance liabilities and payments with respect to insurance contracts relating to nonceded business	(13,396)	(56,250)	(246,300)		(315,946)
Commissions and other acquisition expenses	(11,722)	(36,365)	(78,016)		(126,103)
General and administrative expenses	(22,259)	(26,668)	(72,794)		(121,721)
Financing income (expenses)	-	*(77)	*(1,849)	1,060	*(866)
Proffit before tax	5,464	21,625	34,881	23,730	85,700

* Reclassification

NOTE 4 - OPERATING SEGMENTS (continued):

	December 31, 2012				
	Life assurance	Health insurance	General insurance	Equity and other liabilities	Total
	ILS in thousands				
Assets					
Intangible assets	-	-	-	15,732	15,732
Deferred acquisition expenses	-	1,510	55,217	73,464	130,191
Financial investments:					
Marketable debt instruments	-	120,241	715,068	264,337	1,099,646
Nonmarketable debt instruments	-	-	20,331	57,594	77,925
Shares	-	-	-	68,284	68,284
Other	-	-	53,802	39,685	93,487
Total financial investments	-	120,241	789,201	429,900	1,339,342
Cash and cash equivalents	6,929	16,795	19,816	50,000	93,540
Reinsurance assets	8,658	5,752	571,122	-	585,532
Premiums collectible	66	13,553	160,536	-	174,155
Other assets	895	-	32,773	16,885	50,553
TOTAL ASSETS	16,548	157,851	1,628,665	585,981	2,389,045
Liabilities					
Liabilities with respect to insurance contracts and nonprofit participating investment contracts	25,433	126,525	1,257,382	-	1,409,340
Other liabilities	11,457	12,081	370,186	8,877	402,601
TOTAL LIABILITIES	36,890	138,606	1,627,568	8,877	1,811,941

NOTE 4 - OPERATING SEGMENTS (continued):

	December 31, 2011				
	Life assurance	Health insurance	General insurance	Equity and other liabilities	Total
	ILS in thousands				
Assets					
Intangible assets	-	-	-	9,983	9,983
Deferred acquisition expenses	-	1,866	52,072	64,720	118,658
Financial investments:					
Marketable debt instruments	-	98,182	672,438	207,936	978,556
Nonmarketable debt instruments	-	-	31,343	27,516	58,859
Shares	-	-	-	50,934	50,934
Other	-	-	-	37,312	37,312
Total financial investments	-	98,182	703,781	323,698	1,125,661
Cash and cash equivalents	9,389	20,781	63,392	10,000	103,562
Reinsurance assets	8,125	4,779	512,891	-	525,795
Premiums collectible	(84)	12,255	144,042	-	156,213
Other assets	707	3,127	37,856	18,743	60,433
TOTAL ASSETS	18,137	140,990	1,514,034	427,144	2,100,305
Liabilities					
Liabilities with respect to insurance contracts and nonprofit participating investment contracts	21,881	120,828	1,242,581	-	1,385,290
Other liabilities	11,390	9,249	267,233	7,376	295,248
TOTAL LIABILITIES	33,271	130,077	1,509,814	7,376	1,680,538

NOTE 4 - OPERATING SEGMENTS (continued):

Additional information relating to general insurance segment

	For year ended December 31, 2012						
	Compulsory car insurance	**Car damages insurance**	**Apartments**	**Professional liability**	**Property branches and Miscellaneous (*)**	**Other liability branches (*)**	**Total**
				ILS in thousands			
Gross premiums	115,247	200,477	96,381	45,864	44,443	51,362	553,774
Reinsurance premiums	(1,616)	(115)	(15,683)	(38,227)	(42,987)	(43,348)	(141,976)
Premiums relating to nonceded business	113,631	200,362	80,698	7,637	1,456	8,014	411,798
Change in balance of unearned premiums relating to nonceded business	(5,992)	(6,736)	(3,273)	1,093	(24)	(394)	(15,326)
Premiums earned on nonceded business	107,639	193,626	77,425	8,730	1,432	7,620	396,472
Investment income, net and financing income	28,410	7,291	4,864	5,812	1,277	6,771	54,425
Commission income	-	-	2,623	11,369	10,662	12,612	37,266
Total income	136,049	200,917	84,912	25,911	13,371	27,003	488,163
Increase in insurance liabilities and payments with respect to insurance contracts	(1,966)	(127,957)	(25,399)	(22,602)	(28,183)	(87,744)	(293,851)
Share of reinsurers of increase in insurance l liabilities and payments with respect to insurance contracts	19,763	-	2,052	13,526	26,424	73,972	135,737
Increase in insurance liabilities and payments with respect to insurance contracts relating to non ceded business	**17,797	(127,957)	(23,347)	(9,076)	(1,759)	(13,772)	(158,114)
Commission, marketing expenses and other acquisition expenses	(11,868)	(23,894)	(11,112)	(12,899)	(8,241)	(9,960)	(77,974)
General and administrative expenses	(20,793)	(24,920)	(24,672)	(6,481)	(3,047)	(3,169)	(83,082)
Financing expenses	-	-	(84)	(1,169)	(288)	(1,714)	(3,255)
Total expenses	(14,864)	(176,771)	(59,215)	(29,625)	(13,335)	(28,615)	(322,425)
Profit (loss) before taxes on income	121,185	24,146	25,697	(3,714)	36	(1,612)	165,738
Gross liabilities with respect to insurance contracts as of December 31, 2012	578,753	126,232	53,900	185,635	57,578	255,284	1,257,382

(*) Property lines and other include mainly results from the property insurance sector, the operations of which constitute 86% of total premiums in these sectors. Other liability sectors include mainly results from the product liability insurance sector, the operations of which constitute 54% of total premiums in these sectors.

(**)As for reducing the period of "surplus reserve" compulsory vehicle sector, see note 2.r.1.a.

NOTE 4 - OPERATING SEGMENTS (continued):

Additional information relating to general insurance segment

	Compulsory car insurance	Car damages insurance	Apartments	Professional liability	Property branches and Miscellaneous (**)	Other liability branches (**)	Total
	For year ended December 31, 2011						
	ILS in thousands						
Gross premiums	104,074	182,504	87,437	49,173	36,286	46,106	505,580
Reinsurance premiums	(1,452)	(107)	(14,661)	(38,671)	(35,005)	(39,846)	(129,742)
Premiums relating to nonceded business	102,622	182,397	72,776	10,502	1,281	6,260	375,838
Change in balance of unearned premiums relating to nonceded business	(68)	(1,834)	(4,643)	(1,326)	(300)	(1,035)	(9,206)
Premiums earned on nonceded business	102,554	180,563	68,133	9,176	981	5,225	366,632
Investment income, net and financing income	16,627	4,168	*3,095	*3,118	*710	*3,303	*31,021
Commission income	-	-	2,385	10,323	9,226	10,349	32,283
Total income	119,181	184,731	73,613	22,617	10,917	18,877	429,936
Increase in insurance liabilities and payments with respect to insurance contracts	(78,748)	(124,083)	(29,381)	(21,592)	(31,090)	(54,873)	(339,767)
Share of reinsurers of increase in insurance l liabilities and payments with respect to insurance contracts	16,592		3,267	12,740	28,465	47,473	108,537
Increase in insurance liabilities and payments with respect to insurance contracts relating to non ceded business	(62,156)	(124,083)	(26,114)	(8,852)	(2,625)	(7,400)	231,230
Commission, marketing expenses and other acquisition expenses	(12,009)	(23,486)	(8,596)	(13,470)	(7,083)	(8,274)	(72,918)
General and administrative expenses	(19,376)	(25,303)	(19,801)	(6,419)	(2,574)	(3,216)	(76,689)
Financing expenses	-	-	*(115)	*(1,733)	*(419)	*(1,871)	*(4,138)
Total expenses	(93,541)	(172,872)	(54,626)	(30,474)	(12,701)	(20,761)	(384,975)
Profit (loss) before taxes on income	25,640	11,859	18,987	(7,857)	(1,784)	(1,884)	44,961
Gross liabilities with respect to insurance contracts as of December 31, 2011	638,301	117,770	53,062	173,348	51,932	208,168	1,242,581

(*) Reclassification

(**) Property lines and other include mainly results from the property insurance sector, the operations of which constitute 86% of total premiums in these sectors. Other liability sectors include mainly results from the product liability insurance sector, the operations of which constitute 54% of total premiums in these sectors.

NOTE 4 - OPERATING SEGMENTS (continued):

Additional information relating to general insurance segment

	For year ended December 31, 2010						
	Compulsory car insurance	Car damages insurance	Apartments	Professional liability	Property branches and Miscellaneous (**)	Other liability branches (**)	Total
	ILS in thousands						
Gross premiums	107,545	181,221	74,176	45,517	33,405	45,479	487, 343
Reinsurance premiums	(1,481)	(112)	(9,622)	(38,616)	(32,875)	(41,135)	(123,841)
Premiums relating to nonceded business	106,064	181,109	64,554	6,901	530	4,344	363,502
Change in balance of unearned premiums relating to nonceded business	6,885	1,325	(3,993)	(1,102)	(77)	(895)	2,143
Premiums earned on nonceded business	112,949	182,434	60,561	5,799	453	3,449	365,645
Investment income, net and financing income	21,872	4,901	*2,809	*3,832	*712	*3,667	*37,793
Commission income	-	-	1,481	9,713	8,409	10,799	30,402
Total income	134,821	187,335	64,851	19,344	9,574	17,915	433,840
Increase in insurance liabilities and payments with respect to insurance contracts	(122,113)	(133,692)	(23,431)	(9,452)	(25,289)	(24,901)	(338,878)
Share of reinsurers of increase in insurance l liabilities and payments with respect to insurance contracts	42,698	-	1,400	5,244	24,517	18,719	92,578
Increase in insurance liabilities and payments with respect to insurance contracts relating to non ceded business	(79,415)	(133,692)	(22,031)	(4,208)	(772)	(6,182)	(246,300)
Commission, marketing expenses and other acquisition expenses	(15,237)	(26,961)	(10,975)	(12,231)	(5,190)	(7,422)	(78,016)
General and administrative expenses	(19,647)	(25,540)	(17,529)	(5,709)	(1,887)	(2,482)	(72,794)
Financing expenses	-	-	*(42)	*(781)	*(182)	*(844)	*(1,849)
Total expenses	(114,299)	(186,193)	(50,577)	(22,929)	(8,031)	(16,930)	(398,959)
Profit (loss) before taxes on income	20,522	1,142	14,274	(3,585)	1,543	985	34,881
Gross liabilities with respect to insurance contracts as of December 31, 2010	617,434	116,614	46,265	155,639	42,101	166,387	1,144,440

(*) Reclassification

(**) Property lines and other include mainly results from the property insurance sector, the operations of which constitute 86% of total premiums in these sectors. Other liability sectors include mainly results from the product liability insurance sector, the operations of which constitute 54% of total premiums in these sectors.

NOTE 5 - INTANGIBLE ASSETS (SOFTWARE):

	Software
	ILS in thousands
Cost:	
Balance as of January 1, 2010	28,405
Additions in 2010(*)	5,804
Reduction in 2010	(7,976)
Balance as of December 31, 2010	**26,233**
Additions in 2011(*)	5,353
Reduction in 2011	-
Balance as of December 31, 2011	**31,586**
Additions in 2012(*)	11,202
Reduction in 2012	(3,214)
Balance as of December 31, 2012	**39,574**
Accumulated amortization:	
Balance as of January 1, 2010	22,120
Additions in 2010	3,136
Retirements in 2010	(7,976)
Balance at December 31, 2010	**17,280**
Additions in 2011	4,323
Reduction in 2011	-
Balance as of December 31, 2011	**21,603**
Additions in 2012	5,453
Reduction in 2012	(3,214)
Balance as of December 31, 2012	**23,842**
Depreciated balance:	
At December 31, 2012	**15,732**
At December 31, 2011	9,983
At December 31, 2010	8,953

* Additions in respect of computer software include mainly additions in respect of self development: in 2010 – ILS 1,458 thousands; 2011 – 2,428 thousands and 2012 – ILS 2,073 thousands.

NOTE 6 - DEFERRED ACQUISITION EXPENSES

a. Composition

	December 31	
	2012	2011
	ILS in thousands	
Life assurance	73,464	64,720
Health insurance	1,510	1,869
General insurance	55,217	52,069
Total	130,191	118,658

b. Changes in deferred acquisition expenses (life assurance and health insurance):

	Life assurance	Health insurance	Total
	ILS in thousands		
Balance as of January 1, 2011	50,910	1,308	52,218
Additions in 2011:			
Acquisition commission	926		926
Other acquisition expenses	26,150	1,869	28,019
Total additions	27,076	1,869	28,945
Current amortization in 2011	(4,433)	(1,308)	(5,741)
Amortization relating to cancellations in 2011	(8,833)	-	(8,833)
Total amortization	(13,266)	(1,308)	(14,574)
Balance as of December 31, 2011	64,720	1,869	66,589
Additions in 2012:			
Acquisition commission	-		-
Other acquisition expenses	29,029	1,510	30,539
Total additions	29,029	1,510	30,539
Current amortization in 2012	(7,919)	(1,869)	(9,788)
Amortization relating to cancellations in 2012	(12,366)	-	(12,366)
Total amortization	(20,285)	(1,869)	(22,154)
Balance as of December 31, 2012	73,464	1,510	74,974

NOTE 7 - PROPERTY AND EQUIPMENT:

a. Composition of assets and accumulated depreciation thereon, grouped by major classifications, and changes therein in 2012, are as follows:

	Computers and communications equipment	Office furniture and equipment	Leasehold improvements	Total
Cost:				
Balance at beginning of year	19,323	5,800	15,379	40,502
Additions during year	2,380	176	360	2,916
Retirements during year	(2,445)	-	-	(2,445)
Balance at end of year	19,258	5,976	15,739	40,973
Accumulated depreciation:				
Balance at beginning of year	12,099	2,365	7,295	21,759
Additions during year	3,103	450	1,221	4,774
Retirements during year	(2,445)	-	-	(2,445)
Balance at end of year	12,757	2,815	8,516	24,088
Depreciated balance at end of year	6,501	3,161	7,223	16,885

b. Composition of assets and accumulated depreciation thereon, grouped by major classifications, and changes therein in 2011, are as follows:

	Computers and communications equipment	Office furniture and equipment	Leasehold improvements	Total
Cost:				
Balance at beginning of year	18,037	7,197	15,395	40,629
Additions during year	1,326	165	33	1,524
Retirements during year	(40)	(1,562)	(49)	(1,651)
Balance at end of year	19,323	5,800	15,379	40,502
Accumulated depreciation:				
Balance at beginning of year	8,654	3,291	6,094	18,039
Additions during year	3,485	636	1,250	5,371
Retirements during year	(40)	(1,562)	(49)	(1,651)
Balance at end of year	12,099	2,365	7,295	21,759
Depreciated balance at end of year	7,224	3,435	8,084	18,743

c. Composition of assets and accumulated depreciation thereon, grouped by major classifications, and changes therein in 2010, are as follows:

	Computers and communications equipment	Office furniture and equipment	Leasehold improvements	Total
Cost:				
Balance at beginning of year	16,809	6,956	12,125	35,890
Additions during year	3,216	1,089	3,270	7,575
Retirements during year	(1,988)	(848)		(2,836)
Balance at end of year	18,037	7,197	15,395	40,629
Accumulated depreciation:				
Balance at beginning of year	6,849	3,335	5,049	15,233
Additions during year	3,793	635	1,045	5,473
Retirements during year	(1,988)	(679)		(2,667)
Balance at end of year	8,654	3,291	6,094	18,039
Depreciated balance at end of year	9,383	3,906	9,301	22,590

NOTE 8 - OTHER RECEIVABLES:

	December 31	
	2012	2011
	ILS in thousands	
Prepayment of expenses:		
Expenses accompanying insurance Transactions	18,297	17,586
Sundry expenses	2,333	2,116
Total prepaid expenses	20,630	19,702
Employees	123	118
Postdated checks	209	90
Insurance companies re subrogation claims	9,753	8,663
Miscellaneous	2,953	2,283
Total other receivables	33,668	30,856

NOTE 9 - PREMIUMS COLLECTIBLE:

a. Composition:

	December 31	
	2012	2011
	ILS in thousands	
Linked to Consumer Price Index	28,840	23,403
Linked to dollar	15,174	15,114
Unlinked	136,199	122,840
	180,213	161,357
Less:		
Provision for doubtful debts	(6,058)	(5,144)
Total (*)	174,155	156,213
(*) Includes transfers, payments by standing order and payments though credit card companies	156,576	139,738

(**)For the balance of premiums to be collected from related parties, see Note 28

NOTE 9 - PREMIUMS COLLECTIBLE (continued):

b. Aging:

	December 31	
	2012	**2011**
	ILS in thousands	
Unimpaired premiums collectible:		
Not in arrears	169,258	153,455
In arrears:		
Less than ninety days	649	426
Between 90 and 180 days	4,248	2,332
Total unimpaired premiums collectible	174,155	156,213
Impaired premiums collectible	6,058	5,144
	180,213	161,357
Deduct - provision for doubtful debts	(6,058)	(5,144)
Total premiums collectible	174,155	156,213

c. The change in the provision for doubtful debts is set out below:

	Year ended December 31	
	2012	**2011**
	ILS in thousands	
Balance as of beginning of year	(5,144)	(4,499)
Change in provision during year through profit and loss	(914)	(645)
Balance as of end of year	(6,058)	(5,144)

NOTE 10 - FINANCIAL INVESTMENTS:

	As of December 31, 2012		
	At fair value through profit or loss	**Loans and receivables**	**Total**
	ILS in thousands		
Marketable debt assets	1,099,646	-	1,099,646
Nonmarketable debt assets	-	77,925	77,925
Listed shares	68,284	-	68,284
Other	93,487	-	93,487
Total	1,261,417	77,925	1,339,342

	As of December 31, 2011		
	At fair value through profit or loss	**Loans and receivables**	**Total**
	ILS in thousands		
Marketable debt assets	978,556	-	978,556
Nonmarketable debt assets	-	58,859	58,859
Listed shares	50,934	-	50,934
Other	37,312	-	37,312
Total	1,066,802	58,859	1,125,661

NOTE 10 - FINANCIAL INVESTMENTS (continued):

a. Composition of marketable debt instruments (earmarked upon initial recognition for category of financial assets at fair value through profit or loss)

	December 31	
	2012	2011
	ILS in thousands	
Government debentures	810,322	697,519
Other marketable debt instruments that are not convertible	289,324	281,037
Total marketable debt instruments	1,099,646	978,556

b. Composition of nonmarketable debt instruments (presented as loans and receivables):

	Carrying amount		Fair value	
	2012	2011	2012	2011
	ILS in thousands			
Nonconvertible debt instruments presented as loans and receivables including deposits with banks	77,925	58,859	83,480	59,832

c. Details regarding interest and linkage in respect of debt instruments:

	*Effective interest	
	2012	2011
	Percentages	
Marketable debt instruments:		
Linkage basis:		
Linked to the CPI	3.67%	4.02%
ILS	4.98%	4.87%
Linked to the dollar	2.14%	3.56%
Linked to the Euro	-	4.62%
Nonmarketable debt instruments:		
Linkage basis:		
Linked to the CPI	5.29%	5.24%
Linked to the dollar	2.28%	1.93%

* Weighted average

NOTE 10 - FINANCIAL INVESTMENTS (continued):

d. Shares:

	December 31	
	2012	2011
	ILS in thousands	
Marketable shares - designated upon initial recognition at fair value through profit or loss	68,284	50,934

e. Other financial investments:

	December 31	
	2012	2011
	ILS in thousands	
Marketable shares - designated upon initial recognition at fair value through profit or loss	93,487	37,312

f. Interest rates used in determining fair value

The fair value of financial nonmarketable debt instruments, the data regarding the fair value of which is presented in the financial statements for disclosure purposes only, is determined by discounting the estimated future cash flows in respect of these assets. The discount rates are based on government debentures yields and margins of corporate bonds as measured in the TelAviv Stock Exchange with the addition of premium in respect of nonmarketability, As measured in the TelAviv Stock Exchange Ltd, with the addition of a premium in respect of nonmarketability. The interest used in capitalization are set by "Fair Spread Ltd.", which provides quoted interest rates in proportion to various risk ratings.

	December 31	
	2012	2011
	Percentages	
AA rating or more	1.79%	2.14%
A rating	5.23%	4.61%
BBB rating	5.68%	-
Lower than BBB rating	10.06%	11.52%

NOTE 10 - FINANCIAL INVESTMENTS (continued):

g. Hierarchy of fair value of financial assets:

Fair value hierarchy is determined as follows:

- Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).
- Level 3 Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

All of the Company's marketable financial investments (excluding nonmarketable debt instruments) that are measured at fair value through profit or loss constitute level 1 assets. The balance presented in the financial statements for cash and cash equivalents, premiums collectible, trade receivables and other receivables corresponds to or approximates their fair value since the effect of discounting is immaterial for these items.

NOTE 11 - CASH AND CASH EQUIVALENTS:

	December 31	
	2012	**2011**
	ILS in thousands	
Cash and deposits available for withdrawal on demand:		
Denominated in New Israel Shekels	79,831	84,086
Denominated in dollars	10,889	15,540
Denominated in other currencies	2,820	3,936
Cash and cash equivalents	93,540	103,562

As of the date of the balance sheet, cash and cash equivalents deposited with banks were credited with interest at rates based upon the daily bank deposit rate (0.75% - 2.54%).

NOTE 12 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS:

a. Composition of share capital

	Number of shares		
	Authorized	**Issued and fully paid**	
	December 31		
	2012 and 2011	**2012**	**2011**
Ordinary ILS 1 shares	45,000,000	5,630	5,630
Preferred ILS 1 shares	100	100	100

b. Change in share capital

On December 14, 2010, the board approved an issuance of bonus shares at ILS 1,000 par value, capitalizing ILS 74 million of retained earnings of the company (which were classified into equity and share premium).

NOTE 12 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS (continued):

c. Rights attached to shares

The rights attached to ordinary shares are comprised of the right to receive dividends, rights attendant upon the liquidation or windingup of the Company, and the right to appoint the directors of the Company.

The rights attached to preferred shares are comprised of voting rights at general meetings of the Company.

d. Other capital reserve:

	Other reserves
	ILS in thousands
Balance as of January 1, 2011	10,898
Benefit component with respect to sharebased payments and grant of other benefits to employees by controlling shareholder	186
Balance as of December 31, 2011	11,084
Benefit component with respect to sharebased payments and grant of other benefits to employees by controlling shareholder	-
Balance as of December 31, 2012	11,084

e. Equity management and equity requirements:

1. The policy of management is to maintain a sound equity base in order to ensure that the Company is in a position to continue operations that produce a return for shareholders. Management also considers that a sound equity base is required in order to support future business operations. The Company is subject to the capital requirements of the Supervisor of Insurance.

NOTE 12 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS (continued):

e. Equity management and equity requirements (continued)**:**

2. Set forth below are data regarding the required and existing capital of the company in accordance with the Shareholders' Equity Regulations and amendments thereto and the directives of the Supervisor of Insurance.

	December 31	
	2012	**2011**
	ILS in thousands	
Amount required by equity amended regulations (a)	436,785	394,619
Amount as of December 31 computed in accordance with the equity regulations:		
Primary equity	577,104	419,767
Secondary equity	-	-
Total equity as of December 31 computed in accordance with the equity regulations	577,104	419,767
Surplus	140,319	25,148

Aside from the general requirements of the Companies' Law, the payment 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 Supervisor's instructions constitute surplus that is not distributable.

(a) with regard to the company and in accordance with parameters defined in the amendedequity regulations, the required equity includes, inter alia, capital requirements with respect to the following:

	December 31	
	2012	**2011**
	ILS in thousands	
Operations related to general insurance	108,966	114,822
Exceptional life assurance risks	22,762	19,268
Deferred acquisition expenses in relation to life assurance	73,464	64,720
Investment assets and other assets	48,054	51,984
Catastrophe risk related to general insurance	158,058	118,666
Operating risks	25,477	25,159
Total	436,785	394,619

NOTE 12 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS (continued):

e. Equity management and equity requirements (continued)**:**

3. On December 29, 2011, the Supervisor issued a letter on dividend distribution by insurance companies. This letter was issued further to previous letters of the Supervisor in which insurers were required to get an advance approval of the Supervisor before paying dividends, and set criteria for applying for approval and criteria for distribution where no approval is needed.

4. On August 4, 2011, the Supervisor published Insurance Circular 2011-1-3 with regard to "composition of recognized equity of an insurer". The purpose of the circular is to set rules and principles regarding the composition of the equity of an insurer and the characteristics of the equity's components. The circular is composed of two parts:

   In the first part, the Supervisor sets a framework of rules and principles regarding the composition of the equity of an insurer and the characteristics of its components; which complies with the principles of the Solvency II Directive (hereafter - "the directive"). This framework shall serves as a basis for determining the composition of the equity of an insurer upon application of the directive as above in Israel, including the changes and amendments made therein.

   In the second part - a Temporary Order is issued regarding the composition of the equity of an insurer until the time of application of the said directive in Israel, at a date to be set by the Supervisor.

   Under the circular, the equity of an insurer shall be composed of the amounts of components and instruments included in three tiers: primary capital, secondary capital and tertiary (Tier 3) capital. Under the circular, the equity components and equity instruments shall be classified into the three tiers in accordance with their characteristics, based on the extent of their subordination, their capacity of absorbing losses, permanence and availability as specified below:

   Primary capital - the principal and most qualitative level of an insurer's capital which consists of components and instruments that have matured, which are subordinated with regard to any of the insurer's other obligations (financial or insurance), are available to absorb the insurer's losses in the normal course of business and in case of insolvency or liquidation, and which are perpetual and are not governed by any restrictions, conditions or allocations;

   Secondary capital - the layer of capital which consists of matured components and instruments, which are subordinated with regard to any other obligation (financial or insurance), excluding primary capital, are perpetual or have been issued for a long period relative to the average maturity periods of insurer's obligations, are capable of absorbing losses in the normal course of the insurer's business and in a case of insolvency or liquidation, and do not include any restrictions or allocations;

   Tierthree capital - consisting of matured instruments and components which are subordinated with regard to any other obligation (financial or insurance) excluding primary and secondary capital, which have been issued for the intermediate term, are capable of absorbing losses mainly in a case of insolvency or liquidation and which do not include restrictions, conditions or allocations. Company's management is of the opinion that the circular will not have a material effect on the equity requirements with which the company is required to comply.In the opinion of the company, the circular does not have a material effect on the capital requirements of the company.

NOTE 12 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS (continued):

e. Equity management and equity requirements (continued)**:**

In July 2012, the published clarifications regarding the calculation of the capital requirements for insurance companies (hereafter - the "clarifications"), the main points of which are: clarifications regarding the capital required in respect of investments, capital requirements in respect of operating risk, deficit or surplus arising in profit-sharing policies, classification of derivative financial instruments, reporting regarding investment obligations in investment funds, external rating and capital surplus/deficit of insurance companies in respect of activity between the report date and the publication date.

The said clarifications had no material effect on the capital requirements of the company.

NOTE 13 - LIABILITIES WITH RESPECT TO NONPROFIT PARTICIPATING INSURANCE CONTRACTS AND INVESTMENT CONTRACTS

	As of December 31					
	Gross		Reinsurance		Retained amount	
	2012	2011	2012	2011	2012	2011
	ILS in thousands					
Insurance contracts in life assurance sector	25,433	21,881	8,658	8,125	16,775	13,756
Insurance contracts in health insurance sector	126,525	120,828	5,752	4,779	120,773	116,049
Insurance contracts in general insurance sector	1,257,382	1,242,581	571,122	512,891	686,260	729,690
Total liabilities with respect non-profit participating insurance contracts and investment contracts	1,409,340	1,385,290	585,532	525,795	823,808	859,495

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR:

a.1. Liabilities with respect to insurance contracts in general insurance sector by category:

	As of December 31					
	Gross		Reinsurance		Retained amount	
	2012	2011	2012	2011	2012	2011
	ILS in thousands					
Compulsory car insurance and liability branches:						
Provision for unearned premiums	97,413	95,008	37,022	39,908	60,391	55,100
Excess of income over expenses (accumulation)	105,817	199,795	16,320	28,273	89,497	171,522
Pending claims	816,441	725,015	458,463	389,954	357,978	335,061
Total liabilities in compulsory car insurance and liability branches	1,019,671	1,019,818	511,805	458,135	507,866	561,683
Property and miscellaneous branches:						
Provision for unearned premiums	152,134	140,226	22,573	20,697	129,561	119,529
Pending claims	85,577	82,537	36,745	34,059	48,832	48,478
Total liabilities in property and miscellaneous branches	237,711	222,763	59,318	54,756	178,393	168,007
Total liabilities with respect to insurance contracts in general insurance sector	1,257,382	1,242,581	571,123	512,891	686,259	729,690
Deferred acquisition expenses:						
Compulsory car insurance and liability branches	16,405	15,957	6,998	7,308	9,407	8,649
Property and miscellaneous branches	38,812	36,113	4,441	4,411	34,371	31,702
Total	55,217	52,070	11,439	11,719	43,778	40,351
Liabilities with respect to general insurance contracts, after deduction of deferred acquisition expenses:						
Compulsory car insurance and liability branches (see paragraph b(1) below)	1,003,266	1,003,861	504,807	450,827	498,459	553,034
Property and miscellaneous branches (see paragraph b(2) below)	198,899	186,650	54,877	50,345	144,022	136,305
Total liabilities with respect to general insurance contracts, after deduction of deferred acquisition expenses	1,202,165	1,190,511	559,684	501,172	642,481	689,339

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

a.2. Insurance liabilities with respect to insurance contracts in general insurance sector by method of computation

	As of December 31					
	Gross		Reinsurance		Retained earnings	
	2012	2011	2012	2011	2012	2011
	ILS in thousands					
Actuarial valuations:						
Ms. Avital Koler	893,380	799,855	495,209	424,012	398,171	375,843
Total actuarial valuations	893,380	799,855	495,209	424,012	398,171	375,843
Additional liability with respect to difference between actuarial valuation and amount reflected in financial statements	8,638	7,697			8,638	7,697
Provision for unearned premiums	249,547	235,234	59,594	60,606	189,953	174,628
Excess of income over expenses (accumulation)	105,817	199,795	16,320	28,273	89,497	171,522
Total insurance liabilities with respect to insurance contracts in general insurance sector	1,257,382	1,242,581	571,123	512,891	686,259	729,690

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

b. Movement in liabilities with respect to insurance contracts in general insurance sector, after deduction of deferred acquisition expenses:

b1. Compulsory car insurance and liability branches:

	As of December 31					
	Gross		Reinsurance		Retained amounts	
	2012	2011	2012	2011	2012	2011
	ILS in thousands					
Balance as of beginning of year	1,003,861	924,843	450,827	395,080	553,034	529,763
Ultimate cost of claims with respect to current underwriting year	167,006	162,251	72,078	77,598	94,928	84,653
Change in balances as of beginning of year as result of linkage to Consumer Price Index and investment income in accordance with capitalization discount reflected in liabilities	29,499	32,198	5,534	6,419	23,965	25,779
Change in estimate of ultimate cost of claims with respect to previous underwriting years	11,742	(41,558)	39,028	14,329	(27,286)	(55, 887)
Total change in ultimate cost of claims	208,247	152,891	116,640	98,346	91,607	54,545
Payments in settlement of claims during course of year:						
With respect to current underwriting year	(2,875)	(2,017)	(807)	(509)	(2,068)	(1,508)
With respect to previous underwriting years	(111,989)	(80,783)	(49,899)	(25,207)	(62,090)	(55,576)
Total payments for period	(114,864)	(82,800)	(50,706)	(25,716)	(64,158)	(57,084)
Accumulation with respect to current underwriting year	25,115	26,388	978	1,346	24,137	25,042
Accumulation added to profits on closing of underwriting year	(49,102)	(55,058)	(14,218)	(19,741)	(34,884)	(35,317)
Remaining change in accumulation	(69,991)	37,597	1,286	1,512	(71,277)	36,085
Total change in accumulation for period	(93,978)	8,927	(11,954)	(16,883)	(82,024)	25,810
Balance as of end of year	1,003,266	1,003,861	504,807	450,827	498,459	553,034

1. The opening and closing balances include pending claims, accumulation, unearned premium, net of deferred acquisition costs.
2. The ultimate cost of claims includes the balance of outstanding pending claims (without accumulation), provision for premium shortfall, unearned premium net of deferred acquisition costs together with the total of payments made in respect of claims including direct and indirect expenses incurred in the settlement of claims.
3. Payment for settlement of claims during the year includes direct and indirect general and administrative costs incurred in, and attributable to, the settlement of claims; the costs are allocated between the various underwriting years.

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

b. Movement in liabilities with respect to insurance contracts in general insurance sector, after deduction of deferred acquisition expenses

b2. Property and miscellaneous branches

	As of December 31					
	Gross		Reinsurance		Retained amount	
	2012	2011	2012	2011	2012	2011
	ILS in thousands					
Balance as of beginning of year	186,650	171,511	50,345	41,363	136,305	130,148
Ultimate cost of claims with respect to events occurring in year under review	193,116	197,223	34,014	38,685	159,102	158,538
Change in ultimate cost of claims with respect to events in prior years	(11,576)	(12,672)	(5,540)	(6,954)	(6,036)	(5,718)
Payments made in course of year in settlement of claims:						
With respect to events occurring in year under review	(136,259)	(137,633)	(14,113)	(15,598)	(122,146)	(122,035)
With respect to events occurring in prior years	(42,240)	(39,753)	(11,675)	(10,259)	(30,565)	(29,494)
Total payments	(178,499)	(177,386)	(25,788)	(25,857)	(152,711)	(151,529)
Change in provision for unearned premiums, after deduction of deferred acquisition expenses	9,208	7,974	1,846	3,108	7,362	4,866
Balance as of end of year	198,899	186,650	54,877	50,345	144,022	136,305

1. The opening and closing balances include outstanding pending claims, a provision for premium shortfall and unearned premiums, net of deferred acquisition expenses.

2. The cumulative cost of claims in respect of event in the reported year includes the balance of outstanding pending claims at the end of the reported year with the addition of total payments for claims in the reported period, including direct and indirect expenses incurred in the settlement of claims.

3. Payments for settlement of claims during the year include payments in respect of events that proceeded the reported year with the addition of the change in the balance of outstanding pending claims in respect of events that proceeded the reported year.

4. Payment to settlement of claims during the year includes direct and indirect general and administrative costs incurred in, and attributable to, the settlement of claims; the costs are allocated between the various underwriting years.

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

c1. Review of development of gross liabilities with respect to insurance contracts, after deduction of deferred acquisition expenses, in compulsory motor insurance and liability branches as of December 31, 2012:

	Underwriting year										
	2003	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**Total**
	NIS in thousands, as linked to the Consumer Price Index for November 2012 (*)										
Claims paid (on cumulative basis) as of end of year:											
After first year	2,108	3,109	2,998	2,867	2,466	3,378	3,487	2,650	2,046	2,875	
After two years	15,129	16,408	15,699	17,573	16,997	13,944	16,123	12,694	19,869		
After three years	27,024	31,153	28,635	29,728	32,480	29,504	34,601	23,255			
After four years	37,057	48,275	39,747	40,240	44,355	42,437	71,943				
After five years	48,398	66,663	45,892	49,099	56,070	57,574					
After six years	59,966	79,723	52,413	55,845	62,567						
After seven years	68,469	85,785	57,370	61,576							
After eight years	71,232	98,684	65,812								
After nine years	73,857	102,561									
After ten years	75,857										
Estimate of cumulative claims (including payments) as of end of year:											
After first year	154,020	166,370	163,442	173,353	188,417	177,935	231,599	203,568	207,428	208,493	
After two years	169,215	185,217	173,190	184,980	199,472	183,725	237,876	199,132	227,245		
After three years	171,408	198,879	176,674	188,559	204,692	185,609	240,467	209,766			
After four years	132,736	162,067	135,067	151,508	171,370	173,351	193,042				
After five years	137,041	164,798	135,134	153,647	181,254	138,027					
After six years	100,209	134,990	103,021	114,215	141,031						
After seven years	99,876	142,453	98,530	113,425							
After eight years	95,307	129,695	99,546								
After nine years	93,614	117,540									
After ten years	92,422										
Surplus (shortfall) after release of accumulation (**)	7,787	17,450	3,475	790							33,690
Rate of deviation after release of accumulation (%)	7.8%	12.9%	3.4%	0.7%							6.5%
Cost of accumulated claims through December 31, 2012	92,422	117,540	99,546	113,425	141,031	138,027	193,042	209,766	227,245	208,493	1,540,537
Accumulated payments through December 31, 2012	75,857	102,561	65,812	61,576	62,567	57,574	71,943	23,255	19,869	2,875	543,889
Balance of pending claims	16,566	14,979	33,734	51,849	78,464	80,453	121,099	186,511	207,376	205,618	996,648
Pending claims for years up to and including the 2002 underwriting year											23,024
Total liability with respect to insurance contracts, car insurance and liability branches after deffered acquisition expenses											16,406
Deffered acquisition expenses as of December 31, 2012 (excluding accumulation)											1,003,266

(*) The data presented above have been adjusted in order to reflect the effects of inflation. The use of such adjusted data accordingly allows the development review to be implemented on the basis of real values.

(**) The difference between the evaluation of the accumulated claims in the fourth year and the evaluation of the accumulated claims as of the date of the financial statements.

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

c2. Review of development of retained amounts of liabilities with respect to insurance contracts, after deduction of deferred acquisition expenses, in compulsory motor insurance and liability branches as of December 31, 2012:

	Underwriting year										
	2003	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**Total**
	NIS in thousands, as linked to the Consumer Price Index for November 2012 (*)										
Claims paid (on cumulative basis) as of end of year:											
After first year	2,107	2,884	2,821	2,750	2,301	3,352	2,512	2,141	1,529	2,068	
After two years	15,038	15,514	15,139	15,545	14,069	12,356	13,369	8,998	8,973		
After three years	26,254	29,559	27,526	26,317	27,269	25,392	24,452	18,321			
After four years	35,549	44,338	38,284	35,008	38,540	36,950	37,434				
After five years	45,443	54,067	44,063	41,672	46,844	44,763					
After six years	51,675	66,699	50,270	47,748	52,772						
After seven years	57,874	71,311	54,846	53,208							
After eight years	60,384	75,460	61,483								
After nine years	62,998	77,986									
After ten years	64,991										
Estimate of cumulative claims (including payments) as of end of year:											
After first year	111,225	111,382	111,005	108,013	111,903	113,226	122,866	120,659	120,022	128,465	
After two years	115,966	116,972	114,633	109,446	114,757	116,352	126,215	113,589	118,737		
After three years	118,985	121,473	116,298	111,588	117,179	119,445	129,386	117,417			
After four years	118,643	119,029	114,683	111,889	117,964	120,003	85,163				
After five years	120,380	121,285	116,584	113,569	120,151	77,762					
After six years	80,558	97,606	81,904	76,672	84,190						
After seven years	75,802	93,756	76,241	75,299							
After eight years	71,888	87,437	74,774								
After nine years	73,446	86,237									
After ten years	71,741										
Surplus (shortfall) after release of accumulation (**)	8,817	11,369	7,131	1,373							32,595
Rate of deviation after release of accumulation (%)	10.9%	11.6%	8.7%	1.8%							8.4%
Cost of accumulated claims through December 31, 2012	71,741	86,237	74,774	75,299	84,190	77,762	85,163	117,417	118,737	128,465	919,786
Accumulated payments through December 31, 2012	64,991	77,986	61,483	53,208	52,772	44,763	37,434	18,321	8,973	2,068	421,999
Balance of pending claims	6,751	8,251	13,291	22,091	31,418	33,000	47,729	99,097	109,763	126,396	497,787
Pending claims for years up to and including the 2002 underwriting year											10,079
Total liability with respect to insurance contracts in compulsory car insurance and liability branches after adjustment for deffered acquisition expenses											9,407
Deffered acquisition expenses as of December 31, 2012 (excluding accumulation)											127,068

(*) The data presented above have been adjusted in order to reflect the effects of inflation. The use of such adjusted data accordingly allows the development review to be implemented on the basis of real values.

(**) The difference between the evaluation of the accumulated claims in the fourth year and the evaluation of the accumulated claims as of the date of the financial statements.

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

c3. Review of development of gross liabilities with respect to insurance contracts, after deduction of deferred acquisition expenses, in compulsory motor insurance branch as of December 31, 2012:

	Underwriting year										
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	Total
	NIS in thousands, as linked to the Consumer Price Index for November 2012 (*)										
Claims paid (on cumulative basis) as of end of year:											
After first year	2,107	2,831	2,781	2,731	2,256	3,349	2,423	1,856	1,293	1,755	
After two years	15,026	15,313	15,031	15,164	13,743	12,097	12,740	8,176	5,752		
After three years	26,091	29,206	27,379	26,428	26,669	25,386	23,125	17,156			
After four years	35,220	45,236	38,099	34,845	38,036	36,726	34,315				
After five years	44,902	62,619	43,869	42,742	45,898	48,768					
After six years	54,939	75,185	50,022	48,739	51,725						
After seven years	61,113	81,153	54,510	54,182							
After eight years	63,589	88,518	63,003								
After nine years	66,199	91,988									
After ten years	68,190										
Estimate of cumulative claims (including payments) as of end of year:											
After first year	107,296	114,385	112,003	114,993	116,889	117,915	123,816	121,562	117,022	119,205	
After two years	115,125	127,918	116,978	116,869	121,057	119,863	133,021	115,451	113,522		
After three years	115,040	139,072	118,973	118,597	123,990	122,102	134,572	120,588			
After four years	127,166	141,281	120,893	121,098	126,815	130,219	94,714				
After five years	129,370	141,107	121,789	126,447	129,910	87,625					
After six years	91,759	114,958	91,120	87,916	93,657						
After seven years	86,846	118,355	87,415	87,502							
After eight years	86,493	106,028	87,980								
After nine years	85,060	105,155									
After ten years	84,055										
Surplus (shortfall) after release of accumulation (**)	7,704	9,803	3,140	414							23,478
Rate of deviation after release of accumulation (%)	8.4%	8.5%	3.4%	0.5%							5.3%
Cost of accumulated claims through December 31, 2012	84,055	105,155	87,980	87,502	93,657	87,625	94,714	120,588	113,522	119,205	994,005
Accumulated payments through December 31, 2012	68,190	91,988	63,003	54,182	51,725	48,768	34,315	17,156	5,752	1,755	436,835
Balance of pending claims	15,865	13,167	24,977	33,320	41,932	38,858	60,400	103,432	107,770	117,449	557,170
Pending claims for years up to and including the 2002 underwriting year											21,583
Total liability with respect to insurance contracts in compulsory car insurance and liability branches after adjustment for deffered acquisition expenses											16,406
Deffered acquisition expenses as of December 31, 2012 (excluding accumulation)											562,348

(*) The data presented above have been adjusted in order to reflect the effects of inflation. The use of such adjusted data accordingly allows the development review to be implemented on the basis of real values.
(**) The difference between the evaluation of the accumulated claims in the fourth year and the evaluation of the accumulated claims as of the date of the financial statements.

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

c.4. Review of development of retained amounts of liabilities with respect to insurance contracts, after deduction of deferred acquisition expenses, in compulsory motor insurance branch as of December 31, 2012:

	Underwriting year										
	2003	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**Total**
	NIS in thousands, as linked to the Consumer Price Index for November 2012 (*)										
Claims paid (on cumulative basis) as of end of year:											
After first year	2,107	2,831	2,781	2,731	2,259	3,349	2,423	1,856	1,293	1,755	
After two years	15,026	15,313	15,031	15,164	13,745	12,097	12,740	8,176	5,752		
After three years	26,091	29,206	27,379	25,839	26,672	24,665	23,125	17,156			
After four years	35,220	43,803	38,099	34,256	37,893	35,813	34,315				
After five years	44,902	53,402	43,869	40,812	45,731	43,158					
After six years	51,092	65,968	50,022	46,809	51,558						
After seven years	57,267	70,564	54,510	52,252							
After eight years	59,742	73,605	61,137								
After nine years	62,352	76,075									
After ten years	64,344										
Estimate of cumulative claims (including payments) as of end of year:											
After first year	107,296	105,840	106,210	102,931	106,099	106,486	113,212	106,877	101,473	109,942	
After two years	111,382	111,019	109,206	103,952	108,282	108,314	115,548	100,480	96,091		
After three years	114,137	114,953	111,069	106,050	110,258	111,091	117,882	103,176			
After four years	117,861	116,510	113,043	107,983	112,700	113,000	74,495				
After five years	119,529	117,951	114,922	110,194	114,400	69,379					
After six years	79,736	94,790	80,444	73,210	79,366						
After seven years	74,118	89,891	74,905	71,974							
After eight years	71,045	83,528	73,495								
After nine years	72,663	84,029									
After ten years	70,984										
Surplus (shortfall) after release of accumulation (**)	8,753	10,761	6,949	1,236							31,353
Rate of deviation after release of accumulation (%)	11.0%	11.4%	8.6%	1.7%							8.3%
Cost of accumulated claims through December 31, 2012	70,984	84,029	73,495	71,974	79,366	69,379	74,495	103,176	96,091	109,942	832,931
Accumulated payments through December 31, 2012	64,344	76,075	61,137	52,252	51,558	43,158	34,315	17,156	5,752	1,755	407,503
Balance of pending claims	6,640	7,954	12,357	19,722	27,808	26,221	40,181	86,020	90,339	108,186	425,428
Pending claims for years up to and including the 2002 underwriting year											9,919
Total liability with respect to insurance contracts in compulsory car insurance and liability branches after adjustment for deffered acquisition expenses											9,407
Deffered acquisition expenses as of December 31, 2012 (excluding accumulation)											108,698

(*) The data presented above have been adjusted in order to reflect the effects of inflation. The use of such adjusted data accordingly allows the development review to be implemented on the basis of real values.

(**) The difference between the evaluation of the accumulated claims in the fourth year and the evaluation of the accumulated claims as of the date of the financial statements.

NOTE 14 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

NOTE 15 - ADDITIONAL DATA CONCERNING LIFE ASSURANCE SECTOR:

a.1 Details of liabilities with respect to insurance contracts and investment contracts by reference to financial exposure

Data pertaining to year ended December 31, 2012:

	Policies not containing savings element		Total
	Risk sold as individual policy		
	Private	Group	
Insurance reserves	701	15	716
Pending claims	24,696	21	24,717
Total	25,397	36	25,433

Data pertaining to year ended December 31, 2011:

	Policies not containing savings element		Total
	Risk sold as individual policy		
	Private	Group	
Insurance reserves	698	9	707
Pending claims	21,140	34	21,174
Total	21,838	43	21,881

a2. Details of liabilities for insurance contracts and investments contracts by insurance exposure

Information for the year ended December 31, 2012:

	Policies not containing savings element		Total
	Risk sold as single policy		
	Private	Group	
Insurance reserves	701	15	716
Outstanding claims	24,696	21	24,717
Total	25,397	36	25,433

NOTE 15 - ADDITIONAL DATA CONCERNING LIFE ASSURANCE SECTOR (continued):

Information for the year ended December 31, 2011:

	Policies not containing savings element		Total
	Risk sold as single policy		
	Private	Group	
Insurance reserves	698	9	707
Outstanding claims	21,140	34	21,174
Total	21,838	43	21,881

b. Details of results by type of policy

Data pertaining to year ended December 31, 2012:

	Policies not containing savings element		Total
	Risk sold as single policy		
	Private	Group	
Gross risk premiums	89,235	241	89,476
Profits (loss) from life assurance business	3,753	171	3,924
Graduated premiums with respect to insurance contracts	28,504	-	28,504

Data pertaining to year ended December 31, 2011:

	Policies not containing savings element		Total
	Risk sold as single policy		
	Private	Group	
Gross risk premiums	77,688	104	77,792
Profits (loss) from life assurance business	10,995	(32)	10,963
Graduated premiums with respect to insurance contracts	23,667	-	23,667

NOTE 15 - ADDITIONAL DATA CONCERNING LIFE ASSURANCE SECTOR (continued):

Data pertaining to year ended December 31, 2010:

	Policies not containing savings element		**Total**
	Risk sold as single policy		
	Private	**Group**	
Gross risk premiums	66,928	194	67,122
Profits from life assurance business	5,432	32	5,464
Graduated premiums with respect to insurance contracts	18,109	-	18,109

NOTE 16 – BREAKDOWN OF LIABILITIES IN RESPECT OF INSURANCE CONTRACTS IN HEALTH INSURANCE

a. **Breakdown of liabilities in respect of insurance contracts by insurance and financial exposure**

Data pertaining to year ended December 31, 2012 (ILS in thousands):

	Long-term	**Short-term**	**Total**
By insurance exposure insurance			
Reserves	-	4,314	4,314
Pending claims	91,465	30,746	122,211
Total	91,465	35,060	126,525

Personal injuries is the most significant item in long-term healthcare coverage, and travel insurance in the short-term

Data pertaining to year ended December 31, 2011 (ILS in thousands):

	Long-term	**Short-term**	**Total**
By insurance exposure insurance			
reserves	-	5,340	5,340
Pending claims	76,086	39,402	115,488
Total	76,086	44,742	120,828

Personal injuries is the most significant item in long-term healthcare coverage, and travel insurance in the short-term

NOTE 16 - BREAKDOWN OF LIABILITIES IN RESPECT OF INSURANCE CONTRACTS IN HEALTH INSURANCE (continued):

b) Detailed results by type of policy in the healthcare sector

Data pertaining to year ended December 31, 2012 (ILS in thousands):

	Long-term	Short-term	Total
Gross premiums	154,574	42,631	*197,205
Income from healthcare insurance business	32,954	7,073	40,027
Annualized premium - new	39,255	2,881	42,137

* Of which individual premiums at ILS 186,155 thousand and group premiums at ILS 11,050 thousand. Personal injuries is the most significant item in longterm healthcare coverage, travel insurance and collective personal injuries in the shortterm.

Data pertaining to year ended December 31, 2011 (ILS in thousands):

	Long-term	Short-term	Total
Gross premiums	132,174	39,746	*171,920
Income from healthcare insurance business	18,389	(2,479)	15,910
Annualized premium - new	41,067	3,021	44,088

* Of which individual premiums at ILS 160,673 thousand and group premiums at ILS 11,247 thousand. . Personal injuries is the most significant item in longterm healthcare coverage, travel insurance and collective personal injuries in the shortterm.

Data pertaining to year ended December 31, 2010 (ILS in thousands):

	Long-term	Short-term	Total
Gross premiums	111,104	33,417	*144,521
Income from healthcare insurance business	17,269	4,356	21,625
Annualized premium - new	36,413	2,922	39,335

* Of which individual premiums at ILS 137,063 thousand and group premiums at ILS 7,458 thousand. Personal injuries is the most significant item in longterm healthcare coverage, travel insurance and collective personal injuries in the shortterm.

NOTE 17 - MOVEMENT IN LIABILITIES WITH RESPECT TO LIFE ASSURANCE CONTRACTS AND HEALTH INSURANCE CONTRACTS

	Life assurance	Health insurance
	ILS in thousands	
Balance as of January 1, 2011	25,076	105,152
Increase in premiums treated as liabilities	75	1,573
Changes in pending and IBNR claims	(3,270)	14,103
Balance as of December 31, 2011	21,881	120,828
Increase in premiums treated as liabilities	9	(833)
Changes in pending and IBNR claims	3,543	6,531
Balance as of December 31, 2012	25,433	126,525

NOTE 18 - TAXES ON INCOME:

a. Taxing statutes applicable to Company:

1. General

   AIG Israel Insurance Co. Ltd. is a financial institution, as that term is defined in the ValueAdded Tax Law, 1975. The tax chargeable on the income of financial institutions is comprised of company tax and profits tax.

2. Amendment to ValueAdded Tax Law

   In addition to the amendment referred to in the previous paragraph, the Knesset also passed an amendment (Amendment No. 35) to the ValueAdded Tax Law, which amendment determined that, as from the 2009 tax year, the entirety of the payments made in respect of payroll tax shall be deductible for the purposes of computing the profits tax chargeable on financial institutions. For the 2008 tax year, one half of the payroll tax payments made for that year shall be deductible. The amendment further determined that, as from the 2009 tax year, profits tax would also be levied on the employer’s payments to the National Insurance Institute. For the 2008 tax year, profits tax would be levied on one half of the employer’s payments to the National Insurance Institute.

NOTE 18 - TAXES ON INCOME (continued):

a. **Taxing statutes applicable to Company** (continued):

3. Special tax arrangements for insurance industry:

   a. Arrangement with tax authorities

   The Association of Insurance Companies and the tax authorities have entered into a special arrangement ("the tax arrangement"). The arrangement, which is subject to renewal and revision each year, deals with particular tax issues that are unique to the industry and which relate to tax years up to and including the 2007 tax year. The arrangement deals, inter alia, with the following issues:

   - The period of amortization of life assurance deferred acquisition expenses for tax purposes;
   - The rate at which expenses are attributable to income chargeable at preferential rates (interest and dividend income chargeable at a tax rate lower than the rate of company tax);
   - The taxation of income stemming from assets held as cover for profit participating liabilities;
   - The taxation of income stemming from marketable securities.
   - Guidelines on the firsttime implementation of IFRS (for more information on the tax implication of the firsttime adoption of IFRS in Israel, see also 5 below).

   No agreement has yet been signed in respect of tax years 2010, 2011 and 2012. Management continued to compute its taxable income for these years based on the principles of the tax agreement, except in relation to gains from marketable securities.

NOTE 18 - TAXES ON INCOME (continued):

a. Taxing statutes applicable to Company (continued):

5. Effect of adoption of IFRS in Israel on tax liability

Commencing January 1, 2008, the company prepares its financial statements in accordance with IFRS.

IFRS vary from Accounting Principles Generally Accepted in Israel and accordingly, preparation of financial statements in accordance with IFRS may reflect a financial position, results of operations and cash flows that are materially different from the ones presented in financial statements presented in accordance with accounting principles generally accepted in Israel.

In accordance with the law for the amendment of the Income Tax Ordinance (No. 174 – Temporary Order as to Tax Years 2007, 2008 and 2009), 2010 that was passed in the Knesset on January 25, 2010 and published in the official gazette on February, 4, 2010 and in accordance with the Law for Amendment of the Income Tax Ordinance (no. 188), 2012, passed in the Knesset on January 9, 2012 and published in the official gazette on January 12, 2012 (hereafter together – the temporary order), Accounting Standard No. 29 issued by the Israel Accounting Standard Board would not apply upon determining the taxable income for tax purposes in respect of tax years 2007-2011; this would be the case even if the said accounting standard was applied for the said tax years in the financial statements. The meaning of the amendment to the ordinance is that IFRS would actually not be applied upon computation of the income reported for tax purposes for the said tax years.

On October 31, 2011 the Government of Israel published a law memorandum in connection with the amendment to the Income Tax Ordinance (hereafter – the law memorandum) resulting from application of IFRS in the financial statements. Generally, the law memorandum adopts IFRS. Nevertheless, the law memorandum suggests making several amendments to the Income Tax Ordinance, which will serve to clarify and determine the manner of computation of taxable income for tax purposes in cases where the manner of computation is not clear and IFRS do not comply with the principles of the tax method applied in Israel. At the same time, the law memorandum generally adopts IFRS.

Since the temporary order applies to tax years 2007-2012 as above, at this stage management expects that the new legislation shall not apply to tax years preceding tax year 2012.

The company computed its taxable income for tax years 2007 to 2012 based on Israeli accounting standards applicable prior to adoption of IFRS in Israel, subject to certain adjustments. Therefore, the temporary order did not have any effect on the computation of current and deferred tax balances relating to the said tax years.

NOTE 18 - TAXES ON INCOME (continued):

b. Tax rates applicable to the company

The statutory tax applicable to financial institutions, including the company, is comprised of corporate tax and profit tax.

under the provisions of the Law for Amendment of the Income Tax Ordinance, 2005, of August 2005, the corporate tax rates is to be gradually reduced as from 2009 and thereafter, as follows: 2 – 26%, 2011 and thereafter – 25%

On July 14, 2010 the Economic Rationalization Law (Legislation Amendments for the Implementation of the Economic Plan for the years 2009 and 2010), 2009 (hereafter – Amendment 2009), was passed in the Knesset; this law determined, inter alia a further gradual reduction of the corporate tax rate as from 2011, as follows: 2011 – 24%, 2012 – 23%, 2013 – 22%, 2014 – 21%, 2015 – 20%, 2016 and thereafter – 18%. As a result of Amendment 2009, the tax expenses decreased by ILS 652 thousands (on the basis of deferred tax balances as of December 31, 2009); this decrease was charged as an income to the statement of comprehensive income in 2009.

On December 6, 2011, the "Tax Burden Distribution Law" Legislation Amendments (2011) was published in the official gazette. Under this law, the previously approved gradual decrease in corporate tax is discontinued. Corporate tax rate will increase to 25% as from 2012. As a result of the 2011 amendment the company's deferred tax liability as of December 31, 2011 increased by ILS 1.3 million; this increase was expensed in the statement of comprehensive income.

In addition to corporate tax as above, being a financial institution, the company is required to pay profits tax; the rate of this tax in 2009 was 15.5% applicable to half of the annual profits and 16.5% applicable to the remaining half of the annual profits; in 2010 the rate was 16%. In accordance with the provisions of Amendment No. 35 to the Value Added Tax Law, 1975, commencing 2008 a payroll tax will be deductible in the calculation of profit tax applied to financial institutions.

In the third quarter of 2012, the VAT Order (Tax Rate Applicable to Not for Profit Organizations and Financial Institutions) (Amendment), 2012 ("the Amendment") was published in the official gazette, stipulating that the rate of profit tax and payroll tax that applies to Israeli operations of a financial institution will be increased to 17% of the payroll paid by the financial institutions and the profit derived by the financial institution (instead of 16%). Under the 2012 Amendment, the amendment shall apply to payroll paid for work carried out in September 2012 and thereafter and to a third of the profit derived in the course of that tax year. In light of the amendment, the overall tax rate (corporate tax and profit tax) applicable to the company commencing 2012 as a whole shall by 35.53% instead of 35.34% that applied in the year prior to the coming into effect of the Amendment.

The effect of the Amendment on the company's 2012 financial statements, computed on the basis of deferred tax balances as of December 31, 2012, was reflected in an increase in deferred tax liabilities (net) at the total amount of ILS 132 thousands; this amount was expensed in statement of comprehensive income in 2012.

In light of the changes in corporate tax rates as above, set forth below are the applicable tax rate; (as to the difference between the theoretical tax and taxes on income as per statement of income – see f. below):

	Rate of corporate Tax	Rate of Profit Tax	Overall Tax Rate for Financial Institutions
		%	
Year:			
2010	25	16.00	35.34
2011	24	16.00	34.48
2012	25	16.33	35.53
2013 and hereafter	25	17.00	35.90

NOTE 18 - TAXES ON INCOME (continued):

c. Final Tax assessments

The company has been issued final tax assessments through tax year 2009.

d. Taxes on income included in the income statements:

	For the year ended December 31		
	2012	2011	2010
	ILS in thousands		
For the reported year:			
Current	(85,941)	(21,525)	(29,394)
Deferred, in respect of creation and reversal of temporary differences, see also e. below	(1,501)	(2,595)	(1,845)
In respect of previous years	1,011	1,177	1,873
Adjustment of deferred tax balances due to changes in tax rates	-	-	-
	(86,431)	(22,943)	(29,366)

e. Deferred taxes

Deferred assets and liabilities are offset when there is an enforceable legal right to offset current tax assets against current tax liabilities and when the deferred taxes are in respect of taxes on income levied by the same tax authority. The offset amounts are as follows:

Composition:

	Deferred acquisition costs	Vacation recreation pay	Provision For severance Pay	Provision for doubtful accounts	Property and equipment	Other	Total
	ILS in thousands						
Balance of tax asset (liability) as of January 1, 2011	(8,185)	354	619	1,551	(168)	1,047	(4,782)
Changes charged to income	(2,179)	110	(20)	222	10	571	(1,286)
Effect of changes in tax rate	(1,500)	12	124	45	(33)	44	(1,308)
Balance of tax asset (liability) as of December 31, 2011	(11,864)	476	723	1,818	191	1,662	(7,376)
Changes charged to income	(2,001)	2	99	323	(21)	225	(1,373)
Effect of changes in tax rate	(206)	7	13	33	(3)	28	(128)
Balance of tax asset (liability) as of December 31, 2012	(14,071)	485	835	2,174	(215)	1,915	(8,877)

The deferred taxes are presented in the balance sheet among deferred tax liabilities.

	December 31	
	2012	2011
	ILS in thousands	
Deferred tax assets	(4,575)	(3,954)
Deferred tax liabilities	13,452	11,330
	8,877	7,376

NOTE 18 - TAXES ON INCOME (continued):

f. Theoretical tax

Following is a reconciliation of the theoretical tax expense, assuming all income and expenses, profits and losses in the statement of income are taxed at the statutory tax rates, and the tax expense charged in the taxes of income (loss):

	Year ended December 31		
	2012	2011	2010
	ILS in thousands		
Income before taxes on income	243,768	67,306	85,700
Overall statutory tax rate applicable to financial institutions (see b. above)	35.53%	34.48%	35.34%
Taxes computed based on the statutory tax rate	(86,611)	(23,207)	(30,291)
Increase (decrease) in taxes arising from:			
Nonallowable expenses for tax purposes	215	203	(1,371)
Difference between the measurement basis of income for tax purposes Deduction in respect of depreciation	4	8	10
Updating of deferred tax balances in respect of change in tax rates	(126)	(1,308)	
Taxes in respect of previous years	1,010	1,177	1,873
Update deferred tax expense in prior years required	(933)	-	-
Other	10	184	413
Taxes on income	(86,431)	(22,943)	(29,366)
Average effective tax rate	35.46%	34.09%	34.26%

NOTE 19 – OTHER PAYABLES AND SURPLUS RESERVES:

	December 31	
	2012	2011
	ILS in thousands	
Employees and other payroll related liabilities	17,547	15,937
Suppliers and service providers	41,958	34,941
Commissions payable	9,238	8,488
Premiums paid in advance	14,546	11,401
Other	5,076	3,648
	88,365	74,415

NOTE 20 –PREMIUMS – RETAINED:

	Year ended December 31, 2012		
	Gross	Reinsurance	Retained amount
	ILS in thousands		
Life insurance premiums	89,476	21,000	68,476
Health insurance premiums	197,205	21,695	175,510
General insurance premiums	553,774	141,976	411,798
Total premiums	840,455	184,671	655,784
Less - change in balance of unearned premium	(13,297)	1,030	(14,327)
Total earned premiums	827,158	185,701	641,457

	Year ended December 31, 2011		
	Gross	Reinsurance	Retained amount
	ILS in thousands		
Life insurance premiums	77,792	18,816	58,976
Health insurance premiums	171,920	18,540	153,380
General insurance premiums	505,580	129,742	375,838
Total premiums	755,292	167,098	588,194
Less - change in balance of unearned premium	(20,239)	(9,386)	(10,853)
Total earned premiums	735,053	157,712	577,341

	Year ended December 31, 2010		
	Gross	Reinsurance	Retained amount
	ILS in thousands		
Life insurance premiums	67,122	16,402	50,720
Health insurance premiums	144,521	13,299	131,222
General insurance premiums	487,343	123,841	363,502
Total premiums	698,986	153,542	545,444
Less - change in balance of unearned premium	(8,682)	(10,728)	2,046
Total earned premiums	690,304	142,814	547,490

NOTE 21 – NET REVNEUES FROM INVESTMENTS AND FINANCING INCOME:

	Year ended December 31		
	2012	**2011**	**2010**
	ILS in thousands		
Income (loss) from assets held against non profit participating liabilities, shareholders' equity and others:			
Income (loss) from financial investments excluding interest, linkage differences, exchange differences and dividends on assets at fair value through profit or loss	50,394	(17,781)	22,835
Income from interest, linkage differences and exchange differences, exchange differences, on financial assets through profit or loss	40,302	*34,217	*34,250
Income from interest on deposits and cash and nonmarketable securities	3,372	*5,478	*4,433
Income from dividends	3,171	3,419	4,376
Total revenues from net investments and financing income	97,239	25,333	65,894

* Reclassification

NOTE 22 – REVNEUES FROM COMMISSIONS:

	Year ended December 31		
	2012	**2011**	**2010**
	ILS in thousands		
Reinsurance commissions, net of change in deferred acquisition costs relating to reinsurance	47,628	41,457	36,952

As to commissions from related parties , see note 28.

NOTE 23 – PAYMENTS AND CHANGES IN LIABILITIES IN RESPECT OF RETAINED INSURANCE CONTRACTS

	Year ended December 31		
	2012	**2011**	**2010**
	ILS in thousands		
Total payments and changes in liabilities in respect of life insurance contracts:			
Gross	30,624	14,340	19,264
Reinsurance	(10,107)	(5,016)	(5,868)
Life insurance contracts - retained	20,517	9,324	13,396
Total payments and changes in liabilities in respect of general insurance contracts:			
Gross	293,851	339,767	338,878
Reinsurance	(135,737)	(108,537)	(92,578)
General insurance contracts retained	158,114	231,230	246,300
Total payments and changes in liabilities in respect of health insurance contracts:			
Gross	79,215	75,842	58,887
Reinsurance	(6,946)	(5,860)	(2,637)
Health insurance contracts retained	72,269	69,982	56,250
Total payments and changes in liabilities in respect of retained insurance contracts	250,900	310,536	315,946

NOTE 24 – COMMISSIONS, MARKETING EXPENSES AND OTHER ACQUISITION COSTS:

	Year ended December 31		
	2012	**2011**	**2010**
	ILS in thousands		
Acquisition costs:			
Acquisition commissions	40,587	37,157	33,732
Marketing and other expenses (reclassified from general and administrative expenses)	118,318	112,602	104,432
Change in Acquisition costs	(11,533)	(18,353)	(12,061)
Total commissions and other marketing and acquisitions expenses	147,372	131,406	126,103

NOTE 25 – GENERAL AND ADMINISTRATIVE EXPENSES:

	Year ended December 31		
	2012	2011	2010
	ILS in thousands		
Payroll and related expenses	163,271	150,651	133,989
Depreciation and amortization	10,228	9,694	8,609
Maintenance of offices and communication	23,642	23,471	24,481
Marketing and advertisement	49,239	47,731	47,854
Legal and professional consultation	7,122	8,748	8,233
Other	22,910	24,178	17,112
Total (*) (**)	276,412	264,473	240,278
Less:			
Amounts classified to changes in liabilities and payments in respect of insurance contracts	(16,016)	(15,608)	(14,125)
Amounts classified to commissions, marketing expenses and other acquisition expenses	(118,318)	(112,602)	(104,432)
General and administrative expenses	142,078	136,263	121,721
(*)General and administrative expenses include expenses in respect of share based payment in the total amount of	-	186	317
(**)Management and general expenses include expenses relating to mechanization in the total amount of	13,603	15,538	10,307

NOTE 26 – FINANCING EXPENSES:

	Year ended December 31		
	2012	2011	2010
	ILS in thousands		
Interest and exchange differences income (expenses)	(2,206)	*1,380	*(866)

* Reclassification

NOTE 27 – RISK MANAGEMENT:

General

The Company operates in the following operative segments: general insurance, health insurance and life insurance (only risk component). The Company's operations expose it to the following risks:

Insurance risks
Market risks
Liquidity risks
Credit risks
Operative risks

a. Description of risk management procedures and methods:

1. Risk management in the Company is based on the responsibility of the business bodies for the risks they take, the supporting units that include actuary, controller and risk management dealing with identification, mapping, follow up and control.

2. The Company has professional/insurance forums headed by the CEO and senior managers of the various company department; these forums discuss the issues of the profitability of the various branches and performed periodic assessments of risk factors and accordingly make managerial decisions.

3. The process of launching of new products includes identification and through assessment of the risks inherent in a products and determining the ways to manage and control the products. Where there is a concern that the underwriting results have been affected adversely by factors other than coincidental fluctuations, thorough tests are being made, inter alia, to assess the inherent risk, and if necessary, the assessment of reserves is adjusted. Similar tests are performed upon renewal of transactions.

4. In accordance with the regulatory requirements set to insurance companies, the Supervisor of Insurance has set requirements in connection with the unique risks, as follows:

   - Investment management - the Supervision Law and the Regulations regarding investment of insurer's capital set provisions regarding the manner of management of investments (threshold requirements for investments diversification, restrictions as to the types of investments and liquidity);
   - Insurance liabilities - provisions were set as to the assessment of the liabilities and presentation thereof (both from the actuarial and accounting aspects);
   - Capital requirements - provisions were set as to the minimum capital requirements due to the liabilities and the insurance operations.

5. The risk management policy is intended to support the attainment of the Company's business targets by limiting the potential losses at various risk levels and while taking into account the changes in the business environment and the requirements of the law and regulators.

NOTE 27 – RISK MANAGEMENT (continued):

a. Description of risk management procedures and methods (continued)**:**

The company has a risk management committee headed by the company's CEO; other members in the committee are a member of the board of directors, the officer in charge of risk management, the CFO, the appointed actuary and other member of the company's management. This committee convenes on a regular basis. In addition, there are other two subcommittees, which report to the risk management committee, a committee for management of insurance risk and a committee for management of operating risks.
Set forth below are the main Company bodies in charge of risk management on a current basis:

- Insurance risks - these risks are being managed the committee for management of insurance risk. Company's profit centers are subject to a constant supervision on a current basis, of the regional corresponding profit centers and of the AIG HQ in the USA in any matter related to approval of new projects and follow up of business results.
- Market risks - managed by the local investment committee and the regional credit committee of the AIG concern.
- Reinsurance - managed by the Company's risk committee concern and the profit centers thereof.
- Principal operative risks - managed by the managers of the departments and supervised by the company's CEO, the Information Systems CFO and the risk manager.

6. In addition, the Company is subject to the risk management guidelines and policy of the AIG concern. The Company reports to the AIG concern HQ, on a current basis the data reported includes information regarding the frequency of the exposure to the wide variety of potential risks and the amounts of the potential exposure.

7. The Company uses a policy of limiting the exposure to catastrophes by determining maximal coverage amounts in certain contract and by purchasing appropriate reinsurance coverage. The purpose of the insurance and reinsurance policy is to limit the exposure to catastrophes to a predetermined maximal loss and accordingly to the Company's risk factors, as determined by the Board of Directors.

b. Legal requirements

On October 3, 2006, the Supervisor of Insurance published Insurance circular No. 14-1-2006 that settles the appointment of the risk manager in an insurance company, his working procedures and his relationships with other office holders in the insurance company ("risk management circular"). The material risks included in this circular are the insurance and financial risks mentioned above. In accordance with this circular, the risk management includes the identification of the material risks that may affect the insurer's strength, the insurer's meeting its commitments to its insured people and bodies and the material risks arising from the assets held against the insurer's liabilities (including the appropriateness of the reinsurance settlement).

In addition, the Supervisor of Insurance published circulars that include provisions regarding management of specific exposure; these circulars refer mainly to: preparations to operating at the time of crisis, management of exposure to reinsurers, prevention of embezzlements and fraud (from inside and outside the Company) and management of information security risks and credit risks. The Company worked in the past and is still working to implement these circulars and to assimilate appropriate procedures and controls. The company is making preparations for the application of the Supervisor's circulars regarding Solvency II.

NOTE 27 – RISK MANAGEMENT (continued):

c. Market risks

Market risk is the risk that the fair value of the future cash flows from financial assets, financial liabilities or insurance liabilities would change as a result of the changes in the market prices. Market risks include, among others, risks arising from changes in the rates of interest, share prices, consumer price index and exchange rates of foreign currencies.

1. Market Risk Sensitivity Tests

Set forth below is a sensitivity analysis relating to the effect of the changes of the above factors on the income (loss) for the year and on the comprehensive income (capital). The sensitivity analysis is made for the financial assets, financial liabilities and the insurance contract liabilities in respect of the relevant risk variable as of each reporting date and under the assumption that all other variables are fixed. The change in interest, for example, is analyzed under the assumption that all other parameters have not changed. It is assumed that the said changes do not reflect permanent impairment in the value of assets presented at amortized cost and therefore the said sensitivity test does not include impairment losses in respect of these assets.
The sensitivity test reflects only direct effects.

It should also be indicated that the sensitivities are not linear; thus, larger or smaller changes compared to the changes described above do not necessarily constitute a simple extrapolation of the effect of the relevant changes.

Data as of December 31, 2012:

	Rate of interest (1)		Investments in capital instruments (2)		Rate of change in the consumer price index		The rate of change in the exchange rate of the foreign currency	
	+1%	-1%	+10%	-10%	+1%	-1%	+10%	-10%
	ILS in thousands							
Profit (loss)	(49,697)	49,524	16,177	(16,177)	2,360	(2,360)	3,953	(3,953)
Comprehensive income (shareholders' equity)(3)	(49,697)	49,524	16,177	(16,177)	2,360	(2,360)	3,953	(3,953)

Data as of December 31, 2011:

	Rate of interest (1)		Investments in capital instruments (2)		Rate of change in the consumer price index		The rate of change in the exchange rate of the foreign currency	
	+1%	-1%	+10%	-10%	+1%	-1%	+10%	-10%
	ILS in thousands							
Profit (loss)	(41,918)	41,817	8,825	(8,825)	570	(570)	7,569	(7,569)
Comprehensive income (shareholders' equity)(3)	(41,918)	41,817	8.825	(8,825)	570	(570)	7,569	(7,569)

(1) The sensitivity test of the change in interest was made both in respect of fixed interest rates and in respect of variable interest instruments. As to fixed interest instruments - the exposure is in respect of the book value of the instrument; as to variable interest instruments, the exposure is in respect of the cash flow arising from the financial instrument.

(2) Investments in instruments that do not have a fixed cash flow or alternatively, the Company does not have data regarding this cash flow.

(3) The sensitivity tests regarding the comprehensive income also reflect the effect on the income (loss) for the reported period.

NOTE 27 – RISK MANAGEMENT (continued):

c. Market risks (continued):

2. Direct interest risk

The direct interest risk is the risk that a change in the market interest rate will cause a change in the fair value of the financial assets or liability. This risk relates to assets that are paid off in cash. The addition of the word "direct" underscores the fact that change of interest can also affect other types of assets but not directly, such as the impact of a change in the interest rate on share prices.

Set forth below is a breakdown of the assets and liabilities by exposure to interest risks:

	Nonprofit participating assets and liabilities as of December 31	
	2012	**2011**
	ILS in thousands	
Assets with direct interest risk:		
Marketable debt instruments	1,099,646	978,556
Cash and cash equivalents	93,540	103,562
Total assets with direct ineterst risk	1,193,186	1,082,118
Total assets without direct interest risk	1,195,863	1,018,187
Total assets	2,389,045	2,100,305
Liabilities with direct interest risk:		
Liabilities in respect of insurance contracts non depending yield	4,102	-
Liabilities for employee rights upon Retirements	2,326	2,047
Liabilities in respect of reinsurers	231,465	197,723
Total liabilities with direct interest risk	237,893	199,770
Total liabilities without direct interest risk	1,574,048	1,480,768
Shareholders' equity	577,104	419,767
Total equity and liabilities	2,389,045	2,100,305
Total assets, net of liabilities	577,104	419,767

Assets without direct interest risk include nonmarketable assets, shares, property and equipment, deferred acquisition costs and other assets as well as groups of balance sheet financial assets. Therefore, the interest risk in respect of those assets is relatively low; (collectible premiums, current balances of insurance companies and accounts receivables).

Liabilities without a direct interest risk include liabilities in respect of nonprofit participating insurance contracts and investment contracts, liabilities in respect of deferred taxes, net, liabilities in respect of current taxes and other accounts payable.

NOTE 27 – RISK MANAGEMENT (continued):

c. Market risks (continued):

3. Breakdown of assets and liabilities of the Company by linkage bases

	As of December 31, 2012				
	In ILS unlinked	**In ILS linked to the CPI**	**In foreign currency (Dollar, Euro and other) or linked thereto**	**Nonmonetary items and others**	**Total**
	ILS in thousands				
Intangible assets				15,732	15,732
Deferred acquisition costs				130,191	130,191
Property and equipment				16,885	16,885
Reinsurance assets	16,009	525,691	43,832		585,532
Premiums to be collected	131,003	28,840	14,312		174,155
Other accounts receivables	11,483	108	1,446	20,631	33,668
Other financial investments:					
Marketable debt instruments	287,098	787,095	25,453		1,099,646
Nonmarketable debt instruments		75,284	2,641		77,925
Shares				68,284	68,284
Other			8,090	85,397	93,487
Total other financial investments	287,098	862,379	36,184	153,681	1,339,342
Other cash and cash equivalents	79,833		13,707		93,540
Total assets	525,426	1,417,018	109,481	337,120	2,389,045
Total shareholders' equity				577,104	577,104
Liabilities:					
Liabilities in respect of insurance contracts and investment contracts that are nonprofit participating contracts	222,887	1,127,096	59,357		1,409,340
Liabilities in respect of deferred taxes - net				8,877	8,877
Liabilities for employee rights upon retirement	2,326				2,326
Other accounts payable and surplus reserves	320,812	48,548	10,594	11,444	391,398
Total liabilities	546,025	1,175,644	69,951	20,321	1,811,941
Total liabilities and shareholders' equity	546,025	1,175,644	69,951	597,425	2,389,045
Total balance sheet exposure	(20,599)	241,374	39,530	(260,305)	

NOTE 27 – RISK MANAGEMENT (continued):

c. Market risks (continued):

3. Breakdown of assets and liabilities of the Company by linkage bases (continued):

	As of December 31, 2011				
	In ILS unlinked	**In ILS linked to the CPI**	**In foreign currency (Dollar, Euro and other) or linked thereto**	**Nonmonetary items and others**	**Total**
	ILS in thousands				
Intangible assets				9,983	9,983
Deferred acquisition costs				118,658	118,658
Property and equipment				18,743	18,743
Reinsurance assets	11,911	464,924	48,960		525,795
Premiums to be collected	118,353	23,404	14,456		156,213
Other accounts receivables	9,309	10,952	1,727	19,702	41,690
Other financial investments:					
Marketable debt instruments	317,686	622,350	38,520		978,556
Nonmarketable debt instruments		56,156	2,703		58,859
Shares				50,934	50,934
Other			14,068	23,244	37,312
Total other financial investments	317,686	678,506	55,291	74,178	1,125,661
Other cash and cash equivalents	84,086		19,476		103,562
Total assets	541,345	1,177,786	139,910	241,264	2,100,305
Total shareholders' equity				419,767	419,767
Liabilities:					
Liabilities in respect of insurance contracts and investment contracts that are nonprofit participating contracts	200,615	1,120,825	63,850		1,385,290
Liabilities in respect of deferred taxes - net				7,376	7,376
Liabilities for employee rights upon retirement	2,047				2,047
Other accounts payable and surplus reserves	273,729		374	11,722	285,825
Total liabilities	476,391	1,120,825	64,224	19,098	1,680,538
Total liabilities and shareholders' equity	476,391	1,120,825	64,224	438,865	2,100,305
Total balance sheet exposure	64,954	56,961	75,686	(197,601)	

NOTE 27 – RISK MANAGEMENT (continued):

c. Market risks (continued):

4. Breakdown of exposure of economic sectors to investments in equity instruments:

	As of December 31, 2012 (ILS in thousands)			
	Listed on TA100 index	**Listed on TA MidCap index**	**Total**	**% of total**
Economic sector:				
Industry	17,771	-	17,771	26.0
Banks	14,900	-	14,900	21.8
Construction and real estate	9,715	-	9,715	14.2
Financial services	7,002	-	7,002	10.4
Investment and holdings	6,370	-	6,370	9.3
Communication and computer services	4,455	-	4,455	6.5
Food and tobacco	3,127	-	3,127	4.6
Oil exploration	2,688	-	2,688	3.9
Commerce	1,390	-	1,390	2.0
Electricity and water	866	-	866	1.3
Total	**68,284**	**-**	**68,284**	**100.0**

	As of December 31, 2011 (ILS in thousands)			
	Listed on TA100 index	**Listed on TA MidCap index**	**Total**	**% of total**
Economic sector:				
Industry	15,808	-	15,808	31.0
Banks	9,700	-	9,700	19.0
Communication and computer services	6,696	-	6,696	13.1
Construction and real estate	4,824	-	4,824	9.5
Investment and holdings	3,981	300	4,281	8.4
Financial services	3,416	-	3,416	6.7
Food and tobacco	1,983	-	1,983	3.9
Commerce	1,872	-	1,872	3.7
Oil exploration	1,405	-	1,405	2.8
Electricity and water	703	-	703	1.4
Other services	246	-	246	0.5
Total	**50,634**	**300**	**50,934**	**100.0**

NOTE 27 – RISK MANAGEMENT (continued):

d. Liquidity risk

A liquidity risk is the risk that the Company would be required to dispose of its assets at inferior prices in order to meets its obligations. The Company is exposed to risks stemming from the uncertainty as to the dates in which it would be required to pay insured entities or individual the amounts their claims in proportion to the scope of funds that will be available for that purpose on that date. A potential need to recruit funds unexpectedly and during a shortterm period may require significant disposal of assets over a shortterm period and the sale thereof at prices that would not necessarily reflect their market prices.

Management of assets and liabilities

The Company manages its assets and liabilities in accordance with the requirements of the Supervision Law and regulations promulgated thereunder.

The tables presented below include the estimated repayment dates of the amounts of the undiscounted insurance liabilities of the Company.

The estimated repayment dates of the liabilities in respect of general insurance contracts were included in the table as follows:

Insurance liabilities estimated by an actuary - on the basis of an actuarial estimate.
Insurance liabilities in nonstatistical insurance branches and in branches not assessed by an actuary, except for the property branches as well as excess of income over expenses (accumulation) is reported in the column "without definite fixed repayment date".

The estimated repayment dates of the liabilities in respect of life and health insurance contracts were included in the tables on the basis of an actuarial estimate.

Liabilities in respect of life insurance contracts and health* insurance contracts:

	Less than one year	Between 1 and 5 years	Between 5 and 10 years	Between 10 and 15 years	More than 15 years	Without fixed repayment date	Total
	ILS in thousands						
As of December 31, 2012	69,279	67,583	6,982	2,485	5,629	-	151,958
As of December 31, 2011	60,234	66,607	7,644	2,697	5,527	-	142,709

Liabilities in respect of general insurance contracts:

	Less than one year	Between 1 and 3 years	Between 3 and 5 years	More than 5 years	Without fixed repayment date	Total
	ILS in thousands					
As of December 31, 2012	401,105	205,188	162,193	374,441	114,455	1,257,382
As of December 31, 2011	371,412	178,672	155,718	329,266	207,513	1,242,581

* Liabilities for reinsurers would be repaid within 18 months from the end of the current year. Financial liabilities in respect of accounts payable are expected to be repaid during the year.

NOTE 27 – RISK MANAGEMENT (continued):

e. Insurance risks

The insurance risks include, inter alia, the following:

Underwriting risks: The risk that erroneous pricing would be used as a result of deficiencies in the underwriting process and from the differences between the risk upon pricing and determining the premium and actual events so that the premiums that are collected are not sufficient to cover future claims and expenses. The differences may arise from incidental changes in the business results and from changes in the cost of the average claim and/or the frequency of the claims due to various factors.

Reserve risks: The risk for an erroneous estimation of the insurance liabilities that may bring about a situation where the actuarial reserves are insufficient to cover all the liabilities and claims. The actuarial models in accordance with which the Company assesses its insurance liabilities are based on the assumption that the pattern of behavior and claims in the past represents future events. The Company's exposure is composed of the following risks:

1. Model Risk the risk of electing an erroneous model of pricing and/or for assessment of the insurance liabilities.
2. Parameter risk – the risk for usage of erroneous parameters, including the risk that the amount to be paid for settlement of the insurance liabilities of the Company or that the date of the settlement of the insurance liabilities would be different from the expected amount or date.

Catastrophe risk: Exposure to the risk that a single event of extensive effect (a catastrophe) such as natural catastrophe, war, terrorism, would cause an accumulation of damages of extensive scope. The material catastrophic event to which the Company is exposed to in Israel is and earthquake

The amount of the maximal loss expected in the general insurance business as a result from the exposure to a single large damage or accumulation of damages due to a very big event at a maximal possible loss (MPL) probability of 1.34%is ILS 829.1 million (gross) and ILS 47.2 million (retained).

As to the data regarding the various insurance products in respect of which the insurer is exposed to an insurance risk, see the breakdown of the insurance liabilities by insurance risk in note 4 - additional data as to the general insurance segment and breakdown of assets and liabilities in respect of life insurance contracts by insurance exposure and in note 16 - the breakdown of insurance liabilities arising from health insurance.

e1. Insurance risk embedded in life insurance contracts

General

Set forth below is the description of the various insurance contracts and the assumptions used for computation of the liabilities related to those products, based on the type of the product. In general, based on the supervisor's instructions, the insurance liabilities are computed by an actuary, based on accepted actuarial methods and consistently with previous year. The liabilities are computed in accordance with the relevant coverage data, such as age and sex of the insured person, the period of insurance, the date of commencement of the insurance, the type of the insurance, periodic premium and the amount of insurance.

NOTE 27 – RISK MANAGEMENT (continued):

Actuarial methods used for computation of the insurance liabilities:

1) The "individual personal accidents" plans include pure risk products (death as a result of an accident, disability as a result of accident) that are sold as independent policies. For those plans the liability is computed on an actuarial basis. The computation is made using the "Gross Premium Reserve" method that includes in the expected proceeds all the premium components and reduces the expected expenses and commissions.

2) The liability in respect of pending claims related to health and personal accidents include mainly provisions for pending claims for risks of death and disability from accident, and a provision for IBNR.

3) The liability in respect of life insurance contracts for groups is composed o the liability in respect of unearned premium and provision to IBNR

4) The computation is made on a gross basis. Some of reinsurance is computed based on the agreements.

The main assumptions used for computation of insurance liabilities:

1) Rate of discount

   In the life insurance sector that includes pure risk products with fixed premium the discount rate used is of 2.5%.

2) The rates of mortality and illness:

   a) The mortality rates used to compute the insurance liabilities under life insurance policies in respect of mortality of insured individuals are identical to the rates used to determine the tariff.

   b) The rates of illness refer to the frequency of claims in respect of serious illnesses. These rates were determined based on researches made by reinsurers. The higher the assumption regarding rate of illness will be, the higher the insurance liability as a result of serious illnesses.

Sensitivity analyses in life insurance:

As of December 31, 2012 (in thousands of ILS):

	Rate of illness and mortality	
	+10%	**-10%**
Profit (loss)	(1,438)	1,582

e2. Insurance risk embedded in health insurance contracts and personal insurance contracts

General

Set forth below is the description of the various insurance contracts and the assumptions used for computation of the liabilities related to those products, based on the type of the product. In general, based on the supervisor's instructions, the insurance liabilities are computed by an actuary, based on accepted actuarial methods and consistently with previous year. The liabilities are computed in accordance with the relevant coverage data, such as age and sex of the insured person, the period of insurance, the date of commencement of the insurance, the type of the insurance, periodic premium and the amount of insurance.

NOTE 27 – RISK MANAGEMENT (continued):

Actuarial methods used for computation of the insurance liabilities:

1) The "individual personal accidents" plans include pure risk products (death as a result of an accident, disability as a result of accident) that are sold as independent policies. For those plans the liability is computed on an actuarial basis. The computation is made using the "Gross Premium Reserve" method that includes in the expected proceeds all the premium components and reduces the expected expenses and commissions.

2) The liability in respect of pending claims related to health and personal accidents include mainly provisions for pending claims for risks of death from accident, serious illnesses and disability from an accidents and a provision for IBNR - Incurred by not Reported Losses. For the personal accidents sectors - both individual and group - the Link Ration models were set up on the basis of accumulated cost of the claims (payments of the claims with the addition of individual assessments and - Average Cost per Claim. The models are settled at the level of quarterly damage.

3) The data used in the models are claims below a certain scope; there is a separate level to larger claims; the frequency of claims and the size of an average claim are derived from this model.

4) The computation is made on a gross basis. Some of the reinsurance is computed based on the agreements.

The main assumptions used for computation of the insurance liabilities:

1) Rate of discount

In the Personal accidents – individual sector the gross premium reserve is computed on the basis of a risk free interest.

2) The rates of mortality and illness

The rates of illness refer to the frequency of claims in respect of serious illnesses, disability as a result of accidents and death as a result of an accident. These rates were determined based on the Company's past experience. The higher the assumption regarding rate of illness will be, the higher the insurance liability as a result of serious illnesses and disability as a result of an accident.

Sensitivity analysis in health insurance and personal accidents insurance

As of December 31, 2012 (ILS in thousands):

	Rate of illness	
	+10%	**-10%**
Profit (loss)	(12,703)	11,286

3) Rates of cancellations

The rates of cancellations affect the insurance liabilities in respect of part of some of the health insurances. Insurance contracts can be cancelled by the Company due to unpaid premiums or at the request of the owner of the policy. The assumptions as to the rates of cancellations are based on the company's past experience based on the type of the products, the estimated useful life of the product and sales trends. A 10% increase or decrease in the cancellations assumption is immaterial for the profit item since the gross premium reserve is relatively small.

NOTE 27 – RISK MANAGEMENT (continued):

e3. Insurance risk in general insurance contracts

A summary of the main insurance sectors in which the Company operates

The Company writes insurance contracts in the field of general insurance, mainly in the compulsory car insurance sector, liabilities, car damages insurance and property insurance

Compulsory car insurance covers the owner of the policy and the driver for any liability they may incur as a result of the provisions of the Road Accidents Victims Compensation Law, 1975, for bodily damage caused as a result of usage of motor vehicle to the driver, the passengers or pedestrians hit by the car. Compulsory car insurance claims are characterized
by a long tail, i.e., sometimes a long period of time elapses from the date the event takes place to the final settlement of the claim.

The liability insurances are designed to cover the liability of an insured person for any damage he may cause to a third party. The two main types of insurance are: liability to a third party, liability of employers, other liability insurances such as professional responsibility, liability arising due to products and directors and office holders' responsibility. The timing of the filing of the claims and the settlement thereof is influenced from several factors, such as the type of coverage, the terms of the policy and legislation and legal precedents. Normally, the claims in the liability insurance are characterized by a long tail. i.e., sometimes a long period of time elapses from the date the event takes place to the final settlement of the claim.

Policy for insurance of car damages and third party car damages entitle the insured person with property damage coverage. The coverage is usually limited to the value of the damaged car. The tariff for vehicle damage insurance requires the approval of the supervisor and the same applies for the approval of the policy as a whole; the said tariff is an actuarial tariff and partially differential (varies in accordance with the risk). The said tariff is based on several parameters, both parameters that are related to the vehicle insured under the policy (such as the type of the vehicle, year of manufacture etc.) and parameters related to characters of the person insured (age of the drivers, claims history etc.). The underwriting procedure is partially performed through the tariff itself and partly based on a system of procedures that are designed to examine the claims history of the person insured that include presentation a noclaim certificate from a previous insurer (for the last three years), presentation of up to date certificate of defense, etc. The implementation of the procedures is mechanically combined into procedure of issuance of the policies.

In most of the cases the car damages insurance policies are issued for a oneyear period. Also, in most cases, claims in respect of these policies are settled close to the time in which the insurance event happened.

Property insurance policies are intended to provide the insured person coverage against physical damage to his property and loss of profits due to the damage caused to his property.

The main risks covered by property insurance policies are fire risks, explosion, burglary, earthquake and natural catastrophe. The property insurance policies sometimes include coverage for loss of profits originating in physical damage to property. Property insurance constitutes an important part of apartments insurance, business insurance, engineering insurances, freight (sea freight, land freight, air freight) etc.). In most cases, claims regarding those policies are settled close to the time in which the insurance event happened.

NOTE 27 – RISK MANAGEMENT (continued):

Principles of computation the actuarial assessment in general insurance:

General:

a) The liabilities in respect of general insurance contracts include the following components:
- Reserve for premium that has not yet been earned.
- Deficient premium.
- Pending claims

The provision for premium that has not yet been earned and the deferred acquisition costs are computed independently of any assumption and are therefore they are not exposed to the reserve risk. As to the manner in which these provisions are computed see the note referring to accounting policy.

b) In accordance with the instructions of the supervisor, the pending claims are computed by an actuary based on accepted actuarial methods consistently with previous year. The election of the actuarial method appropriate for each insurance sector and for each year of event/underwriting is being made using discretion in accordance with the extent to which the method is suitable for the sector and sometimes the various methods are combined. The assessments are based mainly on past experience of the development of payments regarding claims and/or developments in the amount of payments and specific assessments. The assessments include assumptions regarding the cost of an average claims, costs of handling of claims and the frequency of the claims. Further assumptions may be in respect of changes in rates of interest, exchange rates and the timing of payments. The payments of the claims include direct and indirect claims for settlement of claims, net of subrogation and excess insurance.

c) The usage in actuarial methods that are based on developments of claims is mainly appropriate when there is stable and satisfactory information regarding payments of claims and/or specific assessments used in order to assess the total expected cost of claim. Where the information available regarding the actual experience regarding the claims is insufficient the actuary sometime uses a computation weighting a known estimate (made by the Company and/or the sector) such as loss ratio and the development of actual claims. A greater importance is given to the assessment that is based on experience as time elapses and further data is accumulated regarding the claims.

d) Also included are quantitative assessments and discretion is used as to the extent that past trends would not continue in the future. For example, due to oneoff event, internal changes, such as a change in the mix of the portfolio, the underwriting policy and procedures and due to the effects of external factors such as legal rulings, legislation, etc. When changes as above are not fully reflected in the past experience the actuary updates the models and/or makes specific provisions based on statistical and/or legal assessments as appropriate.

e) In cases of large claims of nonstatistical characters, the provision is determined (gross and retained) based on an opinion issued by Company's experts and in accordance with the recommendations of its legal advisors.

f) The share of the reinsurers in the pending claims is estimated taking into account the type of the agreement (proportionate/disproportionate), actual experience in the claims and the premium transferred to reinsurer.

g) The assessment of the pending claims in respect of the Company's share in the pool was based on a computation performed by the pool.

NOTE 27 – RISK MANAGEMENT (continued):

Breakdown of actuarial methods in the principal insurance sectors:

a) The vehicle damage insurance

In the vehicle damage sector, the liabilities are computed based on the development of the claims payments and the development of the payments amounts and the specific assessment, while referring to the types of coverage such as comprehensive/third party coverage and the types of damages such as self damage/third party/theft/total loss. For the last months of damage in respect of which there are not enough data the average method is also used when determining the cost of claim.

b) Compulsory vehicle insurance

In the compulsory vehicle insurance the liabilities are computed based on the development of payments and pending amounts in respect of claims of smaller amounts (not exceeding ILS 1 million). The liabilities in respect in amounts exceeding ILS 1 million are computed in accordance with actuarial models that are based on development payments and pending claims. The share of the reinsurers in the claims in respect of excess contracts is computed in accordance with the model for larger claims (more than ILS 1 million) and in accordance with the actual claims of amounts in excess of ILS 1 million.

There is also an additional provision of ILS 21.6 million in respect of changes in legislation and rulings.

c) Liabilities insurance

In the liabilities insurance the liabilities are computed based on the development of identified claims. For periods in respect of which there are not enough data ,the cost of claims is computed using the loss ratio method. In large claims the specific assessments of the claims department are also taken into account.

d) Property insurance and other

In property insurance and other insurance, the liabilities are computed based on the development of the claims payments and/or development of the payments and pending claims.

The principal assumptions that were taken into account for purpose of actuarial assessment:

a) Pending claims in compulsory vehicle and Liabilities insurance were not capitalized.

b) No addition was made to the basis of the provision in the compulsory vehicle insurance and liabilities insurance in respect of risk margin (standard deviation).

NOTE 27 – RISK MANAGEMENT (continued):

f. Credit risk data:

1. Distribution of debt instruments by location:

	December 31, 2012		
	Marketable	Nonmarketable	Total
	ILS in thousands		
Domestic	1,092,716	75,284	1,168,000
Abroad	6,930	2,641	9,571
Total debt instruments	1,099,646	77,925	1,177,571

	December 31, 2011		
	Marketable	Nonmarketable	Total
	ILS in thousands		
Domestic	956,310	58,859	1,015,169
Abroad	22,246	-	22,246
Total debt instruments	978,556	58,859	1,037,415

2. Breakdown of assets by ratings:

a1. Debt assets (excluding cash and cash equivalents and other receivables):

	Domestic rating			
	As of December 31, 2012			
	-AA and above	BBB through A+	Lower than BBB	Total
	ILS in thousands			
Debt assets in Israel:				
Marketable debt assets:				
Government bonds	803,392	-	-	803,392
Corporate bonds	163,464	122,806	3,054	289,324
Total marketable debt assets in Israel	966,856	122,806	3,054	1,092,716
Nonmarketable debt assets:				
Government bonds	-	-	-	-
Corporate bonds	14,817	2,718	155	17,690
Deposits with banks and financial institutions	57,594	-	-	57,594
Total nonmarketable debt assets in Israel	72,411	2,718	155	75,284
Total domestic debt instruments	1,039,267	125,524	3,209	1,168,000

	International rating			
	As of December 31, 2012			
	A and above	BBB	Lower than BBB	Total
	ILS in thousands			
Debt assets abroad:				
Marketable debt assets :				
Government bonds	6,930	-	-	6,930
Total marketable debt assets abroad	6,930	-	-	6,930
Nonmarketable debt assets:				
Corporate bonds	-	-	2,641	2,641
Total nonmarketable debt assets abroad	-	-	2,641	2,641
Total debt assets abroad	6,930	-	2,641	9,571

NOTE 27 – RISK MANAGEMENT (continued):

	Domestic rating			
	As of December 31, 2011			
	AA and above	BBB through A+	Lower than BBB	Total
	ILS in thousands			
Debt assets in Israel:				
Marketable debt assets:				
Government bonds	677,098	-	-	677,098
Corporate bonds	178,620	100,592	-	279,212
Total marketable debt assets in Israel	855,718	100,592	-	956,310
Nonmarketable debt assets:				
Government bonds	-	-	-	-
Corporate bonds	23,923	4,717	2,703	31,343
Deposits with banks and financial institutions	27,516	-	-	27,516
Total nonmarketable debt assets in Israel	51,439	4,717	2,703	58,859
Total domestic debt instruments	907,157	105,139	2,703	1,015,169

	International rating			
	As of December 31, 2011			
	AA and above	BBB through A+	Lower than BBB	Total
	ILS in thousands			
Debt assets abroad:				
Marketable debt assets :				
Government bonds	20,421	-	-	20,421
Total marketable debt assets abroad	20,421	-	-	20,421
Nonmarketable debt assets:				
Corporate bonds	1,825	-	-	1,825
Total nonmarketable debt assets abroad	1,825	-	-	1,825
Total debt assets abroad	22,246	-	-	22,246

a2. Credit risk in respect of other financial assets (in Israel)

	Domestic rating				
	As of December 31, 2012				
	A and above	BBB	Lower than BBB	Not rated	Total
	ILS in thousands				
Accounts receivable - excluding balances of reinsurers	-			206,136	206,136
Cash and cash equivalents	93,347			193	93,540
	93,347			206,329	299,676

	Domestic rating				
	As of December 31, 2011				
	A and above	BBB	Lower than BBB	Not rated	Total
	ILS in thousands				
Accounts receivable - excluding balances of reinsurers				196,638	196,638
Cash and cash equivalents	103,387			175	103,562
	103,387			196,813	300,200

NOTE 27 – RISK MANAGEMENT (continued):

3. Additional data regarding credit risks:

   a. The systems of ratings of domestic debt instruments and debt instruments abroad vary from one another. It should be indicated that in accordance with the Capital Market circular 2008-6-1, regarding the publication of data for conversion of the Israeli rating system and the international rating system, the supervisor instructed that through January 1, 2009 the rating companies that received the approval of the Commissioner of Capital Market, Insurance and Savings to operate as a rating company in accordance with the Capital Market circular 2004/1 are to publish a system for the conversion of the Israeli rating into the international rating.

   b. As to the balances of reinsurers - of ILS 585,532 - see the note relating to assets of reinsurance.

4. Breakdown of exposure of economic sectors to investments in marketable and marketable financial debt instruments:

	As of December 31, 2012	
	Balance sheet credit risk	
	Amount	% of total
	ILS in thousands	
Economic sector:		
Banks	124,781	10.5
Construction and real estate	100,869	8.6
Investment and holdings	47,780	4.1
Other business services	31,679	2.7
Industry	27,972	2.4
Communication and media	18,766	1.6
Financial services	10,336	0.9
Commerce	5,066	0.4
	367,249	31.2
Government bonds	810,322	68.8
Total	**1,177,571**	**100.0**

	As of December 31, 2011	
	Balance sheet credit risk	
	Amount	% of total
	ILS in thousands	
Economic sector:		
Banks	95,488	9.2
Construction and real estate	69,339	6.7
Investment and holdings	77,788	7.5
Other business services	35,513	3.4
Industry	29,540	2.9
Communication and media	14,399	1.4
Financial services	12,760	1.2
Commerce	5,069	0.5
	339,896	32.8
Government bonds	697,519	67.2
Total	**1,037,415**	**100.0**

NOTE 27– RISK MANAGEMENT (continued):

5. Reinsurance

The Company insures some of its businesses under reinsurance, most of which is being performed through reinsurers abroad. Nevertheless, the reinsurance does not release the direct insurers from their obligations to the insured entities or individuals under the terms of the insurance policies.

The Company is exposed to risks arising from uncertainty as to the ability of the reinsurers to pay their share in the liability in respect of insurance contract (the reinsurance assets) and their obligations in respect of claims that were paid. This exposure is managed by holding a followup on a current basis with regard to the reinsurer's situation in the world market and a followup with respect of the fulfillment of the reinsurer's financial liabilities.

Under the guidelines set by the Supervisor, the Board of Directors set one a year, maximal exposure levels to the reinsurer with which the Company entered (or will enter) into reinsurance agreement; such levels are based on the reinsurers' international rating. Also, the Company's exposures are divided between various reinsurers; the most significant of these exposures are to reinsurers of high international ratings.

a. In 2012, most of the Company's general insurance contracts (include earthquake exposure) were with insurance companies, as follows:

- Chartis Overseas
- New Hampshire Insurance Company
- National Union Fire Insurance Company of Pittsburgh, PA
- American Home Assurance Company
- AIG Europe Ltd

b. The above-mentioned companies are global AIG Corporation companies and were granting A rating by the leading international rating agencies; (Chartis Overseas is only rted by Fitch).

NOTE 27 – RISK MANAGEMENT (continued):

c. Data regarding the exposure to credit risks as of December 31, 2012:

Rating group	Total premiums to reinsurers for 2012	Credit balances (B)	Reinsurance assets: Life insurance	Reinsurance assets: Property insurance	Reinsurance assets: Liabilities insurance	Deposits of reinsurers	amount of letters of credit received from reinsurers	Total exposure (a)	Debts in arrears: 0.5-1 year	Debts in arrears: In excess of 1 year
	ILS in thousands									
-AA or above										
GEN RE	3,124	(111)	892	-		1,166		(385)		
SWISS RE	16,122	(2,085)	6,459	-		6,316		(1,942)		
Other	1,438	216	-	-		-		216		
A										
Partner Reinsurance Co Hd	2,629	(188)	1,307	-	-	809		310		
American Home Assurance Co.	14,203	(445)	-	5,785	48,211	22,317		31,234		
Chartis Overseas Ltd	95,163	(2,983)	-	38,763	323,013	149,526		209,267		
National Union Fire Insurance Co. Of Pittsburgh, PA	15,624	(490)	-	6,364	53,032	24,549		34,357		
New Hampshire Insurance Co.	17,044	(534)	-	6,943	57,853	26,781		37,481		
Other companies in the AIG international corporation	16,176	(3,436)	-	32,207	4,499	-		33,270		
Other	2,922	173	-	204	-	-		377		
	163,761	(7,903)	1,307	90,266	486,608	223,982		346,296		
BBB+										
Other	226	16	-	-	-	-		16		
	226	16	-	-	-	-		16		
Total	184,671	(9,876)	8,658	90,266	486,608	231,464		344,201		

NOTE 27 – RISK MANAGEMENT (continued):

c. Data regarding the exposure to credit risks as of December 31, 2011

			Reinsurance assets						Debts in arrears	
Rating group	**Total premiums to reinsurers for 2011**	**Credit balances (B)**	**Life insurance**	**Property insurance**	**Liabilities insurance**	**Deposits of reinsurers**	**amount of letters of credit received from reinsurers**	**Total exposure (a)**	**0.5-1 year**	**In excess of 1 year**
					ILS in thousands					
AA or above										
GEN RE	4,025	(866)	1,236	-		1,436		(1,066)		
SWISS RE	14,306	(2,730)	6,732	-		5,638		(1,636)		
Other	873	(247)	-	-		-		(247)		
	19,204	(3,843)	7,968			7,074		(2,949)		
A										
Partner Reinsurance Co Hd	816	(58)	157	-	-	325		(226)		
American Home Assurance Co.	9,840	648	-	7,336	41,783	17,590		32,177		
Chartis Overseas Ltd	65,927	4,345	-	49,153	279,945	117,857		215,586		
National Union Fire Insurance Co. Of Pittsburgh, PA	10,824	713	-	8,070	45,961	19,349		35,395		
New Hampshire Insurance Co.	11,808	778	-	8,804	50,139	21,108		38,613		
Other companies in the AIG international corporation	44,817	(3,674)	-	7,980	18,351	14,420		8,237		
Other	3,862	397	-	149	-	-		546		
	147,894	3,149	157	81,492	436,179	190,649		330,328		
Total	167,098	(694)	8,125	81,492	436,179	197,723		327,379		

NOTE 27 – RISK MANAGEMENT (continued):

g. **Operating risks –** as part of the management of its operating risk management, the company set up a disaster recovery plan (DRP) and a business continuity planning (BCP) in order to prepare for a damages to its operating infrastructure. In addition the Company performs risk and embezzlement surveys in the various departments in order to map and strengthen the internal audit and control procedures.

The company has established a risk management committee headed by the company's CEO; other members in the committee are a member of the board of directors, the officer in charge of risk management, the CFO, the appointed actuary and other member of the company's management. This committee convenes on a regular basis. In addition, there are other two subcommittees, which report to the risk management committee, a committee for management of insurance risk and a committee for management of operating risks.

The Company commenced implementation of the provisions of Section 404 of the Sarbanes Oxley Law that was applied to institutional entities; the Company also performs an operating risks survey in order the map the exposures and to improve coping with these risks.

NOTE 28 – BALANCES AND TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES

Interested parties as defined in the Israeli Securities Regulations (Preparation of Annual Financial Statements), 2010.
Related parties - as defined in IAS 24 - "Related Party Disclosures".

a. Balances with interested parties and related parties

	December 31	
	2012	2011
	ILS in thousands	
Premium to be collected	18	20
Reinsurance assets	576,670	517,927
Accounts receivable	804	755
Accounts payable and surplus reserves	3,206	2,003
Liabilities of reinsurers	231,061	202,156

b. Transactions with interested parties and related parties

Office holders in the Company may purchase' from time to time' insurance contracts issued by the company under market conditions and in the ordinary course of business.

	December 31		
	2012	2011	2010
	ILS in thousands		
Premiums - gross	366	363	470
Reinsurance premiums	158,211	143,215	134,107
Income from commissions	43,932	39,893	36,354
Increase in insurance liabilities and payments in respect of insurance contracts	146,684	114,397	95,215
Administrative and general expenses	8,881	8,730	7,318
Financial income (expenses)	(3,443)	(4,349)	(1,926)

NOTE 28 – BALANCES AND TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES (continued):

c. Benefits to key management personnel

Key management personnel, which are being an integral part of related parties as defined by IAS24, includes members of the bored and members of senior management.

	For the year ended December 31					
	2012		2011		2010	
	No. of people	Amount	No. of people	Amount	No. of people	Amount
			ILS in thousands			
Shortterm benefits	14	9,385	16	9,360	15	7,575
Other longterm benefits	14	1,450	16	2,054	15	1,578
Sharebased payment	8	-	8	186	8	317
		10,835		11,600		9,470

d. Benefits to related parties and other interested parties:

	For the year ended December 31					
	2012		2011		2010	
	No. of people	Amount	No. of people	Amount	No. of people	Amount
			ILS in thousands			
Fees to directors	4	704	4	512	3	456
	4	704	4	512	3	456

e. Income and expenses from related parties and interested parties:

1.Employment terms with related parties

Some of the Company's financial and insurance operations are performed with related parties and interested parties at the ordinary course of business and at market prices. As to details regarding material transactions with related party, see section b. above and note 27f.

2. Sharebased payments plan and bonuses to employees:

a. Sharebased payments

The company is part of global AIG Corporation, which adopted in recent years share based payment plans for employees of the AIG group; the plans include grant of options and other equity instruments not registered for trade (hereafter – RSU) and convertible into global AIG Corporation shares. In the past the plans included granted of options and RSU; however, the quantity thereof in 2012 is negligible and so is the probability of exercise thereof.

NOTE 28 – BALANCES AND TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES (continued):

e. Income and expenses from related parties and interested parties (continued):

2. Sharebased payments plan and bonuses to employees (continued):

b. Bonuses to key management personnel

Short-term benefits include bonuses and other benefits to key management personnel, amounting to ILS 1,901 thousands (2011 – ILS 1,590 thousands; 2010 – ILS 1,334 thousands); some of the benefits were granted by global AIG Corporation and vest over the employee service period.

NOTE 29 - CONTINGENT LIABILITES AND COMMITMENTS:

Contingent liabilities class actions:

a. A motion to certify a ILS 22.5 million class action lawsuit was brought against the company in November 2010. The lawsuit relates to an up to 35% discount on premiums provided to women clients just because they are women, which allegedly discriminates against men, just because they are men. The petitioner alleges that the company is discriminating against men because according to its data, women are safer drivers and are involved in much fewer car accidents, and that this discrimination is done solely for generating profit. The petitioner argues that this is a form of illegal discrimination that runs counter to the provisions of the Law of Prohibition of Discrimination in Products, Services and Admittance to Entertainment Venues and Public Places, 2000 ("Discrimination Prohibition Law").

On March 1, 2011, the company filed its response to the request. In its response, the company made several material arguments relating to the petition, including the inability of the claimant to establish a personal claim against the company for the following reasons: a) using the risk principle in insurance policy pricing is fundamental in the insurance business, and therefore may not be a discrimination under the Discrimination Prohibition Law; b) driver gender is information permitted for use in pricing a policy; c) the plaintiff suffered no damage and in any event much less than presented by the plaintiff; d) there is no ground of infringement of individual autonomy; e) the company is shielded against a damages claim since it acted in compliance with the law and guidelines of the Israel Supervisor of Insurance; f) the claims by the petitioner are an illegitimate attempt to indirectly attack the provisions of the law; g) the petitioner does not meet other conditions for certifying the lawsuit as a class action.

A hearing, without examination of affiants, was set to June 27, 2011.

NOTE 29 - CONTINGENT LIABILITES AND COMMITMENTS (continued):

On March 16, 2011, the applicant filed his response to the company's reply; in this response it is claimed that the claims made by the company in its reply should be rejected. The applicant claims, inter alia, that the company admits that it discriminates against men; he also claims that the company's claim that it operates lawfully should be rejected. According to the

applicant he has a valid cause of action and he indeed, suffered damages. The applicant also claims that the application to approve the claim as a class action brings forward joint issues and the Court's hearing a class action will be the most effective and fair way to discuss the applicant's claims.

A preliminary hearing took place on June 27, 2011. The Court resolved that at this stage, it accepts the Supervisor of Insurance's position with regard to the matter discussed by the Court. The court ordered that the Supervisors shall file his position in writing within 60 days.

The preliminary hearing that was set to September 27, 2011 was postponed at the agreement of the two parties to the claim to January 8, 2012.

On September 22, 2011, The Attorney General has filed the Court a notice, which was received by the company's legal advisors on November 20, 2011. In his notice, the Attorney General writes that after considering the matter, he decided not to use the authority granted to him by law and enabling him to take part in the legal procedure discussed herein. Nevertheless, The Attorney General's notice included a review of the matter; in his review, The Attorney General wrote that it appears that in the circulars he issued the Supervisor of Insurance allowed the insurers to determine the insurance fees based on the insuree's sex. The Attorney General also indicates in his notice that the company's insurance policy, which offers different rates to men and women was approved by the Supervisor of Insurance. It was also indicated that the use of a factor with statistical significance (such as the sex of the insuree) enables the insurer to characterize more accurately the insurance risk and to determine a premium that suits the insuree. Prohibiting the insurer from using a specific factor increases the uncertainty of the insurance risk; this causes, in turn an excess risk premium which increases market rates. The Attorney General claims that where the premium collected by an insurer does not correspond to the risk, certain insurees subsidize other insurees by paying more than they actually should.

On November 20, 2011, the applicant filed a response to the Attorney General's notice to the effect that the notice and especially the manner in which claims were presented therein are unacceptable to him and infringe his procedural rights. The applicant claims that the notice issued by the Attorney General is not in agreement with the Court's resolution, does not include the Supervisor of Insurance's position and does not refer to the issue discussed in the legal procedure. According to the applicant, the Attorney General's notice does not include a reference to the provisions of the Discrimination Prohibition Law, but includes the Attorney General's position in the matter, without him actually taking part in the procedure. The applicant thus requests the Court to summon the representative of the Attorney General to participate in the hearing set to February 8, 2012 in order to present his position in the matter discussed here, or alternatively, to remove the Attorney General's notice from the Court's files, or alternatively, to remove certain sections of the said notice, which, according to the applicant, constitute a digression for a review of the law.

NOTE 29 - CONTINGENT LIABILITES AND COMMITMENTS (continued):

A further hearing took place on January 8, 2012. In this hearing the Court ruled that the parties shall submit the summary of their position in writing, as follows: the summary of the applicant's claims shall be filed within 45 days as from January 8, 2012 and the summary of the company's claims shall be filed within 45 days after filing of the summary of the applicant's claims. The Court also rules that the applicant shall have the right to file his response to the summary of the company's claims within 15 days from the date of filing the company's claims, should he wish to do so.

Further to negotiations held between the legal counsel of the company and the legal counsel of the applicant, it was agreed that the applicant shall file, at the agreement of the company, an application to withdraw the lawsuit in accordance with Section 16 of the Class Action Law; as part of this application, the applicant shall request that the Court approves the withdrawal of the application and of the lawsuit and rejects the personal claim without receipt of any payment and without issuing an order to pay expenses.
On May 7, 2012, the parties issued a joint notice reporting to the Court that the applicant came to the conclusion that there is no point in continuing the legal proceedings relating to the application and the lawsuit; according to the said notice, the parties have agreed that the applicant shall withdraw his application and lawsuit without receipt of any payment or issuance of an order to pay expenses. In addition, it was indicated in the notice that the parties shall file an application to withdraw the application and the lawsuit in accordance with Section 16 to the Class Action Law within 21 days ("the joint notice").
On July 2, the parties filed the joint notice to the Court and on July 3, 2012, the Court ruled that it accepts the withdrawal application and ordered that the application and lawsuit are stroked off without issuing an order for payment of expenses. The ruling also stipulates that there is no need or justification to publish the resolution with regard to which the ruling was issued.

b. A lawsuit and a motion to certify a class action were filed against the company in February 2011. The lawsuit was brought against 5 more insurers. The lawsuit argues that the company is not paying the real amount of indemnification for diminished car value after being damaged in an accident, but rather pay reduced indemnification. The argument is that the computation of this reduced diminished value pay is done according to the report of the Sasson Committee, which established guidelines for computing diminished value.

The plaintiff argues that this allegedly misleading practice caused him a financial loss. The remedy the plaintiff requests is a declaration that the company has to appropriately disclose to its clients the method of computing diminished value in advance, as early as when issuing an offer to a client. Therefore, the plaintiff requested to refund the premium paid by any insurance client for vehicle insurance, which allegedly was entered into misleadingly. According to plaintiffs' estimation, 47,264 vehicles are insured by the company every year, with an average premium of ILS 2,000 less 20% of clients who had insured events, which amount to ILS 529,390,400. This amount applies to all vehicle insurance clients in the past 7 years. An alternative remedy is to repay ILS 150 for each insured, which is the difference between 5% and 1.5% in selfinsured retention. The amount required to cover all vehicle insurance client in the 7 years prior to filing the claim was ILS 39,704,700.

As yet another alternative, the diminished value component in a policy is about ILS 800 per client. The amount required to repay that to all insurance clients in the company in the past 7 years is ILS 264,678,400.

NOTE 29 - CONTINGENT LIABILITES AND COMMITMENTS (continued):

In a hearing which took place on May 13, 2012, the plaintiff agreed to withdrawn his claim. In light of the excessive demands of the plaintiff concerning professional fees and compensation to the class action plaintiff, it was agreed that the issue of legal fees and amount awarded to the plaintiff will be determined at the discretion of the Court and each of the parties shall file its arguments regarding this matter.

After the company filed its arguments, the Court ordered that only ILS 10,000 shall be paid to the plaintiff and his legal council.

On September 9, 2012, the plaintiffs lodged an appeal to the Supreme Court asking to cancel the above-mentioned ruling and reinstating the proceedings regarding compensation to the plaintiffs, expenses and legal fees, or alternatively asking that the Supreme Court shall order the increase of the relevant amounts.

The Supreme Court shall hear the appeal on December 23. 2012. The plaintiffs are requested to file a summary of their arguments on June 18, 2013 and the defendants are required to file a summary of their arguments on August 15, 2013.

In the opinion of the company's legal advisors, the chances that the Court shall allow the appeal are lower than the chances that the Court shall reject it.

c. A legal claim was filed against the company and 6 other insurance companies in December 2012; the plaintiffs also filed an application to approve the claim as a class action. 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 2008, 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.

Total damages claimed from the company in respect of property insurance amount to ILS 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.

At this preliminary stage of the legal claim, the company's legal advisors learn the claim; when they conclude reviewing the matter they will be able to assess the chances of the claim.

NOTE 29 - CONTINGENT LIABILITES AND COMMITMENTS (continued):

d. A legal claim was filed against the company and 14 other insurance companies on January 13, 2013; the plaintiff also filed an application to approve the claim as a class action. According to the plaintiff – Ms. Ilanit Nadav – she was insured under a compulsory vehicle insurance policy with the Israel Motor Insurance Pool (hereafter – "the pool"). According to the policy issued to the plaintiff, the insurance period commences at the date of payment of premium but not before April 1, 2008. The plaintiff paid the premium on April 7, 2008 – a day after she was injured in a car accident. The plaintiffs insurance claim for indemnification for damage caused in the accident was rejected and it was determined that at the date on which the accident happened she did not have a valid insurance policy.

According to the plaintiff, the pool has charged her for insurance premium in respect of 6 days on which she was not insured (1-6.4.2008). Therefore, she demands repayment of the insurance premium in respect of these 6 days.
The company is being sued in respect of its share in the pool (average of 2.5%) and in respect of the compulsory vehicle insurances it uses to insure directly.
According to the statement of claim, 18% of the persons and entities insured under compulsory vehicle insurance policies pay the premium after the due date. On average, insured persons and entities pay the premium 3 days after the due date. According to computations of the plaintiff, the amount claimed from the company is ILS 1,050,000..
At this preliminary stage of the legal claim, the company's legal advisors learn the claim; when they conclude reviewing the matter they will be able to assess the chances of the claim.

The following table lists outstanding motions to certify class actions filed against the company:

	Number of motions	Claimed amount in thousand
Motions to certify class actions -		
amount claimed from the company specified	3	552,737

NOTE 30 – CONDENSED NOMINALHISTORICAL DATA FOR TAX ADJUSTMENT RETURN ONLY:

a. Balance sheets:

	December 31 2012	December 31 2011
	Nominal ILS in thousands	
Investments	1,432,882	1,229,223
Property and equipment	32,605	28,711
Amounts receivable	793,355	723,698
Deferred acquisition expenses	130,191	118,658
	2,389,033	2,100,290
Shareholders' equity	577,092	419,752
Liabilities for employee rights upon	2,326	2,047
retirement net	8,877	7,376
Deferred income taxes	1,409,340	1,385,290
Insurance provisions and pending claims	391,398	285,825
Other liabilities	2,389,033	2,100,290

NOTE 30 – CONDENSED NOMINALHISTORICAL DATA FOR TAX ADJUSTMENT RETURN ONLY (continued):

b. Statement of income

	2012	2011	2010
	Nominal ILS in thousands		
Gross premiums earned	827,158	735,053	690,304
Premiums earned by reinsurers	(185,701)	(157,712)	(142,814)
Premiums earned retained	641,457	577,341	547,490
Investment income – net and financing income	97,239	*25,333	*65,894
Commission income	47,628	41,457	36,952
TOTAL INCOME	786,324	644,131	650,336
Increase in insurance liabilities and payments with respect to insurance contracts	(403,690)	(429,949)	(417,029)
Share of reinsurers of increase in insurance liabilities and payments with respect to insurance contracts	152,790	119,413	101,083
Increase in insurance liabilities and payments with respect to insurance contracts (retained)	(250,900)	(310,536)	(315,946)
Commission and other acquisition expenses	(147,372)	(131,406)	(126,103)
General and administrative expenses	(142,075)	(136,239)	(121,694)
Financing Income (expenses)	(2,206)	*1,380	*(866)
TOTAL EXPENSES	(542,553)	(576,801)	(564,609)
INCOME BEFORE TAXES ON INCOME	243,771	67,330	85,727
Taxes on income	(86,431)	(22,943)	(29,366)
INCOME FOR THE YEAR AND TOTAL COMPREHENSIVE INCOME FOR THE YEAR	157,340	44,387	56,361

*Certain amounts were reclassified, see note 2.t.

c. Statement of changes in shareholders' equity:

	Share capital	Share premium	Capital reserve	Retained earnings	Total
	Nominal ILS in thousands				
Balance as of December 31, 2010	6	230,643	11,013	133,517	375,179
Changes in 2011					
Issuance of bonus shares					
Benefit component with respect to grant of equity instruments and other benefits to employees			186		186
Net income				44,387	44,387
Dividend paid					
Balance as of December 31, 2011	6	230,643	11,199	177,904	419,752
Changes in 2012					
Issuance of bonus shares					
Benefit component with respect to grant of equity instruments and other benefits to employees					
Net income					
Dividend paid				157,340	157,340
Balance as of December 31, 2012	6	230,643	11,199	335,244	577,092

Comments

The above nominal data have been updated in accordance with IFRS but they are not drawn up in accordance with IFRS; they are attached in order for them provide the basis for the company's Adjustments Report for Tax Purposes, and are presented within these financial statements for that reason alone.