AIG Israel Insurance Company Ltd

Financial Report for Year Ended 2016

Contents

Chapter A: Description of corporate business

For the year ended December 31, 2016

AIG Israel Insurance Company Ltd
Private Company No. 51-230488-2
("The Company)

March 21, 2017

Description of corporate business for the year ended December 31, 2016

This report constitutes a description of the Company's business as of December 31, 2016, and reviews the Company and the development of its business as occurred in 2016 ("the reported period"). The information in this report as updated as of December 31, 2016 ("the report date"), unless otherwise is explicitly indicated.

Under Regulation 8C of the Israel Securities Regulations (Periodic and Immediate Reports), 1970, the guidance in regulations 8(b), 8A and 8B of the regulations as above do not apply to the information in the periodic report of an insurer.

The Company is an insurer as this term is defined in the Supervision of Financial Services Law (Insurance), 1981 ("the Supervision Law"). Therefore, this report is prepared based on the Insurance Business Supervision Regulations (Report Information), 1998 ("the Reporting Regulations") and according to the guidance issued by the Supervisor of Capital Markets, Insurance and Savings in the Israel Ministry of Finance ("the Supervisor"), including Insurance Circular 2014-1-3 dated January 20, 2014, and Insurance Circular 2015-1-4 dated January 26, 2015.

Forward looking information

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

The financial information included in this report is reported amounts. All information in this report are in thousands NIS unless otherwise is indicated.

The business of the Company is in fields that require considerable professional knowhow that involves many professional terms that are essential for understanding the business of the Company. To present a description of the corporation that is as clear as possible, those professional terms are used along with an explanation, to the extent possible. The description in this report on insurance products and coverage types is for the purpose of this report only, and may not serve for the interpretation of the products and coverage, and the full and binding terms in the insurance programs.

Please read the all parts of this periodic report as one unit.

Table of Contents:

1. Part A: the activity of the Company and the development of its business

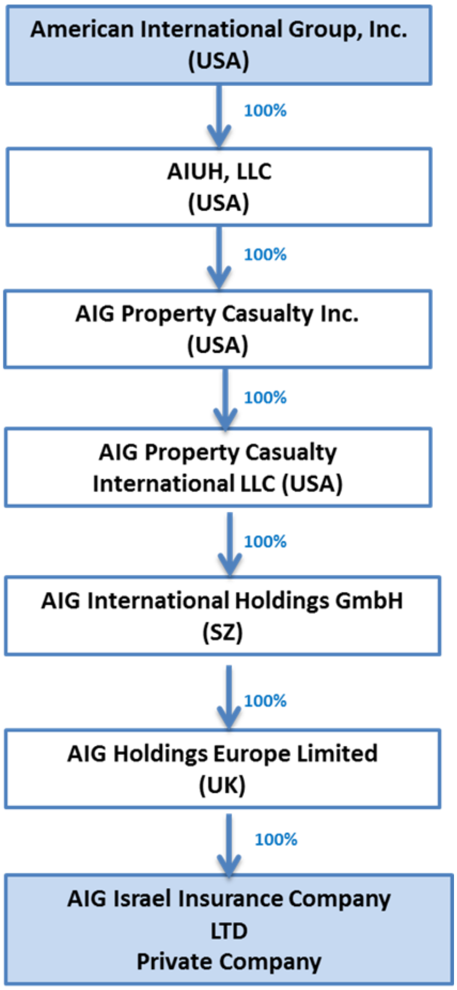
1.1 The activity of the Company and the development of its business

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

The ultimate parent of the Company is American International Group Inc. (hereinafter: "**the global AIG corporation**" or "**AIG**"). The global AIG corporation is a leading global insurance and financial services corporation, rated BBB+ as of report date by Standard & Poor's.

On June 1, 2016, as part of restructuring of the AIG Global Corporation, all shares of the Company owned by AIG Europe Holdings Limited ("AEHL") were transferred to the ownership of AIG Holding Europe Limited ("AHEL"). As of the date of this report, the sole shareholder of the Company is AHEL, which holds the entire issued and paid up share capital of the Company. AHEL is a company in the AIG Global Corporation.

The following is the holding structure of the Company.



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

The Company is operating in three business divisions (home and vehicle insurance, life and health insurance and commercial insurance), headquarters, distribution channels and customer service.

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

1.2 Areas of activity

Most activity of the Company is to retail customers. The main activities of the Company and their general characteristics are as follows:

1.2.1 General insurance - property vehicle

General

The Company began its activity in this segment in 1997. Property vehicle insurance is also known as comprehensive vehicle insurance or "third-party insurance" and is voluntary. Property vehicle insurance is included in the general insurance business, and is focused on property damage to vehicles of the customer and those caused to a third party.

The language of a property vehicle insurance policy is subject to the standard policy terms in the Insurance Business Supervision Regulations (Terms of Private Vehicle Insurance Contract), 1986 ("the standard policy").

The standard policy include coverage against loss or damage caused to the insured vehicle as a result of the following risks: fire, thunderbolt, explosion, accidental collision, capsizing, accident of any type, theft and any damage caused by theft, while theft or attempted theft was occurring; flood; storm; snow; volcano eruption; deliberate damage; and liability coverage to third party due to property damages.

The language of the standard policy is mandatory, and it is only possible to extend its coverage in terms of scope, risks, and covered property and persons.

Property vehicle insurance is divided into two main categories:

a. Insurance to private vehicles of up to 3.5 ton – Vehicles in this category are insured under the standard policy.
b. Insurance to vehicles of more than 3.5 tons – the policy for vehicles in this category is not subject to the terms in the standard policy.

Differential rates

Insurance rates are actuarially calculated and differential (variable and risk-adjusted), subject to approval by the Supervisor. The rate is determined based on a number of factors, including: vehicle model, engine size, production year, number of drivers, age and gender, years of driving experience, claim history, etc.

As of the date of this report, the Company price its insurance coverage based on the following criteria: vehicle characteristics, ownership and use, number of drivers, characteristics of drivers, years of driving experience of drivers and claims history.

1.2.2 **General insurance - compulsory vehicle**

General

The Company began its activity in this segment in 1997. Compulsory vehicle insurance, also known in Israel as compulsory insurance is mandatory. The Motor Vehicle Insurance Ordinance (New Version), 1970 ("the Motor Vehicle Ordinance") obligate a vehicle user or anyone who permits another person to use a vehicle to purchase compulsory insurance for bodily injuries only that may be inflicted to the driver and/or passengers and/or pedestrians hit by the insured vehicle. The Motor Vehicle Ordinance states, among other things, that no person can use, or cause or allow another person to use a motor vehicle unless an insurance policy in effect exists in the name of his name or the other person's name.

The wording of a compulsory vehicle policy is subject to the terms of the standard policy that are present in the Financial Services Supervision Regulations (Insurance) (Terms of Motor Vehicle Compulsory Insurance Contract), 2010 ("compulsory vehicle standard policy").

The compulsory vehicle standard policy covers, under the Motor Vehicle Ordinance, the owner of the vehicle and driver for liabilities they may face under the Compensation to Victims of Road Accidents Law, 1975 (CVRAL). CVRAL states that the user/driver of a motor vehicle must compensate a victim for a bodily harm caused to him/her in an accident in which the vehicle is involved and also sets a liability that is absolute and complete, independent of guilt.

Reserves

The computation of general insurance reserves is done based on Supervision on Financial Services Regulations (Insurance) (Computation of General Insurance Reserves), 2013 ("the Computation of General Insurance Reserves regulations") and in accordance with the relevant provisions in the "Measurement, Equity and Management of Assets and Liabilities" chapter of the Regulation Codex. This chapter includes, among other things, guidelines for measurement of liabilities in life, general and health insurance. It also includes, among other things, provisions regarding insurance reserves, best practice for calculation of general insurance reserve for financial reporting purposes, aggregation of segments, determining the amounts of reserves in respect of policies which were sold close to balance sheet date and in respect of risks arising subsequent to balance sheet date.

In this context we note that in March 2016, the Supervisor issued Insurance Circular 2016-1-4, titled "Amendment of Provisions of the Consolidated Circular – Chapter 1 in Part 2 Heading 5 – Measurement". The circular includes amendments the measurement chapter of the codex and provides, among other things, that the guidance on calculation of the share of reinsurers in deferred acquisition expenses in general insurance segments is to be applied in the financial statements for the first quarter of the reported period, at the latest, and that the cancellation of the provision in the measurement chapter regarding calculating the share of reinsurers in unearned premium in general insurance and health insurance segments comes into effect in the financial statements for the first quarter of the reported period.

Differential rates – information and supervision

A database of compulsory vehicle insurance rates is maintained for information, and is authorized by law to collect information about that segment. Under the Motor Vehicle Insurance Regulations (Creation and Management of Databases), 2004, insurance companies are legally obligated to transfer to the database information about drivers of insured vehicles, as defined by the Supervisor, as well as premium rates, payments and pending claims in scale and dates specified in those regulations.

The Supervisor gave a franchise to a service provider to manage that database, to issue reports that will be used, among other things, to assess the risks in the compulsory vehicle insurance sector, and determine the cost of pure risk that underlies the rate. The reports of the franchise holder serve as basis for the rate that is then used by the Supervisor as reference to test compulsory insurance rates.

The Supervisor sets the principles for determining compulsory vehicle insurance rates and regulates them through circulars that he issues from time to time. Those circulars specify the factors that an insurance company can use for determining premiums, the procedures that insurers need to comply with to approve premiums, maximum rates per customer and the process for approval by the Supervisor.

The factors for differential rate determination include, among other things engine size; sex, age of the youngest driver expected to drive the vehicle; years of driving experience of the youngest driver who is expected to drive the vehicle; number of past bodily damage claims and/or number of license suspensions in the previous three years of all drivers who are expected to use the vehicle; airbags installed; ESP system installed; ABS system installed. Beginning in January 2017, the following factors: FCW and LDW systems are installed.

Insurance companies may determine the premium using the risk premium and risk classification criteria set by the information and regulation rate database to align premiums to the covered risk.

As of the date of this report, the Company determined insurance rates using the following criteria: age and sex of the youngest driver who is expected to use the vehicle, make and year of vehicle, engine size, year of experience of youngest driver who is expected to use the vehicle, number of past claims and/or license suspensions in the previous three years of all drivers who are expected to use the vehicle and whether airbags are installed in the vehicle; ABS and ESP systems.

Residual insurance ("the Pool")

The Israeli Vehicle Insurance Pool is an entity that insures the risks of vehicles that are rejected by compulsory vehicle insurers (residual insurance). This arrangement is provided by Motor Vehicle Insurance Regulations (Residual Insurance Arrangements and Mechanism for Setting Rate), 2001 ("the Pool Regulations"). The Pool operates as a normal insurance company and its rates are competitive relative to other insurers in the market. All insurance companies active in compulsory vehicle insurance are partners in the Pool, and each bears losses and gains from its income proportionally to its share in the compulsory vehicle insurance market. The share of the Company in residual insurance in 2014 was 3.1% and in 2015 and 2016 was 3.2%.

The Road Accident Victims Compensation Fund ("Karnit")

Karnit is a corporation created under the CVRAL and is tasked with compensating victims who are eligible to compensation under that law and may not claim compensation from an insurer due to the following cases: the hitting driver is unknown, the hitting driver has no valid and paid compulsory vehicle insurance certificate, or the insurance does not cover the liability, the insurer of the vehicle is in liquidation or the insurer was appointed a special manager. Under the provisions of Compensation of Road Accident Victims Order (Financing of the Fund)(Amendment), 2003, insurance companies are required to transfer to Karnit 1% of net compulsory vehicle insurance premiums from policies they underwrite since that date.

In addition, according to the Road Accident Victim Compensation Order (Funding the Cost of Rendering Services), 2009, an insurer needs to give Karnit 9.4% of premium for each of the policies issued against the transfer of liability to any medical expenses included in the government healthcare funding to health funds.

In this context, note that in April 2016, the Compensations for Victims of Road Accidents Law (Amendment No. 25), 2016 was published in the official gazette. The amendment, among other things, introduces a provision that if the Supervisor finds an amount in the Karnit account in excess of what is necessary for financing its activity and ensuring its stability, she, with agreement of the Minister of Justice, may instruct Karnit to refund those amounts to motor vehicle insurance customers, either directly or through any other way that will be determined.

Following that, in September 2016, the Supervisor issued a circular on refunding amounts from Karnit to the compulsory insurance customer population. The circular indicates that it appeared from the 2015 financial statements of Karnit that Karnit has an excess amount of NIS 1.2 billion, which is more than required to finance its operations and ensure its stability. As such, the circular contained provisions for refunding the excess amount in Karnit to the motor vehicle insurance population. In addition, in November 2016, the Supervisor issued a circular that establishes provisions for refunding amounts to insurance customers, the format of reporting to Karnit, guidance about reporting files, the information that an insurance company is required to report, the method of submitting reporting files to Karnit and controls by Karnit over those reports.

<u>Arrangements for distributing the compensation burden among insurance companies</u>

According to CVRAL, in a multiple-vehicle accident, each driver will be liable to bodily damages caused to passengers of the vehicle which was insured through that driver.

Arrangement for a victim outside a vehicle – in case of a victim is located outside a vehicle in a multiple-vehicle accident, the drivers are liable to that person together and separately, and are required to divide that burden in equal parts among them.

Car-Motorcycle arrangement – In a road accident that involves one or more motorcycles and one or more non-motorcycle vehicles, the non-motorcycle insurers to the insurers of the motorcycle 75% of bodily injury compensation that the insurers of the motorcycle are liable to pay due to the accident, except for compensation to victims outside the vehicle. The insurers of the non-motorcycle vehicle are liable together and separately towards the insurer of the motorcycle, and are required to divide the liability burden among them in equal parts.

Light-heavy vehicle arrangement – According to the Road Accident Victims Compensation Order (Arrangements for Dividing the Compensation Burden Among Insurers), 2001, in the event of a road accident involving one or more heavy trucks (over 4 tons) and one or light vehicles, the insurers of the heavy must pay the insurers of the light vehicle 50% of bodily injury compensation as those defined in the CVRAL, while the insurers of the light vehicle are required to pay their liability for the accident, except a payment under the car-motorcycle arrangement or compensation payment to victims outside a vehicle. The insurers of the heavy vehicle are liable together and separately towards the insurers of the light vehicle and among themselves, and are required to bear this liability in equal parts.

1.2.3 <u>**General insurance – home insurance**</u>

<u>General</u>

The Company began its activity in this sector in 1997. Comprehensive home insurance, also known as home insurance, is a key insurance product of the individual insurance business, and is part of the general insurance.

The language of the home insurance policy is subject to the standard policy in Insurance Business Supervision Regulations (Terms of Insurance Contract for Homes and Their Contents), 1986 ("the home insurance regulations" and "the home insurance standard policy", respectively). The home insurance standard policy includes coverage against loss or other damages that may result from factors such as fire, lightning, smoke, explosion, wind in excess of 30 knots, including rain, snow or hail that fell at that time; aircraft crash, object falling from an aircraft and supersonic boom from an aircraft, contact or crash of a vehicle into the apartment, certain malicious actions, theft, robbery and break-in or attempt to commit them, illegal gathering and rioting, earthquake and flooding from an external source.

The standard policy is a minimum policy. Its language is binding, and it is only possible to add more coverage in terms of coverage amount, risks and the assets and liabilities covered. Rates of the standard home insurance policy are regulated and approved by the Supervisor.

1.2.4 General insurance – commercial insurance

General

The Company commenced its operations in this sector in 2000. The commercial insurance segment of the Company includes the following segments: professional liability insurance, property loss and comprehensive insurance for businesses, third-party liability insurance, product liability insurance, employers' liability insurance and engineering insurance.

The Company manages this insurance business in two main categories:

a) Liabilities insurance

Liabilities insurance covers the legal liability of the customer for damage that may be caused to any third party. The main liability types marketed by the Company are: professional liability insurance, officers and directors' liability insurance, third-party liability insurance, product liability insurance, and employers' insurance.

For the most part, the period of the insurance is one year, but the time for processing the claim is on average longer than property insurance. The main determining factors are: the complexity of factual and legal procedures, the timeframe for the liability and damage and filing the claim, longer statute of limitations relative to property insurance. Therefore, liability insurance is considered to have a longer claim trail.

This has two main consequences:

- Impact of capital market and presence of capital gain from investing reserves and of pending claims on the capital of the Company.
- Impact of legal presence and case law on the exposure of the Company in every individual claim.

In some liability insurance products, such as third-party and employers' liability, coverage is event-based. That is, coverage is given to events that occurred during the insurance period and the claim can be filed after the end of the insurance period, subject to the statute of limitations in the law.

In professional and directors and officers liability insurance products, coverage is based on the date of filing the claim. That is, coverage is given to claims that are filed during the insurance term, even if the reason to the coverage was created before the beginning of the insurance period.

According to the Insurance Contract Law, 1981 (hereafter – "the Insurance Contract Law"), the statute of limitations on insurance compensation is three years after the occurrence of the insured event. However, in liability insurance, claiming for compensation is not subject to statute of limitations as long as a third-party claim against the insurer is not subject to statute of limitations.

To increase its share in all those commercial insurance segments. To achieve this objective, the Company utilizes the expertise and financial robustness of the AIG corporation, which is a global leader in this industry. Additionally, the Company is constantly seeking to provide appropriate coverage to its customers and to develop new customized products.

b) Property loss and engineering insurance

Property loss insurance and engineering insurance is intended to provide customers coverage against physical damage to property. The main insurance products marketed by the Company are: contractors' insurance, mechanical failure insurance and electronic equipment insurance.

The main risks covered in those policies are fire, explosion, break-in, earthquake and other natural calamities. The policy covers damages directly caused to property as well as indirect damages (loss of income, etc.) For the most part, the term of those policies is one year, and claims are processed close to the time of the insurance event, and for that, such policies are considered to have a short claim tail.

1.2.5 **Health insurance**

General

The Company began its activity in the healthcare segment in 1998. Healthcare insurance in the Company includes the following sub-segments: personal injury insurance, serious illness insurance and travel insurance.

Health insurance policies are subject, among other things, to the provisions of the Insurance Contract Law, the Supervision Law and the regulations thereunder, including the Supervision of Insurance Businesses Regulations (Terms in Insurance Contract) (Provisions About Preexisting Medical Conditions), 2004, and the Financial Services Supervision Regulations (Insurance) (Collective Health Insurance), 2009 (hereafter – " Collective Health Insurance Regulations"), as well as the directives and guidance issued by the Supervisor from time to time.

The Company manages segment in three main categories:

a) Personal injury insurance

A personal injury insurance policy provides a predetermined monetary compensation in case of hospitalization, disability and death resulting from an accident. Contrary to policies in disease and hospitalization policies, which provide coverage for illness, personal injury insurance covers only the results of an accident.

b) Serious illness insurance

A policy that covers the diagnosis of serious illness as defined by the policy. Insurance benefits are paid as a lump sum in case of diagnosing a serious illness or a medical event, without the customer having to prove any expense.

c) Travel insurance

A product providing insurance coverage to different expenses to people traveling overseas for a number of risk types: cancellation or curtailment of a trip due to reasons listed in the policy, hospitalization and non-hospitalization medical expenses, medical flights, loss and/or stolen property, third-party liability and compensation in cases of disability or accidental death. It is also possible to buy additional coverage such as: extreme and winter sports, laptop coverage, etc. It is also possible to buy coverage for special situations such as: aggravation of preexisting medical condition and coverage for pregnant women. The product is sold in different packages to cater for different types of customers: long-term travelers, families, etc. The policy is sold online and by sales reps.

Health insurance for covering medical expenses is managed by the Company under the life insurance segment, as explained below.

1.2.6 **Life insurance – risk only**

General

The Company began its activity in the life insurance segment in 1999. The Company provides policies to individual customers who are interested in life insurance, including to private customers who are interested in such product, including private lenders who take housing loans.

Life insurance

Life insurance policy promises a payment of a lump sum to beneficiaries in case of death of the customer. Usually in such policies, the policy expires when the customer dies or when he/she reach a certain age. Extensions offered to such policies are total permanent disability, accident disability, accident death and critical illness insurance.

Mortgage-related life insurance

A life insurance policy provides the mortgage bank a reimbursement of outstanding loan in the event of death of the customer (the mortgage customer). Those policies can be extended to include permanent total disability.

Health insurance for covering medical expenses

Health insurance policies that cover medical expenses such as "Complementary Additional Health Insurance" and "First Shekel". Policies like "Complementary Additional Health Insurance" complement or extend the coverage and services provided under complementary health coverage of health funds, to complete the coverage that is missing due to legislation, regulations, plan terms and health fund instructions. The policies include, among other things, insurance coverage for medical expenses that are caused to the customer as a result of requiring surgery, non-government sponsored medicine, transplants and ambulatory services.

"Full coverage" policies provide coverages and services for medical expenses that were caused to the insurance customer as a result of surgery, drug that are not covered by the government (the "basket"), organ transplants and ambulatory services, regardless of complementary health insurance provided by health funds.

1.3 **Investments in capital and share transactions**

In 2016 and 2015, no investments have been made in the capital of the Company and no transactions in its shares were made, except as indicated in paragraph 1.1 above.

1.4 **Dividend distribution**

The limit on the ability of the Company to pay out dividends is derived from Supervision of Insurance Business Regulations (Minimum Equity Required of an Insurer), 1998 ("**minimum capital regulations**") and Supervisor regulations associated with this matter. Those regulations determine the minimum capital level required from an insurer, which is derived from the scale of operation, reinsurance arrangements and outstanding claim amounts.

According to the minimum capital regulations, the Company is prohibited from distributing dividend if their capital is lower than the capital established in those regulations. In addition, there is an additional restriction on dividend distribution in the Companies Law, 1999 ("**the Companies Law**") and in letters of the Supervisor to insurance companies that list the criteria for, and limits on dividend distributions by an insurer and the terms required by the Supervisor for approving a dividend distribution.

For more information about regulatory guidance on dividend distribution and the dividends distributed by the Company to its controlling shareholder in 2014-2016, see note 13 to the financial statements.

In accordance with the Company's capital management policy, which also includes its dividend payout policy, the Company has to hold capital that is 120% of the minimum regulatory capital, and also comply with a solvency ratio of 130% under a regimen based on Solvency II, and subject to certain conditions, the Company will pay dividend above that threshold.

As of December 31, 2016, the Company has surplus equity over the level of equity required by the minimum capital regulation by a total of NIS 169.1 million.

For information about an offer to distribute a dividend amounted to NIS 50 million after December 31, 2016 – see note 13c(3) to the financial statements.

2. **Part B – Description and information on activity segments of the Company**

2.1 **Activity segment 1 – Property vehicle insurance**

2.1.1 Products and services

The Company sells a range of standard insurance products, including: comprehensive insurance (including against theft or accident), comprehensive insurance without theft coverage, comprehensive insurance without accident coverage, third-party insurance and third-party two-wheel vehicle insurance. On top of those standard policies, customers can buy more coverage and/or related services such as towing services, replacement care, window breakage, radio and tape/CD player and VIP services.

In 2016, the Company did not develop material new products and services in this segment.

For more information about the general characteristics of this segment, see 1.2.1 above.

2.1.2 **Competition**

According to data made public by insurance regulators, 13 insurance companies are active in this segment, and the market is highly competitive. According to the financial statements for the first nine months of 2016, the main competition in this segment, by premium turnover are Menorah Insurance Company Ltd ("**Menorah**") (13.9%), IDI Insurance Company Ltd ("**Direct Insurance**") (12.7%), the Phoenix Insurance Company Ltd ("**the Phoenix**") (12.2%), Migdal Insurance Company Ltd. ("**Migdal**") (9.6%) and Harel Insurance Company Ltd ("**Harel**") (9.5%). The market share of the Company in this segment in total premiums during that period is 4%.

The approach taken by the Company to address this fierce competition in this segment is using advanced pricing and actuary methods, marketing campaigns, operating restructuring and ongoing improvement of customer service.

In that context note that the insurance company service index for 2015 was published in April 2016 ("the service index"). The service index enables clients to compare between different insurance products and it is designed to increase the competition in the insurance market since it reflects the level of service provided by insurance companies by principal insurance products. For each insurance product a service index is calculated, which his based on four components: (1) payment of claims – the percentage of claims approved and paid and how quickly these claims were handled; (2) Handling clients' queries – clients' satisfaction of insurers' handling their queries; (3) Public complaints – weighting of complains which were lodged and assessed by the Capital Market Division; (4) Phone response time – ratio of calls that got responded within 3 minutes. Data published by the Ministry of Finance show that the Company is ranked first in the overall service rating, claims rating, and satisfaction rating of customers in property vehicle insurance.

The Company believes that the publication of the service index will increase competition in the property vehicle sector; the Company estimates that the service index may help the Company to become the lead player in this insurance sector.

The information included in this section constitutes forward looking information, which is based, among other things, on the current results of the Company. Actual results may be different than the estimated results, and may vary significantly, among other things, as a result of regulatory changes applicable to the Company and declining ratings in the four elements of service index.

2.1.3 **Customers**

a. The Company sells the product mainly to individual private customers through direct marketing.

b. The following is the distribution of premiums in this segment (in thousands of NIS):

	2016	2015	2014
Private customers	255,114	226,806	202,952
Through agent mediation	59,009	57,371	53,620
Total	314,123	284,177	256,572

c. The Company is not dependent on any single customer.

d. No customer contribute 10% or more of total revenue of the Company

e. Renewals rate in 2016 in terms of premiums for policies that were in effect in the previous year is 77.8%.

f. The rate of customers who are also insured in compulsory vehicle insurance in 2016 is 85.4%.

g. The following information shows customers in property vehicle insurance in terms of premium in 2016 in percentage terms by years of first engagement:

First year of the first policy with the Company:	%
2016	34%
2015	16%
2014	11%
Until 2013	39%
Total	100%

2.2 **Activity segment 2 – Vehicle compulsory insurance**

2.2.1 **Products and services**

This segment has only one product – standard compulsory insurance policy. The insurance coverage under the policy includes any liability that might arise under CVRAL, other liability (non-CVRAL) that the customer may be liable for bodily damage to another person by or due to using the insured vehicle and bodily damage caused to the insured in a road accident.

As indicated above, under CVRAL, this is "total liability" coverage. Accordingly, road accident victims are entitled to compensation from the insurer of the vehicle, without a requirement to prove guilt of any of the persons involved. However, the CVRAL presents a number of limits and exceptions that revoke the right for compensation (e.g. a person who caused an accident intentionally), and limits the amounts of compensation, such that non-monetary damage compensation is limited to a fixed amount specified in CVRAL and compensation for lost income and disability income that are limited at three times the average salary in the Israeli economy.

Those claims are characterized by a long claims tail.

As indicated above, the vehicle compulsory insurance segment has only one product.
For more information about the general characteristics of this segment, see 1.2.2 above.

2.2.2 Competition

Most insurance companies in Israel are active in the compulsory vehicle insurance market, which results in fierce competition. More competition comes from Direct Insurance and the direct marketing arms of other insurance companies. The competition is mainly reflected in lowering insurance rates to customers.

The largest insurance companies in the segment, by premium base are: Migdal, Ayalon Insurance Company Ltd ("Ayalon"), Harel, Menorah and the Phoenix. According to the information for the first nine months of 2016, the total share of those companies in gross insurance premiums in this segment is 50.7%. The share of the Company of the gross total insurance premiums in the reported period is 3.0%.
Since the insurance coverage offered by all insurance companies is identical, and since it is possible to compare the insurance rates charged by insurance companies on the website of the Supervisor, customers are very sensitive to change in insurance premiums. The approach taken by the Company to address this fierce competition in this segment is using advanced pricing and actuary methods, operating restructuring and ongoing improvement of customer service. Data published by the Ministry of Finance show that the Company is ranked first in the satisfaction index in the compulsory vehicle insurance sector.

The Company estimates that the annual publication of the service index will increase competition in the compulsory vehicle insurance sector.

2.2.3 Customers

a. The Company sells the product mainly to individual private customers through direct marketing.
b. The distribution of premium in this segment is as follows (in thousands of NIS):

	2016	2015	2014
Direct marketing	132,273	130,371	121,499
Through insurance agents	13,811	16,411	24,773
Total	146,084	146,782	146,272

c. The Company is not dependent on any single customer.
d. No single customer represents 10% or more from company revenue.
e. Renewals rate in 2016 in terms of premiums for policies that were in effect in the previous year is 73.3%.
f. The rate of customers who are also insured in property vehicle insurance in 2016 is 91.6%.
g. The following information shows customers in compulsory vehicle insurance in terms of premium in 2016 in percent by years of first engagement:

First year of the first policy with the Company:	%
2016	30%
2015	17%
2014	12%
Through 2013	41%
Total	**100%**

2.3 **Activity segment 3 - Home insurance**

2.3.1 **Products and services**

Home insurance is designed to give customers coverage for damage or loss caused to the home and/or its contents. This type of insurance includes extensions such as third-party liability and liability to home workers. As part of a home insurance it is possible to buy additional coverage and/or services such as piping and water damages, emergency services, coverage of all risks for valuables, etc.

Home insurance policies are sold to asset owners who are interested to insure their home and/or contents. When the insurance is bought for mortgage purposes, the insurance mostly covers the structure only and the mortgage bank is registered as a nonrecourse beneficiary.

In 2016, the Company did not develop any material new products in this insurance segment.

For more information about the general characteristics of this segment, see 1.2.3 above.

2.3.2 **Competition**

According to information released by insurance regulators, 13 insurance companies are active in this segment, resulting in fierce competition. According to data in the financial statements for the first nine months of 2016, the main competitors in this segment, by premium turnover are the Phoenix (14.4%), Clal (14.2%), Harel (13.1%) Migdal (12.4%) and Menorah (11.3%). The share of the Company in the total premium turnover in the reported period is 6.3%.

Since the insurance coverage offered by all insurance companies is similar, and since it is possible to compare the insurance rates charged by insurance companies on the website of the Supervisor, customers are very sensitive to the issue of insurance premiums. The approach taken by the Company to address this competition in this segment is using advanced pricing and actuary methods, marketing campaigns, operating restructuring and ongoing improvement of customer service. Data published by the Ministry of Finance show that the Company is ranked first in the service index for home insurance.

The Company believes that smart use by the insurance public population in the home insurance calculator and publication of the service index annually will increase competition in the home insurance sector. The Company estimates that the service index may help the Company to become the lead player in this insurance sector.

The information included in this section constitutes forward looking information, which is based, among other things, on the current results of the Company. Actual results may be different than the estimated results, and may vary significantly, among other things, as a result of regulatory changes applicable to the Company and lower rating in the four factors underlying the service index.

2.3.3 **Customers**

a. The Company sells its products in this segment mainly to private customers through direct marketing.
b. The Company is not dependent on any single customer.
c. Renewals rate in 2016 in terms of premiums for policies that were in effect in the previous year is 87.8%.
d. The following information shows customers in home insurance in terms of premium in 2016 in percent by years of first engagement:

First year of the first policy with the Company	**%**
2016	19%
2015	13%
2014	11%
Until 2013	57%
Total	**100%**

2.4 Activity segment e - Commercial insurance

2.4.1 Products and services

a. Liability insurance

Those types of insurance contracts cover the liability of the insurance customer to damages caused to a third party. Those insurance contracts are divided into a number of segments, and the main ones are:

- Professional liability insurance – Coverage to professionals to protect them against claims filed against them for damages caused to third parties as a result of mistakes and professional negligence.

- Directors and officers insurance – Coverage for directors and officers for an action, a failure or illegal action they performed while in office. Generally, the policy covers the liability of an officer under the Companies Law and other legislation (in Israel and overseas), which impose a duty of care and fiduciary duty and other duties that apply to directors and/or officers that impose personal responsibility.

- Third-party liability insurance – Coverage against bodily injury or property damage caused to a third party, excluding vehicle coverage and employers' insurance. The liability covered by this insurance is for the most part pursuant to the Torts Ordinance [New Version], 1968 ("**the Torts Ordinance**").

- Defective products liability insurance – Insurance coverage against injury or damage resulting from a defect in a product that was manufactured, marketed, assembled or maintained by the customer. Such policy is pursuant to two main pieces of legislation: (1) Warranty for Defected Products Law, 1980 which imposes liability on the manufacturer (as defined by the law) and apples to bodily injury only; (2) the Torts Ordinance, which makes a manufacturer liable to bodily injuries and property damages.

- Employers' liability insurance – Covers employees from bodily injury claims (accident or illness) caused to an employee during work due to negligence of the employer. Usually, the policy covers the liability of the employer under the Torts Ordinance in any amount not covered by the Israel National Insurance Institute.

b. Property insurance, contractors, mechanical failure and electronic equipment

- Property insurance – coverage to customers in case of damage to property as a result of fire or lightning. Customers can buy additional coverage such as break-in, natural disasters, earthquake, explosion and insurance for loss income as a result of the insurance event.

- Contractors insurance – Coverage against unexpected damage to the insured assets during the construction of projects and buildings. The customer buys under the policy coverage for liability to third parties and employees as part of performing the construction works.

- Mechanical breakage – Coverage of damages caused by breakage in machines and other engineering equipment.

- Electronic equipment – Coverage against loss of or damage to electronic equipment, including external information storage equipment.

Those segment are reinsurance intensive, among other things, due to the monetary scale of outstanding claims in those segments.

In 2016, the Company did not develop new material products in this insurance segment.

For more information about the general characteristics of this segment, see 1.2.4 above.

2.4.2 **Competition**

This segment is characterized by intense competition from leading companies in this market. According to information in the financial statements for the first nine months of 2016, the main competitors in this segment by premium turnover are Harel (22.1%), Migdal (12.7%), the Phoenix (12.0%), Clal (10.9%) and Ayalon (10.1%). The share of the company in the professional liability and other liability from total premium turnover in the reported period is 3.8%, and the share of the Company in the property and engineering insurance by premium turnover in that period is 1.3%. The Company addresses this competition by utilizing the expertise and financial robustness of the global AIG corporation, which is a global leader in this segment. In addition, the Company is constantly aspiring to align coverage to customers' needs and develop customized new products.

2.4.3 **Customers**

The company is not dependent on any single customer.

2.5 Activity segment 5 – Health insurance

2.5.1 Products and services

Health insurance that exist in the Company are designed to compensate or indemnify customers for medical expenses in case of injury and/or medical conditions and to provide various healthcare services through contracted providers. In addition, the Company sells a variety of personal injury products, both to individual and collective customers. Health insurance products include personal accident policy, families and groups; serious illness policy; overseas travel.

For more information about the general characteristics of this segment, see paragraph 1.2.5 above.

2.5.2 Competition

This segment is characterized by intense competition from the leading insurance companies in the segment. According to the financial statements for the first nine months of 2016, the leading insurers in this segment by premium turnover are Harel (39.8%), the Phoenix (18.2%) and Clal (17.3%). The share of the Company of total segment premium turnover in the reported period is 2.1%.

The share of the Company in personal accident segment of the total premium turnover in the segment in the reported period is 11.7% and the share of the Company in the serious illness and overseas travel of total premium turnover in this segment is negligible.

The Company faces the competition in this segment by constantly considering developing new products, new and innovative tools and constantly improving customer service.

Data published by the Ministry of Finance show that the Company is ranked first in the service index in personal injury insurance and overseas travel insurance and ranked first in availability index for medical expenses.

The Company estimates that the annual publication of the service index will increase competition in the health insurance sector. The Company estimates that the service index may help the Company to become the lead player in this insurance sector.

The information included in this section constitutes forward looking information, which is based, among other things, on the current results of the Company. Actual results may be different than the estimated results, and may vary significantly, among other things, as a result of regulatory changes applicable to the Company and lower rating in the four factors underlying the service index.

In 2016, the Company did not develop material new products in this segment.

2.5.3 **Customers**

a. The following is the distribution of premiums by customer type in this segment (thousands of NIS):

	2016	**2015**	**2014**
Private customer – personal accidents insurance	171,196	172,613	169,880
Private customers – serious illness insurance	27,101	24,342	19,506
Overseas travel insurance	19,850	16,428	15,119
Group policies	1,184	2,213	3,273
Total	291,331	215,596	207,778

b. The Company mainly sells its products to privates customers through direct marketing. The sale of personal accident insurance policies is mainly done through insurance agents.
c. In the overseas travel segment, there is dependency on an agreement related to Leumi Card customers.
d. The sale of overseas travel policies is done through a special call center at the Company's offices serving mainly Leumi Card credit card customers. This agreement was renewed in 2017 for a 5-year period. In May 2016, an agreement was signed between the Company and credit card company Isracard Ltd ("**Isracard**"). Under that agreement, among other things, the Company provides overseas travel insurance coverage Isracard customers, and provide the customers the services in relation to the overseas travel insurance. Services to Isracard customers will begin in October 2016. Maintaining the present level of this activity in the segment is dependent on continuation of those agreements.
e. The rate of cancelations in 2016 in health policies that were in effect during the year in terms of premium was 18.2% of gross premiums.

2.6 **Activity segment 6 – Life insurance**

2.6.1 **Products and services**

The Company sells risk only life insurance policies to private customers (including life insurance for mortgage purposes). The policies cover death and include extensions for permanent disability and total disability, accidental disability, accidental death, critical illnesses and health insurance providing coverage of medical expenses.

In risk policies, the beneficiaries are those designated by the insurance customer (if any such beneficiaries were indeed designated by the customer). In risk policies for protecting mortgages and other loans, the lending bank is registered as a nonrecourse beneficiary up to the outstanding amount of the loan on the date of an insurance event plus inflation linkage and interest, early repayment fee and arrears interest for up to 12 months of repaying the loan.

As discussed above, health insurance for coverage of medical expenses is managed in the company within the life insurance segment. In early February 2016, the Company was granted approval to market all its health insurance products, according to a reform by the Supervisor in the health insurance market.

For more information about the general characteristics of this segment, see 1.2.6 above.

2.6.2 **Competition**

The life insurance segment is characterized by fierce competition. Most insurance companies are active in this insurance segment and 93.3% of the life insurance market is dominated by the five large insurance companies: Migdal, Clal, Harel, the Phoenix and Menorah. The share of the Company in the life insurance segment out of total premium turnover in the reported period is 0.5%.

Since clients can compare the life and mortgage insurance premiums charged by all insurance companies by using the life insurance calculators available in various websites, clients are very sensitive to the issue of insurance premiums. The Company faces this competition by ongoing improvement of customer service, branding and highlighting unique features of the Company, and increasing operating efficiency.

In this context, note that in 2016, the Supervisor launched two new calculators related to this segment – a life insurance rate calculator and a calculator for comparing health insurance, both available on the Supervisor's website. The purpose of the life insurance rate calculator is to allow the insurance customer population to compare between rates of insurance companies, and the purpose of the health insurance calculator is to allow the insurance customer public to compare between health insurance policies and rates of different companies.

The Company believes that the availability of those calculators on the Supervisor's website allows insurance customers perform effective comparison between insurance rates of different companies, which will increase competition in the life insurance and health insurance segments and may affect the market share of the Company in those segments. Company's estimation constitutes forward looking information, which is based on information available to the Company at the time of publication of this report. Actual results may be different than the estimated results, and may vary, among other things, as a result of the behavior of competing insurers and Company clients in those segments.

Also, in the opinion of the Company, the annual publication of the service index will intensify the competition in the life insurance sector.

2.6.3 **Customers**

The Company is not dependent on any single customer or a limited number of customers. The Company sells the product mainly to private customers through direct marketing. The Company does not have collective customers.

3. Part C – Additional information about general insurance segments not included among activity segments.

All insurance segments of the Company are included in Part B of this report.

4. Part D – Additional enterprise-level information

4.1 Restrictions and regulation applicable to the activity of the Company

The activity of the Company is subject to the provisions of different laws that are designed to ensure that insurance companies are run adequately. The following is a summary of main legal provisions:

Insurance Contract Law – This law governs mainly the relationship between parties to the insurance contract. In November 2016, the Insurance Contract Law (Amendment No. 8), 2016 was published in the official gazette. That amendment revised Section 28A to the Insurance Contract Law, which empowers a court to rule on special interest, as compensation, if an insurance company does not pay insurance benefits that were not contested in good faith according to the timing established by that law. The amendment increased the interest rate that a court can order to pay an insurance customer up to a ceiling of twenty times the interest rate set in the definition of "linkage differences and interest" in the Adjudication of Interest and Linkage Law, 1961 (compared to three times before the amendment). In addition, the definition of "personal insurance" for which it is possible to receive this compensation was extended, such that it will cover insurance for illness and hospitalization and insurance under the Motor Vehicle Ordinance.

The Supervision Law – The Supervision Law defines the role of the Supervisor and establishes her powers in relation to supervision over insurance companies. In August 2016, the Supervision of Financial Services Law (Legislation Amendments), 2016 was published in the official gazette. Among other thigs, the amended law creates the Capital Markets, Insurance and Savings Authority which will be independent in exercising its powers for exercising its duties and that the Minister of Finance, with approval of the government, will appoint a Supervisor of Capital Markets, Insurance and Savings for one term of five years. In addition, the law determined that the roles of the authority will be as listed below: protecting insurance customers and customers of other regulated entities; ensuring the stability and proper management of regulated entities; promotion of competition in the capital, insurance and savings markets and in the financial system and promotion of technological and business innovation, and that in exercising its duties the authority will implement and follow in its decisions the economic policy of the government in pension savings and healthcare and nursing care coverage.

Senior Officers Compensation Law – In April 2016, the Compensation to Officers of Financial Corporations Law (Special Permit and Non-Deductibility for Tax Purposes of Exceptional Benefit), 2016. The law sets a pay limit to officers in financial institutions up to ILS 2.5 million, and that beyond that threshold, compensation expenses of a company will not be tax deductible. In addition, it was determined that an employee of a financial corporation will not be able to receive compensation that exceeds 35 times the employment cost of the employee with the lowest salary in the organization.

a. **Regulations enacted under the Supervision Law – The following is a summary of key regulations enacted under the Supervision Law and which pertain to the Company's activity:**

- Minimum Capital Regulations – Indicate the minimum capital required by an insurer and the mechanism for computation.

- The Supervision of Financial Services (Provident Funds) (Investment Rules Applicable to Financial Institutions), 2012 and the Supervision of Insurance Business Regulations (Mode of Investment of the Capital and Reserves of an Insurer and the Management of its Obligations), 2001 ("**the investment regulations**"). The regulations set investment rules for institutional investors and corporate governance for investment activity, respectively. For more information on the investment segment of the Company see paragraph 4.4 of this report.

- The computation of General insurance reserves regulations, govern, among other things, the method and frequency for computing general insurance reserves.

- Details of Report Regulations – Those regulations govern all provisions concerning the contents, information and accounting principles for preparing financial statements of insurance companies.

- The Supervision of Financial Services Regulations (Insurance) (Financial Statements), 2007, require insurance companies, among other things, to prepare annual and quarterly financial statements.

- The Supervision of Financial Services Regulations (Insurance) (The Board of Directors and its Committees), 2007, which discuss the Board of Directors and its authorities and set rules for the proper function of the board and its committees, its composition, issues that must be discussed and be decided, attendance and legal quorum, board committees, delegation of powers, etc.

For more information about corporate governance applicable to those companies, see Part E. of this report.

- The discounting regulations and the Vinograd Committee recommendations

  On June 8, 2014, the Vinograd Committee was appointed, with the mandate to examine whether the data used by the Israel National Insurance Institute (NII) to calculate benefits for workplace injuries are up-to-date, and whether modifications are needed in life expectancy tables and interest rates used in discounting NII workplace injury benefits. Recommendations of the committee were published in March 2016, and they include, among other things, recommendations to adjust payments according to the current, higher, life expectancy and discounting one-off payments using interest rate of 2% instead of 3% due to lower interest rates in recent years.

  In June 2016, National Insurance Regulations (Discounting) (Amendment), 2016 ("the amendment to the discounting regulations") was published, adopting the Vinograd Committee recommendations. However, in August 2016, it was announced on the website of the Ministry of Finance that the Minister of Finance decided, with agreement of the Welfare Minister, that the above amendment to the Discounting Regulations will be cancelled, which would have increased the discount interest rate, and as a result, to increase compulsory vehicle insurance rates.

  In September 2016, another amendment was published in the official gazette, which postponed the amendment to the discounting regulations to October 1, 2017 ("**the effective date**"), such that its provisions will apply to calculation of discounted value in the effective date and thereafter. As indicated above, the amendment to the discounting regulations is supposed to lower the discounting interest rate, and as a result to increase rates in compulsory vehicle insurance.

As of the date of this report, management believes that the implementation of the Vinograd Committee recommendations by the Company, according to the amendment of the discounting regulations, will cause an increase in liability for Company insurance contracts in the compulsory vehicle segment by a gross amount of ILS 32 million and ILS 23.4 million in retention (including impact of "the Pool"). For more information about the impact of the Vinograd Committee recommendations on the results of the Company, see note 3 to the financial statements.

The information included in this section constitutes forward looking information, which is based, among other things, on present activity of the Company. Actual results may be different than the estimated results, and may vary significantly from the above forecast, due to many factors, chief among them are regulatory changes applicable to the Company, and the if development of claims in the future is significantly different than Company estimates.

b. **Regulatory codex**

Compulsory vehicle insurance segment

- In January 2016, the Supervisor published circular 2016-1-1 "Amendment of the Consolidated Circular in the Compulsory Vehicle Insurance Sector" ("The Amendment to Codex – Compulsory Vehicle Sector"). As part of the said amendment, the Supervisor regulated the following issues: (1) updating the insurance fees of private vehicles in residual insurance; (2) An identical risk premium shall be set to drivers of the same risk regardless of whether the person is insured under a collective insurance policy or not. (3) Allowing insurance companies to refund premiums to careful drivers at the end of the insurance period; and (4) cancellation of the automatic linkage of compulsory vehicle insurance premiums to the CPI. Most of the provisions of the circular shall apply to vehicle insurance policies, the insurance period of which commences on March 1, 2016 and thereafter. This circular cancelled, among other things, the provisions of the regulatory codex that allowed insurance companies to set different net insurance rates for vehicle fleets and collectives relative to those offered to vehicles that are not part of a fleet or collective, but in November 2016, the Supervisor issued Circular 2016-1-18 which amended Circular 2016-1-1 and determined that those provisions applied only to collectives.

- In August 2016, the Supervisor issued Circular 2016-1-10, titled "Amendment of Provisions of the Unified Circular in Compulsory Vehicle Insurance". The circular updates residual insurance rates for tri-wheeled motorcycles and adds 5 safety systems for motorcycles that provide discounted insurance rates. In November 2016, the Supervisor issued Circular 2016-1-19, which amended the previous circular that motorcycle insurance for any driver and insurance for two identified drivers will take into account safety systems in calculating insurance rates.

- In August 2016, a circular was issued listing factors in compulsory vehicle insurance. The circular updates the factors in compulsory vehicle insurance and its provisions apply to premiums effective from October 1, 2016.

- In September 2016, the Supervisor issued another circular titled "Amendment of Provisions of the Unified Circular in Compulsory Vehicle Insurance". This circular updates insurance premiums for cars that are insured by the Pool, and sts the Pool's rate beginning on January 1, 2017.

Home insurance segment

- On November 30, 2016, an amendment to the provisions of the home insurance codex was issued, and will become effective on June 1, 2017. The amendment deals with covering water damages as part of the extension for water and other liquid risk. The amendment eliminates the use of service providers and pre-payment for all policies (capitation), and in practice creates two new types of coverage: arrangement plumber and any plumber, and an insurance customer may choose between them.
  The Company estimates that this amendment will lead to higher costs for insurance companies in relation to this coverage, and at the same time to an increase in rates and self-insured retentions charged in this coverage.

Health insurance segment

- In January 2016, the regulatory codex was added part 3 title 6, "Provisions for Health Plans and Policies". This part includes specific guidance for healthcare plans and policy, and became effective in early March 2016.

- In January 2017, the Supervisor issued Circular 2016-1-26, titled "Amendment of Provisions of the Codex in the Overseas Travel Chapter." The purpose of that amendment was to set guidance on the drafting of overseas travel policies and the way to market them, such that it ensures proper coverage and fair selling process. Among other things, the circular set the following key provisions: determination that insurance payments need to correspond to the expected costs in the case of an insurance event, and considering, among other things, the costs expected in the destination country; determination that coverages will comprise a basic tier for the insurance plan and a list of add-ons that can be purchased on top of the basic policy, and imposing a duty on insurance companies to inform customers on the implications of pre-existing conditions, and when necessary, to offer an extension to cover that medical condition.

Reporting to the Supervisor chapter

- In November 2016, the Supervisor issued Circular 2016-1-23, titled "Amendment of provisions of the Codex regarding reports to the Supervisor in health insurance. The purpose of the amendment is to require insurance companies to report to the Supervisor information about existing coverages that are currently all reported in different reporting forms under "medical expenses".

- In January 2017, another amendment to the provisions of the reporting to the Supervisor chapter codex was issued, designed to changes the method of reporting and reporting address, and improve the content and quality of reporting, and reduce the frequency of certain filings.

c. **Circulars, clarifications, decisions and Supervisor positions:**

Circulars

The following is summary of the key matters concerning the activity of the Company that were addressed by the Supervisor in circulars, clarifications, decisions and opinions of the Supervisor in the reported period and until shortly before the date of issuing this report, and which were not included in the review of lines of business:

- In January 2016 and January 2017, the Supervisor issued Insurance Circular 2016-1-2 and Insurance Circular 2016-1-24, titled "Update of Guidance on the Structure of Required Disclosure Regarding Financial Statements of Insurance Company in Accordance to International Financial

Reporting Standards (IFRS)." The purpose of those circulars was to update the disclosure provisions set by Insurance Circular 2010-1-4.

- In April 2016, the Supervisor issued an in-principle ruling on the method for marketing personal injury policies. The ruling contain, among other things, specific provisions to correct weaknesses in marketing personal injury policies, including, notifications to customers and refunding premiums under the law in certain cases, and issuing reports and other filings to the Supervisors.

- In June 2016, the Supervisor issued Circular 2016-1-8, which is designed to amend the guidance on reporting to the Supervisors on rates and in life insurance policies as determined in Life Insurance Circular 2015-1-24.

- In June 2016, the Supervisor issued Insurance Circular 2016-1-7, titled "Acceptance to Insurance Plan". The purpose of the circular is to regulate the practices of insurance companies and insurance agents when accepting customers to insurance plans.

- In June 2016, a third update was published to the Supervisor's position, titled "Risk Management in Financial Institutions – Comparative Industry-wide Review". The Document reviews the findings collected by the Supervisor on risk management in insurance companies following an industry-wide examination that was performed across insurance companies (the objective of the examination was to obtain a snapshot of risk management infrastructure). The document establishes the position of the Supervisor on certain findings that emerged in the examination and discusses the proper implementation of its guidance in risk management.

- In July 2016, the Supervisor issued Circular 2016-9-9, titled "Settlement of Claims and Handling Customer Complaints". The purpose of the circular was to setting clear outline and rules for settling claims by financial institutions, given the impact on benefits to claiming customers, and to give them more clarity as to the options available to them in different stages of the procedure. In November 2016, the Supervisor issued an amendment to that circular, which requires financial institutions to implement a procedure for inquiry and producing lessons learned in cases where a deficiency identified while handling a customer complaint in the financial institution is found to by a systemic weakness. Further, in February 2017, a supervisor position was issued clarifying the circular regarding reexamination of qualification to benefits. The position of the Supervisor clearly states how to reexamine rights of a customer that is claiming benefits, according to the provisions of the circular.

- In July 2016, the Supervisor issued a position paper on findings of an audit of business continuity – an October 2015 exercise. The position paper reviews the findings of that exercise, and especially the difference between subpar implementation in financial institutions and best practices.

- In August 2016, the Supervisor issued Circular 2016-10-3 on engagement of financial institutions with licensed insurance agents. The purpose of that circular was to align the work procedures set by Circular 2004/14 "Engagement of an Insurer with an Insurance Agent" from handling premiums paid to the insurer through insurance agents and any engagement agreement between a licensed insurance agents and a financial institution.

- In August 2016, the Supervisor issued guidance on business continuity management and emergency readiness. The document contains instructions for business continuity exercise simulating a war scenario, which was performed in November 2016.

- In August 2016, the Supervisor issued a letter titled "Dividend distribution by Insurance Companies". The purpose of that letter was to set rules for dividend distributions by insurance companies, and that within the framework of preparations for a Solvency II-based regimen. For more information, see note 13 to the financial statements.

- In August 2016, the Supervisor issued Circular 2016-10-5 on digital signatures. The purpose of that circular was to allow verification of customer identity and to determine the methods for securing the contents of documents that are transferred from a customer to a financial institution by technological means, and that in order to streamline work processes and improve reliability of information in the market.

- In August 2016, the Supervisor issued Circular 2016-9-14 on the management of cyber risks by financial institutions. The purpose of the circular was to set principles for securing assets of financial institutions to ensure protection of customer rights by maintaining confidentiality, integrity and availability of information assets, information technology systems, business procedures and orderly activity of the financial institution. The circular defines, among other things, the principles for managing cyber risks in a financial institution and the duty by financial institutions to manage those risks based on the principles of cyber protection.

- In September 2016, the Supervisor issued an update to a circular that was issued in February 2016 and that set investment rules for financial institutions. The update amended the provisions that regulate lending by financial institutions, securities lending and investment in non-marketable debt instruments.

- In September 2016, the Supervisor issued Circular 2016-1-13 titled "Fixed-Premium Life Insurance Plans". The purpose of that circular was to set principles for refunding insurance customers in the event of cancelling policies or reducing their amounts in fixed-rate risk policies.

- In September 2016, the Supervisor issued an amendment to a circular on annual and quarterly statements to customers of financial institutions. The purpose of the circular was to establish, among other things, a format for annual and quarterly reporting for life insurance products and to expand the disclosure duty imposed on financial institutions, and that in order to make those statements in the future a tool that will allow customers to monitor those products. In February 2017, the Supervisor issued another update to that circular.

- In October 2016, the Supervisor issued Circular 2016-10-9 on annual reporting of premiums, policies and fees of financial institutions. The provisions of the circular regulate the reports that financial institutions are required to file to the Supervisors as to the scale of activity in the distribution market, including, the amounts of premiums transferred to them, distribution commissions and fees that are recorded in favor of insurance agents in the systems of a financial institution.

- In October 2016, the Supervisor issued Circular 2016-1-17 on a web interface to tracing insurance products. The purpose of the circular was to allow insurance customers to easily and quickly retrieve information about their insurance portfolio across insurance companies, and to examine the terms of insurance products in their portfolio.

- In October 2016, a position of the Supervisor was issued concerning regulation of investment activity. The purpose of that position paper was to present best practices and worst practices that were identified in audits of financial institutions. The position paper mainly focuses on the activity of investment committees, but discusses other organs of financial institutions.

- In January 2017, the Supervisor issued Circular 2016-10-13 on the involvement of unlicensed entities in selling and marketing insurance products that are not collective. The purpose of that circular was to provide more elaborate guidance on the engagement of regulated entities with non-regulated ones in relation to marketing or selling a non-group insurance product.

- In February 2017, the Supervisor issued Circular 2017-1-1, titled "Retrieval of Personal Information". The purpose of the Circular was to determine provisions that will allow retrieval of personal information by insurance customers. The circular determined, among other things, that retrieval of information will be done using various technology tools that allow access to different insurance products and for settlement of claims.

- In February 2017, the Supervisor issued Circular 2017-1-3 titled "Cancellation of Insurance Policies". The purpose of the circular is to make policy cancellation more accessible to insurance customers, and that through a uniform provision that require insurance companies to offer customers a range of options to cancel policies and specifying the actions required, which when performed lead to cancellation of a policy.

Drafts

The following is a summary review of drafts released by the Supervisor in the reported period and through shortly before the date of issuing this report and that may have material impact on the Company:

- In January 2016, a draft of Supervision of Financial Services Regulations (Insurance) (Limitations on Appointment and Term of Service of Key Officers in a Financial Institution), 2016. The purpose of the draft regulation was to increase the effectiveness of control and monitoring mechanisms in financial institutions, to limit the potential for conflicts of interest, enhance the independence of a financial institution and its key officers and to ensure the reliability of key officers. Among other things, the draft proposes to prohibit a controlling shareholder of a financial institution, or a relative thereof, to serve as key officer of a financial institution, except as a director, to rule that a person may not assume the duties of a key officer of a financial institution, unless he/she was appointed to that position according to the law, and to rule that no person may undermine the independent judgment of a key officer.

- In July 2016, the Supervisor issued a draft of Supervision of Financial Services Regulations (Insurance) (Group Health Insurance) (Amendment), 2016. The draft proposes, among other things, to allow different entities to be health policy holders, even if there is no affiliation between them and the group of insurance customers, and provisions were set to ensure that those entities will act for the benefit of the group of insurance customers vis-à-vis the insurer, including giving powers to the Supervisor to issue complementary provisions on this issue.

- In August 2016, the Supervisor issued a draft of Supervision of Financial Services (Insurance) (Maximum Fee for Reinsurance in Housing Mortgage Insurance) (Amendment), 2016. The proposed amendment states that the maximum fee that can be paid to agents for life insurance that is purchased to cover housing mortgage loans may not exceed 20% of ongoing premium that is paid for the insurance. In addition, in the first year of life insurance related to housing mortgages, the maximum fee may be up to 60% of the premium paid in that year only, provided that the policy is not cancelled for 6 years since inception. If the policy is cancelled as above, a proportion of the fee, for the remaining period until the end of the 6 years from policy inception, must be refunded.

- In September 2016, the Supervisor issued a draft regulation titled "Practices of an Insurer during the Life of a Policy". The purpose of the circular is to present in one document all guidance regarding the practices of insurers in interfaces with insurance customers, to protect insurance customers, and reduce knowledge gap between insurers and customers in different stages over the life of a policy.

- In October 2016, the Supervisor issued a draft circular on the involvement of sales reps in the process of marketing and selling insurance products. The purpose of the draft is to regulate the use of sales reps (who do not hold a license to be insurance agents) by insurance agents for marketing and selling insurance products.

- In January 2017, the Supervisor issued a draft regulation titled "Transmission of Information Files via Vault Applications". The purpose of the draft is to detail the requirements from financial institutions for the use of vaults to allow maintaining information confidentiality.

- In January 2017, a bill of the Supervision of Financial Services Law (Insurance) (Amendment – Mortgage Loan Insurance in the Event of Unemployment), 2017. The purpose of the bill is to determine that the Supervisor may issue provisions for mortgage loan insurance coverage in the event that the lender loses his/her source of income, such that the policy will cover mortgage payments over the period of entitlement to unemployment benefits, plus additional 3 months; and to prevent a bank require buying such insurance as precondition to a mortgage loan.

- In February 2017, the Supervisor issued draft amendment to a circular titled "Settlement of Claims and Handling Customer Complaints", and draft amendment to an insurance circular titled "Acceptance to Insurance Plan". The purpose of the drafts is to prevent problematic practices by financial institutions in relation to settling claims and acceptance of customers. On the same date, another draft amendment was issued on drafting provisions of insurance plans. The purpose of that draft was to restrict the use of insurers of insurance contract wording that limit the ability of insurance customers to exercise rights under the policy.

4.2 Entry and exit barriers

4.2.1 Key entry barriers

Key barriers on entering the different activity areas of the Company are as follows:

a. Licenses and permits: According to the Supervision Law, practicing in each insurance sector required obtaining an insurer license from the Supervisor. In addition, holding more than five percent of a specific type of controlling instrument in an insurance company is conditioned on obtaining a permit to hold controlling instruments from the Supervisor, and controlling an insurance company also requires a controlling permit from the Supervisor.

b. Capital: An insurer has to comply with capital requirements. For more information about regulatory capital requirements that apply to the Company and compliance of the Company, see 5.5 below and note 13 to the financial statements.

c. Infrastructure: Given the complexity of the insurance products and their daily management, an insurance company needs to create an organizational, IT and operating infrastructure and continuously maintain it.

d. Expertise, experience and reputation: Being an insurer requires a focused professional knowledge and understanding of different insurance aspects, mainly involving actuary, underwriting, investment, reinsurance, marketing and risk management. In addition, to set rates and underwriting terms for new policies, it is important to have experience and a broad actuarial database.

e. Minimum revenue: An insurance Company must generate minimum revenue to cover the high operating costs involved in investment in buying, maintaining and upgrading systems and infrastructure, including the need to comply with regulatory change that take place from time to time.

f. Reinsurance: the ability and knowhow to buy adequate protection from reinsurers and to engage in reinsurance contracts with them.

4.2.2 Key exit barriers

The key barriers on exiting the different activity areas of the Company are as follow:

a. Liquidation or dissolution of insurance business: A liquidation or dissolution of an insurer are subject to oversight by the Supervisor, who may order the insurer to act in a certain way upon dissolution of its business or to ask a court to order the dissolution to be controlled or overseen by the court.

b. Run-off: The around policies with long claims tail may continue for many years until all claims for policies sold prior to the termination of the activity are settled and until all rights of existing insurance customers are satisfied or until the sale of the insurance activity.

4.2.3 Limitations in control permit

The main limits in a permit to control a company are as follows:

a. Maintaining control over the Company: AIG committed to hold all controlling instruments in the Company and intermediate companies in the Company's chain of control at all times, and that its holding rates in the Company may not change in any way unless the Supervisor has gave an advanced, written agreement and subject to the terms and conditions he set. In addition, the control permit requires an advanced approval by the Supervisor for control over AIG.

b. Prohibition on transferring rights to controlling instruments to a third party: AIG committed to maintain all controlling instruments of the Company free and clear at all times.

c. Capital replenishment: A company in the AIG control chain irrevocably committed to replenish the capital of the Company, if required, up to the amount required by the Minimum Capital Regulation while AIG is controlling the Company.

d. Interested party transactions: AIG, the entities it controls and companies in the control chain of the Company are entitled to management fee from the Company only under a written management agreement that is submitted to the Supervisor at least sixty days prior to its effective date, provided that the Supervisor has not opposed that agreement prior to its effective date. The above limitation does not apply to providing services in the ordinary course of business and at arm's length by such companies.

e. Change to articles of association: Any change in the articles of association of the Company that may impact the control over the Company or any term of the controlling permit is subject to an advance, written approval by the Supervisor.

4.3 Key success criteria

a. Changes in the macroeconomic situation in Israel and globally, including changes in the security situation, inflation, interest rates, unemployment, the average salary, etc, may have material impact on the Company's business results. Changes in the regulatory policy for capital markets and volatility in the capital markets, in general, and bond yields, in particular, may have material impact on the business results of the Company.

b. The political and security situation in Israel affects the fiscal and monetary situation of the Israeli economy and the position of the capital market. In addition, different security arrangement may have impact on the prevalence of car theft in Israel and thus, have material impact on the results in the property vehicle insurance business.

c. The Israeli insurance market is competitive, especially so in retail insurance, which is the main activity of the Company. Raising rates given the competition in this market may impact profitability of the Company. For more information about the competition in the Company's different areas of activity and measures that the Company is taking to deal with this competition, see paragraphs 2.1.2, 2.2.2, 2.3.2, 2.42, 2.5.2 and 2.6.2 in this report.

d. Frequent changes in regulatory require3ments and case law may have material impact on the business results of the Company.

e. In addition, the Company believes that the key factors for success in its activity include: frequent revision of actuary assumptions that underlies rates; improvement of quality, professionalism and underwriting data reliability; the quality of reinsurance and stability of reinsurers; customer mix and loyalty; customer retention levels; cutting operating costs; marketing and distribution; owning IT and supporting systems; quality of investment portfolio management and investment income; streamlining claims management and settlement costs; achieving a high rate of subrogation; improving the quality of customer service to customers; low frequency of natural disasters; reducing the scale of insurance fraud; recruiting and retaining quality human capital; the ability of the Company to improve agreements with suppliers; quality of collection and creating new distribution channels, and continuous improvement of digital services.

Those success factors have not materially changed in 2016 except for the financial situation that changes frequently and impacts the Company in much the same way as it impacts the entire insurance market.

4.4 **Investments**

Investments of the Company are managed by the Company's external portfolio managers according to instructions by the Investments Committee, which was set up pursuant to the Supervision Law and investments regulations, and according to investment asset chapter in the regulation codex, as well as other provisions of the Supervisors concerning investments.

The investment policy of an insurer is determined by the Company's board based on recommendations of the investment committee according to the law. The Company mainly implements a prudent and conservative investment policy including:

- Investment in listed government bonds
- Investment in high-rated corporate bonds
- Investment in bonds with short to long average term to maturity
- Investment in shares through instruments that track leading share indices in Israel and internationally

Credit risks involved with those investments are managed according to the law and the policy of the board through the investments committee and the distress debt center of the Company. The Company is not required to appoint a specialized credit committee. The risk management policy includes exposure limits, including, limits on exposure to one debtor, a group of creditors, linkage basis, industry, liquidity and credit rate.

For more information about the investment management policy of the Company, please go to: http://www.aig.co.il-אודות/aigמדיניות-השקעות/

For more information on the composition of Company investments, see notes 11 and 28 to the financial statements. For information about the contribution of investment components on the proprietary portfolio, go to: http://www.aig.co.il/אודות-aig/תיק-הנוסטרו

For more information about the composition of net investment income and net financing income, see note 22 to the financial statements.

4.5 Reinsurance

a. General

Reinsurance engagements of the Company are made on an annual basis according to the activity area. All engagement agreement with reinsurers are discussed annually by the board and reported annually to the Supervisor according to the Supervisor's guidance. In each insurance segment, the reinsurance coverage is adjusted to the nature of risk and its level. The types of coverage that the Company commonly uses:

- **Proportional reinsurance**: Those reinsurance arrangements include quota share and surplus insurance. In quota share insurance, the relative division between the reinsurer and the insurance company is identical for all policies in a given insurance area. That proportion is used for dividing both premiums and claims. In a surplus insurance, the insurance company predefines the risk level it assumes, and the remaining risk in each policy is transferred to the reinsurer, meaning that the share of the reinsurance in the risk can vary from one policy to the other.

- **Non-proportional reinsurance**: Excess of loss insurance ("**XOL**") – this type of reinsurance covers claims or events over a certain amount, i.e., the insurance cover exceptionally high multiple-risk individual claims. Any amount below the predetermined amount is covered by the insurance company only and not by the reinsurance.

- **Facultative reinsurance**: Those reinsurance arrangements cover special risks embedded in specific policies. For the most part, such business is reinsured in this way when the insurance amount exceeds the capacity of reinsurance contracts mentioned above.

The reinsurance exposure policy is established by the risk management and equity committee of the Company. This policy is based on internal actuarial assessments, various models and claim history. As part of this policy, the sectors in which it is more efficient to transfer the risk to reinsurers based on risk management factors and the size of capital held by the Company. According to the provisions of the Supervision Regulations, the board approves once annually the retention that the Company holds by activity segments and the exposures to reinsurers.

b. **American International Overseas Association companies**:

A major share of reinsurance is by the following three insurance companies (referred to together as: "**AIOA companies**"):

Company name	**Participation (%)**
New Hampshire Insurance Company	12%
National Union Fire Insurance Company of Pittsburgh, PA	78%
American Home Assurance Company	10%

Those three companies are members of the global AIG corporation, and are related parties of the Company

As of the date of this report, those three reinsurers are rated A+ by S&P.

For more information about total premiums transferred in 2016 to reinsurers, see note 28 and 5 to the financial statements. For more information about balances and transactions with interested and related parties, see note 29 to the financial statements.

c. **Property vehicle insurance**

The Company engaged in the reported period in this sector in an XOL reinsurance contract with AIOA. The premiums recorded in favor of AIOA in the reported period were NIS 115 thousand. No fees are paid under this contract.

d. **Compulsory vehicle insurance**

The Company engaged in the reported year in this insurance segment in an XOL reinsurance contract with AIOA. The premiums recorded in favor of that company in the reported year was NIS 2,016 thousand. No fees are paid under this contract.

e. **Home insurance**

The Company entered in the reported year into a surplus reinsurance contract with AIOA. Fee is fixed as a share of premium (approximately 25%).

For catastrophe events (e.g. earthquakes and other natural disasters), the Company purchases in addition to a proportional reinsurance coverage also XOL reinsurance for home insurance. The assessment of the risk for a catastrophe event, and the expected damage was made by a professional team. According to updated calculation using special statistical models, the maximum probable loss (MPL) after self retention is 1.15%. The Company protects itself against earthquake events, including one in 250 year magnitude events. The MPL for calculating catastrophe risks in general insurance in calculating minimum required capital is 1.75%.

As of December 31, 2016, the insurance amount covered by proportional reinsurance in relation to earthquakes is NIS 2,549 million, while amounts covered in non-proportional reinsurance amount to NIS 49,998 million.

As of the date of this report, the Company acquired reinsurance coverage of NIS 660 million over the Company's retention, which is NIS 40 million for catastrophe.

The following is a list of premiums in home reinsurance (in thousands of NIS):

Home reinsurance premium:	**2016**	**2015**	**2014**
Proportional	4,656	7,513	7,686
Proportional - earthquake	2,317	4,078	7,645
Non-proportional - earthquake	7,613	5,400	8,639
Total	14,586	16,991	23,970

Note that this table does not refer to underwriting years but to the general calendar results at the segment level as presented in note 5 to the financial statements and may not indicate the underwriting results of reinsurers by underwriting years.

The premium recorded in favor of the AIOA companies in the reported year is NIS 12,148 thousand, and fees amount to NIS 2,700 thousand. The premiums recorded in favor of AIG Europe Ltd in the reported year was NIS 1,902 thousand.

f. **Health insurance**

The Company entered in the reported year into the following reinsurance contracts in this segment:

- A surplus reinsurance contract, with fee as a fixed percent of premium (35%). Reinsurers in this contract are AIOA.

- A Quota Share reinsurance contract in a certain critical illness sector. The reinsurer in this contract is Swiss Re, which is rated AA- by S&P.

- In 2015 the Company entered into XOL reinsurance contracts from the amount of Company retention with AIOA companies, which covers from the amount of retention of the Company and up to $70 million in the reported year and up to NIS 245 million in 2016. The Company intends to renew that engagement for 2017.

The premiums recorded in favor of AIOA companies in the reported year are NIS 1,543 thousand. Commissions from reinsurance amounted to NIS 112 thousand.

g. **Commercial insurance**

The Company engaged in the reported year in quota share and surplus reinsurance contracts in liabilities, professional liability, property, contractors, mechanical breakage and electronic insurance contract with AIOA. The premiums recorded in the reported year to the related companies amounted to NIS 110,443 thousand. The Company received fees on those contracts at a fixed rate of 26% to 35% from premium.

The Company does not purchase XOL catastrophe coverage in property insurance and commercial insurance due to the lower retentions to which the Company is exposed.

h. **Life insurance**

The Company engaged in surplus reinsurance contracts with Swiss Re, which is rated AA- by S&P and with Partner Re, which is rated A+ by S&P. Previously, the Company engaged with Gen Re, which is rated AA+ by S&P.

Fees on those contracts are at a fixed rate of premium in the first underwriting years.

In 2016, the Company engaged in a XOL insurance contract to cover catastrophe events with AIG Reinsurance Company Ltd, which is a company in the AIG global corporation, a related party of the Company and rated +A by S&P. The Company intends to renew the engagement for 2017.

The following is information about premiums transferred to those companies:

Reinsurer name	**Total reinsurance premiums (NIS in thousands)**	**% of total reinsurance premiums**
Swiss Re	17,077	80%
Partner Re	2,768	13%
Gen Re	1,166	5%
AIRCO	355	2%
Total	21,366	%100

j. Summary of reinsurance results in general and health insurance (in thousands of NIS):

	Property vehicle			**Compulsory vehicle**			**Home insurance**		
	2016	**2015**	**2014**	**2016**	**2015**	**2014**	**2016**	**2015**	**2014**
Reinsurance premiums	115	116	108	2,016	2,051	2,040	14,586	16,991	23,970
Income / (loss)	115	116	108	(28,583)	60,623	(11,420)	8,970	6,462	13,649

	Health			**Commercial (*)**			**Total**		
	2016	**2015**	**2014**	**2016**	**2015**	**2014**	**2016**	**2015**	**2014**
Reinsurance premiums	3,037	2,408	5,606	122,040	122,757	106,577	141,794	144,323	138,301
Income / (loss)	(504)	(962)	(460)	(55,284)	(9,886)	(48,405)	(75,286)	56,353	(46,528)

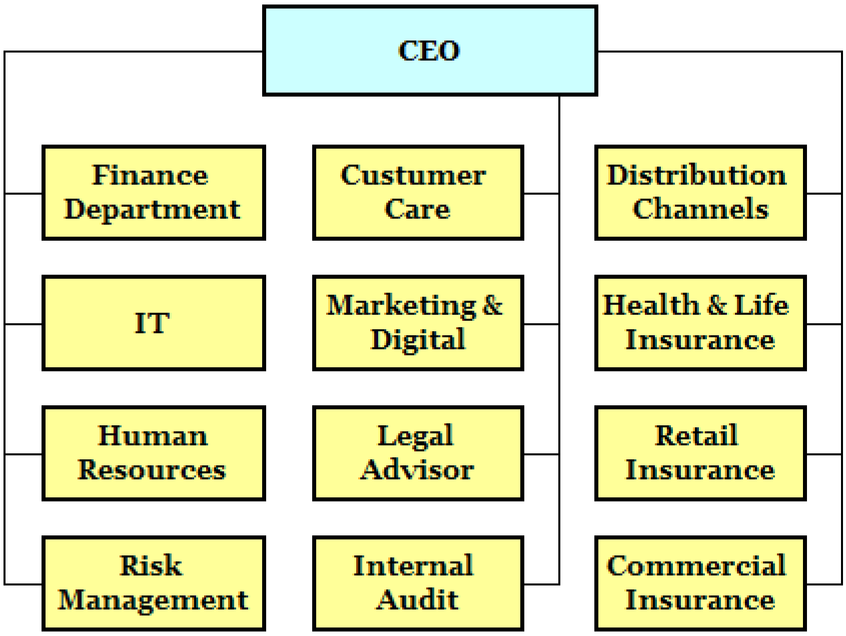
(*) Reinsurance premiums in commercial insurance are proportional contracts only, and include earthquake premium of NIS 12,051 thousand in 2016 and NIS 11,946 thousand in 2015.

For more information on reinsurance results, see note 28.f.5.3 to the financial statements.

4.6 **Human capital**

a. General

The following is an organizational structure of the Company as of the date of this report:



The organizational structure of the Company is based on operations through a head office, located in Petach Tikva, Israel.

As of December 31, 2016, the Company had 829 employees, compared with 904 employees at the end of 2015. Some 70% of employees work in sales and services, compared to 72% in 2015.

The Company has no dependence on any single employee.

The Company believes in the importance of improving its human capital, and is conducting from time to time professional seminars to managers and other employees about different areas of activity. The Company is investing special efforts to train new employees in sales and customer service centers. In addition, trainings are also provided by AIG outside of Israel on professional matters with the attendance of managers and other employees of the Company.

The Company is constantly reviewing its workforce and an option for improving efficiency in connection with its employees.

The weighted number of employees in the Company based on full-employment equivalent as of December 31, 2016 and 2015, based on the organizational structure if as follows:

Activity area:	**2016**	**2015**
Sales and services centres	502	558
Claims	73	72
Headquarters - business divisions	46	48
IT	44	47
Administrative and general	22	20
HR	22	19
Finance	19	21
Marketing	13	8
Total	741	793

b. Executives:

- Senior management, including the CEO, comprised on the date of issuing this report 13 executives compared to 14 at the end of 2015.
- For more information about management – see Regulation 26A in Chapter D to the report "Additional Information on the Corporation".
- As of December 31, 2016, the board of the Company includes 7 directors, 3 of them are external (independent) directors. For more information see Regulation 26 in Chapter D of the "Additional Information on the Corporation" chapter.

c. Compensation policy of the Company

General

Company's employees, who are not executive, may be eligible to an annual bonus. The bonus will be paid based on the Company's financial position and its meeting of its business targets; payment of the bonus is subject to the approval of the Company's board of directors. The amount of the potential annual bonus is set based on the rank of employees as a range of several salaries. This range is based on the level of performance of the employees compared to other employees in the relevant department in the Company or in the Group.

Some employees may be eligible to monthly or quarterly bonuses on top of their basic salary; this bonus is based on the scope of activities they are in charge of. This type of bonus may be payable to marketing and sales employees, i.e., Company employees who sell or market products to clients such as sales managers, portfolio managers, employees engaged in retaining a portfolio, customer service employees and sales center employees. This type of bonus changes from time to time in accordance with the business targets of the Company. The targets such employees need to meet in order to become eligible to the bonus are determined in a manner that will not encourage employees to behave unfairly to clients in order to become eligible to the bonus.

Control and supervision employees – the eligibility of those employees to annual bonus is not determined in accordance with their meeting any performance targets relating to the activities they are in charge of.

Officers (who are not directors) – The Company compensation policy to offices are according to legal requirements, including the provision of the circular titled "Compensation Policy in Financial Institutions" and the amendment of that circular. In early, 2016, a new compensation plan was adopted for officers of the Company. The provisions of the plan state, among other things, that payment of compensation for each year of qualification is spread over four years, and that subject to meeting personal annual goals, officers are entitled to a bonus whose overall ceiling and its progressive payment are predetermined by the compensation committee and board of the Company. The amount of bonus to officers is determined according to the rate of meeting those goals, multiplied by the number of salaries as determined by the compensation committee and board of the Company. Actual payment of the annual bonus is spread in such way that only 50% of the bonus amount is paid in March of the year subsequent to the year of entitlement, and the remainder is spread using the straight-line method over the next three years, and that subject to meeting the predetermined profitability goals. The goals at the Company level include premium goals, profitability, service level and personal goals, which include personal and department goals, as well as goals related to risk management and compliance. The degree of meeting personal goals is determined by the direct superior of the officer.

According to this compensation plan, no bonus is paid to officers if the Company fails to meet the capital level as required by law.

Approval of the goals of each annual plan, review of actual results and approval of bonus payment are approved by the compensation committee and the board of the Company.

The previous compensation plans for 2011 to 2015 included elements of both annual bonus and long-term compensation. The long-term plans in effect as of December 31, 2016 began on January 1, 2014 (ending December 31, 2016) and January 1, 2015 (ending December 31, 2017). The long-term compensation plan include compensation to officers according to a number of criteria that relate to performance of the Company and is a long-term plan for three-year bonus periods. In each three-year bonus periods, a number of different targets are computed for each of the three calendar years in that bonus period. Each annual target for a calendar year is set and approved by the Board of Directors of the Company. At the end of each three-year bonus period, performance is compared to targets for the bonus period, i.e. for three years.

The annual compensation for each bonus period is computed as the percentage of meeting the targets for the bonus period multiplied by the amount in the personal target for each officer, which is composed of his/her average salary during the bonus year, times the "salary component" that was set by the Board of Directors of the Company according to his/her role in the Company.

Directors – the salary of Company's independent directors is determined in accordance with the provisions of The Companies Regulations (Rules Regarding Compensation and Expenses to Independent Directors), 2000 ("the Compensation Regulations"). The salary of directors who are not independent directors does not exceed the amounts set in the Compensation Regulations.

For further details regarding the employment terms of senior office holders in the Company, see Regulation 21 in Part D of the annual report.

For more information about the compensation policy of the Company, go to:
https://www.aig.co.il/about_aigמדיניות-התגמול/

4.7 **Marketing and distribution**

The Company sells coverage directly to customers without involvement of insurance agents. This methodology is characterized by a direct relationship between the Company and its existing and prospect customers. This relationship is maintained by the main centers of the Company (sales and service) through technology, including computer software that allow Company employees using computer system to access detailed information for making decisions on the activity areas.

The call center and website are major marketing and sales resources of the Company. A disruption of those communications resources over time may materially impact the activity of the Company. The Company also sells retail policies (vehicle, home insurance and personal injury) and commercial insurance through insurance agents. Agents receive commissions at a percentage of premiums according to the rate of collection of those premiums.

As part of promoting its marketing efforts, the Company uses, among other things, advanced methods for storing databases allowing automated connectivity as well as decision-supporting systems and auxiliary systems like: a telephone system, recording applications, email, telemarketing, document scanning, fax, sending automated email and more. The Company has a computer system that monitors work flow.

The main marketing channels of the Company are as follows:

- Media advertising (TV and radio) – main channel
- Advertising and selling online, billboards and print
- Insurance agents
- Cooperation with companies
- Use of databases of the company for cross-sales and up-sales.

a. Property vehicle insurance

Policies in this segment are marketed mainly through direct marketing. The average commission paid to agents (before VAT) is 15.3% of gross premium.

b. Compulsory vehicle insurance

Policies in this segment are marketed mainly through direct marketing. The average commission paid to agents (before VAT) is 5.7% of gross premium.

c. Home insurance

Policies in this segment are marketed mainly through direct marketing. Additionally, the Company sells policies in the segment through customers who are interested to buy life insurance for mortgage lending purposes and contacted the Company thanks to marketing efforts in life insurance.

d. Health insurance

Policies in this segment are marketed mainly through direct marketing. In addition, the Company sells its products in this segment through telemarketing (cross sale), a limited number of insurance agencies and the Company's website (mainly overseas travel). As to travel overseas travel insurance see section 2.5.3 above.

Marketing of personal accident policies is also made by an insurance agency wholly-owned by Meitav Dash Investments Ltd.

Part of shares of group personal injury policies is done through insurance agents. The average commission paid to agents (before VAT) is 17.5% of gross premium.

e. Commercial insurance

Policies in this segment are marketed exclusively through insurance agents. As of the date of this report, the average commission paid to agents (before VAT) in the liability business is 14% of gross premium, in professional liability 19.5% and in property and engineering 9%.

f. Life insurance

The Company sells most policies to customers directly without involvement of insurance agents.

For information about material changes in the reported period that relate to commissions or payments to marketing channels, se section 4.1 to the report.

4.8 Suppliers and services providers

a. General

The Company buys products and services from numerous suppliers including advertising and marketing providers, equipment and maintenance providers, legal services providers, appraisers, investigators, healthcare institutions, software and hardware providers, auto repair and parts services, towing services, auto glass repair, damage repair, car leasing, etc. The cost of some of those purchases is recognized within cost of claims in the different insurance segments, and mainly in compulsory and property insurance.

The Company selects its suppliers according to cost, quality, quality, availability and expertise. Usually, engagement with providers is for a predefined period (automatic annual renewal) and do not involve exclusive arrangements.

b. Compulsory vehicle insurance

The Company purchases products and services from different providers, including advertising and marketing providers; legal services providers; appraisers; investigators; vehicle repair and parts services; used car dealers for damaged or retrieved after theft; towing; auto glass repair, etc. A significant part of the cost of those purchases is carried to the cost of claims. The Company is not materially dependent on any supplier or services providers.

c. Compulsory vehicle insurance

The Company purchases products and services in this segment from different providers, including: advertising and marketing providers; legal services providers; hospitalization and other healthcare services; investigators; etc. A significant part of the cost of those purchases is carried to the cost of claims. The Company is not materially dependent on any supplier or services providers.

d. Home insurance

The Company engaged in agreements with different service providers rendering services related to covering water damages and home emergency services. A customer holding an extended policy with additional types of coverage is serviced by the relevant provider according to the relevant service contract. A significant part of the cost of those purchases is carried to the cost of claims. The Company is not materially dependent on any supplier or services providers.

e. Health insurance

The Company purchases in this segment products and services from various providers, including healthcare service providers, advertising and marketing services, legal services providers, investigators, overseas traveler assistance services, etc. A significant part of the cost of those purchases is carried to the cost of claims. The Company is not materially dependent on any supplier or services providers.

f. Commercial insurance

The Company purchases in this segment legal, appraisal and investigation services. A significant part of the cost of the above services is carried to the cost of claims. The Company is not materially dependent on any supplier or services providers.

g. Life insurance

The Company purchases in this segment products and services from various providers, including healthcare and legal service providers, investigators, advertising and marketing providers, etc. The cost of those purchases is carried to the cost of claims. The Company is not materially dependent on any supplier or services providers.

h. Non-segment specific service providers

- **Computer and software suppliers** – The Company is engaged with a number of software and hardware providers for both purchasing new products and for regular maintenance of its systems. The two main suppliers for maintaining the insurance system are Comtech Ltd and Dortel Software Systems Ltd. In 2015 and 2016, the Company made a significant investment in a new CRM system. The Company is dependent on those suppliers to a certain degree.

  The total payment to those suppliers in NIS millions are as follows:

Provider	2016	2015
Dortel	2.8	3.2
Comtech	3.1	3.5
Rail Comerce	2.0	2.2

- **Marketing and advertising service providers** – The Company sells most of its products through direct marketing to customers and therefore its marketing and advertising purchases are material relative to other insurance companies. The primary advertising service providers of the Company in this area in 2016 were the advertising agencies Reuveni Pridan Ltd, Pearl View, They Say and Unik Public Image. For more information about the scope of expenses in this area, see note 25 to the financial statements.

4.9 Property, plant and equipment

a. Property, plant and equipment (PPE) of the Company is located at the Company's headquarters at 25 Hasivim St., Petach Tikva, and in the emergency sites of the Company in the Haifa area. For more information, see notes 6 and 8 to the financial statements.

b. Computer systems – The Company has an internal information technology (IT) unit, providing automation services to Company units, and is uses the services of suppliers and software companies, as necessary, for ensuring the required computing services. The main development and production site is located at Company headquarters in Petach Tikva, and there is also a backup site for emergencies in the Haifa area.

   The main core systems of the Company include the insurance systems and financial systems that are installed on an IBM AS-400 computer.

   In 2016, the Company invested NIS 20.9 million in hardware and software. A significant part of that investment relates to the new CRM system. The balance of depreciated cost of computer systems (including computer software) in the Company as of December 31, 2016 was NIS 40.8 million.

4.10 Seasonality

a. The following table presents gross premiums (general insurance and life insurance) by quarters:

2016 Quarter	1	2	3	4	Total
Property vehicle insurance	86,404	74,886	84,787	68,046	314,123
Compulsory vehicle insurance	40,644	34,462	39,335	31,643	146,084
Home insurance	28,094	23,786	27,985	23,568	103,433
Commercial insurance	53,674	19,761	31,037	33,338	137,810
Health insurance	53,003	53,632	56,823	55,873	219,331
Life insurance	31,513	31,052	31,670	31,916	126,151
Total	**293,332**	**237,579**	**271,637**	**244,384**	**1,046,932**

2015 Quarter	1	2	3	4	Total
Property vehicle insurance	74,860	67,936	74,705	66,676	284,177
Compulsory vehicle insurance	41,297	35,612	37,002	32,871	146,782
Home insurance	29,131	22,750	28,083	22,282	102,246
Commercial insurance	36,781	30,585	36,008	37,797	141,171
Health insurance	52,355	52,494	57,442	53,305	215,596
Life insurance	30,307	30,356	31,018	31,435	123,116
Total	**264,731**	**239,733**	**264,258**	**244,366**	**1,013,088**

b. The mechanism for computing reserves for unexpired risk in general insurance is mitigating the impact of seasonality on income turnover.

4.11 Intangible assets

a. is the registered trademark of the global AIG corporation.

b. The Company has permission to use the eight registered trademarks of the AIG – trademarks number 143541, 249430, 143544, 148118, 148119, 148120, 151905, 184361, 249429.

c. The trademark AIG ISRAEL 1-800-400-400 for communication with the sales centre of the Company is a major brand of the Company and an intangible asset. This telephone number is protected, among other things, through trademark no. 184361.

d. The Company owns six databases – claims information, suppliers and agents, employees, job candidates, customers and prospect customers. Those databases store, among other things, information given by customers when buying policies and more information provided in relation to services it provides (such as processing claims). The databases use the Company in the ongoing operation of its business and for marketing insurance policies.

e. For more information on intangible assets - see note 6 to the financial statements.

4.12 **Risk factors**

There are a number of risk factors affecting the profitability and stability of the Company. The following table presents risk factors and their impact on the Company:

	Risk factors	**Significant impact**	**Moderate impact**	**Small impact**
Macro risks	Economic slowdown in Israel		√	
	Interest		√	
	Inflation		√	
	Share and bond prices		√	
	Credit spreads		√	
	Exchange rates			√
	International market risks			√
	Credit risk		√	
	Asset/liability alignment risk			√
Industry risks	Portfolio retention		√	
	Competition		√	
	Earthquake	√		
	Terrorism			√
	Epidemic		√	
	Regulation and compliance	√		
	Theft, accidents and fire		√	
	Reinsurance stability		√	
Company-specific risks	Legal risks		√	
	Model, parameters, underwriting risks		√	
	Operating risks		√	
	IT risk	√		
	Liquidity risk			√
	Reputation risk	√		
	Wrok relations			√

The impact of the above risk factors is based on the discretion of management based on the judgment of management based on the existing assessment as of the date of this report. This assessment is general and it is possible that different factors may have indirect impact if occurring concurrently.

For more information on the overall risk exposure of the Company – see note 28 to the financial statements.

4.13 **Material agreements and cooperation agreement**

In October 2016, Company began full activity in relation to providing overseas travel coverage to Isracard customers under an agreement that was signed by the Company and Isracard in the second quarter of 2016.

4.14 **Other forecasts and assessments on the business of the Company**

This section, by nature, includes forward-looking information, as defined by the Israel Securities Law, which is uncertain and based on assessments and intentions of the Company as of the date of the report. Company assessments may not materialize or partially materialize or in a different way than assessed by the Company.

The business strategy of the Company and its main targets for each line of business are as follows:

- Maximizing profit from all sources of income of the Company, while focusing on maximizing underwriting profit in each line of business separately.
- Providing high-quality customer service
- Exercising business discipline in underwriting and investment operation
- Maintaining the strength of Company brand
- Focusing on customer retention
- Increasing sales in each insurance line of business, both in the direct channel and through agents
- Balancing between the insurance lines of business without relying on any given line of business
- Constantly exploring new means of distribution
- Constant awareness to customer needs, and accordingly, developing new stand-alone and bundled products
- Control over the extent of Company expenses
- Improving operating efficiency of anything related to decision-support systems
- Priority for investment in digital services
- Nurturing excellence in all Company units
- Careful compliance with regulation.

5. Part E – Corporate governance information

5.1 Information about independent directors

As of the date of the report, the Company's Board of Directors has 7 directors, of which 3 are independent directors. In the reported period, the Board held 12 board meetings.

In January 2016, Mr. Arie Nachmias commenced his tenure as an intendent director in the Company.

In March 2017, Mr. Jules Polak was appointed independent director of the Company, according to a letter from the Supervisor, dated January 25, 2017.

For more information about external directors of the Company, see Regulation 26 of the Additional Information Report of the corporation.

5.2 Internal auditor

a. **Information about the internal auditor and beginning of service**:

The internal auditor of the Company is Mr. Thomas Lowe. Mr. Lowe is an accountant (holds a South African license) and has thirteen-year experience in the AIG corporation, including ten years of different rolls in the internal audit system of AIG and three years in financial positions in Europe. He began his services in this roll on September 1, 2013.

b. **Securities holding and conflict of interest**:

The internal auditor has no business relations with the Company or a related entity. The internal auditor holds two ordinary shares in a related AIG company. This shareholding may not affect his work in any way.

c. **Work relations and additional roles:**

The internal auditor is a Company employee who has no other rolls outside the Company. The internal auditor is assisted by two internal audit employees of the Company, and when necessary, uses external service providers and the internal audit resources of AIG.

d. **Scale of employment**:

The internal auditor' scope of employment is derived from the work plan approved by the Audit Committee and is subject to changes as a result of the business activity. In 2016, the internal auditor invested 4,370 hours in his work. In 2017, the scope of employment was set to 4,300 hours.

In addition to the internal audit performed by the internal auditor, the internal auditor performs periodic audits by the internal audit function of AIG. Those audits mainly focus on the financial, risk management and IT aspects.

e. **Compensation**:

The internal auditor is compensated by a monthly salary under a personal work contract, at amounts that reflect his position and responsibility. In 2016, the compensation of the internal auditor and his team was NIS 1.5 million. Total compensation to the internal auditor in 2015 was NIS 1.4 million.

The board believes that the compensation of the internal auditor may not affect his professional judgment.

5.3 Independent auditors

The independent auditors of the Company are Kesselman & Kesselman Certified Public Accountant. The partner responsible for the internal audit services is Noam Hadar CPA.

The date of being appointed as independent auditor is March 1996.

The following is the independent auditors' fee in NIS (excluding VAT) for services provided in 2016 and 2015 and the number of hours invested:

2016	Fee for audit and tax services	Audit related services	Special tax services	Other services[1]	Total
NIS thousand	646	149	128	125	1,048
Hours	4,738	550	326	622	6,236

2015	Fee for audit and tax services	Audit related services	Special tax services	Other services	Total
NIS thousand	735	149	167	94	1,145
Hours	4,547	550	239	363	5,699

5.4 Effectiveness of internal controls and the procedures over financial reporting and disclosure of the Company

Controls and procedures related to disclosure:
A financial institution management, in cooperation with CEO and CFO of that financial institution assessed as of the end of the reported period the effectiveness of the controls and procedures in relation to the disclosure of the financial institution. Based on this assessment, CEO and CFO of the financial institution concluded that as of the end of that period, the controls and procedures related to disclosure of the financial institution are effective in order to record, process, summarize and report the information that the financial institution is require to disclose in the annual financial statements according to the provisions of the law and the reporting requirements set by the Supervisor of Capital Markets, Insurance and Savings and on the times indicated in such regulations.

Internal control over financial reporting:
During the covered period ended December 31, 2016, no change has occurred in the internal control of the financial institutions over financial reporting that has had a material impact, or is likely to have a material impact on the internal control of the financial institutions over financial reporting.

[1] Other services include translation and consulting services.

5.5 Preparation to implement Solvency II

The following is a disclosure on the preparations made by the Company to implement the Solvency II directive ("**the directive**" or "**Solvency II**").

In April 2016, the Supervisor issued Circular 2016-1-5, whose purpose is to provide instructions for the performance of the 2015 IQIS exercise, including several revisions relative to IQIS4.

IQIS5 is the last quantitative survey before implementation of the new solvency regimen, which is based on the Solvency II directive.

The main revisions in the circular related to stabilization of risk-free interest curves through extrapolation up to the Ultimate Forward Rate, recognized capital composition, lower capital requirement when investing in infrastructures (capital and debt), update of the formula for calculating capital requirement for general insurance premiums and reserves risk, and update of guidelines on special auditor's special report focusing on Best Estimate (BE) and risk margin.

In addition, in September 2016, the Supervisor issued guidelines for disclosure about Solvency II in the financial statements of insurance companies. As part of the disclosure guidance, provisions were set for the purpose of required disclosure in relation to the Solvency II regiment in the financial statements of insurance companies, including, for the purpose of solvency ratios as computed under IQIS5.

According to IQIS 5 results, capital surplus of the Company increased as of December 31, 2015, under the Solvency II regimen relative to capital surplus under the existing Israeli regimen (see a. above). The solvency ratio of the Company as calculated in IQIS 5 using the December 31, 2015 information was 182% before the dividend amounted to ILS 105 million distribution to AEHL and 165% after that payout.

The board of the Company discussed exercise findings in July 2016, and the Company filed the exercise to the Supervisor in August 2016.

In February 2017, the Supervisor issued a circular on the provisions for implementing Solvency II-based regimen. The directive includes a comprehensive examination of risks that insurance companies are exposed to and standards for management and measurement, and is based on three tiers: a quantitative tier, dealing with risk-based solvency; a qualitative tier, concerning internal control processes, risk management, corporate governance and Own Risk and Solvency Assessment (ORSA); and a third tier, concerning promotion of market discipline, disclosure and reporting.

Except for a number of aspects that were adapted to the Israeli market, the provisions of the circular are based, as much as possible, on the quantitative tier of the directive and its accompanying provisions, and that in order to maintain uniformity and allow the Israeli supervisory regimen to be recognize as compatible to that in Europe.

The circular states that an insurance company has to maintain economic solvency according to the provisions of the circular and its appendices, without detracting from the duty to comply with the minimum capital regulations and the Supervisor guidance issued thereunder, and that the Capital Markets, Insurance and Savings Authority will concurrently act to amend the regulations, such that their provisions in relation to minimum required capital will not apply to insurance companies covered by the provisions of the circular, and that after an insurance company obtains certification of the Supervisor for performing an audit of circular compliance in its annual financial statements.

The provisions of the circular will come into effect beginning on June 30, 2017, but insurance companies will be permitted to calculate, until the end of 2018, required solvency capital as of the date of the annual statements only.

In this respect, it is important to note that the provisions of the circular determine, among other things, that the period from June 30, 2017 to December 31, 2021 ("**the deployment period**"), the following provisions will apply in relation to solvency capital requirement (SCR) in the deployment period:

- The solvency capital requirement in the deployment period as of June 30, 2017 may not be less than 60% of the solvency required capital as per the guidance in the appendix to the circular ("SCR");
- The solvency required capital in the deployment period as calculated using data as of December 31, 2017 will be 65% of the SCR;
- The solvency required capital in the deployment period as calculated using data as of December 31, 2018 and data as of June 30, 2019, will be 70% of the SCR;
- The solvency required capital in the deployment period as calculated using data as of December 31, 2019 and data as of June 30, 2020, will be 80% of the SCR;
- The solvency required capital of an insurance company in the deployment period as calculated using data as of December 31, 2020 and data as of June 30, 2021, will be 90% of the SCR.
- The solvency required capital of an insurance company in the deployment period as calculated using data as of December 31, 2021 and thereafter, will not be less than SCR.

AIG Israel Insurance Company Ltd

Shay Feldman	Ralph Mucerino
CEO	Chairman of the Board

March 15, 2016

Chapter B: Directors Report of Company's Business for the Year Ended December 31, 2016

Table of Contents

Chapter B: Directors Report

1. Condensed description of the company

Organizational structure

The company is a private insurance company and does not hold any subsidiaries or related companies. The company has no activities abroad which are conducted through branches and investees

For further details as to the organizational structure of the company, including its holdings structure, its operations and the description of the development of its business – see Section 1.1 in Chapter A (description of company's business) in the company's periodic report.

Lines of business

For details regarding the company's lines of business and changes therein in the course of the reported period, see Section 1.2 and 2.1-2.6 in Chapter A (description of company's business) in the company's periodic report.

For details regarding the composition of premiums in the lines of business, see Section 4 below.

Dependence on clients or marketing entities

For details regarding dependence on clients or marketing entities, see Sections 2.1.3, 2.2.3, 2.3.3, 2.4.3, 2.5.3, 2.6.3, and 4.7 in Chapter A (description of company's business) in the company's periodic report.

Developments or material changes in agreements with reinsurers

For details regarding developments or material changes in agreements with reinsurers see Section 4.5 in Chapter A (description of company's business) in the company's periodic report.

Event or matter outside the ordinary course of company's business

N/A.

Chapter B: Directors Report

2. Description of business environment

Trends in the insurance sector, their effect on company's business in the reported period and on its financial statements data

General

In accordance with data published by the Capital Market, Insurance and Savings Authority, there are more than 15 Israeli insurance companies currently active in Israel; most of these companies are engaged in general insurance. In accordance with these data, as of September 30, 2016, insurance fees arising from the general insurance business amounted to NIS 16,619 million (excluding Karnit); the share of the 5 largest insurance companies – Harel, Clal, Phoenix, Migdal and Menorah – amounted to NIS 9,640 million, which constituted 58% of the total premiums in the Israeli general insurance sectors.

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

Developments in the company's macro-economic environment

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

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

	2016	2015	2014
Government bonds indexes:			
General government bonds	0.9%	1.6%	6.6%
Linked government bonds	0.7%	(0.2%)	5.8%
NIS government bonds	1.2%	2.8%	7.2%
Corporate bonds indexes:			
Tel Bond 60	2.3%	(0.4%)	0.9%
Tel Bond NIS	2.4%	4.7%	4.0%
Shares indexes -			
Tel-Aviv 125 (formerly Tel-Aviv 100)	(2.5%)	2.0%	6.8%

For details regarding the composition of the company's investments see notes 11 and 28 to the financial statements.

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

Chapter B: Directors Report

Characteristics and developments in principal insurance lines of the company

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

The effect of new laws, regulations and provisions on company's business in the reported period and on financial statements data

For details about the effect of the provisions of the law on company's business, Section 4.1 in Chapter A (description of company's business) in the company's periodic report.

Penetration into new fields of operation and marketing thereof

In the course of the reported period, the company did not penetrate into new fields of operations.

3. Financial information regarding the company's lines of business

The following are principal comprehensive income data (in thousands of NIS):

	2016	2015	2014
Gross premiums earned	1,037,400	988,885	923,251
Premiums earned by reinsurers	(168,023)	(160,623)	(149,576)
Premiums earned – retained amount	869,377	828,262	773,675
Investment income, net and financial income	18,475	18,616	49,127
Income from commissions	43,553	37,061	38,427
Total income	931,405	883,939	861,229
Payments and changes in liabilities in respect of insurance contracts – gross	(756,904)	(480,825)	(577,858)
Share of reinsurers in increase in insurance liabilities and payments with respect to insurance contracts	192,796	59,958	148,974
Payments and changes in liabilities in respect of insurance contracts – retained amount	(564,108)	(420,867)	(428,884)
Total other expenses	(320,290)	(319,010)	(301,548)
Income before taxes on income	47,007	144,062	130,797
Taxes on income	(15,833)	(53,971)	(47,894)
Income for the year and total comprehensive income for the year	31,174	90,091	82,903

The following are principal balance sheet data (in thousands of NIS):

	December 31	
	2016	**2015**
Other assets	253,139	233,285
Deferred acquisition expenses	141,827	149,675
Financial investments and cash	1,696,771	1,691,620
Reinsurance assets	658,559	548,150
Total assets	**2,750,296**	**2,622,730**
Shareholders' equity	753,860	827,686
Liabilities in respect of insurance contracts	1,646,765	1,417,989
Other liabilities	**349,671**	**377,055**
Total equity and assets	**2,750,296**	**2,622,730**

Chapter B: Directors Report

Shareholders' equity and capital requirements

As of December 31, 2016, company's shareholders' equity exceeds the shareholders' equity required as of that date under the Minimum Equity Regulations NIS 169.1 million.

For information about an offer to distribute a dividend amounted to NIS 50 million after December 31, 2016 – see note 13c(3) to the financial statements.

To the best of the company's knowledge, as of balance sheet date no events have taken place that might indicate of financial difficulties or a deficiency in minimal required s equity. Also, in the opinion of the company, it will not be required to raise funds in the forthcoming year for the purpose of meeting the minimal equity requirement.

For details on the amounts of capital adequacy required from the company, existing amounts under minimum capital regulations and payment of dividend in the reported period, see note 13 to the financial statements. For information about solvency of the Company as calculated under IQIS5, see section 5.5 chapter A (description of corporate business) in the periodic report.

4. Results of operations

In 2016, the company continued to increase its gross premiums (an increase of 3.3%) compared with gross premiums in 2015. Total gross premiums in the reported period amounted to NIS 1,047 million, compared with NIS 1,013.1 million in 2015.

Total premium in retention in the reported period amounted to NIS 883.7 million, compared to NIS 845.7 million in the corresponding period, a 4.5% increase.

The following are principal data regarding premiums by principal operating segments (in thousands of NIS):

	Vehicle property insurance	Compulsory motor vehicle insurance	Personal property insurance	Health insurance	Commercial insurance	Life insurance	Total
2016							
Gross premiums	314,123	146,084	103,433	219,331	137,810	126,151	1,046,932
Premiums – retained amount	314,008	144,068	88,847	216,295	15,770	104,785	883,773
Total gross as % of total	30.0	14.0	9.9	20.9	13.2	12.0	100.0
Total net as % of total	35.4	16.3	10.1	24.5	1.8	11.9	100.0
2015							
Gross premiums	284,177	146,782	102,246	215,596	141,171	123,116	1,013,088
Premiums – retained amount	284,061	144,731	85,255	213,188	18,414	100,026	845,675
Total gross as % of total	28.0	14.5	10.1	21.3	13.9	12.2	100.0
Total net as % of total	33.6	17.1	10.1	25.2	2.2	11.8	100.0
2014							
Gross premiums	256,572	146,272	104,123	207,778	122,395	115,884	953,024
Premiums – retained amount	256,464	144,232	80,153	202,172	15,818	92,553	791,392
Total gross as % of total	27.0	15.3	10.9	21.8	12.8	12.2	100.0
Total net as % of total	32.5	18.2	10.1	25.5	2.0	11.7	100.0

The following are principal comprehensive income data by principal operating segments (in thousands of NIS):

	2016	2015	2014
Income (loss) from vehicle property insurance	(4,958)	(11,742)	26,643
Income (loss) from compulsory motor vehicle	(18,448)	59,882	17,750
Income from personal property insurance	15,457	9,419	14,479
Loss from commercial insurance	(9,424)	5,795	2,159
Income from health insurance	42,041	58,356	38,783
Income from life insurance	14,086	11,607	4,951
Other – income not charged to insurance segments	8,253	10,745	26,032
Income before taxes	47,007	144,062	130,797
Taxes on income	(15,833)	(53,971)	(47,894)
Income for the year and total comprehensive income for the year	31,174	90,091	82,903

The following are explanations of the development of some of the above presented data:

a. Income before tax in the reported period was NIS 47 million compared to NIS 144.1 million in 2015. The decrease resulted from lower underwriting results of the Company. This decline is fully explained by a significant increase in claim ratios in vehicle compulsory, health and commercial (professional liability) insurance activity.

b. Income from net investment in the reported period was NIS 18.5 million compared to a NIS 18.6 million in 2015. Gains from higher corporate bond yields were offset by lower return on government bond and shares.

c. Loss from property vehicle insurance during the reported period was NIS 5 million, compared to a NIS 11.7 million loss in 2015. The main reason for the losses in 2015 and 2016 is the significant increase in average claim amounts paid. This increase is seen in property vehicle products sold through both direct marketing and agents. As a result of a move to loss in 2015, the Company recorded for the first time in 2015 a reserve for deficient premium at NIS 11.3 million. In 2016, the Company examined in depth the factors that led to this increase in average claim amount and took a number of steps that were available to it in order to reduce the claim ratio. As a result of those efforts, claims ratio seemed to somewhat trend down in 2016, which allowed a release of NIS 8.9 million from the reserve for deficient premiums, which as of December 31, 2016 was NIS 2.5 million.

d. Loss from compulsory vehicle insurance was NIS 18.4 million in the reported period compared to a NIS 59.9 million income in 2015. The decrease in profit was mainly attributed to a significant increase in the claims ratio. The main factors that contributed to this are as follows:

- An increase of liability following the conclusions of the Vinograd Committee (see section 4.1 in Chapter A – description of corporate business – in the periodic report and note 3 to the financial statements) by a gross amount of NIS 32 million and NIS 23.4 million in retention (before tax), including expected future decline in discount interest rate. This increase includes NIS 5.2 million relating to the Company's share in the Pool.
- The reported period is the first in which business results in vehicle compulsory insurance are calculated without the "accumulation". In 2015, the accumulation for underwriting year 2012 was released, at the amount of NIS 40.4 million.
- In 2015, IBNR reserve for closed years decrease significantly.

e. Income from home insurance in the reported period was NIS 15.5 million from NIS 9.4 million in 2015. The increase in income was mainly due to improvement in claims ratio, resulting from absence of significant natural damages, compared to the corresponding period, which was afflicted by natural damages.

f. Loss from professional liability insurance in the reported period was NIS 12 million compared with an income of NIS 3.5 million in 2015. The decrease in income was mainly due to development in the number of claims in directors and officers coverage, and mainly relating to one claim of NIS 7 million in retention. Additionally, in 2015, IBNR reserve decreased significantly.

g. Income from other property lines was NIS 2.3 million during the reported period, compared with a profit of NIS 0.7 million in 2015. The increased profit is mainly due to improved expense ratio, and mainly from an increase in commission income from reinsurers.

h. Income from other liabilities business was NIS 0.3 thousand in the reported period compared with an income of NIS 1.6 million in 2015. The decrease in income was mainly due to an increase in claims ratio.

i. Income from health insurance was NIS 42 million in the reported period compared to a NIS 58.4 million in 2015. The decrease in income is mainly due to improved claims ratio. The lower claims ratio in 2015 was driven by a significant decline in the IBNR reserve.

j. Income from life insurance was NIS 14.1 million in the reported period compared to a NIS 11.6 million income in the 2015. The increase in income was mainly due to an increase in the expense ratio, net of an increase of the claims ratio.

The following are the results of operations in the property insurance lines:

a. **Underwriting profits (in thousands of NIS):**

	2016	2015	2014
Vehicle property	(7,614)	(13,644)	22,527
Home insurance	13,746	7,802	11,626
Other property segments	2,065	576	(208)

b. **Principal data regarding the loss ratio ("LR")[1] and the combined ratio ("CR")**

	2016		2015		2014	
	LR%	CR%	LR%	CR%	LR%	CR%
Property motor vehicles:						
Gross	78%	103%	81%	105%	69%	91%
Retained amount	78%	103%	81%	105%	69%	91%
Home insurance:						
Gross	41%	78%	47%	86%	36%	76%
Retained amount	43%	84%	48%	91%	40%	85%
Other insurance segments:						
Gross	94%	116%	6%	29%	208%	236%
Retained amount	114%	(13%)	118%	67%	212%	119%

c. **Compulsory vehicle insurance**

The "Pool" losses reduced the reported income for 2016 by NIS 13.9 million compared with a decrease of NIS 7.8 million in 2015.

[1] As to gross data, the loss ratio and expenses ratio are computed on the basis of gross premium earned. With regard to retained amounts data, loss ratio and expenses ratio is computed on the basis of premium earned – retained amount.

5. Cash flows and liquidity

Net cash provided by operating activities in 2016 amounted to NIS 204,631 thousand, compared with NIS 34,613 thousand in 2015.

Net cash used in investing activities in 2016 was NIS 23,112 thousand, compared with NIS 19,442 thousand in 2015.

Net cash used for financing activity (a dividend paid) in 2016 was NIS 105,000 thousand compared with NIS 35,000 in 2015.

As a result of the above, the balance of cash and cash equivalents in the reported period increased by NIS 73,991 thousand and amounted to NIS 136,234 thousand as of December 31, 2016.

6. Sources of funding

All of the company's operations are funded using self-resources and equity. The company does not use any external funding sources.

7. The effect of external factors

For details see section 2 above.

8. Material events subsequent to balance sheet date

a) For information about an offer to distribute a dividend – see note 13c(3) to the financial statements.

b) For information about motions to certify class actions against the Company that were filed after December 31, 2016, see note 31a(10-11) to the financial statements.

AIG Israel Insurance Company Ltd
Date: March 21, 2017

Shay Feldman	Ralph Mucerino
CEO	Chairman of the Board

March 21, 2017

AIG Israel Insurance Company Ltd

Declarations relating to the Financial Statements

Declaration

I, Shay Feldman hereby declare that:

1. I reviewed the interim report of AIG Israel Insurance Company Ltd. (hereafter – "the insurance company") for the year ended December 31, 2016 (hereafter – "the report").

2. Based on my knowledge, the report does not include any misstatement of a material fact or omit to disclose a material fact the presentation of which in the report is necessary for the purpose of ensuring that under the circumstances in which those presentations are included, they will not be misleading regarding the period covered by the report.

3. Based on my knowledge, the quarterly financial statements and other financial information included in the report reflect fairly, in all material respects, the financial position, results of operations, changes in shareholders' equity and cash flows of the insurance company for the date and periods covered by the report.

4. The Company's other certifying officers and I are responsible for establishing and maintaining controls and procedures relating to disclosure[1] and internal controls over financial reporting of the insurance company; and -

   (a) Accordingly, we have designed such disclosure controls and procedures, or have had such disclosure controls and procedures established under our charge, designed to ensure that material information relating to the insurance company is made known to us by others in the insurance company particularly during the period in which the reports were prepared;

   (b) We designed internal controls over financial reporting, or supervised the design of such internal controls designed to provide a reasonable assurance regarding the reliability of the financial reporting and assurance to the effect that the financial statements are drawn up in accordance with International Financial Reporting Standards (IFRS) and in accordance with the directives of the Supervisor of Insurance.

   (c) We assessed the effectiveness of controls and procedures regarding the disclosure of the insurance company and presented our conclusions regarding the effectiveness of disclosure controls and procedures as of the end of the period covered in the report, based on our estimate; and

   (d) We disclosed in the report any change in the insurance company's internal controls over financial reporting which took place in this quarter and had a material effect or is expected to have a material effect on the insurance company's internal controls over financial reporting; and

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

5. The insurance company's other certifying officers and I have disclosed to the insurance company's auditors, the insurance company's board of directors and its audit committee, based on our most recent evaluation of internal controls over financial reporting, the following:

   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the insurance company's ability to record, process, summarize and report financial information; and

   b. Any fraud, whether material or not, that involves management or other employees who have a significant role in the insurance company's internal controls over financial reporting.

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

Shay Feldman - CEO

March 21, 2017

Declaration

I, David Rothstein hereby declare that:

1. I reviewed the interim report of AIG Israel Insurance Company Ltd. (hereafter – "the insurance company") for the year ended December 31, 2016 (hereafter – "the report").

2. Based on my knowledge, the report does not include any misstatement of a material fact or omit to disclose a material fact the presentation of which in the report is necessary for the purpose of ensuring that under the circumstances in which those presentations are included, they will not be misleading regarding the period covered by the report.

3. Based on my knowledge, the quarterly financial statements and other financial information included in the report reflect fairly, in all material respects, the financial position, results of operations, changes in shareholders' equity and cash flows of the insurance company for the date and periods covered by the report.

4. The Company's other certifying officers and I are responsible for establishing and maintaining controls and procedures relating to disclosure[1] and internal controls over financial reporting of the insurance company; and -

   (a) Accordingly, we have designed such disclosure controls and procedures, or have had such disclosure controls and procedures established under our charge, designed to ensure that material information relating to the insurance company is made known to us by others in the insurance company particularly during the period in which the reports were prepared;

   (b) We designed internal controls over financial reporting, or supervised the design of such internal controls designed to provide a reasonable assurance regarding the reliability of the financial reporting and assurance to the effect that the financial statements are drawn up in accordance with International Financial Reporting Standards (IFRS) and in accordance with the directives of the Supervisor of Insurance.

   (c) We assessed the effectiveness of controls and procedures regarding the disclosure of the insurance company and presented our conclusions regarding the effectiveness of disclosure controls and procedures as of the end of the period covered in the report, based on our estimate; and

   (d) We disclosed in the report any change in the insurance company's internal controls over financial reporting which took place in this quarter and had a material effect or is expected to have a material effect on the insurance company's internal controls over financial reporting; and

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

5. The insurance company's other certifying officers and I have disclosed to the insurance company's auditors, the insurance company's board of directors and its audit committee, based on our most recent evaluation of internal controls over financial reporting, the following:

   a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the insurance company's ability to record, process, summarize and report financial information; and

   b. Any fraud, whether material or not, that involves management or other employees who have a significant role in the insurance company's internal controls over financial reporting.

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

____

David Rothstein - CFO

March 21, 2017

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

Management, with the supervision of the Board of Directors of AIG Insurance Company Ltd. (hereafter the "the Insurance Company") are responsible for setting and maintaining effective internal control over financial reporting. The internal controls system of the insurance company was planned in order to provide reasonable assurance to management and Board of Directors to the effect that the financial statements are prepared and presented fairly in accordance with International Financial Reporting Standards and in accordance with the directives of the Supervisor of Insurance.
All internal controls have inherent limitations regardless of the quality of planning. Therefore, even if it is determined that these controls are effective they can only provide a reasonable measure of assurance regarding the preparation and presentation of financial statements.

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

The Insurance Company's management with the supervision of its Board of Directors evaluates the effectiveness of the internal control of the Insurance Company over financial reporting as at December 31, 2016, based on criteria set in the internal control model of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation management believes that as at December 31, 2016 the internal control of the Insurance Company over financial reporting is effective.

Chairman of the Board: Mr. Ralph Mucerino ___________________

CEO: Mr. Shay Feldman ___________________

CFO: Mr. David Rothstein ___________________

Date of approval of financial statements: March 21, 2017

Chapter C: Financial Statements

AIG Israel Insurance Company Ltd

This translation is for convenience purposes only.

AIG ISRAEL INSURANCE COMPANY LTD.

2016 ANNUAL REPORT

AIG ISRAEL INSURANCE COMPANY LTD.

2016 ANNUAL REPORT

TABLE OF CONTENTS

AUDITORS' REPORT

To the shareholders of

AIG ISRAEL INSURANCE COMPANY LTD

ON INTERNAL CONTROL OVER FINANCIAL REPORTING

We have audited the internal control over financial reporting of AIG Israel Insurance Company Ltd (hereinafter - the Company) as of December 31, 2016 based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's board of directors and management are responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying directors' report on internal control over financial reporting. Our responsibility is to express opinions on the internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (PCAOB), as adopted by the Institute of Certified Public Accountants in Israel. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating the risk of material weakness, and testing and evaluating the design and operating effectiveness of internal control. Our audit also included performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with International Financial Reporting Standards (IFRS) and the disclosure requirements in the Supervision of Financial Services Law (Insurance), 1981 and the regulations thereunder. Internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with International Financial Reporting Standards (IFRS) and the disclosure requirements set by the Supervisor pursuant to the Supervision of Financial Services Law (Insurance), 1981 and the regulations thereunder, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control — Integrated Framework issued by the COSO.

We have also audited, in accordance with generally accepted financial principles, the financial statements of the Company as of December 31, 2016 and 2015, and for each of the three year in the period ended December 31, 2016, and our report, dated March 21, 2017, included an unqualified opinion on those financial statements.

Tel Aviv, Israel
March 21, 2017

Kesselman & Kesselman
Certified Public Accountants
Member of PricewaterhouseCoopers International Limited

AUDITORS' REPORT

To the shareholders of

AIG ISRAEL INSURANCE COMPANY LTD.

We have audited the attached statements of financial position of AIG Israel Insurance Company Ltd. ("the Company") as of December 31, 2016 and 2015 and the statements of comprehensive income, changes in equity and cash flows for each of the three-year period ended December 31, 2016. 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 (IFRS) and the disclosure requirements set by the Supervisor pursuant to the Supervision of Financial Services (Insurance) Law, 1981 and the regulations promulgated thereunder, the financial position of the Company as of December 31, 2016 and 2015 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, 2016.

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, 2016, 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 21, 2017 expressed an unqualified opinion on the Company's effectiveness of internal control over financial reporting.

Tel-Aviv, Israel
March 21, 2017

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

Kesselman & Kesselman, Trade Tower, 25 Hamered Street, Tel-Aviv 6812508, Israel,
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AIG ISRAEL INSURANCE COMPANY LTD.

STATEMENTS OF FINANCIAL POSITION

	Note	December 31 2016	December 31 2015
		ILS in thousands	
Assets			
Intangible assets	6	33,816	26,397
Deferred acquisition costs	7	141,827	149,675
Fixed assets	8	11,435	11,469
Reinsurance assets	14, 29	658,559	548,150
Premiums collectible	10	153,534	* 148,698
Current tax assets		1,864	3,250
Other receivables	9	52,490	43,471
		1,053,525	931,110
Financial investments:	11		
Marketable debt instruments		1,310,175	1,200,998
Non-marketable debt instruments		171,285	* 262,104
Marketable shares		-	92,851
Other		79,077	73,424
TOTAL FINANCIAL INVESTMENTS		1,560,537	1,629,377
Cash and cash equivalents	12	136,234	62,243
TOTAL ASSETS		2,750,296	2,622,730

* After reclassification, see note 2u

Ralph Mucerino	**Shay Feldman**	**David Rothstein**
Chairman of the Board	**C.E.O**	**C.F.O**

Date of approval of financial statements by Board of Directors March 21, 2017.

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

AIG ISRAEL INSURANCE COMPANY LTD.

STATEMENT OF FINANCIAL POSITION

	Note	December 31 2016	December 31 2015
		ILS in thousands	
Equity and liabilities			
EQUITY:	13		
Share capital		6	6
Share premium		250,601	250,601
Other capital reserves		11,084	11,084
Retained earnings		492,169	565,995
TOTAL EQUITY ATTRIBUTABLE TO COMPANY SHAREHOLDERS		753,860	827,686
LIABILITIES:			
Liabilities with respect to insurance contracts and investment contracts that are not yield dependent	14	1,646,765	1,417,989
Liabilities with respect to deferred taxes, net	19	779	8,141
Liabilities with respect to employee rights upon retirement, net		2,713	2,781
Liabilities towards reinsurers	30	257,165	279,347
Payables	20	89,014	86,786
TOTAL LIABILITIES		1,996,436	1,795,044
TOTAL EQUITY AND LIABILITIES		2,750,296	2,622,730

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

AIG ISRAEL INSURANCE COMPANY LTD.

STATEMENT OF COMPREHENSIVE INCOME

	Note	2016	2015	2014
		Year ended December 31		
		ILS in thousands		
Gross premiums earned	21	1,037,400	988,885	923,251
Premiums earned by reinsurers		(168,023)	(160,623)	(149,576)
Premiums earned - retained amount	21	869,377	828,262	773,675
Investment income, net and financing income	22	18,475	18,616	49,127
Commission income	23	43,553	37,061	38,427
TOTAL INCOME		931,405	883,939	861,229
Payments and changes in liabilities with respect to insurance contracts, gross		(756,904)	(480,825)	(577,858)
Share of reinsurers in increase in insurance liabilities and payments with respect to insurance contracts		192,796	59,958	148,974
Payments and changes in liabilities with respect to insurance contracts, in retention	24	(564,108)	(420,867)	(428,884)
Commission, marketing expenses and other acquisition costs	25	(242,330)	(239,888)	(230,090)
General and administrative expenses	26	(81,370)	(82,884)	(76,971)
Financing income	27	3,410	3,762	5,513
TOTAL EXPENSES		(884,398)	(739,877)	(730,432)
INCOME BEFORE TAXES ON INCOME		47,007	144,062	130,797
Taxes on income	19	(15,833)	(53,971)	(47,894)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		31,174	90,091	82,903
BASIC EARNINGS PER SHARE:				
Basic earnings per share		5.44	15.72	14.47
Number of shares used in computation of basic earnings per share		5,730	5,730	5,730

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

AIG ISRAEL INSURANCE COMPANY LTD.

STATEMENT OF CHANGES IN EQUITY

	Share capital	Share premium	Other reserves	Retained earnings	Total
	ILS in thousands				
BALANCE AS OF JANUARY 1, 2016	6	250,601	11,084	565,995	827,686
Total comprehensive income for the period				31,174	31,174
Dividend (see note 13c(4))				(105,000)	(105,000)
BALANCE AS OF DECEMBER 31, 2016	6	250,601	11,084	492,169	753,860
BALANCE AS OF JANUARY 1, 2015	6	250,601	11,084	429,216	690,907
Net aggregate impact, as of December 31, 2015, of the accumulation and first-time implementation of the "best practice" (see note 2r (d) (5))				81,688	81,688
Total comprehensive income for the period				90,091	90,091
Dividend (see note 13c(5))				(35,000)	(35,000)
BALANCE AS OF DECEMBER 31, 2015	6	250,601	11,084	565,995	827,686
BALANCE AS OF JANUARY 1, 2014	6	250,601	11,084	381,313	643,004
Total comprehensive income for the period				82,903	82,903
Dividend (see note 13c(6))				(35,000)	(35,000)
BALANCE AS OF DECEMBER 31, 2014	6	250,601	11,084	429,216	690,907

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

AIG ISRAEL INSURANCE COMPANY LTD.

STATEMENT OF CASH FLOWS

	Year ended December 31		
	2016	2015	2014
	ILS in thousands		
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net cash provided by operating (Appendix A)	184,682	10,261	96,078
Interest received	41,449	44,813	45,484
Dividend received	259	2,480	2,337
Income taxes paid	(21,759)	(22,941)	(78,334)
Net cash provided by operating activities	204,631	34,613	65,565
CASH FLOWS FROM INVESTING ACTIVITIES:			
Investment in property and equipment	(6,396)	(6,019)	(1,769)
Investment intangible assets	(16,716)	(13,423)	(12,218)
Net cash used in investing activities	(23,112)	(19,442)	(13,987)
CASH FLOWS FROM FINANCING ACTIVITIES - dividend paid by Company shareholders	(105,000)	(35,000)	(35,000)
Net cash used in financing activities	(105,000)	(35,000)	(35,000)
EFFECT OF CHANGES IN EXCHANGE RATE ON CASH AND CASH EQUIVALENTS	(2,528)	(1,015)	(1,107)
INCREASE (DECREASE) OF CASH AND CASH EQUIVALENTS	73,991	(20,844)	15,471
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	62,243	83,087	67,616
CASH AND CASH EQUIVALENTS AT END OF YEAR	136,234	62,243	83,087

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

AIG ISRAEL INSURANCE COMPANY LTD.

STATEMENTS OF CASH FLOWS

	Year ended December 31		
	2016	2015	2014
	ILS in thousands		
APPENDIX A - CASH FLOWS FROM OPERATING:			
Income before taxes on income	47,007	144,062	130,797
Adjustments with respect to:			
Items not involving cash flows:			
Change in liability with respect to insurance contracts that are not yield dependent	228,776	(134,592)	145,539
Change in Reinsurance assets	(110,409)	139,009	(71,305)
Change in deferred acquisition costs	7,848	(1,461)	(7,694)
Change in liability for employee rights upon retirement, net	(68)	(288)	624
Depreciation of Fixed assets	6,430	5,213	6,354
Depreciation of intangible assets	9,297	7,436	6,607
Losses (gains), net on financial investments:			
Marketable debt instruments	17,594	26,506	4,057
Non marketable debt instruments	3,094	* 9,853	* (5,504)
Marketable shares	4,162	(825)	(3,313)
Marketable index linked certificates	(3,456)	(329)	(675)
Influence of fluctuation in exchange rate on cash and cash equivalents	2,528	1,015	1,107
	165,796	51,537	75,797
Changes in asset and liability items:			
Liabilities towards reinsurers	(22,182)	(1,251)	24,413
Investments in financial assets net	47,446	(110,236)	(85,158)
Premiums collectible	(4,836)	* (16,229)	* (4,944)
Receivables	(9,019)	(3,322)	(1,106)
Payables	2,228	(6,118)	4,100
Current tax assets	(50)	(889)	-
	13,587	(138,045)	(62,695)
ADJUSTMENTS WITH RESPECT TO INTEREST AND DIVIDEND:			
Interest received	(41,449)	(44,813)	(45,484)
Dividend received	(259)	(2,480)	(2,337)
	(41,708)	(47,293)	(47,821)
Net cash provided by operations	184,682	10,261	96,078

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

* After reclassification, see note 2u.

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 does not hold any subsidiaries or related companies. The Company has no foreign operations through branches or investees.

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

On June 1, 2016, as part of restructuring of the AIG Global Corporation, all shares of the Company owned by AIG Europe Holdings Limited ("AEHL") were transferred to the ownership of AIG Holding Europe Limited ("AHEL"). As of the date of approving these financial statements, the sole shareholder of the Company is AHEL, which holds the entire issued and paid up share capital of the Company. AHEL is a company in the AIG Global Corporation.

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

Definitions:

1) The Company – AIG Israel Insurance Company Ltd.

2) The parent company – AIG Holdings Europe Limited

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

4) The Supervision Law – The Supervision of Financial Services (Insurance) Law, 1981.

5) Investment contracts – policies which do not constitute insurance contracts.

6) Reinsurance assets – the reinsurer's share in the reserves for insurance contracts and in the contingent claims.

7) CPI - The Consumer Price index published by the Israeli Central Bureau of Statistics.

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

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

10) Interested party - as defined in the Israeli Securities (Annual Financial Statements) Regulations, 2010.

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

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

13) Outstanding claims - Known outstanding claims, with the addition of the expected progression of claims that have been incurred but not enough reported (I.B.N.E.R.) plus claims that have been Incurred but not reported (I.B.N.R).

NOTE 1 - GENERAL (continued):

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

15) The Investment Regulations – The Supervision of Financial Services (Provident Funds) (Investment Rules Applicable to Financial Institutions) Regulations, 2012.

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

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

18) Regulations for Calculation of General Insurance Funds - The Supervision of Insurance Businesses Regulations (Method of Calculation of Provisions for Future Claims in General Insurance), 1984 as amended.

19) Exposure to reinsurers - Debit balances with the company's reinsurers, including the reinsurer's share in the company's outstanding claims and unexpired risks fund, all being net of the reinsurer's deposits with the company, and amounts of letters of credit given against the liability of a reinsurer.

20) Insurance contract - A contract under which one party (the insurer) takes a significant insurance risk from another party (policy holder), by agreement to indemnify the policy holder if an uncertain a defined future event (insurance event) negatively affects the policy holder.

21) Liability for insurance contracts - Insurance reserves and outstanding claims.

22) Premium - Premium including fees and proceeds for auxiliary services.

23) Premiums earned - premiums that relate to the reporting period.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES:

a. Basis of presentation of financial statements

The Company's financial statements as of December 31, 2016 and 2015 and for each of the three years in the period ended December 31, 2016, 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.

In connection with the presentation of these financial statements, the following should be indicated:

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

2) The financial statements have been prepared under the historical cost convention subject to such adjustments as were required with respect to the revaluation of severance pay plan assets and financial assets at fair value through profit or loss for the purpose of presenting those assets and liabilities at fair value.

3) 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 4 below.

b. Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker in the Group who is responsible for allocating resources and assessing performance of the operating segments.

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)**:**

The table below sets out the changes in the exchange rate of the U.S. dollar ("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, 2016	(1.5)	(0.3)	(0.2)
Year ended December 31, 2015	0.3	(0.9)	(1.0)

As of December 31, 2016, the exchange rate of the U.S. dollar was $1 = ILS 3.845.

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 is presented in comprehensive income under "financing income".

d. Fixed assets

Fixed assets 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 Fixed assets 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.

Fixed assets 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.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

d. Fixed assets (continued):

Write-downs and impairments of value relating to Fixed assets presented at cost are charged to the statement of comprehensive income.

Depreciation is computed by means of the straight-line 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 comparing the carrying amount of the asset and the consideration received for the asset; these gains and losses are recognized in other income or loss.

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 straight-line 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.

Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the company which meet the conditions for recognizing intangible assets as specified below are recognized as intangible assets. Those costs include the software development employee costs and an appropriate portion of the relevant overheads.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

e. Intangible assets (software) (continued)**:**

Expenditure on software development (see below) shall be capitalized as intangible assets when the following conditions are met:

- The technical feasibility of completing the intangible asset so that it will be available for use exists;
- Management intends to complete the intangible asset and use or sell it;
- It would be possible to use or sell the intangible asset;
- The way the intangible asset will generate probable future economic benefits is demonstrable;
- The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
- The ability of management to measure reliably the expenditure attributable to the intangible asset during its development.

Other software development costs that do not meet the above criteria are recognized as cost as incurred. Software development costs previously recognized as an expense are not recognized as an asset on a subsequent period. Capitalized development costs are presented as intangible assets and amortized as from the time the asset is available for use, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by management in accordance with the straight-line method and over its useful live (which does not exceed 5 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 (cash generating 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 previously recognized 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.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

g. Financial assets (continued)**:**

b) Loans and receivables

Loans and receivables are non-derivative 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 profit 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 11.

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):

g. Financial assets (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.

Objective evidence of impairment or a financial asset or a group of financial assets may include observable data that were brought to the attention of the group regarding loss events such as indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization, and where observable data indicate that there is a measurable decrease in the estimated future cash flows and other indications.

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 held to maturity 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.

h. Premiums collectible

The balance of collectible premiums relates to amounts receivable from the company's insureds for insurance policies granted in the ordinary course of business.

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 impairment of accounts receivables. A provision for impairment of accounts receivables 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. For more information about criteria that the Company is using to determine whether such objective evidence exists – see g(4) above. 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 impairment of accounts receivables. Reversal of previously write offs in a subsequent period is credited to the statement of income.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

i. Cash and cash equivalents

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

j. Share capital

Ordinary shares of the company are classified as share capital.

k. Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less.

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.

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.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

m. Current and deferred taxes (continued)

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

A defined contribution plan is a pension plan under which the company pays fixed contributions into a separate entity. The company has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

A defined benefit plan is a pension plan that is not a defined contribution plan.

The company operates various pension schemes. The schemes are generally funded through payments to insurance companies or trustee-administered pension funds. In accordance with their terms, the said pension schemes qualify as defined contribution plans.

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):

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, using a discount rate that is based on the yield curve of corporate bonds, as published by the quoting company Mirvach Hogen.

With respect to the remainder of its employees who are covered by a defined contribution plan. The contributions are recognized as employee benefit expense commensurate with receipt from employees of the service in respect of which they are entitled for the contributions. Prepaid contributions are recognized as an asset to the extent that a refund of the excess amounts or a reduction in the future payments is available.

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.

The company expects that the vacation benefit shall be fully settled in the course of the 24 months period after the end of the reporting period in which the employees provide the relating services. Accordingly, the liability in respect of this benefit is measured in accordance with the additional amount the company expects to be required to pay for the unutilized entitlement accrued as of the end of the reporting period.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

n. Employee benefits (continued):

3) 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.

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 insurance 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 received for policies that commence after balance sheet date are recorded as prepaid premiums within other payables.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

p. Revenue recognition (continued):

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, and include payments for related services (towing, repairs etc.).

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 (which may also be in the form of clearing the debt and transferring it to a credit card company) since coverage is conditioned on paying the premium.

2) Income from commissions

Income from commissions received from reinsurers are charged on the basis of the dates of entitlement to receive the commissions under the agreements, net of change in deferred purchase expenses in respect of reinsurers.

3) Income from investments, net and financing income:

Gains and losses from net investments and finance income include interest income in respect of amounts invested, dividend income, changes in the fair value of financial assets at fair value through profit or loss and gains and losses from exchange differences on assets. Interest income is recognized when they arise using the effective interest method. Dividend income is recognized when the right to receive payment is established. If dividend is received in respect of marketable shares, the company recognizes this income on the Ex dividend day.

q. General and administrative expenses

General and administrative expenses are classified into overheads to settle claims (which are included in the "payments and movement in liabilities with respect to insurance contracts, gross"), into acquisition related expenses (included under "commission, marketing expenses and other acquisition costs") and into a balance of other general and administrative costs included in this item.

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.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts (continued):

The significant accounting policies and methods of computation relating to general insurance business and life insurance business used in the preparation of these financial statements were as follows:

1) General insurance:

a) As to revenue recognition, see p above.

b) The payments and changes in liabilities with respect to insurance contracts gross and retained amount item include, among other things, settlement and direct handling costs of claims paid and indirect expenses to settle outstanding claims, as well as an adjustment of the provision for pending claims (including a provision for direct costs and overheads to settle claims) recorded in previous years.

c) Liabilities for insurance contracts and deferred acquisition costs

Insurance reserves and pending claims included in liabilities in respect of insurance contracts, and the reinsurers' share in the reserve and in the pending claims under reinsurance assets, are computed in accordance with the Control of Financial Services Regulations (Insurance) (Calculation of General Insurance Reserves), 2013 ("the Calculation of Reserves Regulations), the Supervisor's directives, and standard actuarial methods for computing pending claims, which are applied according to the chief actuary's discretion. As from December 31, 2015, the "best practice" was implemented for the first-time, as discussed in (d)(5) above.

d) Liabilities for insurance contracts composed of insurance reserves and pending claims, as follows:

1) The unearned premium reserve reflects the insurance premium for the insurance period subsequent to the balance sheet date.

2) Provision for premium deficiency is recognized if the unearned premium (less deferred acquisition costs) does not cover the expected cost for insurance contracts on the basis of actuarial valuations.

3) Insurance reserves and pending claims:

a. In accordance with the instructions of the Supervisor, the pending claims reflected in the financial statements in relation to the general insurance sector are valued by an actuary, Mr. Ernst Segal, who has reported that she has valued the pending claims in accordance with the provisions of the supervision law, the instructions of the Supervisor, and generally accepted 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.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts (continued):

b. In sectors and claim types where is no statistical significance, IBNR and IBNER provisions have been computed on an actuarial basis. The use of actuarial methods that rely on the claim development is most suitable when stable and sufficient information is available on claim payments and/or individual estimates of the expected total claim cost. When information available from claim experience is insufficient, the actual may sometimes use a calculation that weighs between a known estimate (of the company and/or sector), such as loss ratio, and actual claim development. Greater weight is given to estimations that are based on experience, as time passes and additional claim information is accumulated.

In January 2015, Supervisor Position "Best Practice for Calculation of General Insurance Reserves for Financial Reporting" (hereinafter - "the best practice"). The position of the Supervisor includes, among other things, explanations to several principles: professionalism, consistency, and care, which were not previously defined by the actuarial appraisal circular. The principle of care requires from an actuary to examine that it is fairly likely that reserves in retention is sufficient to cover liabilities of the insurer. For compulsory vehicle and liability insurance, the "fairly likely" test will be a probability of at least 75%. In addition, the Supervisor position also refers to the discount rate of liability flow for optimal estimation. The Supervisor position applies to the financial statements as of December 31, 2015 and thereafter.

c. Provision for overheads to settle pending claims - in accordance with the provisions of IFRS 4, the provisions for pending claims also incorporate a provision for overheads to settle claims.

4) Excess of income over expenses

Through December 31, 2015 – the date of first-time implementation of the "best practice" (see 5. Above), liabilities in compulsory vehicle and liabilities sectors had been calculated in accordance with the "excess of revenue over expenses method", as follows:

Compulsory motor vehicle and other liability sectors – the excess of income over expenses net of provision for pending claims (hereafter – "the accumulation") was not recognized as income before the end of the third year commencing with the year in which the policies were issued; the accumulation was computed in the manner prescribed by the regulations and circulars of the Supervisor.

The accumulation was calculated in accordance with the Calculation of Reserves Regulations and in accordance with the directives of the Supervisor, on the basis of revenue from premiums net of acquisition costs and claims plus investment income at a fixed annual real rate of 3%, without reference to the actual returns obtained, net of reinsurers' share in accordance with the insurance sectors and the relating underwriting year. The accumulation accrued until its release from the year insurance started, as calculated above, was included in liabilities in respect of insurance contracts and the deficit is recognized as an expense.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts (continued):

In accordance with instructions received from the Supervisor, if, in any particular sector, the balance of the accumulation before the share thereof attributable to reinsurers was 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 was reflected in the balance sheet under 'liabilities with respect to insurance contracts and nonprofit participating investment contracts' instead of under 'reinsurance assets.

5) Elimination of the accumulation and implementation of the "best practice" on the calculation of insurance reserves in general insurance, which are implemented for the first-time in the 2015 financial statements:

In January 2013, Supervision of Financial Services (Insurance) (Calculation of Insurance Reserves in General Insurance), 2013 were issued (hereinafter – "the new regulations") and a circular that was revised in January 2015 (hereinafter, together - "the amendment"), which are designed to amend current statutory provisions on calculation of insurance reserves in general insurance.

The amendment replaces Supervision of Insurance Business Regulations (Mode of Calculation of Future Claims in General Insurance), 1984. The key change implemented when the amendment came into effect is that it eliminated the accumulated beginning in the financial statements as of December 31, 2015.

In addition, as a complementary step to this change, a Supervisor position was published in January 2015, which presents to actuaries a best practice for calculation of insurance reserves in general insurance for the purpose of the financial statements to adequately and appropriately reflect insurance liabilities (hereinafter - the best practice). The best practice includes, among other things, reference to the following topics:

1. "Prudence" refers, in the context of reserves calculated by an actuary, is that "the reserve is adequate for covering liabilities of the insurer". That is, there is a fairly reasonable likelihood that the reserve in retention will be sufficient to cover liabilities of the insurer. As to outstanding claims in compulsory vehicle and liabilities insurance, the "very likely" test will be a probability of at least 75%. However, to the extent that there are limitations in the statistical analysis, the actuary needs to exercise judgment, and may use generally accepted actuary methods.

2. Refers to the discount rate for liabilities.

3. Sector aggregation – for the principle of prudence in non-aggregated sectors (as defined in the circular – statistical sectors), each sector must be considered separately, but all underwriting (or damages) years in a particular sector can be aggregated. Aggregated (non-statistical) sectors can be considered together.

4. Determination of the size of reserve for policies sold shortly before balance sheet date and risks after balance sheet date.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts (continued):

The company implemented the amendment for the first time together with the best practice as of December 31, 2015. According to the provisions of IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors", this change is a change in accounting policy. In this regards, IAS 8 states that a change in accounting policy will be implemented retroactively unless it is impractical to determine the specific impact for a certain period or the accumulated impact of the change. Since in this case, retrospective implementation of the change in accounting policy is impractical, the impact of the change was recognized (net of tax) as adjustment to accounting balance as of December 31, 2015, with no retrospective application. Implementation of that change resulted in a net increase of ILS 81,688 thousand reserve balance as of December 31, 2015 (total pre-tax impact, ILS 130,868 thousand).

6) The Company's management believes that the pending claims are sufficient, given that the pending claims are calculated mainly on an actuarial basis and their balance includes appropriate provisions required for IBNR.

e) 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 costs. 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.

f) 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.

g) 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.

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

2) Life insurance:

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

b) As to revenue recognition, see p above.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. Insurance contracts (continued):

c) Life insurance reserves, the portion of those reserves attributable to reinsurers, and deferred acquisition costs have been computed by the Company's actuary, Ms. Dafna Kaufman (December 31, 2015 – Ms. Michal Burger), who has declared 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. For more information about the actuarial methods used to calculate the insurance liabilities, see section e1 to note 28e1.

d) Deferred acquisition costs:

1) In accordance with the provisions of the 'details of report' regulations, the deferred acquisition costs of new life insurance policies (hereafter- "DAC") 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 15 years and the period of the policy.

2) The Company's actuary assesses the recoverability of the DAC every year in order to verify that the liabilities for insurance policies, net of the DAC for policies sold since 1999 is sufficient, and that the policies are expected to generate future income to cover the DAC deduction and the insurance liabilities, operating expenses and commissions in respect of those policies. If necessary, a special reduction is recognized such that the amount of DAC does not exceed the amount coverable by future revenue. According to the Company's actuary declarations, deferred acquisition expenses for policies that were recognized as an asset in the accounts of the Company, can be covered by future.

The assumptions used in this assessment include assumptions regarding cancellations, operating expenses, yield on assets, mortality and morbidity rates, which are determined by the Company's actuary on an annual basis based on past experience and the relevant latest surveys known to the Company as of the date of calculation.

e) Liability adequacy testing for life insurance contracts

The Company tests the adequacy of the liabilities arising from life insurance contracts. If the test indicates that the premiums received are not sufficient to cover the expected claims, a special reserve is recorded for the deficiency. The test is made at the level of each product.

The assumptions used in the above mentioned tests include assumptions regarding cancellations, operating expenses, yield on assets, mortality rates and morbidity rates; the assumptions are set by the actuary every year based on past experience and other relevant studies.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

r. **Insurance contracts** (continued):

3) Health insurance:

a) As to revenue recognition, see p. above.

b) Liabilities in respect of health insurance contracts

As prescribed by the directives of the Supervisor, pending claims included in the financial statements in respect of health insurance are evaluated by the actuary – Mr. Ernst Segal – who declared that she evaluated the pending claims in accordance with Supervision Law, the instructions and directives issued by the Supervisor and acceptable actuarial principles. Ms. Koler declared that to the best of her knowledge and assessment, the reserve for pending claims forms an adequate reserve for covering the insurer's commitments in respect of its liability arising from the said sectors of insurance, both aggregately and separately at their value as of the date of the financial statements. The actuary's valuations apply to gross and retention amounts.

The provisions for pending claims, the direct expenses and overheads arising there from as well as provisions for IBNR were included in the "liabilities in respect of insurance contracts" item.

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. **Dividend distribution**

The distribution of dividends to the Company's shareholders is recognized as a liability in the statement of financial position in the period during which the Company's board of directors approved the distribution of thereof.

u. **Reclassification**

As part of the statement of financial position of the Company as of December 31, 2015, whose information is presented in these financial statements as comparative information, a ILS 58,169 reclassification was performed in balances receivables from credit card companies in relation to amounts receivable on compulsory vehicle policies sold to Company customers. Those amounts were reclassified from "premium for collection" to "non-marketable debt assets". This reclassification is immaterial to the financial statements of the Company.

v. **Change in accounting policy due to changes in regulations and Supervisor directives on calculation of general insurance reserves**

As to changes in accounting policies relating to the elimination of the accumulation and implementing the "best practice" for the calculation of general insurance reserves, which was implemented for the first time in the financial statements as of December 31, 2015 – see r(1)(d)(5) above.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

w. New standards, amendments and interpretations of existing standards, which are effective and mandatory for reporting period beginning on January 1, 2016:

Amendment to IAS 1 – "Presentation of Financial Statements" (hereafter – "amendment to IAS 1")

The amendment to IAS 1 deals with the following issues: materiality and the impact thereof on the disclosures provided in the financial statements, presentation of subtotals, order of presentation of the notes to the financial statements and disclosure of accounting policies.

According to the transition provisions of the amendment to IAS 1, an entity applying the amendment are not required to present disclosures under IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors" relating to application of a new standard or accounting policy.

The adopted the amendment to IAS 1. The first-time adoption of the amendment to IAS 1 had no material impact on the financial statements of the Company.

x. New standards, amendments and interpretations of existing standards, which have not yet become effective and not been early adopted by the Company:

1) Amendment to IFRS 9 – " Financial Instruments" (hereafter – "IFRS 9" or "the standard")

IFRS 9, 'Financial instruments', addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in July 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortized cost, fair value through OCI and fair value through P&L. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI not recycling.

There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. The new impairment model establishes a three stage approach, based on changes in expected credit risk of a financial instrument. Each stage determines how to measure credit losses and how to apply the effective interest method. In addition, for financial assets that have no material financing element, such as receivables, it is possible to implement a simpler method. At initial recognition of a financial asset, an entity recognises a loss allowance equal to 12 months expected credit losses.

For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through other comprehensive income.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

x. New standards, amendments and interpretations of existing standards, which have not yet become effective and not been early adopted by the Company (continued):

IFRS 9 simplifies the requirements for testing hedge effectiveness by dropping the strict quantitative thresholds for testing hedge effectiveness. IFRS 9 requires economic relationship between the underlying hedged risk component and the hedging instrument, and that the hedge ratio is the same used for risk management purposes. The standard retains the requirement for maintaining documentation throughout the hedge period, but documentation is different than that required by IAS 39.

IFRS 9 was applied retrospectively for annual reporting periods beginning on or after January 1, 2018. Early adoption is permitted.

The Company has yet to complete examining the expected impact of IFRS 9 on its financial statements, but according to its present assessment, except for a certain one-off increase that may result in the provision for credit losses, the adoption of IFRS 9 is not expected to have material impact on the financial statements.

2) IFRS 16 "Leases"

IFRS 16 will replace upon first-time implementation the existing guidance in IAS 17 - "Leases". IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases, and is expected to have material impact mainly on the accounting applied by the lessee-side of a lease transaction.

IFRS 16 changes the existing guidance in IAS 17 and require lessees to recognize a lease liability that reflects future lease payments and a "right-of-use asset" in all lease contracts (except for the following), with no distinction between financing and capital leases. IFRS 16 exempts lessees in short-term leases or the when underlying asset has a low value.

For lessors, the guidance in IFRS 16 remains almost unchanged from IAS 17, and lessors will continue to classify leases as operating or financing leases, similarly to the rules in IAS 17.

IFRS 16 changes the definition of a "lease" and whether a contract contains a lease.

IFRS 16 will be effective retrospectively for annual periods beginning on or after January 1, 2019, except as otherwise is prescribed by transitional provisions. Under the provisions of IFRS 16, early adoption is permitted subject to meeting certain conditions. The Company is assessing the expected impact of IFRS 16 on the financial statements. However, according to its present assessment, most of its impact will be reflected in the initial recognition of assets relating to usage rights against lease liabilities, and that that in respect to the operating lease of the Company (mainly leasing the office building and vehicle it is using).

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

x. **New standards, amendments and interpretations of existing standards, which have not yet become effective and not been early adopted by the Company** (continued):

3) Amendment to IAS 12 "Income Taxes" (hereinafter - Amendment to IAS 12)

The Amendment to IAS 12 clarifies the existing guidance in the standard, and does not change it core principles.
The Amendment to IAS 12 clarifies the recognition of deferred tax assets for unrealised losses related to debt instruments measured at fair value, such that the carrying amount of the asset is below its tax base. The Amendment to IAs 12 clarifies especially the following:

- A deductible temporary difference arises if the tax base of the asset exceeds its carrying amount at the end of the reported period.
- As part of examining the existence of future taxable income against which the deferred tax asset can be utilized, an entity needs to assume that it will be able to recover from the asset an amount that exceeds its carrying amount.
- When an entity assesses whether taxable profits will be available against which it can utilise a deductible temporary difference, it considers whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference.

The amendment will apply to annual periods beginning on or after January 1, 2017. According to the provisions of the amendment, early adoption is permitted. The initial application of the Amendment to IAS 12 is not expected to have material impact on the financial statements of the Company.

NOTE 3 - IMPLICATIONS OF THE VINOGRAD COMMITTEE RECOMMENDATIONS

On June 8, 2014, the Vinograd Committee was appointed, with the mandate to examine whether the data used by the Israel National Insurance Institute (NII) to calculate benefits for workplace injuries are up-to-date, and whether modifications are needed in life expectancy tables and interest rates used in discounting NII workplace injury benefits. Recommendations of the committee were published in March 2016, and they include, among other things, recommendations for the amendment of National Insurance Regulations (Discounting), 1978 (hereinafter - the discounting regulations) in relation to updating payments according to the current, higher, life expectancy and discounting one-off payments based on a 4-year average in a way detailed in the recommendations, whereas, as long as no such determination is set, interest rate will be set to 2% instead of 3% as indicated by the regulations so far, and that on the backdrop of lower recent interest rates.

On May 17, 2016, the Amendment to the Discounting Regulations (hereafter – "the Amendment to the Discounting Regulations") was signed by the Minister of Social Affairs, and on June 9, 2016, the Amendment to the Discounting Regulations was published in the official gazette, adopting the recommendations of the Vinograd Committee.

On September 13, 2016, an amendment to the Amendment of the Discounting Regulations was published in the official gazette, postponing the coming into effect of the Amendment to the Discounting Regulations to September 2017. The Amendment to the Discounting Regulations may result with a decrease in the rate of the discounting interest used in the settlement of bodily damage claims, which may lead to an increase in the premiums of compulsory vehicle insurance.

As of December 31, 2016, management estimated that the Amendment to the Discounting Regulations is expected to increase the amounts, which the Company will be required to pay in settlement of insurance contracts of the Company in the vehicle compulsory sector, by a total of ILS 18.1 million pre-tax, (approx. ILS 6.6 million in retention before tax in the last quarter of 2016). This amount is estimated based on an updated estimation of management that the discount interest rate, as above, will be 2% per year over the period until 2019 (inclusive), and that beginning in 2020, the discount interest rate will be lowered to about 1% per year. In addition, the Company's share of the Pool's liabilities resulting from the effects of the Amendment to the Discounting Regulations as of the said date, is ILS 5.2 million pre-tax (ILS 1.7 million in retention before tax in the last quarter of 2016). Accordingly, insurance liability were increased as of that date.

The impact on other segments is totally negligible.

Management believes, based on the opinion of its legal counsel, that the courts may not necessarily adopt the discount interest rate set by the discounting regulations of National Insurance in bodily injury liability cases, and as such, the Company made an estimate of possible impact according to its estimation of such impact.

Note that, in light of the above, there is uncertainty, at this stage, regarding the impact of the Amendment to the discounting regulations on liabilities of the Company, and therefore, it is possible that future claims will unfold significantly differently than Company estimates, and that the Company will later be required to update its estimates.

NOTE 4 - SIGNIFICANT ACCOUNTING ESTIMATES AND AREAS OF DISCRETION

Estimates and judgments are subject are constantly tested, and are based on past experience and other 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:

a. 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 forecasts affect the final level of the provision for insurance liabilities.

NOTE 4 - SIGNIFICANT ACCOUNTING ESTIMATES AND AREAS OF DISCRETION (continued)

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 gross insurance liabilities would have been higher or lower by app. ILS 126 million.

b. Provisions for lawsuits

Several legal claims and applications to approve claims as class actions are pending against the company. In evaluating the chances of legal claims that were filed against the company, it relied on opinions prepared by its legal counsels. These legal opinion are based on the legal counsels' best professional judgment, considering the stage at which the proceedings are at, and the accumulated legal experience with the various issues, this given that the outcomes of the claims as decided by the courts may differ from the estimates. See note 31 for additional information

c. Testing for impairment of deferred purchase expenses in life insurance

As discussed in note 2r2, 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, as necessary, 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.

d. Deferred taxes

The Company recognizes deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. The company regularly reviews its deferred tax assets for recoverability, based on historical taxable income, projected future taxable income, the expected timing of the reversals of existing temporary differences and the implementation of tax planning strategies. If the company is unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or time period within which the underlying temporary differences become taxable or deductible, the company could be required to eliminate a portion of the deferred tax asset or increase the deferred tax liabilities resulting in an increase in its effective tax rate and an adverse impact on operating results.

NOTE 5 - OPERATING SEGMENTS

The Company operates in a number of sectors, as follows: general insurance, health insurance and life insurance, as described below. The activity which is not allocated to segments includes equity, liabilities which are not related to the insurance businesses and the assets held against these liabilities.

a. Life insurance sector

The life insurance sector provides cover for life insurance risk only. The life insurance sector includes only life risk insurance, as well as coverage of other risks such as disability, occupational disability and other health related services.

b. 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.

NOTE 5 - OPERATING SEGMENTS (continued):

c. 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 5 - OPERATING SEGMENTS (continued):

	For year ended December 31, 2016				
	Life insurance	Health insurance	General insurance	Not allocated to operating segments	Total
	ILS in thousands				
Gross earned premiums	126,319	218,858	692,223		1,037,400
Premiums earned by reinsurers	(21,365)	(3,037)	(143,621)		(168,023)
Premiums earned - retained amount	104,954	215,821	548,602		869,377
Investment income, net and financing income	3	1,533	10,608	6,331	18,475
Commission income	3,446	404	39,703		43,553
Total income	108,403	217,758	598,913	6,331	931,405
Payments and change in insurance liabilities and with respect to insurance contracts, gross	(44,105)	(97,000)	(615,799)		(756,904)
Share of reinsurers in increase in insurance liabilities and payments with respect to insurance contracts	10,960	3,137	178,699		192,796
Payments and change in liabilities for insurance contracts, in retention	(33,145)	(93,863)	(437,100)		
Commissions and other acquisition expenses	(46,758)	(53,308)	(142,264)		(242,330)
General and administrative expenses	(14,414)	(28,546)	(38,410)		(81,370)
Financing income	-	-	1,488	1,922	3,410
Total comprehensive income (loss) before tax	14,086	42,041	(17,373)	8,253	47,007

NOTE 5 - OPERATING SEGMENTS (continued):

	For year ended December 31, 2015				
	Life insurance	Health insurance	General insurance	Not allocated to operating segments	Total
	ILS in thousands				
Gross earned premiums	123,046	216,421	649,418		988,885
Premiums earned by reinsurers	(23,095)	(2,408)	(135,120)		(160,623)
Premiums earned retained amount	99,951	214,013	514,298		828,262
Investment income, net and financing income	-	1,236	8,617	8,763	18,616
Commission income	3,907	565	32,589		37,061
Total income	103,858	215,814	555,504	8,763	883,939
Change in insurance liabilities and payments with respect to insurance contracts, gross	(40,010)	(76,333)	(364,482)		(480,825)
Share of reinsurers in increase in insurance liabilities and payments with respect to insurance contracts	11,939	2,805	45,214		59,958
Payments and change in liabilities for insurance contracts, in retention	(28,071)	(73,528)	(319,268)		(420,867)
Commissions and other acquisition expenses	(44,998)	(53,411)	(141,479)		(239,888)
General and administrative expenses	(19,182)	(30,519)	(33,183)		(82,884)
Financing income	-	-	1,780	1,982	3,762
Total comprehensive income before tax	11,607	58,356	63,354	10,745	144,062

NOTE 5 - OPERATING SEGMENTS (continued):

	For year ended December 31, 2014				
	Life insurance	**Health insurance**	**General insurance**	**Not allocated to operating segments**	**Total**
	ILS in thousands				
Gross earned premiums	115,500	208,762	598,989		923,251
Premiums earned by reinsurers	(23,354)	(5,607)	(120,615)		(149,576)
Premiums earned retained amount	92,146	203,155	478,374		773,675
Investment income, net and financing income	51	4,193	24,957	19,926	49,127
Commission income	3,457	1,278	33,692		38,427
Total income	95,654	208,626	537,023	19,926	861,229
Change in insurance liabilities and payments with respect to insurance contracts, gross	(42,011)	(91,717)	(444,130)		(577,858)
Share of reinsurers in increase in insurance liabilities and payments with respect to insurance contracts	10,601	4,799	133,574		148,974
Payments and change in liabilities for insurance contracts, in retention	(31,410)	(86,918)	(310,556)		(428,884)
Commissions and other acquisition expenses	(42,984)	(56,418)	(130,688)		(230,090)
General and administrative expenses	(16,309)	(26,497)	(34,165)		(76,971)
Financing income (expenses)	-	(10)	(583)	6,106	5,513
Total comprehensive income before tax	4,951	38,783	61,031	26,032	130,797

NOTE 5 - OPERATING SEGMENTS (continued):

	December 31, 2016				
	Life insurance	Health insurance	General insurance	Not allocated to operating segments	Total
	ILS in thousands				
Assets					
Intangible assets	-	-		33,816	33,816
Deferred acquisition costs	-	837	61,303	79,687	141,827
Financial investments:					
Marketable debt instruments	-	113,705	755,243	441,227	1,310,175
Nonmarketable debt instruments	-	-	111,887	59,398	171,285
Other	-	-	-	79,077	79,077
Total financial investments	-	113,705	867,130	579,702	1,560,537
Cash and cash equivalents	7,194	19,853	59,187	50,000	136,234
Reinsurance assets	15,066	1,568	641,925	-	658,559
Premiums collectible	65	6,526	146,943	-	153,534
Other assets	2,559	-	51,795	11,435	65,789
Total assets	24,884	142,489	1,828,283	754,640	2,750,296
Liabilities					
Liabilities for insurance contracts and nonprofit participating investment contracts	57,065	119,988	1,469,712	-	1,646,765
Other liabilities	11,781	209	336,902	779	349,671
Total liabilities	68,846	120,197	1,806,614	779	1,996,436

NOTE 5 - OPERATING SEGMENTS (continued):

	December 31, 2015				
	Life insurance	Health insurance	General insurance	Not allocated to operating segments	Total
	ILS in thousands				
Assets					
Intangible assets	-	-	-	26,397	26,397
Deferred acquisition costs	-	673	64,550	84,452	149,675
Financial investments:					
Marketable debt instruments	-	127,681	669,246	404,071	1,200,998
Nonmarketable debt instruments	-	-	* 154,688	107,416	262,104
Shares	-	-	-	92,851	92,851
Other	-	-	-	73,424	73,424
Total financial investments	-	127,681	823,934	677,762	1,629,377
Cash and cash equivalents	8,264	10,116	8,116	35,747	62,243
Reinsurance assets	12,202	2,818	533,130	-	548,150
Premiums collectible	115	8,120	* 140,463	-	148,698
Other assets	2,016	-	44,705	11,469	58,190
Total assets	22,597	149,408	1,614,898	835,827	2,622,730
Liabilities					
Liabilities for insurance contracts and nonprofit participating investment contracts	49,140	115,230	1,253,619	-	1,417,989
Other liabilities	12,606	265	356,043	8,141	377,055
Total liabilities	61,746	115,495	1,609,662	8,141	1,795,044

* Reclassified, see note 2u.

NOTE 5 - OPERATING SEGMENTS (continued):

Additional information relating to general insurance segment:

	For year ended December 31, 2016						
	Compulsory car insurance	**Car damages insurance**	**Home insurance**	**Professional liability**	**Property insurance and others***	**Other liability insurance***	**Total**
	ILS in thousands						
Gross premiums	146,084	314,123	103,433	65,773	38,102	33,935	701,450
Reinsurance premiums	(2,016)	(115)	(14,586)	(57,742)	(36,282)	(28,016)	(138,757)
Premiums in retention	144,068	314,008	88,847	8,031	1,820	5,919	562,693
Change in balance of unearned premiums, in retention	(286)	(11,429)	(3,963)	824	8	755	(14,091)
Premiums earned, in retention	143,782	302,579	84,884	8,855	1,828	6,674	548,602
Investment income, net and financing income	4,472	2,134	752	1,343	251	1,656	10,608
Commission income	-	-	3,552	17,570	9,941	8,640	39,703
Total income	148,254	304,713	89,188	27,768	12,020	16,970	598,913
Payments and change in insurance liabilities and payments with respect to insurance contracts	(164,584)	(236,673)	(41,540)	(93,799)	(32,614)	(46,589)	(615,799)
Share of reinsurers in increase of insurance liabilities and payments with respect to insurance contracts	30,599	-	4,958	73,467	30,525	39,150	178,699
Payments and change in insurance liabilities and payments with respect to insurance contracts, in retention	(133,985)	(236,673)	(36,582)	(20,332)	(2,089)	(7,439)	(437,100)
Commission, marketing expenses and other acquisition expenses	(27,065)	(58,867)	(24,159)	(16,830)	(6,870)	(8,473)	(142,264)
General and administrative expenses	(5,652)	(14,653)	(13,949)	(2,642)	(745)	(769)	(38,410)
Financing expenses	-	522	959	3	2	2	1,488
Total expenses	(166,702)	(309,671)	(73,731)	(39,801)	(9,702)	(16,679)	(616,286)
Total comprehensive income (loss) before taxes on income	(18,448)	(4,958)	15,457	(12,033)	2,318	291	(17,373)
Gross liabilities with respect to insurance contracts as of December 31, 2016	563,257	229,188	72,443	230,229	87,024	287,571	1,469,712
Liability insurance contracts in retention as of December 31, 2016	447,320	229,188	65,787	41,732	3,492	40,268	827,787

* Property insurance and others include mainly results from the property insurance sector, contributing 90% of total premiums in these sectors. Other liability sectors include mainly results from the product liability insurance sector, contributing 35% of total premiums in those sectors.

NOTE 5 - OPERATING SEGMENTS (continued):

Additional information relating to general insurance segment (continued):

	For year ended December 31, 2015						
	Compulsory car insurance	**Car damages insurance**	**Home insurance**	**Professional liability**	**Property insurance and others***	**Other liability insurance***	**Total**
	ILS in thousands						
Gross premiums	146,782	284,177	102,246	62,239	40,167	38,765	674,376
Reinsurance premiums	(2,051)	(116)	(16,991)	(52,726)	(38,212)	(31,819)	(141,915)
Premiums, in retention	144,731	284,061	85,255	9,513	1,955	6,946	532,461
Change in balance of unearned premiums, in retention	(1,013)	(15,292)	(1,595)	328	(207)	(384)	(18,163)
Premiums earned, in retention	143,718	268,769	83,660	9,841	1,748	6,562	514,298
Investment income, net and financing income	4,212	1,257	484	1,209	162	1,293	8,617
Commission income	-	-	4,138	13,571	7,436	7,444	32,589
Total income	147,930	270,026	88,282	24,621	9,346	15,299	555,504
Payments and change in insurance liabilities and payments with respect to insurance contracts	4,888	(216,420)	(48,644)	(72,636)	(1,855)	(29,815)	(364,482)
Share of reinsurers in increase of insurance liabilities and payments with respect to insurance contracts	(58,572)	-	8,177	70,834	(207)	24,982	45,214
Payments and change in insurance liabilities and payments with respect to insurance, in retention	(53,684)	(216,420)	(40,467)	(1,802)	(2,062)	(4,833)	(319,268)
Commission, marketing expenses and other acquisition expenses	(27,511)	(58,625)	(27,432)	(15,077)	(5,162)	(7,672)	(141,479)
General and administrative expenses	(6,853)	(7,368)	(12,097)	(4,251)	(1,384)	(1,230)	(33,183)
Financing expenses	-	645	1,133	-	-	2	1,780
Total expenses	(88,048)	(281,768)	(78,863)	(21,130)	(8,608)	(13,733)	(492,150)
Total comprehensive income (loss) before taxes on income	59,882	(11,742)	9,419	3,491	738	1,566	63,354
Gross liabilities with respect to insurance contracts as of December 31, 2015	475,386	206,560	70,551	155,586	77,626	267,910	1,253,619
Liability for retention insurance contracts in retention as of December 31, 2015	384,669	206,560	61,654	27,338	3,496	36,772	720,489

* Property lines and other include mainly results from the property insurance sector, the operations of which constitute 83% of total premiums in these sectors. Other liability sectors include mainly results from the product liability insurance sector, the operations of which constitute 44% of total premiums in these sectors.

NOTE 5 - OPERATING SEGMENTS (continued):

Additional information relating to general insurance segment (continued):

	For year ended December 31, 2014						
	Compulsory car insurance	Car damages insurance	Home insurance	Professional liability	Property insurance and others*	Other liability insurance*	Total
	ILS in thousands						
Gross premiums	146,272	256,572	104,123	56,414	32,036	33,945	629,362
Reinsurance premiums	(2,040)	(108)	(23,970)	(47,675)	(30,777)	(28,125)	(132,695)
Premiums, in retention	144,232	256,464	80,153	8,739	1,259	5,820	496,667
Change in balance of unearned, in retention	(4,733)	(11,461)	(82)	(1,364)	(136)	(517)	(18,293)
Premiums earned, in retention	139,499	245,003	80,071	7,375	1,123	5,303	478,374
Investment income, net and financing income	10,951	4,116	2,873	3,200	479	3,338	24,957
Commission income	-	-	4,870	13,233	8,212	7,377	33,692
Total income	150,450	249,119	87,814	23,808	9,814	16,018	537,023
Payments and change in insurance liabilities and payments with respect to insurance contracts	(109,602)	(168,861)	(36,945)	(30,731)	(52,706)	(45,285)	(444,130)
Share of reinsurers in increase of insurance liabilities and payments with respect to insurance contracts	13,460	-	4,592	25,395	50,327	39,800	133,574
Payments and change in insurance liabilities and payments with respect to insurance, in retention	(96,142)	(168,861)	(32,353)	(5,336)	(2,379)	(5,485)	(310,556)
Commission, marketing expenses and other acquisition expenses	(26,181)	(48,238)	(29,742)	(12,911)	(5,854)	(7,762)	(130,688)
General and administrative expenses	(10,377)	(5,377)	(11,220)	(4,128)	(1,310)	(1,753)	(34,165)
Financing expenses	-	-	(20)	(253)	(37)	(273)	(583)
Total expenses	(132,700)	(222,476)	(73,335)	(22,628)	(9,580)	(15,273)	(475,992)
Total comprehensive income before taxes on income	17,750	26,643	14,479	1,180	234	745	61,031
Gross liabilities with respect to insurance contracts as of December 31, 2014	666,500	168,599	64,517	262,359	96,557	267,803	1,526,335
Liability for retention insurance contracts in retention as of December 31, 2014	506,731	168,599	56,140	49,839	3,591	40,760	825,660

* Property lines and other include mainly results from the property insurance sector, the operations of which constitute 83% of total premiums in these sectors. Other liability sectors include mainly results from the product liability insurance sector, the operations of which constitute 44% of total premiums in these sectors.

NOTE 6 - INTANGIBLE ASSETS:

	Software
	ILS in thousands
Cost:	
Balance as of January 1, 2015	56,663
Additions in 2015*	13,423
Retirements in 2015	(647)
Balance as of December 31, 2015	**69,439**
Additions in 2016*	
Retirements in 2016	16,716
Balance as of December 31, 2016	(832)
	85,323
Accumulated amortization:	
Balance as of January 1, 2015	36,253
Additions in 2015	7,436
Retirements in 2015	(647)
Balance as of December 31, 2015	**43,042**
Additions in 2016	
Retirements in 2016	9,297
Balance as of December 31, 2016	(832)
	51,507
Depreciated balance:	
At December 31, 2016	**33,816**
At December 31, 2015	**26,397**

* Additions in respect of computer software include mainly additions in respect of proprietary development: in 2016 - ILS 13,998 thousand and in 2015 - ILS 12,366 thousand.

NOTE 7 - DEFERRED ACQUISITION COSTS:

a. Composition

	December 31	
	2016	2015
	ILS in thousands	
Life insurance (see section b.)	79,687	84,452
Health insurance (see section b.)	837	673
General insurance	61,303	64,550
Total	141,827	149,675

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

	Life insurance	Health insurance	Total
	ILS in thousands		
Balance as of January 1, 2015	85,505	962	86,467
Additions (acquisition expenses)	26,160	673	26,833
Current amortization	(6,790)	(962)	(7,752)
Amortization relating to cancellations	(20,423)	-	(20,423)
Balance as of December 31, 2015	84,452	673	85,125
Additions (acquisition expenses)	20,735	837	21,572
Current amortization	(6,399)	(673)	(7,072)
Amortization relating to cancellations	(19,101)	-	(19,101)
Balance as of December 31, 2016	79,687	837	80,524

NOTE 8 - PROPERTY AND EQUIPMENT:

a. Composition of assets and accumulated depreciation thereon, grouped by major classifications, and changes therein in 2016, are as follows:

	Computers and communications equipment	Office furniture and equipment	Leasehold improvements	Total
	ILS in thousands			
Cost:				
Balance at January 1, 2016	26,321	6,871	12,034	45,226
Additions during year	4,152	2,172	72	6,396
Retirements during year	(709)	(1,008)	(3,684)	(5,401)
Balance at December 31, 2016	29,764	8,035	8,422	46,221
Accumulated depreciation:				
Balance at January 1, 2016	19,127	4,145	10,485	33,757
Additions during year	4,382	899	1,149	6,430
Retirements during year	(709)	(1,008)	(3,684)	(5,401)
Balance at December 31, 2016	22,800	4,036	7,950	34,786
Depreciated balance at December 31, 2016	6,964	3,999	472	11,435

b. Composition of assets and accumulated depreciation thereon, grouped by major classifications, and changes therein in 2015, are as follows:

	Computers and communications equipment	Office furniture and equipment	Leasehold improvements	Total
	ILS in thousands			
Cost:				
Balance at January 1, 2015	23,285	6,569	12,887	42,741
Additions during year	5,559	302	158	6,019
Retirements during year	(2,523)	-	(1,011)	(3,534)
Balance at December 31, 2015	26,321	6,871	12,034	45,226
Accumulated depreciation:				
Balance at January 1, 2015	18,127	3,666	10,285	32,078
Additions during year	3,523	479	1,211	5,213
Retirements during year	(2,523)	-	(1,011)	(3,534)
Balance at December 31, 2015	19,127	4,145	10,485	33,757
Depreciated balance at December 31, 2015	7,194	2,726	1,549	11,469

NOTE 9 - OTHER RECEIVABLES:

	December 31	
	2016	**2015**
	ILS in thousands	
Prepaid expenses	21,893	20,118
Employees	364	269
Insurance companies and insurance brokers	18,484	16,079
Related parties (see note 29a)	10,876	4,534
Other	873	2,471
Total other receivables	52,490	43,471

As of December 31, 2016 and December 31, 2015, no provision for impairment of accounts receivables was required.

NOTE 10 - PREMIUMS COLLECTIBLE:

a. Composition:

	December 31	
	2016	**2015 ****
	ILS in thousands	
Premiums collectible (*)	161,597	156,805
Less - provision for impairment of accounts receivables (see c.)	(8,063)	(8,107)
Total premiums collectible	153,534	148,698
(*) Includes backdated checks, payments by standing order and payments though credit card companies	132,438	125,681

For information about linkage terms of premium collectible, see note 28c(3).

The Company has a balance of premium collectible from related parties, see note 29a.

** After reclassification, see note 2u.

NOTE 10 - PREMIUMS COLLECTIBLE (continued):

b. Aging:

	December 31	
	2016	**2015**
	ILS in thousands	
Unimpaired premiums collectible:		
Not overdue	151,704	147,135
Overdue**:		
Less than 90 days	500	739
Between 90 and 180 days	1,330	824
Total unimpaired premiums collectible	153,534	148,698
Impaired premiums collectible	8,063	8,107
	161,597	156,805
Less - provision for impairment of accounts receivables	(8,063)	(8,107)
Total premiums collectible	153,534	148,698

As of December 31, 2016 and December 31, 2015, the Company had no unimpaired premiums collectible that are 180 days or more overdue.

* After reclassification, see note 2u.
** Including an amount as of December 31, 2016 of ILS 18 thousand (as of December 31, 2015 of ILS 49 thousand) for overdue life insurance receivables.

c. Change in provision for impairment of accounts receivables:

	Year ended December 31	
	2016	**2015**
	ILS in thousands	
Balance at January 1	(8,107)	(7,956)
Change in provision during year through profit and loss	44	(151)
Balance at December 31	(8,063)	(8,107)

NOTE 11 - FINANCIAL INVESTMENTS:

Financial investments composition:

	As of December 31, 2016		
	At fair value through profit or loss	Loans and receivables	Total
	ILS in thousands		
Marketable debt assets (a)	1,310,175	-	1,310,175
Nonmarketable debt assets (b)	-	171,285	171,285
Listed shares (d)	-	-	-
Other (e)	79,077	-	79,077
Total	1,389,252	171,285	1,560,537

	As of December 31, 2015		
	At fair value through profit or loss	Loans and receivables	Total
	ILS in thousands		
Marketable debt assets(a)	1,200,998	-	1,200,998
Nonmarketable debt assets(b)	-	* 262,104	262,104
Listed shares (d)	92,851	-	92,851
Other(e)	73,424	-	73,424
Total	1,367,273	262,104	1,629,377

* After reclassification, see note 2u.

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

	December 31	
	2016	2015
	ILS in thousands	
Government bonds	559,286	589,845
Other non-convertible marketable debt instruments	750,889	611,153
Total marketable debt instruments	1,310,175	1,200,998

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

	Carrying amount		Fair value	
	2016	2015	2016	2015
	ILS in thousands			
Presented at amortized cost, excluding bank deposits	114,243	* 164,390	116,602	* 166,729
Bank deposits	57,042	97,714	57,084	97,661
Total non-convertible debt assets	171,285	262,104	173,686	264,390

As of December 31, 2016 and December 31, 2015, ass non-marketable debt assets are not overdue and not impaired.

* After reclassification, arising from receivable balances from credit card companies for issued compulsory vehicle policies, see note 2u.

NOTE 11 - FINANCIAL INVESTMENTS (continued):

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

	Effective interest*	
	2016	**2015**
	Percentages	
Marketable debt assets:		
Linkage basis:		
Linked to CPI	3.24%	3.30%
Linked to USD	-	-
ILS denominated	4.29%	3.40%
Nonmarketable debt assets:		
Linkage basis:		
Linked to CPI	1.77%	1.91%
Linked to USD	-	5.42%
ILS denominated	8.23%	8.5%

* Weighted average

d. Shares:

	December 31	
	2016	**2015**
	ILS in thousands	
Marketable shares - designated upon initial recognition at fair value through profit or loss	-	92,851

e. Other financial investments:

	December 31	
	2016	**2015**
	ILS in thousands	
Marketable shares* - designated upon initial recognition at fair value through profit or loss	79,077	73,424

* Other financial investments mainly include investments in exchange traded funds.

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 bonds yields and margins of corporate bonds as measured in the Tel Aviv Stock Exchange with the addition of premium in respect of non-marketability,
As measured in the Tel Aviv Stock Exchange Ltd, with the addition of a premium in respect of non-marketability. The interest rates used in capitalization are set by "Fair Spread Ltd.", which provides quoted interest rates in proportion to various risk ratings.

	December 31	
	2016	**2015**
	Percentages	
AA rating or more	1.49%	1.86%
A rating	2.84%	4.12%
Lower than BBB rating	-	18.24%

NOTE 11 - 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).

Fair value measurements of 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. Fair value measurements of non-marketable debt assets of the Company are measured at depreciated cost, and their fair value is presented for disclosure purposes only (see b. above) at level 2.

NOTE 12 - CASH AND CASH EQUIVALENTS:

	December 31	
	2016	**2015**
	ILS in thousands	
Cash and deposits available for withdrawal on demand:		
Denominated in New Israel Shekels	116,654	55,999
Denominated in dollars	19,338	5,981
Denominated in other currencies	242	263
Cash and cash equivalents	136,234	62,243

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 (0.02%-0.03%).

NOTE 13 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS:

a. Composition of share capital:

	Number of shares			
	Authorized		Issued and fully paid	
	December 31			
	2016	**2015**	**2016**	**2015**
Ordinary ILS 1 shares	45,000,100	45,000,100	5,730	5,730

b. Rights attached to shares

Rights to vote in shareholders meetings, the right to receive dividends, rights attendant upon the liquidation or winding up 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.

c. Capital management and requirements:

1) Management's policy is to maintain a strong capital base in order to preserve the ability of the Company to continue operating to generate profits for its shareholders and to support future business activity. The Company is subject to the capital requirements set by the Supervisor.

2) The following is information about the required and existing capital of the Company under the Supervision of Financial Services Regulations (Insurance) (Minimum Capital Required of an Insurer), 1998 (hereinafter - the capital regulations) and the directives of the Supervisor.

The amounts of capital held by the Company according to the capital regulations:

	December 31	
	2016	**2015**
	ILS in thousands	
The amount required by the Supervisor's regulations and the directives of the Supervisor (a)	584,790	515,769
The existing amount computed under the capital regulations:		
Initial basic capital	753,860	827,686
Total existing capital, computed according the capital regulations	753,860	827,686
Surplus as of the date of this report	**169,070**	**311,917**
Subsequent events:		
Dividend (3)	50,000	-
Surplus considering subsequent events	119,070	311,917

NOTE 13 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS (continued)**:**

	December 31	
	2016	2015
	ILS in thousands	
(a) The required equity includes, inter alia, capital requirements with respect to the following:		
Operations related to general insurance	117,976	106,236
Exceptional life insurance risks	41,588	36,790
Deferred acquisition costs in relation to life insurance	79,687	84,452
Investment assets and other assets	58,507	44,547
Catastrophe risk related to general insurance	257,227	218,294
Operating risks	29,805	25,450
Total	584,790	515,769

3) On March 21, 2017, prior to the approval of these financial statements, management suggested a ILS 50 million dividend, or ILS 8,726 per share. This offer is on the agenda awaiting approval by the board in its meeting during today. Given that the dividend is expected to be approved during today, this dividend amount was recognized as a "subsequent event".

4) On April 19, 2016, the Board of Directors of the Company approved a ILS 105 million dividend, representing ILS 18.325 per share. The dividend was paid on May 24, 2016.

5) On October 27, 2015, the board of directors of the Company resolved to distribute dividend of ILS 35 million, or ILS 6.11 per share. The dividend was paid on November 19, 2015.

6) On October 28, 2014, the Company's Board of Directors resolved to distribute a dividend in the total amount of ILS 35 million (ILS 6.11 per share). The dividend was paid on December 30, 2014.

d. Solvency II:

1) In November 2014, the Supervisor issued a letter to insurance companies' managers ("the letter") about an outline for implementing Solvency II capital adequacy directive (hereinafter - - the directive). In her letter, the Supervisor announced she intends to publish in 2016 guidance for adjusting the first tier of the directive to the local market, which will replace the present directive. As part of preparations for model implementation, the Supervisor requires insurance companies to perform IQISs that are designed to calibrate the model (simulation of the impact of the directive on the capital of an insurer provided the existing business mix and present balance sheet).

2) On April 21, 2016, the Supervisor issued guidance for performing an IQIS regarding 2015 (hereinafter - IQIS 5). According to the directive, insurance companies were required to file the results of the planned exercise to the Supervision. The Company completed IQIS 5 in July 2016.

   According to IQIS 5 results of the Company, capital surplus of the Company increased as of December 31, 2015, under the Solvency II regimen relative to capital surplus under the existing Israeli regimen (see a. above).

   Note that the model, in its present version, has very high sensitivity to changes in market and other variables and therefore capital requirements it reflects may be highly volatile.

NOTE 13 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS (continued)**:**

3) In August 2016, the Supervisor issued a letter about dividend distributions by insurance companies (hereinafter - "the letter"), which replaces an earlier letter from December 2011. According to the letter, an insurance company will not be allowed to pay dividends unless it has, after the distribution, a solvency ratio of at least 115% according to existing capital regulations, and solvency ratio at the rates indicated below according to the updated quantitative assessment for the implementation of the new solvency regimen (IQIS 5), or according to the guidance for implementing the first tier of the new solvency regimen, calculated without factoring in transitional provisions. The required solvency ratios post-distribution will be at least:

   - Financial statements as of December 31, 2017 – 115%
   - Through the financial statements as of December 31, 2018 – 120%
   - From the financial statements as of December 31, 2019 – 130%

   Insurance companies are required to provide the Supervisor within ten business days from the date of distribution an income forecast of the company for the subsequent two years from the date of dividend distribution, an updated debt service plan for the Company as approved by the Board of Directors of the holding company, a capital management plan as approved by the Board of Directors of the company, minutes of the discussion in the Board of Directors that approved the dividend distribution and background information for the discussion.

4) On September 1, 2016, the Supervisor published several letters, which are addressed to insurance companies and which update the provisions of the Solvency II-based regimen and the guidance relating to disclosure thereof in the financial statements of the insurance companies. Among other things, those provisions include Solvency II disclosure guidance for financial statements of an insurance company, as follows:

   - Disclosure regarding the Company's solvency ratio, which was calculated as part of IQIS5, will be provided in the financial statements for Q3 2016.

   - Furthermore, where the results of the IQIS5 show that a significant capital deficit, the directors report shall include a disclosure relating to certain matters specified in one of the abovementioned letters.

   - Insurance companies shall be required to provide disclosure relating to economic capital, solvency required capital and "SCR" commencing in their financial statements for Q1 2017 in accordance with the relevant provisions to be published by the Supervisor. Disclosure on economic capital, solvency required capital and "SCR" as of December 31, 2016 shall be provided in the financial statements for Q1 2017.

5) In February 2017, the Supervisor issued a circular on the provisions for implementing Solvency II-based regimen. The directive includes a comprehensive examination of risks that insurance companies are exposed to and standards for management and measurement, and is based on three tiers: a quantitative tier, dealing with risk-based solvency; a qualitative tier, concerning internal control processes, risk management, corporate governance and Own Risk and Solvency Assessment (ORSA); and a third tier, concerning promotion of market discipline, disclosure and reporting.

   Except for a number of aspects that were adapted to the Israeli market, the provisions of the circular are based, as much as possible, on the quantitative tier of the directive and its accompanying provisions, and that in order to maintain uniformity and allow the Israeli supervisory regimen to be recognize as compatible to that in Europe.

NOTE 13 - SHAREHOLDERS' EQUITY AND EQUITY REQUIREMENTS (continued)**:**

The circular states that an insurance company has to maintain economic solvency according to the provisions of the circular and its appendices, without detracting from the duty to comply with the minimum capital regulations and the Supervisor guidance issued thereunder, and that the Capital Markets, Insurance and Savings Authority will concurrently act to amend the regulations, such that their provisions in relation to minimum required capital will not apply to insurance companies covered by the provisions of the circular, and that after an insurance company obtains certification of the Supervisor for performing an audit of circular compliance in its annual financial statements.

The provisions of the circular will come into effect beginning on June 30, 2017, but insurance companies will be permitted to calculate, until the end of 2018, required solvency capital as of the date of the annual statements only.

In this respect, it is important to note that the provisions of the circular determine, among other things, that the period from June 30, 2017 to December 31, 2021 ("**the deployment period**"), the following provisions will apply in relation to solvency capital requirement (SCR) in the deployment period:

1) The solvency capital requirement in the deployment period as of June 30, 2017 may not be less than 60% of the solvency required capital as per the guidance in the appendix to the circular ("SCR");
2) The solvency required capital in the deployment period as calculated using data as of December 31, 2017 will be 65% of the SCR;
3) The solvency required capital in the deployment period as calculated using data as of December 31, 2018 and data as of June 30, 2019, will be 70% of the SCR;
4) The solvency required capital in the deployment period as calculated using data as of December 31, 2019 and data as of June 30, 2020, will be 80% of the SCR;
5) The solvency required capital of an insurance company in the deployment period as calculated using data as of December 31, 2020 and data as of June 30, 2021, will be 90% of the SCR.
6) The solvency required capital of an insurance company in the deployment period as calculated using data as of December 31, 2021 and thereafter, will not be less than SCR.

In addition, the circular points out that notwithstanding the above as to the timing of its coming into effect, as to a list of the provisions included therein, the effective date will be December 31, 2017.

NOTE 14 - LIABILITIES WITH RESPECT TO NONPROFIT PARTICIPATING INSURANCE CONTRACTS AND INVESTMENT CONTRACTS:

	As of December 31					
	Gross		Reinsurance		Retained amount	
	2016	2015	2016	2015	2016	2015
	ILS in thousands					
Insurance contracts in life insurance sector	57,065	49,140	15,066	12,202	41,999	36,938
Insurance contracts in health insurance sector	119,988	115,230	1,568	2,818	118,420	112,412
Insurance contracts in general insurance sector	1,469,712	1,253,619	641,925	533,130	827,787	720,489
Total liabilities with respect non-profit Participating insurance contracts and investment contracts	1,646,765	1,417,989	* 658,559	* 548,150	988,206	869,839

* Most are to related-party reinsurance, see note 29a.

NOTE 15 - 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	
	2016	2015	2016	2015	2016	2015
	ILS in thousands					
Compulsory car insurance and liability sectors:						
Provision for unearned premiums	114,528	117,050	41,606	42,835	72,922	74,215
Pending claims	966,529	781,832	510,131	407,267	456,398	374,565
Total liabilities in compulsory car insurance and liability sectors *	1,081,057	898,882	551,737	450,102	529,320	448,780
Property and miscellaneous sectors:						
Provision for unearned premiums	206,970	195,220	22,197	25,831	184,773	169,389
premium deficiency reserve	2,465	11,321	-	-	2,465	11,321
Pending claims	179,220	148,196	67,991	57,197	111,229	90,999
Total liabilities in property and miscellaneous sectors	388,655	354,737	90,188	83,028	298,467	271,709
Total liabilities with respect to insurance contracts in general insurance sector	1,469,712	1,253,619	641,925	533,130	827,787	720,489

NOTE 15 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

a.1. Insurance liabilities with respect to insurance contracts in general insurance sector by category

	As of December 31					
	Gross		Reinsurance		Retained amount	
	2016	2015	2016	2015	2016	2015
Deferred acquisition costs:	ILS in thousands					
Compulsory car insurance and liability sectors	20,534	22,093	11,156	11,963	9,378	10,130
Property and miscellaneous sectors	40,769	42,457	5,085	6,699	35,684	35,758
Total	61,303	64,550	16,241	18,662	45,062	45,888
Liabilities with respect to general insurance contracts, after deduction of deferred acquisition costs:						
Compulsory car insurance and liability sectors (see b(1) below)	1,060,523	876,789	540,581	438,139	519,942	438,650
Property and miscellaneous sectors (see b.2 below)	347,886	312,280	85,103	76,329	262,783	235,951
Total liabilities with respect to general insurance contracts, after deduction of deferred acquisition costs	1,408,409	1,189,069	625,684	514,468	782,725	674,601
* Of that amount, liability for compulsory vehicle	563,257	475,386	115,937	90,717	447,320	384,669

NOTE 15 - 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	
	2016	2015	2016	2015	2016	2015
	ILS in thousands					
Actuarial valuations:						
Mr. Ernst Segal	1,128,665	915,441	578,192	464,473	550,473	450,968
Total actuarial valuations	1,128,665	915,441	578,192	464,473	550,473	450,968
Additional liability with respect to difference between actuarial valuation and amount reflected in financial statements	16,974	14,587	(70)	(9)	17,044	14,596
Provision for unearned premiums	321,498	312,270	63,803	68,666	257,695	243,604
Premium deficiency reserve, not included in actuary estimates	2,575	11,321	-	-	2,575	11,321
Total insurance liabilities with respect to insurance contracts in general insurance sector	1,469,712	1,253,619	641,925	533,130	827,787	720,489

NOTE 15 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

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

b1. Compulsory car insurance and liability sectors:

	As of December 31					
	Gross		Reinsurance		Retained amounts	
	2016	2015	2016	2015	2016	2015
	ILS in thousands					
Balance as of beginning of year	876,789	1,177,875	438,139	591,883	438,650	585,992
Ultimate cost of claims with respect to current underwriting year	210,469	185,706	75,050	67,107	135,419	118,599
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	5,953	10,842	-	-	5,953	10,842
Change in estimate of ultimate cost of claims with respect to previous underwriting years	85,867	(155,632)	67,743	(50,923)	18,124	(104,709)
Total change in ultimate cost of claims	302,289	40,916	142,793	16,184	159,496	24,732
Payments in settlement of claims during course of year:						
With respect to current underwriting year	(1,524)	(2,243)	(332)	(944)	(1,192)	(1,299)
With respect to previous underwriting years	(117,031)	(234,573)	(40,019)	(156,803)	(77,012)	(77,770)
Total payments for period	(118,555)	(236,816)	(40,351)	(157,747)	(78,204)	(79,069)
Accumulation added to profits on closing of underwriting year *	-	(14,695)	-	(5,489)	-	(9,206)
Remaining change in accumulation*	-	(90,491)	-	(6,692)	-	(83,799)
Total change in accumulation for period	-	(105,186)	-	(12,181)	-	(93,005)
Balance as of end of year	1,060,523	876,789	540,581	438,139	519,942	438,650

* For information about elimination of the accumulation and implementation of the "best practice" to calculation of general insurance reserves - see note 2r(d)(5).

1. The opening and closing balances include pending claims, accumulation and 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 15 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

b. Changes in liabilities with respect to insurance contracts in general insurance sector, after deduction of deferred acquisition costs (continued):

b2. Property and miscellaneous sectors:

	As of December 31					
	Gross		Reinsurance		Retained amount	
	2016	2015	2016	2015	2016	2015
	ILS in thousands					
Balance as of beginning of year	312,280	286,714	76,329	96,583	235,951	190,131
Ultimate cost of claims with respect to events occurring in year under review	324,194	297,080	36,437	38,957	287,757	258,123
Change in ultimate cost of claims with respect to events in prior years	(15,832)	(41,484)	(951)	(30,990)	(14,881)	(10,494)
Payments made in course of year in settlement of claims:						
With respect to events occurring in year under review	(210,488)	(193,603)	(9,052)	(8,592)	(201,436)	(185,011)
With respect to events occurring in prior years	(78,171)	(69,056)	(15,638)	(21,403)	(62,533)	(47,653)
Total payments	(288,659)	(262,659)	(24,690)	(29,995)	(263,969)	(232,664)
Change in provision for unearned premiums, after deduction of deferred acquisition costs	13,438	21,308	(2,022)	1,774	15,460	19,534
Change in premium deficiency reserve	2,465	11,321	-	-	2,465	11,321
Balance as of end of year	347,886	312,280	85,103	76,329	262,783	235,951

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

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. 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 15 - 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 costs, in compulsory motor insurance and liability sectors as of December 31, 2016 according to underwriting year in ILS thousands (CPI-adjusted):

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Total
Paid claims (accumulated) at end of year:											
After one year	2,565	3,551	3,641	2,727	2,110	2,934	2,438	2,287	2,244	1,524	
After two years	17,842	14,585	16,642	13,087	20,297	11,164	14,562	13,272	14,109		
After three years	34,011	30,595	35,703	23,864	43,138	28,220	31,882	36,929			
After four years	46,228	43,935	73,807	36,753	73,107	45,341	55,982				
After five years	58,313	59,382	92,096	52,494	83,231	58,963					
After six years	64,943	78,981	105,225	65,834	92,276						
After seven years	75,717	88,265	246,809	74,744							
After eight years	87,318	93,767	257,056								
After nine years	93,248	102,111									
After ten years	94,637										
Assessment of accumulated claims (including payments) at end of year:											
After one year**	195,970	187,069	241,862	209,440	213,974	212,750	216,904	236,233	207,554	210,252	
After two years	209,684	191,891	244,792	205,409	231,908	220,540	231,527	168,873	195,571		
After three years	213,854	191,203	248,067	214,184	235,233	222,624	170,711	184,037			
After four years	176,908	178,981	197,379	163,523	189,160	162,381	219,732				
After five years	187,448	141,478	190,574	160,831	161,215	156,462					
After six years	145,009	142,379	185,196	132,497	156,433						
After seven years	159,990	140,244	294,097	136,871							
After eight years	148,834	127,398	312,123								
After nine years	119,046	128,891									
After ten years	122,467										
Excess (deficit) relative to first year, excluding accumulation* **	**54,441**	**50,090**	**(114,744)**	**26,651**	**32,727**	**5,919**					**55,084**
Rate of deviation relative to first year, excluding accumulated %	30.8%	28.0%	(58.1)%	16.3%	17.3%	3.6%					6.2%
Cost of accumulated claims as of December 31, 2016	**122,467**	**128,891**	**312,123**	**136,871**	**156,433**	**156,462**	**219,732**	**184,037**	**195,571**	**210,252**	**1,822,840**
Accumulated payments through December 31, 2016	94,637	102,111	257,056	74,744	92,276	58,963	55,982	36,929	14,109	1,524	788,332
Balance of pending claims	27,830	26,780	55,067	62,127	64,157	97,499	163,750	147,107	181,462	208,728	1,034,508
Pending claims through underwriting year 2006											**26,015**
Total liabilities in respect of insurance contracts in compulsory vehicle and liabilities sectors, net of deferred acquisition costs as of December 2016											**1,060,522**

* The amounts above are presented in inflation-adjusted values to allow presentation of development based on real valued.

** Estimated accumulated claims at the end of first year includes reserve for unearned premium less deferred acquisition expenses.

*** The difference between estimated accumulated claims in the first year excluding accumulation and estimated accumulated claims as of the date of this report.

NOTE 15 - 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 costs, in compulsory motor insurance and liability sectors as of December 31, 2016 according to underwriting year in ILS thousands (CPI-adjusted):

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Total
Paid claims (accumulated) at end of year:											
After one year	2,393	3,524	2,623	2,203	1,577	2,111	2,086	2,111	1,299	1,192	
After two years	14,766	12,927	13,794	9,276	9,174	8,119	10,252	10,225	8,775		
After three years	28,550	26,339	25,226	18,789	20,072	22,611	23,561	26,440			
After four years	40,146	38,262	38,473	29,019	32,710	35,633	37,377				
After five years	48,713	46,234	48,365	37,413	40,641	45,603					
After six years	54,761	53,537	57,369	45,910	47,701						
After seven years	60,153	59,752	71,993	52,731							
After eight years	66,918	63,521	79,269								
After nine years	70,682	69,082									
After ten years	71,735										
Assessment of accumulated claims (including payments) at end of year:											
After one year**	116,389	119,038	128,311	124,140	123,810	131,088	145,869	157,326	128,713	135,390	
After two years	120,621	121,531	129,894	117,168	121,178	125,962	135,868	104,317	111,170		
After three years	122,444	123,105	133,472	119,909	125,480	127,253	85,603	111,984			
After four years	121,861	123,936	87,177	84,695	88,039	83,041	103,354				
After five years	124,333	79,908	88,277	81,652	78,790	81,632					
After six years	86,821	81,848	89,746	74,336	78,119						
After seven years	88,140	80,363	92,083	77,060							
After eight years	82,921	76,387	95,704								
After nine years	78,430	78,471									
After ten years	78,732										
Excess (deficit) relative to first year, excluding accumulation* **	**43,130**	**45,466**	**(8,527)**	**7,635**	**9,919**	**1,409**					**99,033**
Rate of deviation relative to first year, excluding accumulated %	35.4%	36.7%	(9.8)%	9.0%	11.3%	1.7%					23.9%
Cost of accumulated claims as of December 31, 2016	**78,732**	**78,471**	**95,704**	**77,060**	**78,119**	**81,632**	**103,354**	**111,984**	**11,170**	**135,390**	**951,614**
Accumulated payments through December 31, 2016	71,735	69,082	79,269	52,731	47,701	45,603	37,377	26,440	8,775	1,192	439,904
Balance of pending claims	6,997	9,389	16,435	24,329	30,419	36,030	65,976	85,543	102,394	134,198	511,710
Pending claims through underwriting year 2006											**8,232**
Total liabilities in respect of insurance contracts in compulsory vehicle and liabilities sectors, net of deferred acquisition costs as of December 2016											**519,942**

* The amounts above are presented in inflation-adjusted values to allow presentation of development based on real valued.

** Estimated accumulated claims at the end of first year includes reserve for unearned premium less deferred acquisition expenses.

*** The difference between estimated accumulated claims in the first year excluding accumulation and estimated accumulated claims as of the date of this report.

NOTE 15 - 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 costs, in compulsory motor insurance sector as of December 31, 2016 according to underwriting year in ILS thousands (CPI-adjusted):

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Total
Paid claims (accumulated) at end of year:											
After one year	2,283	3,369	2,437	1,867	1,301	1,766	1,851	1,925	1,161	1,136	
After two years	13,838	12,169	12,815	8,225	5,786	6,999	9,411	9,552	7,526		
After three years	26,841	25,536	23,262	17,258	13,734	20,539	22,449	24,279			
After four years	38,274	36,943	34,517	26,853	22,878	32,846	34,525				
After five years	46,183	49,056	48,527	37,923	30,310	41,675					
After six years	52,044	54,619	57,321	45,310	37,020						
After seven years	57,067	61,013	65,818	51,785							
After eight years	63,222	65,103	74,000								
After nine years	67,094	69,820									
After ten years	68,082										
Assessment of accumulated claims (including payments) at end of year:											
After one year**	118,273	118,613	124,549	122,279	117,714	119,909	138,460	150,909	122,136	136,116	
After two years	121,787	120,572	133,806	116,133	114,194	123,867	140,815	108,835	112,045		
After three years	124,738	122,823	135,367	121,301	116,230	125,296	88,350	118,317			
After four years	127,577	130,988	95,274	88,193	84,609	78,496	102,283				
After five years	130,691	88,143	95,295	85,740	71,931	76,030					
After six years	94,224	86,980	93,064	73,621	69,536						
After seven years	91,661	86,530	87,389	76,494							
After eight years	87,603	79,619	92,034								
After nine years	79,024	82,427									
After ten years	77,052										
Excess (deficit) relative to first year, excluding accumulation*:**	**50,525**	**48,561**	**3,240**	**11,700**	**15,073**	**2,466**					**131,565**
Rate of deviation relative to first year, excluding accumulated %	39.6%	37.1%	3.4%	13.3%	17.8%	3.1%					32.0%
Cost of accumulated claims as of December 31, 2016	**77,052**	**82,427**	**92,034**	**76,494**	**69,536**	**76,030**	**102,283**	**118,317**	**112,045**	**136,116**	**942,333**
Accumulated payments through December 31, 2016	68,082	69,820	74,000	51,785	37,020	41,675	34,525	24,279	7,526	1,136	409,847
Balance of pending claims	8,970	12,607	18,034	24,708	32,515	34,355	67,758	94,039	104,519	134,980	532,486
Pending claims through underwriting year 2006											**20,710**
Total liabilities in respect of insurance contracts in compulsory vehicle and liabilities sectors, net of deferred acquisition costs as of December 2016											**553,197**

* The amounts above are presented in inflation-adjusted values to allow presentation of development based on real valued.

** Estimated accumulated claims at the end of first year includes reserve for unearned premium less deferred acquisition expenses.

*** The difference between estimated accumulated claims in the first year excluding accumulation and estimated accumulated claims as of the date of this report.

NOTE 15 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued):

c4. Review of development of retained amounts of liabilities with respect to insurance contracts, after deduction of deferred acquisition costs, in compulsory vehicle insurance sector as of December 31, 2016 according to underwriting year in ILS thousands (CPI-adjusted):

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Total
Paid claims (accumulated) at end of year:											
After one year	2,286	3,369	2,437	1,867	1,301	1,766	1,852	1,925	1,161	1,136	
After two years	13,840	12,169	12,815	8,225	5,786	6,999	9,411	9,552	7,526		
After three years	26,843	24,811	23,262	17,258	13,734	20,539	21,967	24,279			
After four years	38,131	36,024	34,517	26,853	22,690	32,846	34,042				
After five years	46,015	43,413	43,479	34,750	30,121	41,675					
After six years	51,876	48,924	51,614	42,137	36,832						
After seven years	56,899	54,772	58,674	48,612							
After eight years	63,054	58,261	65,566								
After nine years	66,489	62,954									
After ten years	67,476										
Assessment of accumulated claims (including payments) at end of year:											
After one year**	107,356	107,117	113,882	107,508	102,073	110,592	127,275	138,904	114,978	123,606	
After two years	108,937	108,955	116,230	101,073	96,659	104,209	120,320	94,357	96,386		
After three years	110,924	111,747	118,578	103,786	99,052	106,836	76,037	99,932			
After four years	113,379	113,668	74,936	70,933	68,436	69,110	86,061				
After five years	115,090	69,789	75,767	69,548	62,027	66,543					
After six years	79,849	72,383	77,597	63,782	62,460						
After seven years	79,127	71,994	74,864	65,541							
After eight years	75,351	68,391	75,973								
After nine years	72,286	70,892									
After ten years	72,142										
Excess (deficit) relative to first year, excluding accumulation* **	**41,237**	**42,776**	**(1,037)**	**5,393**	**5,976**	**2,568**					**96,913**
Rate of deviation relative to first year, excluding accumulated %	36.4%	37.6%	(1.4)%	7.6%	8.7%	3.7%					27.5%
Cost of accumulated claims as of December 31, 2016	**72,142**	**70,892**	**75,973**	**65,541**	**62,460**	**66,543**	**86,061**	**99,932**	**96,386**	**123,606**	**819,535**
Accumulated payments through December 31, 2016	67,476	62,954	65,566	48,612	36,832	41,675	34,041	24,279	7,526	1,136	390,098
Balance of pending claims	4,665	7,938	10,407	16,928	25,628	24,868	52,019	75,654	88,860	122,470	429,437
Pending claims through underwriting year 2006											7,824
Total liabilities in respect of insurance contracts in compulsory vehicle and liabilities sectors, net of deferred acquisition costs as of December 2016											**437,261**

* The amounts above are presented in inflation-adjusted values to allow presentation of development based on real valued.

** Estimated accumulated claims at the end of first year includes reserve for unearned premium less deferred acquisition expenses.

*** The difference between estimated accumulated claims in the first year excluding accumulation and estimated accumulated claims as of the date of this report.

NOTE 15 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued)**:**

c5. Accrued information for underwriting years in compulsory vehicle insurance:

For the year ended December 31, 2016:

	Underwriting year						
	2016	**2015**	**2014**	**2013**	**2012**	**2011**	**2010**
	ILS in thousands						
Gross premium	147,584	146,623	146,126	134,861	115,159	104,494	107,202
Gain in retention for underwriting year - accumulated	3,920	33,039	52,455	80,409	43,441	41,181	43,425
Effect of investment revenue on retained income in retention for the underwriting year	941	2,769	5,434	8,796	11,615	14,164	17,159

c6. Accrued information for underwriting years in liability and miscellaneous insurance:

For the year ended December 31, 2016:

	Underwriting year						
	2016	**2015**	**2014**	**2013**	**2012**	**2011**	**2010**
	ILS in thousands						
Gross premium	68,470	69,033	63,061	77,118	97,591	94,436	88,561
Gain in retention for underwriting year - accumulated	2,842	943	8,272	3,008	5,208	2,097	4,634
Effect of investment revenue on retained income in retention for the underwriting year	124	386	701	1,146	2,232	2,730	2,575

NOTE 15 - LIABILITIES WITH RESPECT TO INSURANCE CONTRACTS IN GENERAL INSURANCE SECTOR (continued)**:**

c7. Composition of income (loss) in retention in compulsory vehicle and liability insurance:

	Gain (loss) in respect of open years	Income in respect of underwriting year which was released in the reported year	Adjustments in respect of underwriting years which were released in previous years	Activity not included in calculation of reserves	Comprehensive income
	ILS in thousands				
Year Ended:					
2016	-	-	-	-	(18,448)
2015*	-	40,397	41,776	(22,291)	59,882
2014	-	33,370	8,481	(24,101)	17,750

c8. Composition of income (loss) in retention in liabilities and miscellaneous insurance:

	Gain (loss) in respect of open years	Income in respect of underwriting year which was released in the reported year	Adjustments in respect of underwriting years which were released in previous years	Activity not included in calculation of reserves	Comprehensive income
	ILS in thousands				
Year ended:					
2016	-	-	-	-	(11,742)
2015*	-	7,720	6,907	(9,570)	5,057
2014	(1,467)	5,326	3,888	(5,822)	1,925

* For information about elimination of the accumulation and implementation of the "best practice" to calculation of general insurance reserves - see note 2r(d)(5).

NOTE 16 - ADDITIONAL DATA CONCERNING LIFE INSURANCE SECTOR:

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

Data pertaining to year ended December 31, 2016 (ILS in thousands):

	Policies not containing savings element		Total
	Risk sold as individual policy		
	Private	Group	
Insurance reserves	757	-	757
Pending claims	56,308	-	56,308
Total	57,065	-	57,065

Data pertaining to year ended December 31, 2015 (ILS in thousands):

	Policies not containing savings element		Total
	Risk sold as individual policy		
	Private	Group	
Insurance reserves	925	-	925
Pending claims	48,215	-	48,215
Total	49,140	-	49,140

b. **Details of results by type of policy**

Data pertaining to year ended December 31, 2016 (ILS in thousands):

	Policies not containing savings element		Total
	Risk sold as single policy		
	Private	Group	
Gross risk premiums	126,151	-	126,151
Gain from life insurance business	14,086	-	14,086
New annualized premium	25,280	-	25,280
Payments and change in liabilities for gross insurance contracts	44,105	-	44,105

NOTE 16 - ADDITIONAL DATA CONCERNING LIFE INSURANCE SECTOR (continued):

Data pertaining to year ended December 31, 2015 (ILS in thousands):

	Policies not containing savings element		Total
	Risk sold as single policy		
	Private	Group	
Gross risk premiums	123,116	-	123,116
Gain from life insurance business	11,607	-	11,607
New annualized premium	38,338	-	38,338
Payments and change in liabilities for gross insurance contracts	40,010	-	40,010

Data pertaining to year ended December 31, 2014 (ILS in thousands):

	Policies not containing savings element		Total
	Risk sold as single policy		
	Private	Group	
Gross risk premiums	115,884	-	115,884
Gain from life insurance business	4,915	36	4,951
New annualized premium	41,585	-	41,585
Payments and change in liabilities for gross insurance contracts	42,032	(21)	42,011

NOTE 17 - 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, 2016 (ILS in thousands):

	Long-term	Short-term	Total
By insurance exposure insurance reserves	-	2,396	2,396
Pending claims	99,639	17,953	117,592
Total	99,639	20,349	119,988

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

No difference exists between actuary assessments in healthcare business and overall liability in the financial statements.

NOTE 17 - BREAKDOWN OF LIABILITIES IN RESPECT OF INSURANCE CONTRACTS IN HEALTH INSURANCE (continued)**:**

Data pertaining to year ended December 31, 2015 (ILS in thousands):

	Long-term	Short-term	Total
By insurance exposure insurance reserves	-	1,923	1,923
Pending claims	* 95,026	* 18,281	113,307
Total	95,026	20,204	115,230

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

No difference exists between actuary assessments in healthcare business and overall liability in the financial statements.

* Reclassified

b. Breakdown of results by type of policy in the healthcare sector

Data pertaining to year ended December 31, 2016 (ILS in thousands):

	Long-term	Short-term	Total
Gross premiums	198,297	21,034	* 219,331
Income from healthcare insurance business	37,345	4,696	42,041
Annualized premium - new	29,445	-	29,445

* Of which individual premiums at ILS 217,915 thousand and collective premiums at ILS 1,416 thousand. The most significant coverage in long-term healthcare insurance is personal injuries and travel insurance and collective personal injuries in short-term.

Data pertaining to year ended December 31, 2015 (ILS in thousands):

	Long-term	Short-term	Total
Gross premiums	** 196,955	** 18,641	* 215,596
Income from healthcare insurance business	** 51,389	** 6,967	58,356
Annualized premium - new	42,801	-	42,801

* Of which individual premiums at ILS 212,714 thousand and collective premiums at ILS 2,882 thousand. The most significant coverage in long-term healthcare insurance is personal injuries and travel insurance and collective personal injuries in short-term.

** Reclassified.

NOTE 17 - BREAKDOWN OF LIABILITIES IN RESPECT OF INSURANCE CONTRACTS IN HEALTH INSURANCE (continued):

Data pertaining to year ended December 31, 2014 (ILS in thousands):

	Long-term	Short-term	Total
Gross premiums	** 189,386	** 18,392	* 207,778
Income from healthcare insurance business	** 36,264	** 2,519	38,783
Annualized premium - new	38,200	-	38,200

* Of which individual premiums at ILS 203,496 thousand and group premiums at ILS 4,282 thousand. The most material coverage included in health insurance is individual bodily injuries in the short-term, and overseas travel and collective injury in the short-term.

** Reclassified.

NOTE 18 - CHANGES IN LIABILITIES WITH RESPECT TO LIFE INSURANCE CONTRACTS AND HEALTH INSURANCE CONTRACTS:

	Life insurance	Health insurance
	ILS in thousands	
Balance as of January 1, 2015	51,791	137,135
Decrease (increase) in premiums accounted for as liabilities	70	439
Changes in pending and IBNR claims	(2,721)	(22,344)
Balance as of December 31, 2015	49,140	115,230
Decrease (increase) in premiums accounted for as liabilities	(170)	(1,429)
Changes in pending and IBNR claims	8,095	6,187
Balance as of December 31, 2016	57,065	119,988

NOTE 19 - TAXES ON INCOME:

a. Taxing statutes applicable to Company:

1) General

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

2) Special tax arrangements for insurance industry - Arrangement with tax authorities

The Association of Life Insurance Companies Ltd and the Income Tax Authority have entered into a special arrangement (“the tax arrangement”). The arrangement, which is subject to renewal and revision from time to time, deals with unique tax issues. As of December 31, 2016, tax agreements have been signed, as above, for tax years up to and including the 2015 tax year. The arrangement deals, inter alia, with the following issues:

- Direct expenses of insurance companies for the purpose of acquiring life insurance contracts - (DAC) - deductible deferred policy acquisition costs incurred in 2015 and thereafter shall be deductible for tax purposes in equal portions spread over ten years (compared to deduction over the term of policy but not more than 15 years as performed in the financial statements - see note 2r(2)(d)(1)). Note that deferred acquisition expenses incurred until 2014 (inclusive) are deductible for tax purposes in equal installments with spread over only four years.

- Allocation of expenses to preferred income – allocation of expenses shall be applied to income which is subject to reduced tax rates and to tax exempt income received by the insurance companies ("preferred income"). The allocation of expenses means that some of the preferred income is turned into income taxable at the normal tax rate, in accordance with the rate of allocation. The rate of allocation set in the agreement is dependent on the source of the funds from which the preferred income is derived.

- Taxation of marketable securities – income and/or expenses from securities are reported for tax purposes on realization basis. The said income/expenses do not include linkage differences, interest and amortization of discount in respect of marketable securities that will be reported on accrual basis. Also, the said income/expenses do not include material impairment which is carried directly to income. Such impairment will only be considered as loss for tax purposes on realization basis.

The Company is not member of the Association of Life Insurance Companies Ltd, but an agreement signed between the Company and the ITA indicate that those agreements will also apply to the Company.

Current and deferred taxes in these financial statements were determined based on the principles in those agreements.

NOTE 19 - TAXES ON INCOME (continued)**:**

3) Effect of adoption of IFRS in Israel on tax liability

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 provisions of amendments to the Income Tax Ordinance published in 2010, 2012 and 2014 (hereafter – the temporary orders), 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 2007-2013; 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 temporary orders is that IFRS shall not apply in actual fact at the time of calculation of the taxable income for tax purposes of the said tax years.

On October 30, 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. The legislation procedures relating to the law memorandum have not yet been completed and it is doubtful whether they shall be completed in the near future.

Since the legislation procedures relating to the law memorandum have not yet been completed the Company estimates that the term of the temporary order which applies to the years 2007 to 2013 shall be extended to 2014 through 2016 as well. Therefore Company's management expects that at this stage the new legislation shall not apply to tax years preceding 2017.

Taking into consideration the temporary order which applies to tax years 2007 to 2013 and the Company's estimate regarding the potential extension of the term of the temporary order to 2014 and 2016 as above, the Company computed its taxable income for tax years 2007 to 2016 based on Israeli accounting standards applicable prior to adoption of IFRS in Israel, subject to certain adjustments.

NOTE 19 - 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.

On August 5, 2013, the Law for Change of National Priorities (Legislative Amendments for the Achievement of Budgetary Objectives for 2013 and 2014), 2013 was published in the official gazette, stating among other things, that the above change in corporate tax rate will be 26.5% (instead of 25%) in 2014 and thereafter.

In January 2016, the Law for the Amendment of the Income Tax Ordinance (No. 216) was published, enacting a reduction of corporate tax rate beginning in 2016 and thereafter, from 26.5% to 25%.

In December 2016, the Economic Efficiency Law (Legislative Amendments for Implementing the Economic Policy for the 2017 and 2018 Budget Year), 2016 was published, introducing a gradual reduction in corporate tax rate from 25% to 23%. However, the law also included a temporary provision setting the corporate tax rate in 2017 at 24%. As a result, the corporate tax rate will be 24% in 2017 and 23% in 2018 and thereafter.

As a result of lowering tax rates as above, deferred tax liabilities of the Company were reduced in 2016 by ILS 407 thousand, which were carried as income in profit or loss.

In addition to corporate tax, as a financial institution, the Company is required to pay profit tax, which through September 2015, 2013 was 18% of annual income.

According to Value Added Tax Order (Tax Rate on Non-Profits and Financial Institutions) (Amendment), 2015, beginning on October 1, 2015, profit tax applicable to annual income was reduced to 17%. The change in tax rate for 2015 applies on a linear basis, such that annual profit is liable to profit tax at 17.75%.

Note that under Amendment No. 35 to the Value Added Tax Law, 1975, beginning in 2008, the entire profit tax paid by a financial institution is deductible from the income used for profit tax purposes.

In light of the changes in corporate tax and profit tax rates as above, overall tax rate (corporate tax and profit tax) applied to the Company is as follows: 2014 - 37.71%, 2015 - 37.58% and 2016 - 35.89%.

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:			
2014	26.5	18.00	37.71
2015	26.5	17.75	37.58
2016	25.0	17.00	35.90
2017	24.0	17.00	35.04
2018 and thereafter	23.0	17.00	34.19

NOTE 19 - TAXES ON INCOME (continued):

c. Final tax assessments

As of the date of these financial statements, the Company has been issued final tax assessments through tax year 2013.

d. Taxes on income included in the income statements:

	For the year ended December 31		
	2016	2015	2014
	ILS in thousands		
Current	(22,865)	(56,210)	(59,552)
Creation and reversal of deferred taxes in respect of the reported year	6,172	6,047	10,891
Creation and reversal of deferred taxes in respect of previous years	1,190	(3,921)	5,731
In respect of previous years	(330)	113	(4,964)
	(15,833)	(53,971)	(47,894)

e. Taxes on income relating to equity items:

	For the year ended December 31		
	2016	2015	2014
	ILS in thousands		
Tax element for net accumulated impact as of December 31, 2015 of elimination of the accumulation and first-time implementation of the "best practice" - see note 2r(1)(d)(5)	-	49,180	-

f. 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	Profit From securities	Provision for doubtful accounts	Property and equipment	Other	Total
	ILS in thousands						
Balance of tax asset (liability) as of January 1, 2015	(19,263)	1,929	(2495)	3,000	257	6,305	(10,267)
Changes charged to income	(1,017)	521	7,639	57	49	(5,238)	2,011
Impact of change in tax rate (see b. above)	286	(35)	(73)	(43)	(4)	(16)	115
Balance of deferred tax asset (liability) as of December 31, 2015	(19,994)	2,415	5,071	3,014	302	1,051	(8,141)
Changes charged to income	2,672	(11)	4,088	(16)	(81)	303	6,955
Impact of change in tax rate (see b. above)	1,393	(161)	(526)	(172)	(18)	(109)	407
Balance of deferred tax asset (liability) as of December 31, 2016	(15,929)	2,243	8,633	2,826	203	1,245	(779)

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

NOTE 19 - TAXES ON INCOME (continued):

	December 31	
	2016	2015
	ILS in thousands	
Deferred tax assets:		
Deferred tax assets to be recovered after more than 12 months from date of statement of financial position	1,131	1,335
Deferred tax assets to be recovered within 12 months from date of statement of financial position	14,019	10,518
	15,150	11,853
Deferred tax liabilities:		
Deferred tax liabilities to be recovered after more than 12 months from date of statement of financial position	(15,929)	(19,994)
Deferred tax liabilities to be recovered within 12 months from date of statement of financial position	-	-
	(15,929)	(19,994)
Deferred tax liabilities, Net	**(779)**	**(8,141)**

g. 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		
	2016	2015	2014
	ILS in thousands		
Income before taxes on income	47,007	144,062	130,797
Overall statutory tax rate applicable to financial institutions (see b. above)	35.90%	37.58%	37.71%
Taxes computed based on the statutory tax rate	16,875	54,138	49,324
Increase (decrease) in taxes arising from:			
Income not deductible for tax purposes	461	14	(651)
Updating of deferred tax balances in respect of change in tax rates	(407)	(115)	-
Taxes in respect of previous years	(860)	(113)	(767)
Other	(236)	47	(12)
Taxes on income	15,833	53,971	47,894
Average effective tax rate	**33.68%**	**37.46%**	**36.62%**

NOTE 20 - PAYABLES AND SURPLUS RESERVES:

	December 31	
	2016	2015
	ILS in thousands	
Employees and other payroll related liabilities	22,231	23,325
Suppliers and service providers	32,556	32,205
Premiums paid in advance	12,347	11,912
Commissions payable	8,832	9,604
Related parties (see note 29a)	5,944	3,772
Other	7,104	5,968
	89,014	86,786

NOTE 21 - PREMIUMS - RETAINED:

	Year ended December 31, 2016		
	Gross	Reinsurance	Retained amount
		ILS in thousands	
Life insurance premiums	126,151	21,366	104,785
Health insurance premiums	219,331	3,036	216,295
General insurance premiums	701,450	138,757	562,693
Total premiums gross	1,046,932	163,159	883,773
Less - change in balance of unearned premium **	(9,532)	4,864	(14,396)
Total earned premiums	1,037,400	* 168,023	869,377

	Year ended December 31, 2015		
	Gross	Reinsurance	Retained amount
		ILS in thousands	
Life insurance premiums	123,116	23,090	100,026
Health insurance premiums	215,596	2,408	213,188
General insurance premiums	674,376	141,915	532,461
Total premiums gross	1,013,088	167,413	845,675
Less - change in balance of unearned Premium **	(24,203)	(6,790)	(17,413)
Total earned premiums	988,885	* 160,623	828,262

	Year ended December 31, 2014		
	Gross	Reinsurance	Retained amount
		ILS in thousands	
Life insurance premiums	115,884	23,331	92,553
Health insurance premiums	207,778	5,606	202,172
General insurance premiums	629,362	132,695	496,667
Total premiums gross	953,024	161,632	791,392
Less - change in balance of unearned Premium **	(29,773)	(12,056)	(17,717)
Total earned premiums	923,251	* 149,576	773,675

* For information about reinsurance premiums with related parties, see note 29b below.

** The change in the unearned premium balance mainly arises from general insurance.

NOTE 22 - NET REVNEUES FROM INVESTMENTS AND FINANCING INCOME:

	Year ended December 31		
	2016	**2015**	**2014**
	ILS in thousands		
Income 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	(25,238)	(28,648)	84
Income from interest, linkage differences and exchange differences, exchange differences, on financial assets through profit or loss	38,873	40,688	43,251
Income from interest on deposits and cash and nonmarketable securities	4,646	4,074	3,453
Income from dividends	194	2,502	2,339
Total revenues from net investments and Financing income	18,475	18,616	49,127

* For information about reinsurance premiums with related parties, see note 29b below.

** The change in the unearned premium balance mainly arises from general insurance.

NOTE 23 - REVNEUES FROM COMMISSIONS:

	Year ended December 31		
	2016	**2015**	**2014**
	ILS in thousands		
Reinsurance commissions, net of change in deferred acquisition costs relating to reinsurance	43,553	37,061	38,427

For information about reinsurance premiums with related parties, see note 29b below.

NOTE 24 - PAYMENTS AND CHANGES IN LIABILITIES IN RESPECT OF RETAINED INSURANCE CONTRACTS:

	Year ended December 31		
	2016	**2015**	**2014**
	ILS in thousands		
Total payments and changes in liabilities in respect of life insurance contracts:			
Gross	44,105	40,010	42,011
Reinsurance	(10,960)	(11,939)	(10,601)
Life insurance contracts - retained	33,145	28,071	31,410
Total payments and changes in liabilities in respect of general insurance contracts:			
Gross	615,799	364,482	444,130
Reinsurance*	(178,699)	(45,214)	(133,574)
General insurance contracts retained	437,100	319,268	310,556

NOTE 24 - PAYMENTS AND CHANGES IN LIABILITIES IN RESPECT OF RETAINED INSURANCE CONTRACTS (continued):

	Year ended December 31		
	2016	2015	2014
	ILS in thousands		
Total payments and changes in liabilities in respect of health insurance contracts:			
Gross	97,000	76,333	91,717
Reinsurance*	(3,137)	(2,805)	(4,799)
Health insurance contracts retained	93,863	73,528	86,918
Total payments and changes in liabilities in respect of retained insurance contracts	564,108	420,867	428,884

* Total payments and changes in liabilities in respect of insurance contracts of related-party reinsurers see note 29b below.

NOTE 25 - COMMISSIONS, MARKETING EXPENSES AND OTHER ACQUISITION COSTS:

	Year ended December 31		
	2016	2015	2014
	ILS in thousands		
Acquisition commissions	40,454	42,399	38,935
Marketing and other expenses (reclassified from general and administrative expenses)	194,028	198,950	198,849
Change in Acquisition costs	7,848	(1,461)	(7,694)
Total commissions, marketing expenses and other acquisition expenses	242,330	239,888	230,090

NOTE 26 - GENERAL AND ADMINISTRATIVE EXPENSES:

	Year ended December 31		
	2016	2015	2014
	ILS in thousands		
Payroll and related expenses	186,665	193,237	183,990
Depreciation and amortization	15,727	12,650	12,966
Maintenance of offices and communication	21,698	24,392	24,781
Marketing and advertisement	45,979	46,750	45,928
Legal and professional consulting	6,334	6,139	7,478
Information technology expenses	17,226	15,626	17,314
Other	9,460	9,164	10,138
Total*	303,089	307,968	302,595
Less:			
Amounts classified to changes in liabilities and payments in respect of insurance contracts	(27,691)	(26,134)	(26,775)
Amounts classified to commissions, marketing expenses and other acquisition expenses	(194,028)	(198,950)	(198,849)
General and administrative expenses	81,370	82,884	76,971
* Management and general expenses include expenses relating to automation in the total amount of	49,037	45,824	46,022

NOTE 27 - FINANCING INCOME:

	Year ended December 31		
	2016	2015	2014
	ILS in thousands		
Interest and exchange differences income	3,410	3,762	6,106
Interest expense to reinsurers	-	-	(593)
Total financing income	3,410	3,762	5,513

NOTE 28 - 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

Other risks beyond those listed above include: reputational risk, legal risk and information security risk.

a. Description of risk management procedures and methods

1) The Company manages risk based on the risk management policy approved by the board, which is aligned with rules and guidance of local regulations and the enterprise risk management policies of the AIG global corporation.

2) The risk management policy is designed to support achieving business objectives of the Company and ensure controlled exposure to risks, in tune with changes in the business environment. Monitoring and reporting on the implementation of the policy, including compliance with limits and restrictions are performed according to regulatory requirements and a reporting escalation procedure established by the board and its committees.

3) The risk management process includes an ongoing process of identifying and mapping exposures in different processes, assessment and measurement of exposures and controls, reporting and assessing the alignment to the Company's risk appetite.

4) Risk management in the Company is based on three protection levels:

- First line of defense – business units – responsible for risk management in the scope of their activity.

- Second line of defense – support functions – risk management, compliance and enforcement, actuary, control units, accounting, etc. The role of those functions is, among other things, to ensure that consistent processes are in place to detect, control, track and report risks.

- Third line of defense – internal audit which is in charge of conducting independent audits of the first and second line of defense.

NOTE 28 - RISK MANAGEMENT (continued)**:**

5) The Company has committees and forums to manage risks, in addition to forums on different professional issues, led by CEO and other executives. The Company has committees to manage risk in: capital management, reserve management, operating risk management, insurance risk management, and committee for product development.

6) The Company is active in applying the principles of Solvency II in Israel, serving as a basis for assessing the economic capital required for the activity of the Company. The Company develops risk assessment processes that can have impact on economic capital. In addition, the Company adopted risk appetite at 120% of statutory capital and 130% of capital required under Solvency II. Risk appetite is based on the main risk assessments of the Company and risk appetite scenarios. Risk appetite serves as basis for developing capital management policy and dividend distribution policy of the Company (see also note 13 above).

b. Legal requirements

The Supervisor's guidance on risk management are included, among other things, in the consolidated circular (Title 5, Part 1, Chapter 10) which replaces the sections in Insurance Circular No. 14-1-2006 on the duties of the risk manager and the relationships he/she has with other officers in the Company. Under the consolidated circular, the main duties of the risk manager are:

1) To ensure that high-quality processes are in place for detection of insurance risks, market risks, cash flow risks and counterparty risks that are material and embedded in assets and liabilities and may have impact on the financial stability of the entity.

2) To quantify and assess the potential impact of material risks identified on the financial stability of the entity and on its liability towards insurance clients.

3) To assess risks that are embedded in new activities or product.

4) To present to the board and investment committee existing and potential risks in investment assets for establishing an investment policy and updating it.

5) To periodically report to the board, investment committee and CEO on exposures to risks and their potential impact on the financial stability of the entity.

There are other circulars that enact guidance on managing specific exposures on: readiness for disaster recovery, management of exposure to reinsurers, fraud prevention, management of cyber risks, financial reporting control (SOX) and credit risk management. In addition, circulars have been distributed on Solvency II readiness.

The Company appointed a risk manager who work to implement regulatory requirements in this area.

NOTE 28 - RISK MANAGEMENT (continued)**:**

c. Market risks

The Company's market risks relate to financial assets and liabilities or insurance liabilities. The Company's assets' portfolio arises mainly from its insurance activity. Management of proprietary investments is carried out in compliance with the provisions of the law, Company's investment policy, its credit policy and its risk management policy set out by the Board of Directors and the Investment Committee. Most of the Company's funds are invested in Israel.

Market risk is the risk that the fair value or future cash flows of financial assets, financial liabilities, or insurance liabilities will change as a result of unexpected changes in market prices. Market risk includes, inter alia, risks arising from changes in interest rates, share prices, the CPI, and foreign currencies.

In 2016, the Company's investment manager stepped down. The bond portfolio was transferred to external management by two investment managers. The stock portfolio was transitioned from investment in selected shares to investment in passive instruments. The Company receives investment consulting from the parent company.

1) Market risk sensitivity tests

The following is a sensitivity analysis in relation to the impact of change in those factors on profit (loss) for the year and overall income (capital). The sensitivity test refers to financial risks, financial liabilities and liabilities for insurance contracts and investment contracts for the relevant risk factor as of each balance sheet date, assuming that all other factors remain constant. For example, the change in interest rate is under the assumption that all other variables remain unchanged. The sensitivity analysis does not consider the impact of yield-dependent contracts, as indicated below. In addition, it is assumed that those changes do not reflect permanent impairment of assets that are presented at depreciated cost or available-for-sale assets, and thus, the above sensitivity analysis does not include impairment losses for those assets.

The sensitivity analysis reflects direct impacts only, without secondary impacts. Note also that sensitivity is not necessarily linear, and that the impact of larger or smaller changes or larger changes than those described below may not necessarily be derived through a simple extrapolation.

Data as of December 31, 2016:

	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							
Income (loss)(3)	(27,411)	27,333	5,068	(5,068)	1,448	(1,448)	806	(806)
Comprehensive income (shareholders' equity)(4)	(27,411)	27,333	5,068	(5,068)	1,448	(1,448)	806	(806)

NOTE 28 - RISK MANAGEMENT (continued)**:**

Data as of December 31, 2015:

	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							
Income (loss)(3)	(25,884)	25,787	10,379	(10,379)	2,990	(2,990)	3,083	(3,083)
Comprehensive income (shareholders' equity)(4)	(25,884)	25,787	10,379	(10,379)	2,990	(2,990)	3,083	(3,083)

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. The calculation of the sensitivity analysis considers interest changes since the beginning of the year also for assets acquired during the year.

   The impact of 1% increase/decrease in interest rate on comprehensive income for the insurance liability in the sensitivity analysis is estimated at ILS 167 / (188) thousand (2015 - ILS 217 /(232) thousand).

   The sensitivity analysis is based on the carrying amount and not the economic value. This sensitivity analysis does not consider asset and liability items with direct interest risk, as discussed in note 28c(2).

   Note that the portion of liabilities that was subject to the sensitivity analysis of total liability for non-yield-dependent insurance contracts is 10.4%.

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 are presented net of taxes in accordance with the tax rate applicable in the reported year.

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

NOTE 28 - RISK MANAGEMENT (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 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	
	2016	**2015**
	ILS in thousands	
Assets with direct interest risk:		
Marketable debt instruments	1,310,175	1,200,998
Non-marketable debt asset:		
Non-marketable bonds	56,618	106,221
Other	57,042	97,714
Reinsurance asset	44,000	-
Cash and cash equivalents	136,234	62,243
Total assets with direct interest risk	1,604,069	1,467,176
Total assets without direct interest risk	1,146,227	1,155,554
Total assets	2,750,296	2,622,730
Liabilities with direct interest risk:		
Liabilities in respect of insurance contracts non depending yield	171,574	6,806
Liabilities for employee rights upon retirements	2,713	2,781
Liabilities in respect of reinsurers	216,517	246,603
Total liabilities with direct interest risk	390,804	256,190
Total liabilities without direct interest risk	1,605,632	1,538,854
Shareholders' equity	753,860	827,686
Total equity and liabilities	2,750,296	2,622,730
Total assets, net of liabilities	753,860	827,686

Assets without direct interest risk include shares, property and equipment, deferred acquisition costs and other assets as well as groups of balance sheet financial assets whose interest risk 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 28 - RISK MANAGEMENT (continued)**:**

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

	As of December 31, 2016				
	In ILS unlinked	**In ILS linked to the CPI**	**In foreign currency or linked thereto**	**Non-financial items and others**	**Total**
			ILS in thousands		
Intangible assets	-	-	-	33,816	33,816
Deferred acquisition costs	-	-	-	141,827	141,827
Property and equipment	-	-	-	11,435	11,435
Reinsurance assets	23,242	594,735	40,582	-	658,559
Premiums collectible	90,294	47,443	15,797	-	153,534
Current tax assets	-	1,864	-	-	1,864
Other accounts receivables	19,200	328	11,069	21,893	52,490
Other financial investments:					
Marketable debt instruments	539,658	770,517	-	-	1,310,175
Nonmarketable debt instruments	86,685	84,600	-	-	171,285
Other			6,992	72,085	79,077
Total other financial investments	626,343	855,117	6,992	72,085	1,560,537
Other cash and cash equivalents	116,654		19,580		136,234
Total assets	875,733	1,499,487	94,020	281,056	2,750,296
Total shareholders' equity				753,860	753,860
Liabilities:					
Liabilities for non-yield dependent insurance contracts and investment contracts	317,897	1,273,553	55,315	-	1,646,765
Liabilities for deferred taxes - net	-	-	-	779	779
Retirement benefit obligation	2,713	-	-	-	2,713
Accounts payable	302,905	-	26,135	17,139	346,179
Total liabilities	623,515	1,273,553	81,450	17,918	1,996,436
Total liabilities and shareholders' equity	623,515	1,273,553	81,450	771,778	2,750,296
Total balance sheet exposure	252,218	225,934	12,570	(490,722)	

NOTE 28 - RISK MANAGEMENT (continued)**:**

	As of December 31, 2015				
	In ILS unlinked	**In ILS linked to the CPI**	**In foreign currency or linked thereto**	**Non-financial items and others**	**Total**
	ILS in thousands				
Intangible assets	-	-	-	26,397	26,397
Deferred acquisition costs	-	-	-	149,675	149,675
Property and equipment	-	-	-	11,469	11,469
Reinsurance assets	24,667	479,464	44,019	-	548,150
Premiums collectible	* 62,760	64,500	21,438	-	148,698
Current tax assets	-	3,250	-	-	3,250
Other accounts receivables	17,730	-	4,619	21,122	43,471
Other financial investments:					
Marketable debt instruments	344,848	856,150	-	-	1,200,998
Non-marketable debt instruments	* 86,971	136,600	38,533	-	262,104
Shares	-	-	-	92,851	92,851
Other	-	-	6,298	67,126	73,424
Total other financial investments	431,819	992,750	44,831	159,977	1,629,377
Other cash and cash equivalents	55,999	-	6,244	-	62,243
Total assets	592,975	1,539,964	121,151	368,640	2,622,730
Total shareholders' equity				827,686	827,686
Liabilities:					
Liabilities for non-yield dependent insurance contracts and investment contracts	299,952	1,060,908	57,129	-	1,417,989
Liabilities for deferred taxes - net	-	-	-	8,141	8,141
Retirement benefit obligation	2,781	-	-	-	2,781
Other accounts payable and surplus reserves	332,834	-	14,636	18,663	366,133
Total liabilities	635,567	1,060,908	71,765	26,804	1,795,044
Total liabilities and shareholders' equity	635,567	1,060,908	71,765	854,490	2,622,730
Total balance sheet exposure	(42,592)	479,056	49,386	(485,850)	

* After reclassification, see note 2u.

NOTE 28 - RISK MANAGEMENT (continued)**:**

4) Equity instruments exposure by industry:

As of December 31, 2016, the Company does not hold shares directly.

	As of December 31, 2015 (ILS in thousands)				
	Listed on TA100 index	Listed on TA MidCap index	Abroad	Total	% of total
Industry:					
Manufacturing	30,047	79	-	30,126	32.5
High-tech	21,851	252	-	22,103	23.8
Banking	17,487	-	-	17,487	18.8
Construction and real estate	7,822	185	-	8,007	8.6
Investment and holdings	5,688	48	-	5,736	6.2
Oil and gas	5,508	-	-	5,508	5.9
Insurance	2,379	-	-	2,379	2.6
Commerce	1,021	-	-	1,021	1.1
Other business services	484	-	-	484	0.5
Total	92,287	564	-	92,851	100.0

d. Liquidity risk

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 short term period may require disposal of assets over a short term period and the sale thereof at prices that would not necessarily reflect their market prices. The scale of liquid assets is according to a rate established in the relevant Company policy. The Company approved a liquidity model that is based on the AIG corporate methodology, with necessary local adjustments. The model presents the required level of liquidity based on different scenarios.

NOTE 28 - RISK MANAGEMENT (continued):

Management of assets and liabilities

The Company manages its assets and liabilities in accordance with the requirements of regulatory provisions and based on the approved ALM (Asset Liability Management) policy - a dynamic adjustment between approved assets and liabilities.

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 sectors, which are not assessed by the Company's actuary, as well as excess of income over expenses (accumulation), are 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, 2016	83,435	84,290	4,275	420	4,633	-	177,053
As of December 31, 2015	86,145	64,154	7,335	32	6,704	-	164,370

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, 2016	507,381	296,775	231,042	417,541	16,973	1,469,712
As of December 31, 2015	571,949	214,177	170,191	282,715	14,587	1,253,619

* 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 28 - 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:

- Model Risk the risk of electing an erroneous model of pricing and/or for assessment of the insurance liabilities.
- 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.
- Systemic risk: the risk of unexpected future change in profitability trend in a calendar year.

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 is an earthquake in Israel.

The amount of the 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 1.15%is ILS 988.6 million (gross) and ILS 73.9 million (retained). This rate is computed in accordance with Company's internal models

The expected damage for catastrophe risk in general insurance as part of the required minimum capital computation is 1.75%. The expected loss in the general insurance business from exposure to a large single damage or accumulation of damages for an especially large event at the maximum possible loss (MPL) of 1.75% is ILS 1,528.1 million in gross terms and ILS 236.7 million in self-retention.

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 5 - 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 17 - the breakdown of insurance liabilities arising from health insurance.

NOTE 28 - RISK MANAGEMENT (continued):

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.

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 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 0.68%.

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.

NOTE 28 - RISK MANAGEMENT (continued):

Sensitivity analyses in life insurance:

As of December 31, 2016 (in thousands of ILS):

	Rate of illness and mortality	
	+10%	**-10%**
Profit (loss)	(2,963)	2,881

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.

Actuarial methods used for computation of the insurance liabilities:

- 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.

- 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. Cost drivers were calculated to optimize the estimation.

- This estimate includes a conservativism factor to bring the provision in the account to a level of prudence of 75%.

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

NOTE 28 - RISK MANAGEMENT (continued):

Key assumptions used for the calculation of insurance liabilities:

- In January 2015, a Supervisor position was issued titled "Best Practice for Calculation of General Insurance Reserves for Financial Reporting". The Supervisor's position includes, among other things, explanations for the principles: professionalism, consistency, and prudence, which have not been defined in General Insurance Actuarial Assessment Circular 2015-1-1. The principle of prudence requires an actuary to examine that assessments in liabilities sectors are tuned to a probability of at least 75%. In addition, the Supervisor's opinion also refers to the issue to liabilities cash flow discount rates for optimal assessments.

- According to the position of the Supervisor, beginning in the 2015 year-end, regarding outstanding claims in compulsory and liability segments, testing that it is "fairly likely" that reserves will be sufficient to cover the liabilities of the insurance is set to a probability of at least 75%.

- The Company implements the **Reserve/Premium Risk Statistical Model** ("**the RPS model**"), which is implemented by the AIG Group worldwide, and which also served the Company in 2015, in order to determine stochastically the 75th percentile estimate. This model can be depicted as having three sub-models:

  - The Adaptive Reserve Monitoring System Model (“ARMS Model”)
  - The Reserve and Premium Risk – Coefficient of Variation Model (“CV Model”)
  - The Reserve and Premium Risk – Aggregation Model (“Aggregation Model”)

NOTE 28 - RISK MANAGEMENT (continued):

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.

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 28 - RISK MANAGEMENT (continued):

Sensitivity analysis for health insurance and personal injury insurance as of December 31, 2016 (ILS in thousands):

	Rate of the cancellation (withdrawals, settlements and reductions)		Morbidity and mortality rate	
	+10%	-10%	+10%	-10%
Profit (loss)	157	(168)	(12,232)	11,259

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 no claim 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.

NOTE 28 - RISK MANAGEMENT (continued):

e3. Insurance risk in general insurance contracts (continued):

In most of the cases the car damages insurance policies are issued for a one year 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 home 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.

Principles of computation the actuarial assessment in general insurance:

a) The liabilities in respect of general insurance contracts include the following components:
- Optimized estimation of pending claims
- Conservativism addition to the 75% quartile
- Reserve for premium that has not yet been earned.
- Provision for indirect expenses

b) In January 2015, Insurance Circular "Actuarial Assessment in General Insurance" was published. The provisions of this circular are intended to improve the quality of assessing the general insurance liability (hereinafter - insurance reserves), which are a central tier in assessing the liabilities of the insurer, and regulate the inclusion in the financial statements of a professional opinion by an appointed actuary (hereinafter - actuary) in relation to the assessment of those insurance liabilities. This circular states the scope of actuarial assessment that the general insurance actuary needs to perform, the actuarial report the actuary needs to prepare and a declaration that the actuary is required to sign, which will be attached to the financial statements.

c) In January 2015, a Supervisor position, titled "Best Practice for Calculation of General Insurance Reserves for Financial Reporting" (hereinafter - "the Supervisor's opinion"). The Supervisor's opinion includes, among other things, explanations for the principles: professionalism, consistency, and prudence, which have not been defined in General Insurance Actuarial Assessment Circular 2015-1-1. The principle of prudence requires an actuary to examine that assessments in liabilities sectors are tuned to a probability of at least 75%. In addition, the Supervisor's opinion also refers to the issue to liabilities cash flow discount rates for optimal assessments.

NOTE 28 - RISK MANAGEMENT (continued):

e3. Insurance risk in general insurance contracts (continued):

d) In accordance with the instructions of the supervisor, the pending claims are computed by an actuary based on accepted actuarial methods, initially according to the optimal assessment and later with necessary addition to the 75th quartile. 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.

e) 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.

f) 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 one-off 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.

g) In cases of large claims of non-statistical 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.

h) 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.

i) 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.

j) The provision for unearned premiums is also calculated using a 75% probability, pursuant to the new guidance in the Supervisor's opinion. We examine that it is possible to return deferred acquisition cost and the cost of future claims, including other expenses related to the treatment of the policy and claims.

NOTE 28 - RISK MANAGEMENT (continued):

e3. Insurance risk in general insurance contracts (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.

As of December 31, 2016, the premium deficiency reserve in this sector is ILS 2.5 million.

b) Compulsory vehicle insurance

In the compulsory vehicle liabilities insurance, reserves are computed based on the development of payments and pending amounts in respect of smaller claims (up to the excess point). The liabilities above the excess point are computed using actuarial models that are based on development of frequency multiplied by severity. The share of the reinsurers in the excess of loss claims is calculated using a model for larger claims and based on actual larger claims.

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.

e) Estimation of indirect claim processing expenses

The indirect expense element in paid claims is calculated by the Finance Division. Those expenses include all costs of the Claims Department and allocation of indirect expenses of the Company that are allocated to settle the claims (those include IT expenses, HR, depreciation and Finance)

In late 2015, the model for estimation of indirect claim settlement expenses was reconsidered, and the calculation method using this method was changed was also implemented in 2016. The unallocated loss adjustment expense (ULAE) factor is based on the historical ratio of paid ULAE to paid losses for the latest calendar years. The ULAE reserve was computed assuming one half the cost of settling a claim is incurred upon opening a file and the remainder upon closing it, however in allocating the ULAE reserves by line, some weight was given to consider the length of time until claims are initially reported and ultimately settled.

NOTE 28 - RISK MANAGEMENT (continued):

In light of the fact that this calculation is made on a gross basis and that commercial liability segments have large IBNR amounts, adjustments were made in relation to liabilities segments when calculating retention amounts.

The ULAE reserve was allocated by accident year proportional to the unpaid indemnity reserves held by accident year.
Calendar year paid ULAE is available only in aggregate for all lines combined. The paid ULAE by line was estimated based on an allocation, by accident year, proportional to the paid indemnity losses during the calendar year.

This change of model had no material impact on reported results.

<u>The principal assumptions that were taken into account for purpose of actuarial assessment</u>:

- According to the Supervisor's position, published in a circular on January 15, 2015, beginning from the 2015 year-end in relation to outstanding claims in compulsory and liability segments, testing that it is "fairly likely" that reserves will be sufficient to cover the liabilities of the insurance is set to a probability of at least 75%
- The conservativism margin was obtained using stochastic models that estimate the volatility in claims experience. Those models also estimate random and systemic risks.
- The Company implements the Reserve/Premium Risk Statistical Model ("the RPS model"), which is implemented by the AIG Group worldwide, and which also served the Company in 2015, in order to determine stochastically the 75th percentile estimate. This model can be depicted as having three sub-models:
  - The Adaptive Reserve Monitoring System Model (“ARMS Model”)
  - The Reserve and Premium Risk – Coefficient of Variation Model (“CV Model”)
  - The Reserve and Premium Risk – Aggregation Model (“Aggregation Mod
- Outstanding claims in compulsory vehicle and liabilities segments were not discounted
- As to the implications of the amendment of the discounting regulations of national insurance that was issued in September 2016 following the Vinograd Committee conclusions on increasing company estimates, which was applied in 2016, as to the amounts that it will be required to pay to settle claims for insurance contracts in the compulsory vehicle segment – see note 3 above.

f. Credit risk data:

Credit risk arises from exposure to decrease in the quality of credit or default of borrowers from deterioration of their financial situation. Investments in bonds, capital notes and deposits of companies are mainly rated A or above, which represents a lower credit risk.

Investment in acquisition of bonds is done after a deep analysis of the Company and the investment based on credit criteria and policy as approved by the investments committee. Those debts are monitored continuously, with special attention given to problematic debt.
Once a quarter, the Company holds a debt forum, which is tasked with assessing the status of debt. The purpose of the forum is to discuss high-sensitive/distressed debt, including in cases of rating downgrades. The process for making a decision on the means to be applied to handle such debt is the responsibility of officers who are authorized to make decisions about distressed debt. Reporting on this issue is given to the investments committee of the Company.

NOTE 28 - RISK MANAGEMENT (continued):

1) Distribution of debt instruments by location*

	December 31, 2016		
	Marketable	Nonmarketable	Total
	ILS in thousands		
Domestic	1,310,175	171,285	1,481,460
Abroad	-	-	-
Total debt instruments	1,310,175	171,285	1,481,460

	December 31, 2015		
	Marketable	Nonmarketable	Total
	ILS in thousands		
Domestic	1,200,998	** 242,128	1,443,126
Abroad	-	19,976	19,976
Total debt instruments	1,200,998	262,104	1,463,102

* The classification between domestic debt instruments and debt instruments abroad was made in accordance with the country in which the instrument in traded.

** After reclassification, see note 2u.

2) Breakdown of assets by ratings:

a. Debt assets (excluding cash and cash equivalents, premiums collectible and other receivables)

	Domestic rating			
	As of December 31, 2016			
	-AA and above	BBB through A+	Lower than BBB	Total
	ILS in thousands			
Debt assets in Israel				
Marketable debt assets:				
Government bonds	559,286	-	-	559,286
Corporate bonds	480,066	270,823	-	750,889
Total marketable debt assets in Israel	1,039,352	270,823	-	1,310,175
Non-marketable debt assets:				
Corporate bonds	52,685	3,933	-	56,618
Loans and receivables, excluding bank deposits	57,625	-	-	57,625
Deposits with banks and financial institutions	57,042	-	-	57,042
Total nonmarketable debt assets in Israel	167,352	3,933	-	171,285
Total domestic debt instruments	1,206,704	274,756	-	1,481,460

Debt assets abroad

As of December 31, 2016, the Company has no debt assets overseas.

NOTE 28 - RISK MANAGEMENT (continued):

	Domestic rating			
	As of December 31, 2015			
	-AA and above	BBB through A+	Lower than BBB	Total
	ILS in thousands			
Debt assets in Israel				
Marketable debt assets:				
Government bonds	589,845	-	-	589,845
Corporate bonds	432,260	178,893	-	611,153
Total marketable debt assets in Israel	1,022,105	178,893	-	1,200,998
Nonmarketable debt assets:				
Corporate bonds	76,154	10,091	-	86,245
Loans and receivables, excluding bank deposits	* 58,169	-	-	58,169
Deposits with banks and financial institutions	97,714	-	-	97,714
Total nonmarketable debt assets in Israel	232,037	10,091	-	242,128
Total domestic debt instruments	1,254,142	188,984	-	1,443,126

	International rating			
	As of December 31, 2015			
Debt assets abroad	A and above	BBB	Lower than BBB	Total
	ILS in thousands			
Nonmarketable debt assets:				
Corporate bonds	17,216	-	2,760	19,976
Total nonmarketable debt assets abroad	17,216	-	2,760	19,976
Total debt assets abroad	17,216	-	2,760	19,976

* After reclassification, see note 2u.

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

	Domestic rating				
	As of December 31, 2016				
	A and above	BBB	Lower than BBB	Not rated	Total
	ILS in thousands				
Accounts receivable - excluding balances of reinsurers	-	-	-	204,020	204,020
Cash and cash equivalents	136,234	-	-	-	136,234
	136,234	-	-	204,020	340,254

NOTE 28 - RISK MANAGEMENT (continued):

	Domestic rating				
	As of December 31, 2015				
	A and above	**BBB**	**Lower than BBB**	**Not rated**	**Total**
	ILS in thousands				
Accounts receivable - excluding balances of reinsurers	-	-	-	*193,023	193,023
Cash and cash equivalents	62,243	-	-	-	62,243
	62,243	-	-	193,023	255,266

* After reclassification, see note 2u.

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 balances with reinsurers amounting to ILS 658,559 **thousand**, see note 14. Also see note 28f(5)(3).

4) Breakdown of exposure to investments in marketable and marketable financial debt instruments by industry:

	As of December 31, 2016	
	Balance sheet credit risk	
	Amount	**% of total**
	ILS in thousands	
Industry		
Construction and real estate	342,659	23.1
Banking	230,675	15.6
Other business services	81,103	5.5
High-tech	59,087	4.0
Investments and holdings	52,880	3.6
Commerce	28,801	1.9
Production industry	27,445	1.9
Insurance	20,023	1.4
Oil and gas exploration	18,703	1.3
Hospitality and tourism	3,174	0.2
	864,550	58.5
Loans	57,625	3.8
Government bonds	559,285	37.7
TOTAL	1,481,460	100.0

NOTE 28 - RISK MANAGEMENT (continued):

	As of December 31, 2015	
	Balance sheet credit risk	
	Amount	**% of total**
	ILS in thousands	
Economic sector		
Banks	301,228	20.6
Construction and real estate	245,091	16.8
Investment and holdings	48,301	3.3
Other business services	75,258	5.1
High-tech	56,153	3.8
Oil and gas	39,772	2.7
Commerce	15,162	1.0
Production industry	17,305	1.2
Insurance	16,818	1.2
	815,088	55.7
Loans*	58,169	4.0
Government bonds	589,845	40.3
Total	**1,463,102**	**100.0**

* After reclassification, see note 2u.

5) Reinsurance

The Group's insurance companies insure some of their businesses by means of reinsurance (mostly with global AIG Corporation companies, which are related parties of the Company). However, the reinsurance does not relieve the direct insurers of their obligations towards their policyholders under 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 follow-up on a current basis with regard to the reinsurer's situation in the world market and a follow-up 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. Those exposures are managed by individual assessment of significant exposures to reinsurers, including monitoring and development of risk level indicators, considering all reinsurers with which the Company engages.
Also, the Company's exposures are divided between various reinsurers; the most significant of these exposures are to reinsurers of high international ratings.

1. In 2015 and 2016, most of the Company's general insurance contracts (include earthquake exposure) were with insurance companies, as follows:

   - ("NHIC") New Hampshire Insurance Company
   - ("NUFIC") National Union Fire Insurance Company of Pittsburgh, PA
   - ("AHAC") American Home Assurance Company

NOTE 28 - RISK MANAGEMENT (continued):

The above-mentioned companies are global AIG Corporation companies and they are related parties of the Company. For further details on balances and transactions with related parties see note 29. The said companies have been granted an A+ rating by S&P.

2. In 2015 and 2016, the Company entered into most of the life insurance contracts with the following insurance companies:
   - Swiss Re
   - Partner Re

NOTE 28 – RISK MANAGEMENT (continued):

f. Credit risk data (continued):

3. Information regarding the exposure to credit risks as of December 31, 2016:

			Reinsurance assets						**Debts overdue**	
Rating group	**Total premiums to reinsurers for 2016**	**Net debit (credit) balances**	**Life insurance**	**Property insurance**	**Liabilities insurance**	**Deposits by reinsurers**	**Amount of letters of credit received from reinsurers**	**Total exposure**	**0.5-1 year**	**In excess of 1 year**
	ILS in thousands									
<u>**AA- or above**</u>										
GEN RE	1,166	3	1,943	-	-	(467)	-	1,479	-	-
SWISS RE	18,560	(1,743)	10,860	-	-	(7,424)	-	1,693	-	-
Other	870	-	-	-	-	-	-	-	-	-
	20,596	(1,740)	12,803	-	-	(7,891)	-	3,172	-	-
<u>**A**</u>										
Partner Reinsurance Co Ltd.	2,768	(342)	2,263	-	-	(1,450)	-	471	-	-
AHAC*	13,429	(1,573)	-	8,731	52,165	(20,718)	-	38,605	-	-
NUFIC*	104,741	(12,280)	-	68,100	406,886	(161,597)	-	301,109	-	-
NHIC*	16,114	(1,888)	-	10,477	62,598	(24,861)	-	46,326	-	-
Other companies in the AIG international corporation	5,263	3,272	-	33,161	1,079	-	-	37,512	3,272	-
Other	248	(74)	-	296	-	-	-	222	-	-
	142,563	(12,885)	2,263	120,765	522,728	(208,626)	-	424,245	3,272	-
Total	**163,159**	(14,625)	15,066	120,765	522,728	**(216,517)**	-	427,417	3,272	-

* Global AIG Corporation companies which are related parties of the Company.

NOTE 28 - RISK MANAGEMENT (continued):

f. Credit risk data (continued):

Information regarding the exposure to credit risks as of December 31, 2015:

Rating group	Total premiums to reinsurers for 2015	Net debit (credit) balances	Reinsurance assets: Life insurance	Reinsurance assets: Property insurance	Reinsurance assets: Liabilities insurance	Deposits by reinsurers	Amount of letters of credit received from reinsurers	Total exposure	Debts overdue: 0.5-1 year	Debts overdue: In excess of 1 year
	ILS in thousands									
AA- or above										
GEN RE	1,463	(240)	1,207	-	-	(585)	-	382	-	-
SWISS RE	18,610	(2,109)	9,920	-	-	(7,444)	-	367	-	-
Other	160	-	-	-	-	-	-	-	-	-
	20,233	(2,349)	11,127	-	-	(8,029)	-	749	-	-
A										
Partner Reinsurance Co Ltd.	3,729	(400)	1,075	-	-	(1,454)	-	(779)	-	-
AHAC*	12,811	(1,115)	-	8,084	42,021	(23,712)	-	25,278	-	-
NUFIC*	99,930	(8,697)	-	63,066	327,764	(184,954)	-	197,179	-	-
NHIC*	15,374	(1,338)	-	9,701	50,425	(28,454)	-	30,334	-	-
Other companies in the AIG* i	13,920	2,306	-	33,210	1,085	-	-	36,601	-	-
Other	241	72	-	592	-	-	-	664	-	-
	146,005	(9,172)	1,075	114,653	421,295	(238,574)	-	289,277	-	-
BBB+										
other	1,177	(165)	-	-	-	-	-	(165)	-	-
	1,177	(165)	-	-	-	-	-	(165)	-	-
Total	167,415	(11,686)	12,202	114,653	421,295	(246,603)	-	289,861	-	-

* Global AIG Corporation companies which are related parties of the Company.

NOTE 28 - RISK MANAGEMENT (continued):

g. Operating risks

Operating risk may lead to financial loss, reputational damage, regulatory non-compliance, undermining operating efficiency, lost targets, etc. The exposures may result from failure or inappropriateness of internal processes, human error, information technology failure, regulatory non-compliance or exogenous events. To reduce the operating risk, the Company works to reduce the material risks in accordance with the organizational risk chart and to perform risk control self-assessments by the business unit.

The risk management function in the Company includes appointment of "risk-management champions" in business units who report risk events and collect various key risk indicators for risk analysis and assessment. The risk events and key risk indicators are reported in accordance with the reporting hierarchy. The Company also has an operating risk management committee whose members include the managers of the departments. The internal auditor is invited to take part in the committee's meetings. The committee convenes every quarter and discusses risk management in various processes, risk events, etc.

In 2016, risk management procedures were integrated to have ongoing detection, treatment, monitoring and regular reporting of exposures in the organizational operating processes. In addition, regular training was given to employees on detection and reporting operating risk events. Additionally, an internal campaign was launched within the organization to raise awareness of the importance of reporting risk events.

As part of the overall risk management vision of the organization, an independent control unit was set up in 2016. The control unit constitute a second line of defense, implementing controls in addition to those of the first line of defense.

As part of the operating risk management, the Company designed a disaster recovery plan (DRP) and a business continuity plan (BCP) to recover in an instance of damage to operating infrastructure. In addition, the Company performs once a period a risk survey to detect fraud.

Information security and cyber – The Company manages its information security risk according to a relevant policy it approved. Chief Information Officer prepares to implement regulatory requirements that are expected to be published on cyber security, in addition to professional guidance of the international AIG Corporation.

Further, the Company is operating an internal audit function that performs periodic audits according to an annual and multi-annual plan. This plan reflects the findings of a legally mandatory risk survey and different guidance.

Additional aspects of operating loss are treated under the guidance in SOX 404.

h. Geographic risks

	December 31, 2016					
	Government bonds	**Corporate bonds**	**Index funds**	**Mutual funds**	**Other investments**	**Total balance sheet exposure**
	ILS in thousands					
Israel	559,286	698,983	-	56,545	250,901	1,565,715
North America	-	49,031	10,519	-	-	59,550
Other	-	59,493	12,013	-	-	71,506
Total	**559,286**	**807,507**	**22,532**	**56,545**	**250,901**	**1,696,771**

NOTE 28 - RISK MANAGEMENT (continued):

	December 31, 2015					
	Government bonds	Corporate bonds	Shares	Index funds	Other investments	Total balance sheet exposure
	ILS in thousands					
Israel	589,845	631,341	51,706	53,095	* 218,126	1,544,113
North America	-	72,550	35,361	9,468	-	117,379
Other	-	13,483	5,784	10,861	-	30,128
Total	589,845	717,374	92,851	73,424	218,126	1,691,620

The geographical exposure reported in the table for the different asset classes is based on the ultimate location of exposure, by country or region, as applicable. In cases where it is not possible to identify the location of ultimate exposure, the exposure is reported based on the place where the asset was issued or is traded.

* After reclassification, see note 2u.

NOTE 29 – 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".

Company's key management personnel (which are included together with others in the definition of "related parties" under IAS 24) include members of the Board of Directors and member of senior management (hereafter – "key management personnel").

a. Balances with interested parties and related parties:

		December 31			
		2016		2015	
	Note	Global AIG corporation companies	Key management personnel	Global AIG corporation companies	Key management personnel
		ILS in thousands			
Reinsurance assets	14, 28.f.5.3	643,197	-	535,356	-
Accounts receivable	9	10,876	-	4,534	-
Accounts payable	20	-	5,944	-	3,772
Liabilities to reinsurers	30	227,414	-	248,286	-

NOTE 29 - BALANCES AND TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES (continued):

b. Transactions with interested parties and related parties

	Note	December 31 2016	2015	2014
		ILS in thousands		
Premiums - gross*	21	68	33	30
Reinsurance premiums**	21	(139,547)	(141,661)	(131,882)
Income from commissions**	23	37,014	38,754	36,754
Payments and change in insurance liabilities in respect of insurance contracts**	24	(181,835)	(48,019)	(138,373)
Administrative and general expenses*	26	(18,480)	(10,824)	(15,969)
Administrative and general expenses**	26	(1,036)	(1,167)	(1,132)
Financial income (expenses)**	27	(7)	-	(593)

* Transactions with key management personnel. Officers of the Company may purchase, from time to time, insurance contracts that were issued by the Company, at market conditions and in the ordinary course of business.

** Transactions with Global AIG Corporation companies.

c. Benefits to key management personnel:

	For the year ended December 31 2016 No. of people	Amount	2015 No. of people	Amount *	2014 No. of people	Amount *
			ILS in thousands			
Short-term benefits	13	12,705	14	9,410	14	13,911
Other long-term benefits	13	3,980	14	462	14	1,140
Post-transaction benefits	13	1,795	14	952	14	918
		18,480		10,824		15,969

* Reclassified

d. Benefits to key management personnel – directors:

	For the year ended December 31 2016 No. of people	Amount	2015 No. of people	Amount	2014 No. of people	Amount
			ILS in thousands			
Fees to directors	3	574	4	507	4	612
	3	574	4	507	4	612

e. Income and expenses from related parties and interested parties

1) Transactions with global AIG Corporation companies which are related parties of the Company

Most of the Company's transactions with reinsurers are carried out with global AIG Corporation companies which are related parties of the Company.
As to the amounts of the said transactions, see a. and b. above. See also note 28(f)(5)(c).

NOTE 29 - BALANCES AND TRANSACTIONS WITH INTERESTED PARTIES AND RELATED PARTIES (continued):

2) Bonuses to key management personnel

Short-term and long-term benefits include bonuses and other benefits to key management personnel, amounting to ILS 729 thousand (2015 – ILS 964 thousand and 2014 – ILS 3,108 thousand).

NOTE 30 -LIABILITIES TO REINSURANCE:

	December 31	
	2016	2015
	ILS in thousands	
Deposits of reinsurers (1) ,(2)	216,517	246,603
Deferred acquisition costs in respect of reinsurance	16,241	18,662
Related parties (1) ,(2)	20,238	11,166
Other	4,169	2,916
	257,165	279,347

(1) As to the details of deposits and balances of reinsurers, most of which are related parties – see note 28(f)(5)(c).
(2) See also note 29a.

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS:

a. Contingent liabilities – motions to certify class actions:

1) In December 2012, a lawsuit and a motion for class action certification was filed against 8 insurance companies, including the Company; 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.

The Company issued its response to the motion to certify a class action on June 2, 2013, and on July 7, 2013, the plaintiff filed his response to Company response.

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued)**:**

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

The plaintiffs filed a motion for discovery and a motion to respond to a questionnaire. The Company filed its objection to the motion and a decision was handed down that require limited disclosure of documents.

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

On June 8, 2014 the plaintiffs filed a notice to the effect that they maintain their position that the application to approve the claim as a class action shall be heard by the court. In accordance with the plaintiffs' notice, summations were filed on behalf of the plaintiffs and the insurance companies. After an extension that was given, the plaintiffs filed their response summaries on February 1, 2016. The Court has not yet issued its ruling in the case.

The Company's management believes, based on the opinion of its legal counsel, that it is more likely than not that the claim will be rejected.

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

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

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

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

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

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued)**:**

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

On April 19, 2015, the applicants filed their response to the motion to certify a class action. The applicants reject the claims raised in the reply to the application.

On June 14, 2015, a preliminary hearing was held to discuss the application. In this hearing, the Court informed the parties that it intends to address questions arising from the application to approve the claim as a class action to the Supervisor; the Court asked the parties to provide it, by July 16, 2015, with questions that will be addressed to the Supervisor. On July 16, 2015 the parties filed the Court some questions they wish to refer to the Supervisor as above.

A further preliminary hearing was held on July 20, 2015 to discuss the application to approve the claim as a class action. In this hearing the Court ordered to refer questions to the Supervisor.

On December 21, 2015, the Supervisor informed the Court that she has referred the Court's questions to the Supervisor of Banks.

On March 23, 2016, the Supervisor submitted its position, after reviewing the issues, with the help of the Supervisor of Banks. The regulatory position allegedly supports in principle the arguments that the respondents raised in their arguments to the motion to certify ("the Supervisor's position").

On April 7, 2016, the respondents filed their comments to the Supervisor's position, in which they argued, among other things, that the Supervisor's position supports their own arguments to the motions to certify, and that given the Supervisor's position, the plaintiffs should withdraw their motion to certify and the claim against the Company. The plaintiffs also filed their comments to the Supervisor's position and contended that it does not impact their argument in the motion to certify.

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued)**:**

On April 10, 2016, an additional pretrial hearing was held, in which the court ordered to plaintiffs' attorney, following the Supervisor's opinion, to notify the court whether he agreed to focus the claim and the motion to certify on the issue of the extent of informing customers on the method of insurance amount revaluation (interest rates) on the date of preparing the insurance contract. In this regard, the plaintiffs' attorney will also notify whether he withdraw his claims in relation to policy lifespan. The plaintiffs' attorney is required to file his position to the court by May 11, 2016.

On May 11, 2016, the plaintiffs notified the court that at this stage they decided to withdraw their arguments raised in the motion to certify ("the plaintiffs' notice").

On May 19, 2016, the company filed a motion to dismiss the plaintiffs' notice. On May 24, 2016, an additional pretrial hearing was held, in which the plaintiffs agreed to the court's proposal to focus the action on extent of informing customer pre-contract and during preparing the contract (in distinction from the life of the policy). The court offered the parties to seek arbitration on the issues that remained disputed. The plaintiffs agreed to the proposal.

On June 5, 2016, the Company notified the court that it agreed to refer the remaining limited issues to arbitration, provided that the arbitration will be focused only on the option to provide more clarification in any of the insurance documents. On June 13, 2016, the plaintiffs notified that they agree to limit the claims in the arbitration process. On June 29, 2016, the Company notified the court that in those circumstance and given the response of the plaintiffs, it sees no point in referral to arbitration process, and asked the court to give its decision based on the written arguments that were filed and the position of the Supervisor.

On July 12, 2016, an additional pretrial hearing was held, in which the parties agreed to the court's proposal to refer the remaining disputed issues to an arbitration process. On August 4, 2016 the parties informed the Court of the identity of a mutually-agreed arbitrator.

An arbitration meeting was scheduled to November 23, 2016. After the parties failed to reach agreements in the arbitration, in an additional pretrial hearing, held on January 26, 2017, the court ordered the parties to respond until February 9, 2017 whether they are willing to continue the arbitration and to get an arbitration judgment.
On February 9, 2017, the defendants notified the court that they are ready to continue the arbitration process. Arbitration between the parties is now ongoing.

In light of information and data transferred, at this preliminary stage, management believes, based on the assessment of its legal counsel, that it is more likely than not that the court will not accept the motion to certify a class action.

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

The plaintiffs rely in their legal claim on the Supreme Court's ruling in the Zlutzin vs. Diur La-Olle case (civil appeal 17229/99) according to which even where repairs were not carried out in practice, the insurer (which insures the person who caused the damage) should bear the VAT component. The plaintiffs also rely on In-Principle Ruling issued by the Supervisor titled "In-Principle Ruling on Payment of VAT and Depreciation of Unrepaired Vehicle". This in-principle ruling states that when an insurance customer or a third party claims direct damages from repairing a vehicle and the insurer does not reject that claim, the insurer must pay the customer insurance benefits including, among other things, the VAT applicable in this matter, even if the customer did not repair the vehicle in practice.

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued)**:**

The total amount of damage claimed from the Company is ILS 40,211 thousand.

Concurrently with filing the class action motion, the plaintiff asked the Herzliya Magistrate Court, which is considering individual claims on the Ikea fire damages, to eliminate the VAT element in individual claims and to file a motion for certifying a class action in its respect.

On January 2, 2016, the Court handed down a decision, rejecting the plaintiff's request. The plaintiffs filed a motion to appeal the decision. On September 4, 2016, their decision was rejected.

Given the court decision, the plaintiffs filed a motion to be replaced by Public Trust. On October 5, 2016, the Company filed a response to the motion, in which it was claimed that it would not be appropriate to allow an organization to represent the class. The plaintiffs responded to that response.

On February 20, 2017, a decision was handed down rejecting the motion to replace the plaintiffs by Public Trust, and accordingly, the motion to certified a class action was rejected.

Management estimates, based on the opinion of its legal counsel, that it is more likely than not that the claim will be rejected.

4) On December 17, 2015, the Reserve Forces Association ("the applicants") filed an application to approve a claim as a class action against the Company and another insurance Company ("the respondents").

The applicants claim that the defendants charge reservists for full insurance premiums but only provide them with a partial and deficient insurance coverage, whose value is lower than the value of the premiums collected from reservists. According to the applicants, this situation is caused since the defendants do not insure the reservists during reserve-service periods but still charge the reservists for premiums in respect of those periods.

The group of plaintiffs on whose behalf the applicants wish to file the class action includes anyone who had an insurance policy which included an exclusion regarding reserve-service periods and who paid the defendants insurance premiums in respect of reserve-service periods in the seven years prior to the filing the class action application.

Concurrently to this case, a similar motion for class action certification is reviewed by the Center District Court against other insurance companies. An application to approve a joinder of the two class action applications was filed.

On January 27, 2016, the Central District Court approved procedural arrangement and ordered a joinder of the motion to certify and the other procedure.

On June 23, 2016, the respondents filed to the Central District Court a mutually agreed motion to extend the deadline for filing response for the motion to certify by additional ten days.

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued)**:**

On that same day, the District Court approved the respondents' motion, and the date for filing their responses was set to July 11, 2016.

On July 11, 2016, the Company's response to the motion to certify was file, in which it argued, among other things, that at the factual level, the Company did not engage in unjust enrichment and that its customers serving in reserve suffered no damage, since they receive full and continuous insurance coverage under the provisions of the policy, in which premiums were priced based on the risk that the company bears. At the legal level, the motion to certify has no normative standing. The Company acted lawfully, in compliance with the position of the regulator, and in adherence to the provisions in the relevant policy, including exclusions that explicitly appear in them and known to all customers, and which served as basis for pricing the premiums to begin with.

On September 7, 2016 the applicant filed its response to the Company's response to the motion to certify the claim. The applicant claimed, among other things, that the respondents implement a cross subsidy strategy that disadvantages those clients, who are reservists; the applicant also claimed that the respondents have the ability to price the premium in respect of risks relating to damages that may arise from reserve service.

A preliminary hearing was held on September 18, 2016. At the conclusion of this hearing, the Court explained to the applicant that it may face some obstacles if it still wishes to certify the claim as a class action; the Court advised the applicant to consider whether it insists on the pursuing the application any further.

On March 5, 2017, the parties notified the court that they reached in-principle understandings as to the settlement of the dispute that is the object of the motion to certify. For filing a formal request in relation to settling the dispute, the parties motioned for a short stay, and that the date for filing the motion to withdraw will be extended until April 2, 2017.

On March 6, 2017, the court accepted the motion by the parties.

Management estimates, based on the opinion of its legal counsel, that it is more likely than not that the claim will be rejected.

5) A legal claim and an application to approve the claim as a class action were filed against the Company on December 17, 2015. The applicant claimed that the Company breaches the provisions of its comprehensive car insurance policy which includes the AIG EXTRA compensation clause since it does not pay the insured an extra compensation of up to 15% of the value of the insured car. The applicant claimed that the causes of action are breach of agreement, breach of disclosure obligations, misleading and unjust enrichment.

The group of plaintiffs on whose behalf the applicants wish to file the class action includes any insured of the Company who has a comprehensive car insurance policy which includes an AIG EXTRA clause, but when the conditions of the clause were met did not receive the AIG EXTRA compensation.

In a ruling, dated September 19, 2016, the Court approved the settlement arrangement and ordered the case closed.

6) In the first quarter of 2016, a lawsuit and a motion to certify a class action was filed against the Company. The claim argues that the Company calculates compulsory vehicle premiums based on incorrect vehicle data, which leads to higher premiums than those approved by the Supervisor and that presented on the Supervisor's website that compares prices of different insurance companies.

The amount of personal damages claimed from the Company is negligible. The plaintiff did not specify the amount of damages of the class, but it estimated it at several million ILS.

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued)**:**

After negotiations held between the parties, a motion was filed to approve a settlement agreement.

In a hearing on November 20, 2016, the court ordered to provide a number of clarification as to the settlement agreement.

Clarifications were provided and the court ordered to publish the fact that a settlement agreement has been reached and to send a copy to the attorney so that he could consider whether to object it.

No objections were received from class members, and the Attorney General notified that he did not object.

Management believes, based on the opinion of its legal counsel that it is more likely than not that the settlement agreement will be approved.

7) On June 9, 2016, a motion for certification of a class action was filed against the Company. The plaintiff claims that the Company did not pay salary and statutory employee benefits as legally required. The class action seeks a total of ILS 9,769 thousand.

The response of the Company to the motion to certify the claim as class action was filed on January 1, 2017. The defendants need to file a response to the Company's response by April 18, 2017.

A pretrial hearing was scheduled to July 3, 2017.

According to the assessment of the Company, based on its legal counsel, at this preliminary stage of the case, it is not possible to assess the likelihood of certifying this claim as class action.

8) On August 9, 2016, a motion for class action certification was filed against a number of insurance companies, including the Company. The motion concerns the impact of customer age on pricing premiums in vehicle compulsory and property insurance. The overall amount of damages sought is ILS 100 million. The amount of personal damages sought is negligible.

On December 8, 2016, a mutually-agreed motion to amend the motion to certify was filed, in which, the court was asked to permit the plaintiffs to amend to motion to certify by removing arguments by the defendants regarding compulsory insurance, and continue the proceedings regarding comprehensive insurance only, and that in view of the Meyuhas et al. v. Menorah et. al case.

On December 11, 2016, a ruling was handed down which approved the motion to amend the motion to certify such that it will be filed until January 10, 2017. On January 10, 2017, an extension was granted to the plaintiffs to file the amended motion to certify until January 16, 2017. On January 17 ,2017, an amendment motion to certify a class action was filed.
The Company is required to file its response to the motion to certify by April 10, 2017.
A pretrial hearing was scheduled to May 4, 2017.

At this preliminary stage of the claim, management and its legal counsel are still studying the matter. Management believes, based on its legal counsel, and it is not possible to assess the likelihood of the motion being accepted at this preliminary stage.

9) On November 2, 2016, a lawsuit and a motion to certify a class action was filed against a number of insurance companies, including the Company concerning mortgage loan life insurance.

The motion concerns insurance coverage to homeowners who take mortgage loans where the loan capital is only returned at the end of the loan period ("balloon loans").

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued)**:**

The plaintiff estimates the overall damage to the class at ILS 75 million. The alleged share of the Company in the claimed amount is ILS 15 million. The date for filing a response is April 3, 2017. However, the Company intends, together with the other parties, to motion for a stay.

A hearing on the case is scheduled to July 17, 2017.

Management believes, based on its legal counsel that it is more likely than not that the claim will be rejected.

10) On January 3, 2017, a claim and a motion to certify a class action was filed against the Company.

The plaintiffs claim prohibited discrimination based on marital status in assessing the risk and determining premiums to divorced customers.

The plaintiffs estimate the damage due to excessive premiums at ILS 63,791,494 and the non-monetary damage at ILS 6,368,000, totaling at ILS 70,159,494.

A hearing on the case was scheduled to October 22, 2017.

Management believes, based on its legal counsel, that it is more likely than not that the motion will be rejected.

11) On January 8, 2017, a claim and motion to certify a class action was filed against the Company and another insurance company.

The plaintiffs claim for overcharging from insurance customers and violation of enhanced duties of insurance companies against their customers in relation to the ability to update age and/or years of driving experience when moving into another age and/or driving experience bracket, which entitle to discounted insurance rates.

The amount of claim for all class members in relation to the Company is estimated at NIS 12,250,000. The amount of individual damage claimed from the Company is negligible.

The Company is required to file its response to the motion to certify by April 24, 2017. The plaintiff will be required to file a response to Company arguments by May 24, 2017. A pretrial hearing was scheduled for June 22, 2017.

At this preliminary stage of the lawsuit, the Company's management and its legal counsel are still reviewing the matter. Management believes, based on its legal counsel, that, at this preliminary stage, it is not possible to assess the likelihood that a class action will be certified.

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

Pending applications for approval of legal claims as class actions -	**Number of claims**	**The amount claimed ILS in thousands**
an amount relating to the Company was specified	11	* 175,470

* The above amount of claims includes only the claims for which the Company has an estimate of the total amount of the claim.

Management believes, based on the opinion of its legal counsel, that given the likelihood of these procedures, the financial statements include adequate provisions, where necessary, to cover damages from such claims.

NOTE 31 - CONTINGENT LIABILITES AND ENGAGEMENT IN LEASE AGREEMENTS (continued):

b. Leases:

The Company is engaged in a commercial lease of the real estate in its possession, which is used for Company offices. This lease is non-cancellable and have a lifespan of up to 5 years.

Minimum future lease payment expected to be paid for the non-cancellable operating lease contracts as of December 31 are:

	December 31	
	2016	2015
	ILS in thousands	
First year	4,620	4,620
Second to fifth year	13,860	18,480
	18,480	23,100

NOTE 32 - SUBSEQUENT EVENTS

a. For information about a management offer to distribute a dividend – see note 13c(3).
b. For information about a motion to certify a class action against the Company that was filed after December 31, 2016, see note 31a(10-11) above.

Chapter D: Additional Information

Regulation 25a

Name of company:	**AIG Insurance Co. Ltd.**
No, of company with companies' registrar	51-230488-2
Address:	25 Hasivim St. Kiryat Matalon, Petach Tikva
Telephone no:	03-9272333
Fax no.	03-9272366
Website:	www.aig.co.il
Balance sheet date:	December 31, 2016
Date of financial statements:	March 21, 2017

Regulation 11: List of Investments in Subsidiaries and related Companies as of date of financial statements

None

Regulation 12: Changes in Investments in Subsidiaries and Related Companies in the reported period

None

Regulation 13: Income or Losses of Subsidiaries and Related Companies for the year ended December 31, 2016

None

Regulation 14: List of Loan Balances Extended as of Date of Financial Statements

None. Extending loans is not a principal activity of the company.

Regulation 20: Trade in the Stock Exchange

None. As of date of financial statements there are no securities issued by the company, which are listed in the Stock Exchange.

Regulation 21: Payments to Interested Parties and Senior Office Holders

Set forth below is a breakdown of the payments made by the company and amounts it undertook to pay in the reported year for each of the five office holders receiving the highest salary among office holders who served in their position, regardless of whether they were granted by the company or by others (amounts are denominated in thousands of NIS and excluding payroll tax).

	Salary	Social benefits and related payments	Total
1	4,846	104	4,950
2	885	175	1,060
3	876	150	1,026
4	794	173	967
5	818	138	956

Compensation to CEO

As indicated in paragraph 4.1 to Chapter A (Description of Corporate business) in the periodic report, in 2016, the Compensation to Officers of Financial Corporations Law (Special Permit and Non-Deductibility for Tax Purposes of Exceptional Benefit), 2016. The law sets a pay limit to officers in financial institutions up to ILS 2.5 million, and that beyond that threshold, compensation expenses of a company will not be tax deductible. In addition, it was determined that an employee of a financial corporation will not be able to receive compensation that exceeds 35 times the employment cost of the employee with the lowest salary in the organization. According to this law, in October 2016, the monthly salary of CEO was set to ILS 95,000 plus a bonus that is set according to the officer bonus plan of the Company (see paragraph 4.6c in Chapter A (Description of Corporate Business) in the periodic report) and common benefits (a car, mobile phone and expense reimbursement). This is the cap on the pay to CEO beginning on that date.

Director remuneration

Salary paid to outside directors - ILS 574 thousands, including VAT.

Regulation 21a: Company's controlling shareholders

On June 1, 2016, as part of restructuring of the AIG Global Corporation, all shares of the Company owned by AIG Europe Holdings Limited ("AEHL") were transferred to the ownership of AIG Holding Europe Limited ("AHEL").

As of the date of publication of these financial statements, the controlling shareholder of the company is AEHL, which holds 100% of the ordinary shares of the company. AEHL is a member of American International Group Inc. ("AIG"). AIG is the ultimate parent company or the company.

Regulation 22: Transactions with a controlling shareholder or transactions in the approval of which the controlling shareholder has personal interest, into which the company has entered in the reported year or subsequent to the end of the reported year through the date of publication of this report or which is valid at the time of publication of the report

Transactions covered by Section 270 (4) – exceptions transactions and engagement for obtaining services

See para. 4.5 (reinsurance) in Chapter A – Description of Corporate Business, and note 29 (balances with interested parties and related parties) to the financial statements

Transactions which are not listed in Section 270(4)

No transactions took place with a controlling shareholder or transactions in the approval of which the controlling shareholder has personal interest, which are not listed in Section 270(4).

Exceptional transactions

There were no exceptional transactions with the controlling shareholder or transactions in the approval of which the controlling shareholder had personal interest.

Insignificant transactions

There were no insignificant transactions with the controlling shareholder or transactions in the approval of which the controlling shareholder had personal interest.

Regulation 24: Shares and Convertible Securities Held by an Interested Party in the Company as of date of financial statements

Name of interested party	No. of company with registrar of companies	Name of security	Par value as of 31.12.15	Holding rate		
				In equity	In voting rights	In authority to appoint directors
AIG Europe Holdings Ltd.	Foreign	Ordinary shares	5,730	100%	100%	100%

Regulation 24a: Registered shares capital, issued share capital and convertible securities

The company's registered share capital includes NIS 45,000,100, divided into 45,000,100 ordinary shares of NIS 1 par value each and 100 preferred shares of NIS 1 par value each.

The issued and paid share capital of the company is NIS 5,730, which is distributed into 5,730 ordinary shares of NIS 1 par value each.

Regulation24b: company's shareholders register

For details regarding the sole shareholder of the company, see Regulation 21a to this chapter.

Regulation 26: Company's Directors

1.

Name	Ralph Mucerino (Chairman of the Board)
Passport No.	516514209
Year of birth	1946
Address	175 Water Street – 12th Floor, New York, NY 10038
Nationality	American
Member of Directors Committee	No
Independent director/outside director	No
Employee of the company, subsidiary related company or an interested party?	Yes, President, Distribution Partners & Multinational Clients, U.S Consumer Insurance, AIG
Date of commencement of service as director	13.1.2011
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate, COO of AIU
Relative of another interested party in the company?	No

2.

Name	Robert Quane
Passport No.	548460262
Year of birth	1968
Address	175 Water Street – 26th Floor, New York, NY 10038
Nationality	American
Member of Directors Committee	No
Independent director/outside director	No
Employee of the company, subsidiary related company or an interested party?	Yes, Commercial Property, AIG Inc.
Date of commencement of service as director	27.07.2010
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate , AIG Inc. Head of Global Personal Lines
Relative of another interested party in the company?	No

3.

Name	James Lenton
Passport No.	540160940
Year of birth	1975
Address	London, UK
Nationality	British
Member of Directors Committee	No
Independent director/outside director	No
Employee of the company, subsidiary related company or an interested party?	Yes, Chief Financial Officer , AIG Europe Ltd
Date of commencement of service as director	24.10.13
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate, CPA, Partner in Ernst & Young LLP
Relative of another interested party in the company?	No

On July 31, 2016, James Lenton stepped down as director of the Company.

4.

Name	Neil Minnich
ID No.	452109240
Year of birth	1970
Address	58 Fenchurch Street London EC3M 4AB, England
Nationality	US
Member of Directors Committee	No
Independent director/outside director	No
Employee of the company, subsidiary related company or an interested party?	Yes, Senior Vice President, Head of Accident, Health & Travel, AIG Europe Ltd, AIG
Date of commencement of service as director	10.12.2015
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate, Vice President and Head of Personal Lines UK, AEL
Relative of another interested party in the company?	No

5.

Name	David Klein
ID No.	007256647
Year of birth	1935
Address	30 Jabotinsky St. Kfar Saba
Nationality	Israeli
Member of Directors Committee	Yes. Member of Investments Committee, Compensation Committee and Audit Committee
Independent director/outside director	Yes, investment committee, compensation, audit
Employee of the company, subsidiary related company or an interested party?	No
Date of commencement of service as director	1.4.2011
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	Academic, PhD in Economics, owners of David Klein Financial Consulting Ltd.
Relative of another interested party in the company?	No

6.

Name	Eti Livni
ID No.	003782372
Year of birth	1948
Address	122 Wingate St. Herzliya
Nationality	Israeli
Member of Directors Committee	Yes, Chairperson of Audit Committee, Chairperson of Compensation Committee
Independent director/outside director	Yes, insurance expertise
Employee of the company, subsidiary related company or an interested party?	No
Date of commencement of service as director	26.3.2008
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate, director in the Company for Location and Restitution of Holocaust Victims' Assets Ltd.
Relative of another interested party in the company?	No

7.

Name	Arie Nachmias
ID No.	051604205
Year of birth	1952
Address	1 Hohit St., Giva'at Hasla'im Rosh-HaAyin
Nationality	Israeli
Member of Directors Committee	Yes, Audit Committee, Investments Committee, Compensation Committee
Independent director/outside director	Yes. Has accounting and financial expertise. Has insurance related expertise.
Employee of the company, subsidiary related company or an interested party?	No
Date of commencement of service as director	19.1.2016
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate, BA in Economics Tel Aviv University, M.Sc in Economics & Management Hebrew University, PhD in Management University of Wisconsin–Milwaukee, Head of Masters Degree Program Business Administration Open University, Director in Gal Gemel for Teachers (Provident Fund) Ltd.
Relative of another interested party in the company?	No

8.

Name	Maureen Hackett
ID No.	21909619
Year of birth	1964
Address	175 Water Street, New York, NY 10038
Nationality	US
Member of Directors Committee	No
Independent director/outside director	No
Employee of the company, subsidiary related company or an interested party?	Yes. Head of Individual Segment - Consumer Lines, AIG
Date of commencement of service as director	August 23, 2016
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate. Head of Global Property – Consumer, Executive Vice President' Chief Underwriting Officer, AIG Inc.
Relative of another interested party in the company?	No

9.

Name	Jules Polak
ID No.	026059444
Year of birth	1946
Address	6 Amos St. Ramat Gan
Nationality	Dutch
Member of Directors Committee	Yes. Audit Committee and Compensation Committee
Independent director/outside director	Yes. Has financial and accounting expertise. Has insurance expertise
Employee of the company, subsidiary related company or an interested party?	No
Date of commencement of service as director	March 1, 2017
Education and main occupation during the past 5 years as well as other companies in which he serves as a director	University graduate, CPA, MBA, CEO of Jules Polak Business Management Ltd., Director at IBI Mutual Fund Management (1978) Ltd
Relative of another interested party in the company?	No

Regulation 26a: Senior Office Holders of the Company

1.

Name	Shay Feldman
ID No.	031872245
Year of birth	1974
Position in the company	CEO
Interested party or relative of another office holder or of an interested party in the company?	No
Education and main occupation during the past 5 years	University graduate, BA in Economics and Management (Tel Aviv-Yaffo Academic College), MA in Business Administration and Marketing from Derby University, Senior Vice President Marketing and Personal Insurance EMEA in London
Year of commencement of service	2013

2.

Name	David Rothstein
ID No.	017016973
Year of birth	1958
Position in the company	CFO
Interested party or relative of another office holder or of an interested party in the company?	No
Education and main occupation during the past 5 years	University graduate, CPA
Year of commencement of service	2001

3.

Name	Lior Scheinin
ID No.	028024099
Year of birth	1970
Position in the company	Senior VP Consumer Distribution
Interested party or relative of another office holder or of an interested party in the company?	No
Education and main occupation during the past 5 years	University graduate, BA in Business Administration, VP Personal Insurance
Year of commencement of service	2003

4.

Name	Iris Nachshoni
ID No.	058468414
Year of birth	1963
Position in the company	Chief Information Systems Officer
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate, BA in Computer Science from CUNY NY, VP IT in S. Schestowitz, VP IT in international Mey Eden Group
Year of commencement of service	2012

5.

Name	Yael Nadav
ID No.	028731131
Year of birth	1971
Position in the company	VP Human Resources
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate, MA in Occupational Psychology, VP HR at Tnuva, Senior HR manager at Teva
Year of commencement of service	2016

6.

Name	Nurit Kantor
ID No.	031817356
Year of birth	1974
Position in the company	Senior VP Customers
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate BA and MA in Business Management, VP Customer Service and Sales Bezeq International
Year of commencement of service	2012

7.

Name	Gil Sagiv
ID No.	025469248
Year of birth	1973
Position in the company	VP Marketing
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate, B. Sc Engineering, MBA Business Administration from Tel Aviv University, Chief Marketing Officer and member of management of Kardan Vehicle Ltd. – holder of Avis' franchise in Israel.
Year of commencement of service	2014

8.

Name	Aviram Gavish
ID No.	029312550
Year of birth	1972
Position in the company	VP, Legal, Commercial Insurance and Logistics
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate, lawyer, advocate in England and Wales (in registration process), MA in Commercial Law from the Tel-Aviv University, BA in Law from the Hebrew University of Jerusalem, Director Reinsurance, Ombudsman and Company Secretary in S. Shlomo Insurance Company Ltd.
Year of commencement of service	2012

9.

Name	Olivia Zohar
ID No.	011179322
Year of birth	1970
Position in the company	VP, Risks and Compliance Officer
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate, CPA, MBA, Chief Risks Officer of the Senior Pension Funds
Year of commencement of service	2013

10.

Name	Thomas Lowe
ID No.	327077798
Year of birth	1976
Position in the company	VP, Internal Audit
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	CPA, University graduate, CPA, Senior Manager Internal Audit, Controller, Financial Project Manager
Year of commencement of service	2013

11.

Name	Orna Karni
ID No.	025164567
Year of birth	1973
Position in the company	VP, Manager of life and health insurance lines.
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	B.A – Business Administration, MBA, LL.B, B.A in Law. In the last five years, served as VP Life and Health Insurance in the Company, Head of Life and Health Insurance, Head of Collaborative Initiatives in Clal Insurance Ltd
Year of commencement of service	2014

12.

Name	Yifat Reiter
ID No.	029480548
Year of birth	1972
Position in the company	VP, Head of Personal Injury, Life and Health Insurance
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate. B.A Economics and Financing, MBA, VP Consumer Insurance in the Company
Year of commencement of service	2014

13.

Name	Lee Dagan
ID No.	38345443
Year of birth	1975
Position in the company	VP, Vehicle and Home Insurance
Interested party or relative of another office holder or of an interested party in the company	No
Education and main occupation during the past 5 years	University graduate. B.A Economics and Accounting, MBA, Deputy Supervisor of Capital Markets, Insurance and Savings. VP Professional HQ, Health Division, Clal Insurance Company
Year of commencement of service	2016

Regulation 26b: Number of Independent Signatories as determined by the Company

None

Regulation 27: Auditors of the Company
Kesselman & Kesselman CPAs, 25 Hamered St. Tel-Aviv

To the best of the company's knowledge the auditors, including Mr. Noam Hadar, CPA, who is the engagement partner in the said firm, are not interested parties and/or related to any senior officeholder or interested parties in the company.

Regulation 28: Changes in the Memorandum or Articles of Association of the Company in 2016

None

Regulation 29: Resolutions and Recommendations of the Board of Directors

a. Set forth below are the recommendations of the Board of Directors and the resolutions of the Board of Directors which do not require the approval of a General Meeting:

   1. Payment of dividend (or distribution) as defined in the Companies Law, in any other way, or distribution of bonus shares: For details see note 13 to the financial statements.
   2. Changes to authorized or issued equity of the Company: None.
   3. Changes to the Memorandum or Articles of Association of the Company: None.
   4. Redemption of shares: None.
   5. Early redemption of debentures: None.
   6. Non arm's-length transaction between the company and an interested party thereof, except for a transaction between the Company and a subsidiary thereof. For details see Regulation 22 above.

b. General Meeting resolutions that were taken without being recommended by the Board of Directors. None

c. Resolutions of Special General Meeting.

   1. On February 11, 2016, the Company's General Meeting made the following resolutions: renewal of the liability insurance policy covering Company's office holders and directors and reappointment of Kesselman & Kesselman CPAs as the Company's auditors.

   2. On December 22, 2016, the Company's General Meeting approved the appointment of Ms. Maureen Hackett as a director in the Company's board of directors.

Regulation 29a: Resolutions of the Company

a. Approval of acts under Section 255 to the Companies Law. None

b. An act in accordance with Section 254(a) to the Companies Law, which has not yet been approved. None

c. Transactions that require special approval in accordance with Section 270(1) to the Companies Law and provided that the transaction is an exceptional transaction as defined in the Companies Law; for details see Regulation 22 above.

d. Exemption, insurance or liability to indemnify a office holder as defined in the Companies Law and which is in effect as of the date of publication of the report:

Insurance

The Company entered into an officers' liability insurance policy covering office holders and directors for the period from February 1, 2016 through January 31, 2017. The liability limit is $ 25 million per claim and for the whole insurance period including legal expenses; (but in respect of claims filed in Israel the policy covers legal expenses in excess of the above liability limit to an amount equal to 20% of the said liability limit. The insurance policy was renewed on January 31, 2018 with the same terms and conditions as presented above.

Indemnification

The Company has undertaken in advance to indemnify its office holders in accordance with the wording of the indemnity letters it provided to the office holders. According to the indemnity letters, the Company has undertaken, to the extent allowed by law, to indemnify its office holders for any liability or expense with which he was charged or which he expended in consequence of an act which he/she performed by virtue of holding office in the Company. The accumulated amount of indemnity for all office holders in respect of one or more than one of the event set by the Board of Directors shall not exceed 25% of the Company's equity. The Company has also undertaken to indemnify its office holders for payment which was levied on them as part of payment to a victim of breach; the Company has also undertaken to indemnify its office holders for expenses they accrued as part of a procedure for levying financial sanctions on those office holders, including reasonable legal expenses.

Exemption

As part of an exemption letter issued to its office holders, subject to the provisions of Sections 258-263 to the Companies Law, 1999 and any law that is to replace them, the Company has undertaken to exempt its officers, from all of his/her responsibility for damage caused to the Company, whether directly or indirectly, due to his/her violation of the obligation of caution towards the Company as a result of actions taken in good faith and as part of his/her capacity as office holder in the Company and/or employee of the Company; the exemption will not apply in cases where the obligation of caution was violated intentionally or rashly; nor will the exemption apply if the obligation of caution was violated due to any matter relating to distribution.

AIG Insurance Co. Ltd.

Date: March 21, 2017

Shay Feldman **CEO**	**Ralph Mucerino** **Chairman of the Board**

Chapter E: Actuary Reports

AIG Israel Insurance Company Ltd

GENERAL INSURANCE SECTORS – ACTUARY STATEMENT

AS OF DECEMBER 31, 2016

AIG ISRAEL INSURANCE CO. LTD.

Chapter A - Identity of the actuary

I was requested by AIG Israel Insurance Co. Ltd. to evaluate the provisions listed in Chapter B hereafter in the general insurance sectors for the financial statements ("the provisions") of the insurer AIG Israel Insurance Co. Ltd. at December 31, 2016, as detailed below.

I am a salaried employee of the insurer. I am not an interested party in the insurer nor am I a relative of an interested party of the insurer.

I was appointed to this position on 31.12.2015.

Chapter B - Scope of the actuarial opinion

1. Wording of scope of the actuarial opinion section

1.1 For the purpose of calculating the insurer's provisions, I relied on data that I received from the insurer. My requests for information and data were satisfied adequately for the purpose of evaluating the provisions for financial statements purposes. I reviewed the reasonability and adequacy of the data, including comparing the said data with the data for the year to which the statement refers and the data for previous years.

1.2 Where necessary, my evaluation also relied on data received from other reliable sources. I reviewed the consistency and adequacy of the data and their relevance.

1.3 The actuarial assumptions that I used in my work, as well as the methods for evaluating the provisions specified in section 2 below were determined by me, to the best of my professional judgment, and subject to the instructions, directives and principles specified in section 1 to Chapter C, below.

1.4 To calculate the retention, I asked the entities responsible for the insurer's reinsurance for information concerning the insurer's reinsurance arrangements, the ability to collect claims, and problems with the reinsurers' payment policy. Based on the information that I received, I reviewed the effect and implications of the reinsurance arrangements on the provisions.

1.5 The following matters were also taken into account in my opinion:
The provision that was calculated for the Company's share of the "Pool" (Israel Motor Insurance Pool) was based on an assessment conducted by the Pool's actuary.

1.6 No reserve was taken for the absence of a correlation between the different sectors for the purpose of writing down the total provision for all the sectors included in my evaluation."

2. Data included in the section on the scope of the actuarial opinion

As of December 31, 2016

2.1 Pending Claims

2.1.1 Non-aggregated sectors:

	Gross	Retention
	ILS in thousands	
Motor property	64,063	64,063
Comprehensive home	22,409	18,005
Loss of property	36,996	1,673
Engineering insurance	28,900	636
Compulsory motor	481,222	365,286
Liability employers	56,928	7,460
Third-party liability	138,116	12,280
Product liability	73,933	14,165
Professional liability	189,366	33,654
Other	3,879	397
Total non-aggregated sectors	1,095,811	517,620
Total aggregated sectors	-	-
2.1.2 Total aggregated and non-aggregated sectors	1,095,811	517,620
2.2 Indirect expenses for all sectors	32,854	32,854
2.3 Premium deficiency:		
Motor property	2,465	2,465
Engineering insurance	110	110
Total pending claims, indirect expenses, premium deficiency reserve computed in accordance with actuarial valuation	**1,131,240**	**553,048**

Chapter C – the Opinion

I hereby declare and confirm that in the following sectors, comprehensive flats, motor vehicle insurance – property (owned and third party), motor vehicles (New Version), 1970:

1. I evaluated the insurer's provisions listed in Chapter B in accordance with the instructions, directives and principles set forth below, and all in effect as of the date of the financial statements:

   a. The provisions of the Control of Financial Services (Insurance) Law, 1981, and regulations promulgated thereunder.
   b. Instructions and directives issued by the Supervisor of Insurance;
   c. Supervisor's position regarding calculation of general insurance reserves
   d. Acceptable actuarial principles.

2. After reviewing the data mentioned in Chapter B, I concluded that the data are reasonable and adequate, and that they can be relied on for the purpose of my evaluation.
3. I determined the assumptions and methods used to assess the provisions, to the best of my professional judgment, and in accordance with the instructions, directives and principles specified above.

4. To the best of my knowledge, the provisions specified in Chapter B, section 2.1.1 in respect of the non-aggregated sectors comprehensive flats, property loss, engineering, compulsory motor, employers liability, third party liability, product liability, professional liability and other form an adequate reserve for covering the insurer's commitments in respect of the pending claims, defined above, for each statistical sector listed separately, in effect as of the date of the financial statements.

5. To the best of my knowledge, the total provisions listed in Chapter B, section 2.1.2, form an adequate reserve for covering the insurer's commitments in respect of pending claims in the aggregated and non-aggregated sectors together, in effect as of the date of the financial statements.

6. To the best of my knowledge, the provision specified in Chapter B, section 2.2 forms an adequate reserve for covering the insurer's commitments in respect of indirect expenses to settle the claims in effect as of the date of the financial statements.

7. To the best of my knowledge, the provisions listed in Chapter B, section 2.3, form an adequate reserve for covering the insurer's commitment in respect of a deficit premium at retention level (inasmuch as such deficit premium exists) in the sectors listed, in effect as of the date of the financial statements.

Chapter D – Comments and Clarifications

1. **Comments, clarifications and explanations in connection with the actuary opinion I rendered, to the best of my professional judgment.**

   a. In January 2015 a new Insurance Circular was published - "Actuarial Assessment in General Insurance" - which is designed to enhance the quality of assessment of the reserves for an insurer's liability due to general insurance contracts (hereafter – "insurance reserves), which are an important element in the assessment of an insurer's liability, and to regulate the attachment of the professional opinion of an appointed actuary (hereafter – "the actuary") on these provisions to the financial statements. The circular establishes the scope of the actuarial assessment which the actuary is required to perform, the actuarial report he/she is required to prepare and the statement he/she is required to sign, which must be attached to the financial statements.

   b. In January 2015 the Supervisor published a position paper on "Best Practice for Calculation of Insurance Reserves in General Insurance for Financial Reporting" (hereafter – "the position paper"). The Supervisor's position paper includes, inter alia, explanations of the principles of professionalism, consistency and caution which have not been previously defined in circular 2015-1-1 on Actuarial Valuation in General Insurance. The principle of caution will require the actuary to verify that the valuations made in the liability sectors aim for a probability estimate of 75% at the very least. The Supervisor's position paper also refers to the issue of the discount rate applied to liabilities for best estimate purposes.

   c. In January 2015 a circular was published – "Calculation of Reserves in General Insurance – Update"; in accordance with the this circular, commencing in the financial statements as of December 31, 2015, the reserve in respect of the excess of income over expenses shall not be calculated for the liability insurance sectors and the compulsory vehicle insurance sector.

d. In 2014, the Vinograd Committee was appointed, with the mandate to examine whether the data used by the Israel National Insurance Institute (NII) to calculate benefits for workplace injuries are up-to-date, and whether modifications are needed in life expectancy tables and interest rates used in discounting NII workplace injury benefits. Recommendations of the committee were published in March 2016, and they include, among other things, recommendations for the amendment of National Insurance Regulations (Discounting), 1978 (hereinafter - the discounting regulations) in relation to updating payments according to the current, higher, life expectancy and discounting one-off payments based on a 4-year average in a way detailed in the recommendations, whereas, as long as no such determination is set, interest rate will be set to 2% instead of 3% as indicated by the regulations so far, and that on the backdrop of lower recent interest rates.

   On May 17, 2016, the Amendment to the Discounting Regulations (hereafter – "the Amendment to the Discounting Regulations") was signed by the Minister of Social Affairs, and on June 9, 2016, the Amendment to the Discounting Regulations was published in the official gazette, adopting the recommendations of the Vinograd Committee .

   On September 13, 2016, an amendment to the Amendment of the Discounting Regulations was published in the official gazette, postponing the coming into effect of the Amendment to the Discounting Regulations to September 2017. The Amendment to the Discounting Regulations may result with a decrease in the rate of the discounting interest used in the settlement of bodily damage claims, which may lead to an increase in the premiums of compulsory vehicle insurance.

e. I do not use capitalization interest in the actuary assessment to assess the provisions for pending claims or indirect expenses. It is possible to measure the extent of conservativeness of using a 0% real interest compared with using a risk free capitalization interest including non-liquidity premium:

Effect of risk free interest on capitalization/non-capitalization of provisions for pending claims - gross

Sectors	Best estimate provision before capitalization	Best estimate provision after capitalization	Provision in books	Increment (%)
	ILS in thousands			
Compulsory motor	442,601	435,898	481,222	10.40%
Motor property	60,896	60,613	64,063	5.69%
Comprehensive home insurance	20,391	20,283	22,409	10.48%
Engineering insurance	27,497	27,434	28,900	5.34%
Property	35,201	35,145	36,996	5.27%
Employers' liability	51,800	50,894	56,928	11.86%
Other	3,430	3,317	3,879	16.96%
Product liability	61,817	60,890	73,933	21.42%
Professional liability	167,432	160,455	189,366	18.02%
Third-party liability	125,904	123,882	138,116	11.49%
Total	**996,968**	**978,810**	**1,095,811**	**11.95%**

Effect of risk free interest on capitalization/non-capitalization of provisions for pending claims - retention

Sectors	Best estimate provision before capitalization	Best estimate provision after capitalization	Provision in books	Increment (%)
	ILS in thousands			
Compulsory motor	337,397	333,785	365,286	9.44%
Motor property	60,896	60,613	64,063	5.69%
Comprehensive home insurance	16,383	16,298	18,005	10.47%
Engineering insurance	605	605	636	5.23%
Property	1,592	1,589	1,673	5.27%
Employers' liability	6,788	6,666	7,460	11.91%
Other	351	335	397	18.49%
Product liability	11,844	11,662	14,165	21.46%
Professional liability	29,756	28,502	33,654	18.08%
Third party liability	11,194	11,004	12,280	11.60%
Total	**476,806**	**471,060**	**517,620**	**9.88%**

f. The sensitivity of the conservative amounts is reflected by changing the risk free interest rate used for capitalization (including non-liquidity premium) by 0.5% or 1.0%.

Sensitivity analysis of conservative amounts without capitalization to the risk free interest – ILS in thousands						
Amounts in thousands of ILS	**Provision in books without capitalization**	**Best estimate capitalization: Risk free interest less 1.0%**	**Best estimate capitalization: Risk free interest less 0.5%**	**Best estimate capitalization: Risk free interest**	**Best estimate capitalization: Risk free interest plus 0.5%**	**Best estimate capitalization: Risk free interest plus 1.0%**
All sectors (gross)	1,095,811	1,023,846	1,000,878	978,810	957,595	937,190
Difference in ILS compared with provision without capitalization	-	71,966	94,933	117,001	138,216	158,622
Difference in % compared with provision without capitalization	0.0%	6.6%	8.7%	10.7%	12.6%	14.5%
All sectors (retention)	517,620	488,663	479,709	471,060	462,701	454,619
Difference in ILS compared with provision without capitalization	-	28,957	37,911	46,560	54,919	63,001
Difference in % compared with provision without capitalization	0.0%	5.6%	7.3%	9.0%	10.6%	12.2%

g. The process of assessing the various actuarial provisions involves statistical uncertainty. These assessments are based on certain assumptions which best reflect the information currently available to us. There may be future changes, which will have an effect on these assumptions in terms of legislation, legal rulings and economic and social environments. It is impossible to predict these factors and they may affect the final cost of the claims thus affecting actuarial estimate of the provisions.

2. **Material changes in actuarial assumptions and methods compared with last year's actuarial assessment**

   a. Position of the Supervisor

      As per the circular issued by the Supervisor, dated January 15, 2015 beginning year end 2015, adequate reserve for cover of the liabilities in respect of pending claims in the compulsory and liability sectors shall be interpreted as meaning that it is fairly likely - i.e. a 75% probability at least - that the insurance obligation prescribed will be sufficient to cover the insurer's obligations.

   We have decided to utilize a model that AIG uses globally to stochastically determine reserve variability, which we call the Reserve/Premium Risk Statistical Model ("RPS Model"). We used the same model in the 2015 report. This model can be described as three sub-models:

   1. The Adaptive Reserve Monitoring System Model ("ARMS Model")
   2. The Reserve and Premium Risk – Coefficient of Variation Model ("CV Model")
   3. The Reserve and Premium Risk – Aggregation Model ("Aggregation Model")

   The purpose of the RPS Model is to produce reasonable aggregate estimates of adverse risk or premium risk loss outcomes. The model is statistical in nature. Adverse loss outcomes are generated by developing a stochastic model of individual line of business volatilities and their correlation and dependency across the company.

   We believe our model is complete and considers both variation of random risk and system risk. Our model estimates those by modeling three sources of volatility:

   1) Diversifying process risk: randomness of future outcomes, given a known distribution of possible outcomes.
   2) Parameter risk: Potential error in estimated parameters used to describe the distribution of potential outcomes
   3) Systematic Risk: the risk that calendar year loss trends will change unpredictably in the future.

   Reserve risk and premium risk for each analysis segment is simulated. Coefficient of Variations (standard deviation/mean) for the simulated distributions are derived from the segment analytics previously described.

   Best estimate reserves and expected losses on the unearned premiums were determined by the actuary. Based on the results of the RPS model, a factor was calculated, for each individual segment, to project losses from the mean (best estimate) to the 75th percentile level. These form the basis for the statutory reserves of the company (see also c. below).

   Over the past year I examined my assumptions in relation to external systemic risk. While our model estimates external systemic risk through using historical trends, there may be other external risks that have impact. Therefore, based on assessing a number of additional factors that contribute to the understanding of potential risk factors and based on conversations I had with actuaries, both internal and external, accountants and model developers, I used my best judgment to update my assumptions in related to external systemic risk. My opinion is that the additional reserves that I included in respect of external system risk are quite sufficient.

   The following is an overview of mean, standard deviation, explained variance coefficient and reserves at the 75th percentile level.

AIG Israel Insurance Co. LTD. Best estimate – Retention - ILS in thousands As of December 31, 2016				
	Best estimate of total amount for pending claim settlement	**SD**	**CV**	**75th percentile**
Compulsory motor	273,428	43,791	16%	301,317
Compulsory motor - Pool	63,969	-		63,969
Employers' liability	6,788	1,048	15%	7,460
Motor property	60,896	4,643	8%	64,063
Comprehensive home	16,383	2,189	13%	18,005
Product liability	11,844	3,843	32%	14,165
Professional liability	29,756	6,319	21%	33,654
Loss of property	2,197	238	11%	2,309
Third-party liability	11,194	1,670	15%	12,280
Other	351			397
Total	**476,806**			**517,620**

3. Material changes to provisions described in Chapter B compared to provisions described for the previous reporting period and the reasons for those changes, by sectors

Below is information about provisions by insurance segment as of the 2015 and 2016 year-end and changes in provisions.

The main drivers of change in compulsory motor reserves is the Vinograd Committee, as discussed above, and the impact of this factor on the Company's share in the "Pool", along with an increase of pending claims in the portfolio, including IBNR reserves. The changes in professional liability and product liability lines are mostly due to a negative development in claims in 2016, in respect of previous years.

Comparison of annual actuarial estimate compared with previous years' actuarial estimate - gross			
Sectors	**Reserve as of 31.12.2015**	**Addition as of 31.12.2016**	**Change in reserve**
Compulsory motor	395,905	481,222	85,317
Property motor	47,779	64,063	16,283
Comprehensive home	21,449	22,409	960
Engineering insurance	22,576	28,900	6,323
Property	33,178	36,996	3,818
Employers' liability	48,803	56,928	8,125
Other	3,224	3,879	656
Product liability	58,544	73,933	15,389
Professional liability	117,264	189,366	72,102
Third party liability	137,292	138,116	824
Total	**886,014**	**1,095,811**	**209,798**

Comparison of annual actuarial estimate compared with previous years' actuarial estimate - retention			
Sectors	**Reserve as of 31.12.2015**	**Addition as of 31.12.2016**	**Change in reserve**
Compulsory motor	305,192	365,286	60,095
Property motor	47,779	64,063	16,283
Comprehensive home	17,698	18,005	307
Engineering insurance	451	636	185
Property	1,859	1,673	-186
Employers' liability	6,011	7,460	1,449
Other	403	397	-6
Product liability	10,580	14,165	3,585
Professional liability	19,250	33,654	14,404
Third party liability	12,318	12,280	-38
Total	**421,541**	**517,620**	**96,079**

March 21, 2017	General Insurance Actuary Director	Ernest Segal	
Date	Position	Name of Actuary	Signature

HEALTH INSURANCE SECTOR – ACTUARY STATEMENT

AS OF DECEMBER 31, 2016

AIG ISRAEL INSURANCE CO. LTD.

Chapter A - Identity of the actuary

I was requested by AIG Israel Insurance Co. Ltd. to evaluate the provisions listed in Chapter B hereafter in the health insurance sector for the financial statements ("the provisions") of the insurer AIG Israel Insurance Co. Ltd. at December 31, 2016, as detailed below.

I am a salaried employee of AIG Israel Insurance Co. Ltd. ("the insurer"). I am not an interested party in the insurer nor am I a relative of an interested party of the insurer.

I was appointed to this position on 31.12.2015.

Chapter B - Scope of the actuarial opinion

1. Scope of the actuarial opinion section

a. For the purpose of calculating the insurer's provisions, I relied on data that I received from the insurer. My requests for information and data were satisfied adequately for the purpose of evaluating the provisions for financial statements purposes. I reviewed the reasonability and adequacy of the data, including comparing the said data with the data for the year to which the statement refers and the data for previous years.

b. Where necessary, my evaluation also relied on data received from other reliable sources. I reviewed the consistency and adequacy of the data and their relevance.

c. The actuarial assumptions that I used in my work, as well as the methods for evaluating the provisions specified in section 2 below were determined by me, to the best of my professional judgment, and subject to the instructions, directives and principles specified in section 1 to Chapter C, below.

d. To calculate the retention, I asked the entities responsible for the insurer's reinsurance for information concerning the insurer's reinsurance arrangements, the ability to collect claims, and problems with the reinsurers' payment policy. Based on the information that I received, I reviewed the effect and implications of the reinsurance arrangements on the provisions.

e. The following matters were also taken into account in my opinion:

   1) The provision calculated in respect of incoming businesses (in that regard "**incoming businesses**" as defined in Insurance Business Supervision Regulations (Methods of Calculating Provisions for Future Claims in General Insurance), 1984): an estimate was not calculated since the company does not have business of this type.

   2) The provision that was calculated for co-insurance where the company is not the leading insurer: the company does not have business of this type.

   3) For the "critical illnesses" and "medical expenses-individual" sub-sectors I relied on reserves calculated by the Life Insurance Actuary Director – Ms. Dafna Kaufman.

2. Data included in the section on the scope of the actuarial opinion

1) Provision for pending Claims

a) Sectors for which an actuary provision for pending claims was calculated:

Sub-sector- general insurance	Gross provision	Provision in Retention
	ILS in thousands	
Personal injury – individual	79,996	79,484
Personal injury – group	8,534	8,534
Travel abroad – individual	7,969	7,969
Travel abroad – group	121	121
Critical illness – individual	9,473	8,422
Total reported in life insurance	**106,093**	**104,530**

Sub-sector- life insurance	Gross provision	Provision in retention
	ILS in thousands	
Serious illness – individual	3,724	3,433
Medical expenses – individual	2,415	1,404
Total reported in life insurance	**6,139**	**4,837**

2) Provision for indirect expenses for settlement of claims

Provision for indirect expenses for settlement of claims (gross and retention)		
ILS in thousands		
Type of activity	Health insurance	Life insurance
Individual	6,989	-
Group	621	-
Total	**7,610**	-

3) Provision deriving from conditions of insurance contracts (contract reserve)

In some of the products available in the personal accidents – individual sub-sector, we found that a provision needs to be made which arises from the conditions of the insurance contract.

Sub-sector	Gross provision	Provision in retention
	ILS in thousands	
Personal injury - individual	3,877	3,877

Sub sector	Gross premium deficiency provision	Premium deficiency provision in retention
	ILS in thousands	
Personal injury - group	13	13

4) Provision in respect of profit sharing

No provision was calculated since the company does not have business of this type.

Chapter C – the Opinion

"I hereby declare and confirm that in the following subsectors of health insurance, personal accidents individual and group, critical illness, travel abroad individual and group and medical expenses:

1. I evaluated the insurer's provisions listed in Chapter B in accordance with the instructions, directives and principles set forth below, and in effect as of the date of the financial statements:

   a. The provisions of the Control of Financial Services (Insurance) Law, -1981, and regulations promulgated thereunder.
   b. Instructions and directives issued by the Supervisor of Insurance;
   c. Acceptable actuarial principles.

2. After reviewing the data mentioned in Chapter B, I concluded that the data are reasonable and adequate, and that they can be relied on for the purpose of my evaluation.

3. I determined the assumptions and methods used to assess the provisions, to the best of my professional judgment, and in accordance with the instructions, directives and principles specified above.

4. To the best of my knowledge, the provisions specified in Chapter B form an adequate reserve for covering the insurer's commitments in respect of its liability arising from health insurance contracts included in the health insurance subsectors listed above, in effect as of the date of the financial statements."

Chapter D – Comments and Clarifications

1. A product of group injury - the student product is in run off for over 10 years. This means that the company no longer receives premiums for those insurances but continues to settle claims in respect of past exposure.
2. Position of the Supervisor – As per the circular issued by the Supervisor, dated January 15, 2015, beginning on the 2015 year-end, testing that it is fairly likely that reserves in the compulsory and liability sectors will be sufficient to cover insurer liabilities will be based on an estimate of at least 75% probability.

   The position of the Supervisor does not specifically refer to health insurance segments, but we believe that it should be also applied to those segments.

   We have decided to utilize a model that AIG uses globally to stochastically determine reserve variability, which we call the Reserve/Premium Risk Statistical Model ("RPS Model"). We used the same model in the 2015 report. This model can be described as three sub-models:

   - The Adaptive Reserve Monitoring System Model ("ARMS Model")
   - The Reserve and Premium Risk – Coefficient of Variation Model ("CV Model")
   - The Reserve and Premium Risk – Aggregation Model ("Aggregation Model")

   The purpose of the RPS Model is to produce reasonable aggregate estimates of adverse risk or premium risk loss outcomes. The model is statistical in nature. Adverse loss outcomes are generated by developing a stochastic model of individual line of business volatilities and their correlation and dependency across the company.

We believe our model is complete and considers both variation of random risk and system risk. Our model estimates those by modeling three sources of volatility:

- Diversifying process risk: randomness of future outcomes, given a known distribution of possible outcomes.
- Parameter risk: Potential error in estimated parameters used to describe the distribution of potential outcomes
- Systematic Risk: the risk that calendar year loss trends will change unpredictably in the future.

Reserve risk and premium risk for each analysis segment is simulated. Coefficient of Variations (standard deviation/mean) for the simulated distributions are derived from the segment analytics previously described.

Best estimate reserves and expected losses on the unearned premiums were determined by the actuary. Based on the results of the RPS model, a factor was calculated, for each individual segment, to project losses from the mean (best estimate) to the 75th percentile level. These form the basis for the statutory reserves of the company (see also c. below).

Over the past year I examined my assumptions in relation to external systemic risk. While our model estimates external systemic risk through using historical trends, there may be other external risks that have impact. Therefore, based on assessing a number of additional factors that contribute to the understanding of potential risk factors and based on conversations I had with actuaries, both internal and external, accountants and model developers, I used my best judgment to update my assumptions in related to external systemic risk. My opinion is that the additional reserves that I included in respect of external system risk are quite sufficient.

3. Discount interest rate was used only for calculating provisions arising from insurance contracts. Discount interest was only used to compute the provision deriving from the insurance contract. The interest rate is the ILS risk free interest (linked to the CPI) which was published as of December 31, 2016.

4. I do not discount the reserves; or in other words, I discount them at a real interest of 0%. For comparison purposes, I apply to the reserves a discounting of risk free linked interest, plus illiquidity premium. The comparison makes it possible to measure a further margin for conservatism included in the reserves for pending claims.

   The risk-free, fixed-interest discount rate was set in light of the fact that a considerable portion of the Company's investments are made in government bonds or high-rate corporate bonds.

Effect of risk free interest on discounting/non-discounting of provisions for pending claims – gross

Sectors	Best estimate provision before discounting	Best estimate provision after discounting	Provision made in practice	Increment (%)
	ILS in thousands			
Personal injury – individual	77,316	76,928	79,996	3.99%
Personal injury – group	8,248	8,230	8,534	3.70%
Travel abroad – individual	7,702	7,599	7,969	4.87%
Travel abroad – group	117	116	121	4.55%
Serious illness	9,155	9,123	9,473	3.83%
Total - in health insurance	102,539	101,995	106,093	4.02%
Serious illness – life insurance	3,724	3,712	3,724	0.32%
Medical expenses – life insurance	2,415	2,404	2,415	0.50%
Total reported in life insurance	6,139	6,116	6,139	0.38%

Effect of risk-free interest on discounting/non-discounting of provisions for pending claims – retention

Sectors	Best estimate provision before discounting	Best estimate provision after discounting	Provision made in practice	Increment (%)
	ILS in thousands			
Personal injury – individual	76,821	76,435	79,484	3.99%
Personal injury – group	8,248	8,230	8,534	3.70%
Travel abroad – individual	7,702	7,599	7,969	4.87%
Travel abroad – group	117	116	121	4.55%
Serious illness	8,140	8,111	8,422	3.83%
Total – in health insurance	101,029	100,491	104,530	4.02%
Serious illness – life insurance	3,434	3,422	3,434	0.32%
Medical expenses – life insurance	1,404	1,398	1,404	0.46%
Total reported in life insurance	4,837	4,820	4,837	0.36%

5. The sensitivity of the conservative amounts is reflected by changing the interest rate used for discounting by 0.5% or 1.0%:

Sensitivity analysis of conservativism regarding provisions in the books vs. the best estimate after being discounted based on changes in risk-fee interest – ILS in thousands

Amounts in thousands of ILS	Best estimate provision in books without discounting	Best estimate discounting: Risk free interest less 1.0%	Best estimate discounting: Risk free interest less 0.5%	Best estimate discounting: Risk free interest	Best estimate discounting: Risk free interest plus 0.5%	Best estimate discounting: Risk free interest plus 1.0%
All sectors (gross)	112,232	110,223	109,156	108,111	107,088	106,087
Difference in ILS compared with provision without discounting	-	2,009	3,076	4,121	5,143	6,145
Difference in % compared with provision without discounting	0.0%	1.8%	2.7%	3.7%	4.6%	5.5%
All sectors (retention)	109,368	107,379	106,334	105,311	104,309	103,328
Difference in ILS compared with provision without discounting	-	1,989	3,034	4,057	5,059	6,039
Difference in % compared with provision without discounting	0.0%	1.8%	2.8%	3.7%	4.6%	5.5%

6. The process of assessing the various actuarial provisions involves statistical uncertainty. These assessments are based on certain assumptions which reflect the information currently available to us. There may be future changes, which will have an effect on these assumptions in terms of legislation, legal rulings and economic and social environments. It is impossible to predict these factors and they may affect the final cost of the claims thus affecting actuarial estimate of the provisions.

March 21	Health Insurance Actuary Director	Ernest Segal	
Date	Position	Name of Actuary	Signature

LIFE INSURANCE SECTOR – ACTUARY STATEMENT

As of December 31, 2016

AIG INSURANCE CO. LTD.

Section A.1 - Identity of the actuary

I am a self-employed actuary for AIG Israel Insurance Co. Ltd. I am a full member of the Israel Association of Actuaries (F.IL.A.A) since 1998.

I am not an interested party in the insurer nor am a relative of an interested party.

I was requested by AIG Israel Insurance Co. Ltd. to evaluate the provisions listed in Chapter B below in the life insurance sector for the financial statements ("the provisions") of the insurer AIG Israel Insurance Co. Ltd. at December 31, 2016, as detailed below.

Actuarial calculations in the life insurance segment were performed until September 30, 2016 by the actuary Michal Burger.

Section A.2 - Scope of the actuarial opinion

1. The actuarial opinion

1.1 For the purpose of calculating the insurer's provisions, I relied on data that I received from the insurer. My requests for information and data were satisfied adequately for the purpose of evaluating the provisions for financial statements purposes. I reviewed the reasonability and adequacy of the data, including comparing the said data with the data for the year to which the statement refers and the data for previous years.

1.2 Where necessary, my evaluation also relied on data received from other reliable sources. I reviewed the consistency and adequacy of the data and their relevance.

1.3 The actuarial assumptions that I used in my work, as well as the methods for evaluating the provisions specified below were determined by me, to the best of my professional judgment, and subject to the instructions, directives and principles specified in section A.3 below.

1.4 To calculate the retention, I asked the entities responsible for the insurer's reinsurance for information concerning the insurer's reinsurance arrangements, the ability to collect claims, and problems with the reinsurers' payment policy. Based on the information that I received, I reviewed the effect and implications of the reinsurance arrangements on the provisions. I would like to indicate that the AIG Israel's life insurance proportional reinsurers are not part of the global AIG Corporation.

1.5 The following matters were also taken into account in my opinion:

1) The provision calculated in respect of incoming businesses was calculated by the actuary (in that regard "incoming businesses" as defined in Insurance Business Supervision Regulations (Methods of Calculating Provisions for Future Claims in General Insurance), 1984.

2) As of the date of this report, in segments relevant to this opinion, no joint insurance policies exist where the Company is the leading insurer.

2. Amounts of provisions

1. Provisions for pending claims (claims which have taken place buy have not yet been fully paid, whether approved or not) as well as the direct and indirect expenses arising there from (including provision for claims which have not yet been reported to the insurer):

Sector	Gross provision (NIS thousands)*	Retention provision (NIS thousands)*
Life insurance	19,284	14,875
Disability permanently	13,004	9,549
Disability from accident	17,156	11,544
Unemployment	266	133
Mortality from accident	459	318
Total life individual	50,169	36,419
Total life group	0	0

*** Excluding health insurance**

2. Provision (reserve) arising from terms of a separate life insurance contract:

a. The Company does not have plans on accrual basis.
b. The Company does not have claims that are paid as allowances/annuities
c. The Company does not have policies that provide profit sharing.
d. Complementary amount arising from testing reserve appropriateness – no need was identified for such complementary amount.
e. The company has insurance policies where some of the premium collected in the early years of the contract is designed to provide coverage at a later date – set forth below are the provisions in respect of fixed premium:

Sector	Gross provision (thousands of NIS)	Retention provision (thousands of NIS)
Life individual	683	683

f. Additional provisions for policies with non-monthly premium install installments, for which unearned premium reserve is calculated:

Sector	Gross provision (thousands of NIS)	Retention provision (thousands of NIS)
Life individual	74	60

3. Details on changes in provisions

Below is the amount of changes in provisions (in thousands of NIS) at both gross and retention levels, as follows:

1) For policies that came into effect after the end of the reported period of the last financial statements – the adjustment amount of the provisions – arising from the difference between the premium basic assumptions and the provision basic assumptions – no such adjustment was required.

2) For policies which came into effect before the end of the reported period of the last financial statements – the adjustment amount of the provisions – arising from changes in premiums, methods or the level of premium that is expected to be collected and other adjustments – no such adjustments were required.

Section A.3 – the Opinion

I hereby declare and confirm that in the life insurance sector:

1. I evaluated the insurer's provisions listed in Section A.2 above in accordance with the instructions, directives and principles set forth below, and in effect as of the date of the financial statements:

   a. The provisions of the Control of Financial Services (Insurance) Law, -1981, and regulations promulgated thereunder.
   b. Instructions and directives issued by the Supervisor of Insurance;
   c. Acceptable actuarial principles.

2. After reviewing the data mentioned in Chapter A.2, I concluded that the data are reasonable and adequate, and that they can be relied on for the purpose of my evaluation.

3. I determined the assumptions and methods used to assess the provisions, to the best of my professional judgment, and in accordance with the instructions, directives and principles specified above.

4. To the best of my knowledge, the provisions specified in Section A.2 form an adequate reserve for covering the insurer's commitments in respect of its liability arising from life insurance contracts, in effect as of the date of the financial statements.

Section A.4 – Comments and Clarifications

a. The types of coverage included in this report

1) Coverage for the event of death (risk, mortgage risk)
2) Coverage for total and permanent disability
3) Coverage for accident-caused disability
4) Coverage for accident-caused death
5) Coverage for unemployment

Coverage for serious illness and health services not covered by basic government services are included in the actuarial report for the general segment.

b. Types of reserves and assumptions

In terms of pending claims, the company's life insurance portfolio is very similar to the personal accidents insurance portfolio. All payments made to the insured are compensation where an insurance event takes place. The insurance amounts are paid as a one-off payment except for unemployment allowance insurance under which an allowance is paid for a period of up to a year. Therefore, it is required to validate that the claims experience is examined in accordance with generally acceptable actuarial principles, if the claims experience allows it.

IBNR provisions in life insurance for insurance events outstanding in the Company, as is usually common in insurance companies, is based on holding a rate of premium according to reporting gaps between the insurance event and opening a claim. The amount of premium is irrelevant. If the premium is not priced correctly, then the provision is deficient. If the premium is priced correctly, then this premium method is too conservative, because it also includes expenses and profit factors, and additionally, it does not account for claims that have already been reported. This method totally disregard a number of basic factors such as incidence of claims, claim severity, claims already reported in practice (reported earlier than the average).

In light of the above I decided to adopt the "triangles methods", which are methods that follow up the development of claims over time and which make it possible to estimate pending and unreported claims in accordance with past rates of paid claims or known claims (paid+pending).

c. Statistical and actuarial uncertainty

There is statistical uncertainty in the process of estimating the various actuarial reserves. These estimates are based on certain assumptions and these assumptions best reflect the things that are currently known to us. There may be future changes in the legal, judicial, social and economic environment that will have an effect on these assumptions. These changes may have an unpredictable effect on the total future actuarial reserves.

d. Exposure to future developments and changes

Changes and developments may occur in conditions in the Israeli life insurance market, following regulatory changes, court rulings, technological developments and changes in social and environmental conditions. Those factors may not be predicted in advance, and may have impact on final cost of claims, as well as the actuarial estimate for provisions.

e. Reconciliation of appendix data to the financial statements

The tables in the above appendices were prepared according to the guidelines of the Supervisor, and the composition of the data therein may not necessarily correspond to the information in the Company's financial statements and notes.

March 21, 2017	Life Insurance Actuary Director	Dafna Kaufman F.IL.A.A	
Date	Position	Name of Actuary	Signature