# B Communications Ltd.

# Consolidated Financial Statements

# As at December 31, 2019

**Consolidated Financial Statements**

**Contents**

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## Auditors' Report to the Shareholders of B Communications Ltd.

We have audited the accompanying consolidated statements of financial position of B Communications Ltd (“the Company”) as of December 31, 2019, 2018 and January 1, 2018, and the consolidated statements of profit or loss, comprehensive income, changes in equity and cash flows for each of the three years in the period ended December 31, 2019. These financial statements are the responsibility of the Company's board of directors and management. Our responsibility is to express an opinion on these financial statements based on our audit.

We did not audit the financial statements of certain consolidated subsidiaries, whose assets included in consolidation constitute approximately 1% of total consolidated assets as of December 31, 2019, 2018 and January 1, 2018, respectively, and whose revenues included in consolidation constitute approximately 1% of total consolidated revenues for each of the years ended December 31, 2019, 2018 and 2017. The financial statements of those companies were audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based on the reports of the other auditors.

We conducted our audit in accordance with generally accepted auditing standards in Israel, including standards prescribed by the Auditors Regulations (Auditor’s Mode of Performance), 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 board of directors and management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Company and its subsidiaries as of December 31, 2019, 2018 and January 1, 2018, and the results of their operations, changes in equity and their cash flows for each of the three years in the period ended December 31, 2019 in conformity with International Financial Reporting Standards (IFRS) and with the provisions of the Securities Regulations (Annual Financial Statements), 2010.

Without qualifying our above opinion, we draw attention to that mentioned in Note 1 regarding an investigation of the Securities Authority of alleged violations of the Securities Law and Penal Law with respect to, inter alia, transactions relating to the former controlling shareholder and the investigation file being handed over to the State Attorney Office, and to that mentioned in that note regarding indictment of the Company's former controlling shareholder for various offences including, inter alia, bribery and inclusion of misleading information in an immediate report. As mentioned in the aforesaid note, at this time the Bezeq Group is unable to assess the effects of the investigations, the findings, and their results on the Bezeq Group, and on the financial statements and the estimates used in their preparation, if any.

Furthermore, without qualifying our above opinion, we draw attention to that mentioned in Note 2.I to the financial statements regarding adjustment by way of restatement of the consolidated financial statements as of December 31, 2019, 2018 and January 1, 2018 and for each of the three years in the period ended December 31, 2019, in order to retroactively reflect the effect of correcting the mistake in the calculation of balances of assets and liabilities, and regarding the Bezeq Group still examining the source of the discrepancies and the possibility of additional discrepancies being discovered following the work of the external specialist assisting it. The Company anticipates that these discrepancies, if at all, will not have a material effect on the consolidated financial statements.

In addition, without qualifying our opinion, we draw attention to Note 22 regarding lawsuits filed against the Group which cannot yet be assessed or the exposure in respect thereof cannot yet be calculated.

This opinion replaces our previous opinion rendered by us on April 23, 2020 in connection with the aforesaid financial statements before their restatement.

Somekh Chaikin
Certified Public Accountants (Isr.)

December 21, 2020

## Consolidated Statements of Financial Position as of

**(In millions)**

| | Note | January, 1 2018 Restated NIS | December, 31 2018 Restated NIS | December, 31 2019 Restated NIS |
|---|---|---|---|---|
| **Current assets** | | | | |
| Cash and cash equivalents | 5 | 2,386 | 1,104 | **814** |
| Restricted cash | 15C | - | - | **39** |
| Investments | 6 | 596 | 1,780 | **1,241** |
| Trade receivables, net | 7 | *1,931 | *1,775 | ***1,677** |
| Other receivables | 7 | *335 | *286 | ***342** |
| Assets held for sale | | - | - | **43** |
| Inventory | 3.10 | 125 | 97 | ***96** |
| **Total current assets** | | 5,373 | 5,042 | **4,252** |
| **Non-current assets** | | | | |
| Long-term trade and other receivables | 7 | 493 | 470 | **477** |
| Property, plant and equipment | 8 | 6,940 | 6,313 | ***,** 5,964** |
| Intangible assets | 9 | *5,853 | *4,210 | ***,** 3,163** |
| Deferred expenses and non-current investments | 10 | *570 | *515 | ***,** 340** |
| Broadcasting rights, net of rights exercised | 11 | 454 | 60 | **59** |
| Rights of use assets | 14 | 1,520 | 1,504 | ***1,217** |
| Deferred tax assets | 21 | 1,019 | 1,205 | ***81** |
| Investment property | 13 | - | 64 | **-** |
| **Total non-current assets** | | 16,849 | 14,341 | **11,301** |
| **Total assets** | | 22,222 | 19,383 | **15,553** |

* Restated. See Note 2.I.

** Reclassified.

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

## Consolidated Statements of Financial Position as of (cont'd)

**(In millions)**

| | Note | January, 1 2018 Restated NIS | December, 31 2018 Restated NIS | December, 31 2019 Restated NIS |
|---|---|---|---|---|
| **Current liabilities** | | | | |
| Bank loans and debentures | 15 | 1,858 | 3,997 | **1,007** |
| Leases liabilities | 14 | 393 | 445 | **416** |
| Trade and other payables | 16 | *1,867 | *1,867 | ***1,616** |
| Current tax liabilities | 21 | 160 | 8 | ****11** |
| Provisions | 17 | 94 | 175 | **125** |
| Employee benefits | 20 | 280 | 581 | **654** |
| **Total current liabilities** | | 4,652 | 7,073 | **3,829** |
| **Non-current liabilities** | | | | |
| Bank loans and debentures | 15 | 12,437 | 9,637 | **10,412** |
| Leases liabilities | 14 | 1,142 | 1,106 | **969** |
| Employee benefits | 20 | 272 | 445 | **356** |
| Other liabilities | | 234 | 175 | **139** |
| Provisions | 17 | 40 | 38 | **49** |
| Deferred tax liabilities | 21 | 459 | 302 | **237** |
| **Total non-current liabilities** | | 14,584 | 11,703 | **12,162** |
| **Total liabilities** | | 19,236 | 18,776 | **15,991** |
| **Equity (Deficit)** | 25 | | | |
| Attributable to shareholders of the company | | *1,229 | *174 | ***(241)** |
| Non-controlling interests | | *1,757 | *433 | ***(197)** |
| **Total equity (deficit)** | | 2,986 | 607 | **(438)** |
| **Total liabilities and equity (deficit)** | | 22,222 | 19,383 | **15,553** |

* Restated. See Note 2.I.

** Reclassified.

Date of approval of the financial statements: December 21, 2020

| /s/ Darren Glatt | /s/ Tomer Raved | /s/ Itzik Tadmor |
|---|---|---|
| Chairman of the board | CEO | CFO |

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

## Consolidated Statements of Income for the Year Ended December 31

**(In millions, except per share data)**

| | Note | 2017 Restated NIS | 2018 Restated NIS | 2019 Restated NIS |
|---|---|---|---|---|
| **Revenues** | 26 | 9,789 | 9,321 | **8,929** |
| **Costs and expenses** | | | | |
| Depreciation, amortization, and impairment | | 2,117 | 2,388 | **2,064** |
| Salaries | 27 | 2,007 | 1,995 | **1,937** |
| General and operating expenses | 28 | *3,917 | *3,428 | ***3,321** |
| Impairment losses | 9 | 129 | *2,324 | ***1,340** |
| Other operating expenses (income) | 29 | 20 | 635 | **(188)** |
| | | 8,190 | 10,770 | **8,474** |
| **Operating profit (loss)** | | 1,599 | (1,449) | **455** |
| **Financing expenses (income)** | | | | |
| Finance expenses | | 586 | 620 | **738** |
| Finance income | 15 | (69) | (89) | **(266)** |
| **Financing expenses, net** | 30 | 517 | 531 | **472** |
| **Profit (loss) after financing expenses, net** | | 1,082 | (1,980) | **(17)** |
| Share of loss in equity-accounted investee | | 5 | 3 | **2** |
| **Profit (loss) before income tax** | | 1,077 | (1,983) | **(19)** |
| Income tax expenses (benefit) | 21 | 347 | *(67) | ***1,441** |
| **Net profit (loss) for the year** | | 730 | (1,916) | **(1,460)** |
| **Profit (loss) attributable to:** | | | | |
| Shareholders of the company | | *75 | *(1,066) | ***(853)** |
| Non-controlling interests | | *655 | *(850) | ***(607)** |
| **Net profit (loss) for the year** | | 730 | (1,916) | **(1,460)** |
| **Earnings (loss) per share** | 31 | | | |
| Basic | | *2.51 | *(36.5) | ***(19.7)** |
| Diluted | | *2.51 | *(36.5) | ***(19.7)** |

*Restated. See Note 2.I.

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

## Consolidated Statements of Comprehensive Income for the Year Ended December 31

**(In millions)**

| | 2017 | 2018 | 2019 |
|---|---|---|---|
| | Restated | Restated | Restated |
| | NIS | NIS | NIS |
| **Net profit (loss) for the year** | *730 | *(1,916) | ***(1,460)** |
| Items of comprehensive profit (loss), net of tax | (8) | 42 | **(32)** |
| **Total comprehensive profit (loss) for the year** | 722 | (1,874) | **(1,492)** |
| **Attributable to:** | | | |
| Shareholders of the Company | *73 | *(1,055) | ***(862)** |
| Non-controlling interests | *649 | *(819) | ***(630)** |
| **Total comprehensive profit (loss) for the year** | 722 | (1,874) | **(1,492)** |

* Restated. See Note 2.I.

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

## Consolidated Statements of Changes in Equity

**(In millions except share data)**

| | Attributable to shareholders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share capital | | | | | | | | |
| | Number of Shares [(1)] | Amount | Share premium | Treasury Shares | Other reserves | Retained earnings | Total | Non-Controlling interests | Total equity |
| | | | | | | Restated | Restated | Restated | Restated |
| | NIS 0.1 par value | NIS | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| **Balance as at January 1, 2017** | 29,889,045 | 3 | 1,057 | (**) | (46) | *142 | 1,156 | *2,056 | 3,212 |
| **Changes during 2017:** | | | | | | | | | |
| Dividends to non-controlling interests | - | - | - | - | - | - | - | (948) | (948) |
| Other comprehensive loss, net of tax | - | - | - | - | 1 | (3) | (2) | (6) | (8) |
| Net profit for the year | - | - | - | - | - | *75 | 75 | *655 | 730 |
| Comprehensive income for the year | - | - | - | - | 1 | 72 | 73 | 649 | 722 |
| **Balance as at December 31, 2017** | 29,889,045 | 3 | 1,057 | (**) | (45) | 214 | 1,229 | 1,757 | 2,986 |

* Restated. See Note 2.I.

** Represents an amount less than NIS 1.

(1) Net of treasury shares.

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

## Consolidated Statements of Changes in Equity

**(In millions except share data)**

| | Attributable to shareholders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share capital | | | | | | | | |
| | Number of Shares [(1)] | Amount | Share premium | Treasury Shares | Other reserves | Retained earnings (deficit) | Total | Non-Controlling interests | Total equity |
| | | | | | | Restated | Restated | Restated | Restated |
| | NIS 0.1 par value | NIS | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| ***Balance as at January 1, 2018** | 29,889,045 | 3 | 1,057 | (**) | (45) | *214 | 1,229 | *1,757 | 2,986 |
| **Changes during 2018:** | | | | | | | | | |
| Dividends to non-controlling interests | - | - | - | - | - | - | - | (505) | (505) |
| Other comprehensive profit, net of tax | - | - | - | - | 7 | 4 | 11 | 31 | 42 |
| Net profit (loss) for the year | - | - | - | - | - | *(1,066) | (1,066) | *(850) | (1,916) |
| Comprehensive profit (loss) for the year | - | - | - | - | 7 | (1,062) | (1,055) | (819) | (1,874) |
| **Balance as at December 31, 2018** | 29,889,045 | 3 | 1,057 | (**) | (38) | (848) | 174 | 433 | 607 |

* Restated. See Note 2.I.

** Represents an amount less than NIS 1.

(1) Net of treasury shares.

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

## Consolidated Statements of Changes in Equity (Deficit)

**(In millions except share data)**

| | Attributable to shareholders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share capital | | | | | | | | |
| | Number of Shares [1] | Amount | Share premium | Treasury Shares | Other reserves | Deficit | Total | Non-Controlling interests | Total equity (deficit) |
| | | | | | | Restated | Restated | Restated | Restated |
| | NIS 0.1 par value | NIS | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| **Balance as at January 1, 2019** | **29,889,045** | **3** | **1,057** | **(**)** | **(38)** | ***(848)** | **174** | ***433** | **607** |
| **Changes during 2019:** | | | | | | | | | |
| Issuance of ordinary shares, see Note 25 | **86,427,518** | **9** | **438** | **-** | **-** | **-** | **447** | **-** | **447** |
| Other comprehensive loss, net of tax | **-** | **-** | **-** | **-** | **-** | **(9)** | **(9)** | **(23)** | **(32)** |
| Loss for the year | | | **-** | **-** | **-** | ***(853)** | **(853)** | ***(607)** | **(1,460)** |
| Comprehensive loss for the year | **-** | **-** | **-** | **-** | **-** | **(862)** | **(862)** | **(630)** | **(1,492)** |
| **Balance as at December 31, 2019** | **116,316,563** | **12** | **1,495** | **(**)** | **(38)** | **(1,710)** | **(241)** | **(197)** | **(438)** |

* Restated. See Note 2.I.

** Represents an amount less than NIS 1.

[1] Net of treasury shares.

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

## Consolidated Statements of Cash Flows for the Year Ended December 31

**(In millions)**

| | 2017 | 2018 | 2019 |
|---|---|---|---|
| | Restated | Restated | Restated |
| | NIS | NIS | NIS |
| **Cash flows from operating activities** | | | |
| Net profit (loss) for the year | *730 | *(1,916) | ***(1,460)** |
| Adjustments: | | | |
| Depreciation, amortization, and impairment | 2,117 | 2,388 | **2,064** |
| Loss from impairment of assets | 129 | *2,324 | ***1,340** |
| Share of loss of equity accounted investees | 5 | 3 | **2** |
| Finance expenses, net | 525 | 541 | **416** |
| Capital gain, net | (27) | (13) | **(475)** |
| Income tax expenses | 347 | *(67) | ***1,441** |
| Change in inventory | (35) | (5) | ***(19)** |
| Change in trade and other receivables | *207 | *266 | ***105** |
| Change in trade and other payables | *14 | *(138) | ***(77)** |
| Changes in provisions | 15 | 81 | **(49)** |
| Changes in employee benefits | *(33) | 489 | **(50)** |
| Change in other liabilities | (34) | - | **(8)** |
| Net income tax paid | (473) | (467) | **(325)** |
| **Net cash provided by operating activities** | 3,487 | 3,486 | **2,905** |
| **Cash flows from investing activities** | | | |
| Purchase of property, plant, and equipment | (1,131) | (1,216) | **(1,095)** |
| Investment in intangible assets and deferred expenses | (399) | (390) | **(382)** |
| Proceeds from the sale of PP&E and investment property | 98 | 315 | **404** |
| Change in investments, net | 301 | (1,168) | **569** |
| Net deposits to restricted cash | - | - | **(39)** |
| Tax payments regarding sale of investment property | - | (201) | **(69)** |
| Other | 3 | 42 | **35** |
| **Net cash used in investing activities** | (1,128) | (2,618) | **(577)** |

* Restated. See Note 2.I.

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

## Consolidated Statements of Cash Flows for the Year Ended December 31 (cont'd)

**(In millions)**

| | 2017 Restated NIS | 2018 Restated NIS | 2019 Restated NIS |
|---|---|---|---|
| **Cash flows from financing activities** | | | |
| Proceeds from issuance of debentures and loans received | 2,635 | 1,139 | **2,275** |
| Repayment of debentures and loans | (1,813) | (1,793) | **(4,287)** |
| Interest paid | (537) | (523) | **(496)** |
| Dividends paid by Bezeq to non-controlling interests | (948) | (505) | **-** |
| Payments of principal and interest for leases | - | (422) | **(414)** |
| Proceeds from issuance of shares, net | - | - | **447** |
| Costs for early repayment of loans and debentures | - | - | **(93)** |
| Payments to Eurocom DBS | (61) | - | **-** |
| Others | (11) | (46) | **(50)** |
| **Net cash used in financing Activities** | (735) | (2,150) | **(2,618)** |
| **Net increase (decrease) in cash and cash equivalents** | 1,624 | (1,282) | **(290)** |
| Cash and cash equivalents as at the beginning of the year | 762 | 2,386 | **1,104** |
| **Cash and cash equivalents as at the end of the year** | 2,386 | 1,104 | **814** |

* Restated. See Note 2.I.

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

(All amounts are in millions except where otherwise stated)

## Note 1 - General

### 1. Reporting Entity

B Communications Ltd. (the "Company") is a company incorporated and domiciled in Israel and its official address is 144 Menachem Begin Road, Tel-Aviv 6492102, Israel. The consolidated financial statements of the Company as at and for the year ended December 31, 2019 include the accounts of the Company and its subsidiaries.

It should be noted that these consolidated financial statements are restating the Group's financial statements as of December 31, 2019, which were originally approved by its board of directors on April 23, 2020 as explained in notes 2A and 2I hereafter.

On April 14, 2010, the Company completed the acquisition of 30.44% of the outstanding shares of Bezeq - The Israel Telecommunications Corp. Limited ("Bezeq") and became the controlling shareholder of Bezeq. Bezeq's ordinary shares are registered for trade on the Tel Aviv Stock Exchange.

On February 1, 2016, the Company sold 115,500,000 shares of Bezeq (4.18% of the outstanding shares of Bezeq) for NIS 8.5 per share or NIS 978, net of transaction costs. The Company retained a 26.34% ownership interest in Bezeq, following the closing of the transaction. For more information relating to the Company's control over Bezeq, see Note 12D.

The ordinary shares of the Company are registered for trade on the Tel Aviv Stock Exchange and were registered for trade on the NASDAQ Global Select Market until September 2020 (see note 33).

On December 2, 2019, Searchlight Capital Partners, through its wholly owned entity, Searchlight II BZQ L.P ("Searchlight"), and the Fuhrer family, through its wholly owned entity, T.N.R Investments Ltd. ("Fuhrer Group") completed the acquisition of majority control of the Company such that Searchlight owns 60.18% of and the Fuhrer Group owns 11.39% of the outstanding and issues ordinary shares of the Company (the "Searchlight-Fuhrer Transaction"), respectively.

The Company and its new controlling shareholders received all necessary approvals for the Searchlight-Fuhrer Transaction including approvals from the Israeli Antitrust Authority, Insolvency Court and Ministry of Communications. On November 11th, Searchlight and the Fuhrer Group received their Control Permits from the Minister of Communications.

The Searchlight-Fuhrer Transaction included the purchase by Searchlight and the Fuhrer Group of all of Internet Gold's ("Internet Gold – Golden Line Ltd.") shares in the Company for NIS 225 and an equity investment of NIS 267 in the Company in consideration for newly issued ordinary shares. In addition, Internet Gold invested NIS 310 for NIS 310 par value of newly issued Series C Debentures of the Company and NIS 35 in for 8,383,234 newly ordinary shares of the Company. Other public shareholders invested an additional NIS 28 as part of an ordinary shares rights issuance which was part of the transaction.

As part of the Searchlight-Fuhrer Transaction, the Company issued NIS 100 of new Series E Debentures and NIS 58 of new Series D Debentures. The Company fully redeemed its Series B Debentures as well as repaid NIS 614 of its Series C Debentures, please refer to Note 15.

(All amounts are in millions except where otherwise stated)

## Note 1 - General (cont'd)

### 2. Investigation of the Israel Securities Authority and the Police Force

On June 20, 2017, the Israel Securities Authority ("the ISA") began an open investigation ("the Investigation"), which included searches and seizure of documents at the offices of Bezeq and DBS.

As part of the Investigation, the former chairman of Bezeq's Board of Directors, the former CEO of Bezeq, the former CEO and CFO of DBS, and to the best of Bezeq 's knowledge, other senior officers and officers in Bezeq Group were questioned ("the Parties under Investigation").

On November 6, 2017, the ISA issued a press release regarding the completion of the Investigation and the transfer of the Investigation file to the Tel-Aviv District Attorney (Taxation and Economics). In accordance with the notice, the ISA concluded that there is prima facie evidence establishing the involvement of the main suspects in the case in a number of offenses. It should be noted that in this context, on November 20, 2017, Bezeq and DBS received a "letter of notice to the suspect" according to which the investigation file for investigating Bezeq and DBS as suspects was transferred to the Prosecutor's Office for review.

In addition, according to the Prosecutor's Notice, the latter informed Bezeq's former CEO and the former adviser to Bezeq Group that it is considering bringing charges against them, subject to a hearing, for offenses of fraud and breach of trust in their dealings with the former Director General of the Ministry of Communications. In this connection, the former CEO is also suspected of a reporting offense under the Israel Securities Law and obstruction of justice. In addition, according to the Prosecutor's Notice, the former CEO and former controlling shareholder are also accused of reporting offenses under the Israel Securities Law and of obstruction of justice.

In addition, on February 18, 2018, a joint press release by the ISA and the Israel Police stated that in view of the evidence the ISA found in its investigation, which raised suspicions of additional offenses, a new joint investigation was opened on that date by investigators of the ISA and the Unit for Combating Economic Crime at Lahav 433 ("the New Investigation"), and a number of suspects were arrested, including senior officers of Bezeq Group (including Bezeq's controlling shareholder in the period relevant to the investigation, and the former CEO of Bezeq), who were released under restrictive conditions.

On December 2, 2018, a spokesperson for the Israel Police and the ISA announced that the Investigation had been concluded ("the Announcement"). According to the Announcement, the Investigation case refers mainly to the alleged suspicion of bribery, fraud, and breach of trust by the controlling shareholder (at the times relevant to the Investigation) in Bezeq Group and the Walla! website. With the conclusion of the Investigation, the Israel Police and the ISA Authority believe that there is sufficient evidence in the case to substantiate the suspicions against the main parties involved in the affair, some of whom are former officers of Bezeq (the former controlling shareholder of Bezeq, the former CEO of Bezeq, a former director in Bezeq, and the former VP of strategy and business development of the Bezeq Group).

It should be noted that on February 28, 2019, suspicions against Prime Minister Benjamin Netanyahu were published.

The suspicions include reference to the matters investigated in the New Investigation, including suspicions of exercising authority by Benjamin Netanyahu to promote matters relating to the business of a former controlling shareholder in Bezeq and to his economic interests and the economic interests of the Bezeq Group.

(All amounts are in millions except where otherwise stated)

## Note 1 - General (cont'd)

On September 1, 2019, the Taxation and Economic Division of the Prosecutor's Office announced that it had notified the former controlling shareholder of Bezeq, and other senior officers of Bezeq and of DBS in the relevant period, that it was considering filing an indictment against them subject to a hearing, on suspicion of offenses of serious fraud, breach of trust, and reporting offenses under the Israel Securities Law ("the Prosecutor's Notice"). According to the Prosecutor's Notice, the hearing letter refers to suspicions in various cases, including impairing the work of the independent committee of Bezeq's Board of Directors that was addressing Bezeq's acquisition of DBS shares (for information about the transaction, see Note 12B), fraud related to the receipt of compensation in Bezeq's acquisition of DBS, and impairing the work of the independent committee of Bezeq's Board of Directors that was addressing the agreement between DBS and Spacecom Ltd. ("Spacecom").

On January 28, 2020, an indictment was filed at the Jerusalem district court against the former controlling shareholder in Bezeq, for various offenses, including bribery and misleading information in an immediate report.

Following the opening of the investigations, several civil legal proceedings were opened against Bezeq, former officers of Bezeq, and companies in Bezeq Group of the former controlling shareholder in Bezeq, including motions for certification of a class action and petitions for disclosure prior to filing a motion for certification of a derivative claim. For further information, see Note 22.

Bezeq does not have full information about the investigations, their content, the materials and the evidence in the possession of the legal authorities. Accordingly, Bezeq is unable to assess the effects of the investigations, their findings, and their results on it, as well as on the financial statements, and on the estimates used in the preparation of their financial statements, if any. Once the constraints on carrying out reviews and controls related to issues that arose in the Investigations are lifted, the review of all matters related to subjects that arose in the Investigations will be completed as required.

### 3. Private Investigation by the SEC

In March 2019, the Company was informed by Internet Gold of the issuance of a Formal Order of Private Investigation by the SEC of Internet Gold (no longer a controlling shareholder of the Company). The Formal Order authorizes an investigation of possible violations of the Foreign Corrupt Practices Act with respect to the facts uncovered in the criminal investigations in Israel.

### 4. Definitions

In these financial statements-

1. The Company: B Communications Ltd.
2. The Group: B Communications Ltd. and its subsidiaries, as listed in Note 12.A.
3. Bezeq: Bezeq - The Israel Telecommunication Corp., Limited.
4. Bezeq Group: Bezeq The Israel Telecommunication Corp. Limited and its subsidiaries, as listed in Note 12A.
5. DBS: DBS Satellite Services (1998) Ltd.

(All amounts are in millions except where otherwise stated)

## Note 1 - General (cont'd)

6. Subsidiaries: Companies whose financial statements are fully consolidated, directly or indirectly, with the financial statements of the Company.

7. Associates: Companies, in which the Group's investment is included, directly or indirectly, in the consolidated financial statements on an equity basis.

8. Investees: Subsidiaries or Associates.

9. Related party: As defined in IAS 24 (2009), Related Party Disclosures.

10. Israeli CPI: The consumer price index as published by the Israeli Central Bureau of Statistics.

## Note 2 - Basis of Preparation

### A. Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board. The consolidated financial statements were authorized to be issued by the Company's Board of Directors on April 23, 2020.

These consolidated financial statements are restating the Group's financial statements as of December 31, 2019, which were originally approved by its board of directors on April 23, 2020

As a result of differences found between Bezeq International's actual assets and liabilities balances in the balances in its financial statements, the Group restated its financial statements as described in note 2I hereafter. These restated consolidated financial statements were reapproved by the Company's board of directors on December 21, 2020.

### B. Functional currency and presentation currency

The consolidated financial statements are presented in NIS, which is the Group's functional currency, and have been rounded to the nearest million. NIS is the currency that represents the principal economic environment in which the Group operates.

### C. Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following items:

- Derivative financial instruments, including financial derivatives, at fair value through profit or loss
- Inventories measured at the lower of cost and net realizable value
- Deferred tax assets and liabilities
- Provisions
- Assets and liabilities for employee benefits

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

### D. Operating cycle

The Group's operating cycle is up to one year. As a result, current assets and current liabilities include items the realization of which is intended and anticipated to take place within one year from the date of the financial statements.

### E. Classification of expenses recognized in the statement of income

Costs and expenses in the statement of income are presented and analyzed on the basis of the function of the expenses. The classification is compatible with the understanding of the Group's businesses, which address a wide range of services using common infrastructure. All of the costs and expenses are used to provide services.

### F. Use of estimates and judgments

The preparation of financial statements in conformity with IFRS requires the Group's management to make judgments and use estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

Information about significant estimates and judgments, for which changes in the assessments and assumptions could potentially have a material effect on the financial statements:

| Subject | Principal assumptions | Possible effects | Reference |
|---|---|---|---|
| Measurement of recoverable amounts of cash-generating units | Assumption of expected cash flows from cash-generating units | Recognition of impairment loss | Note 9 |
| Deferred taxes | Assumption of anticipated future realization of the tax benefit, including assumption that it is more likely than not that the carryforward losses in DBS will not be utilized. | Recognition of a deferred tax asset | Note 21 |
| Useful life and expected operation of fixed assets, intangible assets, and other long-term assets | Assumptions of the useful life of groups of fixed assets, intangible assets, and additional assets | Change in the value of fixed assets, intangible assets, additional assets, and depreciation, amortization and impairment expenses | Notes 8, 9, 10 and 11 |
| Uncertain tax positions | The extent of the certainty that the Group's tax positions will be accepted (uncertain tax positions) and the risk of it incurring any additional tax and interest expenses. This is based on an analysis of a number of matters including interpretations of tax laws and the Group's past experience | Recognition or reversal of income tax expenses | Note 21 |
| Provisions and contingent liabilities, including levies | Assessment of the likelihood of claims against Group companies and measuring potential liabilities attributable to claims | Reversal or creation of a provision for a claim, recognition of income /expenses and recognition of profit or loss for such change, respectively | Note 17,22 |
| | The Company's assessments of the estimated payment to the authorities for the levies on the real estate asset in the Sakia property | Change in capital gain for the sale of a real estate asset in the Sakia property | |
| Employee benefits | Actuarial assumptions such as discount rate, future salary increases and churn rate | An increase or decrease in liabilities for employee benefits and a liability for early retirement | Note 20 |
| Unavoidable costs of a contract | Assuming that the economic benefits will exceed the unavoidable costs of the contract | Recognition of a provision for an onerous contract | Note 3.13 |

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

| | | | |
|---|---|---|---|
| The existence of effective control over Bezeq | The practical ability to appoint most of the members of the board of directors of Bezeq, as a result of the control permit in Bezeq, the composition and distribution of the holdings of the other shareholders of Bezeq and the restrictions on these shareholders under the Telecommunications Law | Consolidation of Bezeq's reports or treatment of Bezeq using the equity method. | Note 12D |

### G. Determination of fair value

When preparing the financial statements, the Group is required to determine the fair value of certain assets and liabilities. Further information about the assumptions made in determining fair values is disclosed in Note 19E regarding fair value.

### H. Initial application of new standards

**Initial application of IFRIC 23, Uncertainty Over Income Tax Treatments**

As from January 1, 2019, the Group applies the interpretation of IFRIC 23, Uncertainty Over Income Tax Treatments. IFRIC 23 clarifies application of recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. Application of IFRIC 23 did not have a material effect on the Group's financial statements.

### I. Restatement

At the beginning of November 2020, as part of the preparation of the quarterly report and as part of the process of preparing and closing the financial statements for the period ended September 30, 2020, Bezeq International Ltd. (hereinafter: “Bezeq International”) discovered that there are discrepancies between the assets and liabilities listed in its books and the actual assets and liabilities, resulting, inter alia, from non-imputation of costs from previous years in respect of payment of advances to suppliers to the income statement, as well as from improper capitalization of prepaid expenses.

Following the discovery of the discrepancies, Bezeq International's management began an immediate examination of the issue, and Bezeq International carried out tests, procedures and compensatory actions, while investing much effort and many resources, in order to prepare the financial statements in accordance with International Financial Reporting Standards and in accordance with Disclosure Provisions in Chapter IV of Securities Regulations, 5730-1970, in all material respects.

In this context, the following actions were taken, among others:

1. Bezeq International recalculated certain balances in the statements on its financial position for the years 2016-2019 and for interim periods for the years 2019 and 2020 without relying on past records and existing processes in accounting in relation to the balance sheet items where errors were discovered.

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

2. In light of the change in forecasts resulting from the discrepancies described above, the Company re-examined its valuation as of December 31, 2018 and 2019 through an external valuator.

3. Bezeq International carried out controls and inspections on the recalculation of balances with the assistance of an independent external specialist for the purpose of monitoring. In addition, the existing team was supported by additional accounting employees from Bezeq's subsidiaries, for the purpose of carrying out the work of correcting the statements.

4. Bezeq International’s internal auditor conducted an examination of the matter in cooperation with Bezeq International's Security Division, while in some of the inspections he was assisted by an independent external specialist as stated in section 3 above.

5. Bezeq’s Board of Directors has appointed an independent external examiner for the purpose of an in-depth investigation of the events and circumstances. The examination is underway as of the date of approval of the financial statements.

In light of the fact that Bezeq International's accounting system included many manual entries and poor documentation in a way that does not allow the effect of the transactions on its financial results to be fully traced, Bezeq International reconstructed the balance sheets in which errors were discovered without relying on the manual entries, with the assistance of an external specialist, reasonable controls and additional reports constructed during the process. The described complexity and method of preparing the reports, under tight schedules, did not allow for a full investigation of the discrepancies. Bezeq International is still examining the source of the discrepancies, and it is possible that additional discrepancies will be discovered following the work of the external examiner. The Company anticipates that in light of the manner in which the statements are constructed, such discrepancies, insofar as they exist, will not have a material effect on the Group’s consolidated financial statements.

As of the date of approval of these financial statements, the total impact of the discrepancies discovered in Bezeq International as part of the examinations as of December 31, 2019 was a reduction in the Group's equity according to the following:

1. Errors that occurred until 2010 affected the balance of goodwill recognized at the time of gaining control of Bezeq. The correction of the goodwill balance affected subsequent impairments of cash-generating units recognized by the Group. For more information regarding the impairment of the Internet Services and International Communications segment, see Note 9 below.

2. Reduction of the Group's equity as of January 1, 2018 in the amount of approximately NIS 102 in respect of past balances from the years 2002-2017, with most of the amount (approximately NIS 80) originating in the years 2002-2003.

3. Reduction of the Group's net profits in a cumulative amount of approximately NIS 134 for the period between January 1, 2018 and December 31, 2019.

4. Following the findings of the examination, Bezeq International updated its forecasts for the coming years and performed an updated valuation as of December 31, 2019, following which an additional impairment loss of NIS 66 (NIS 44 net of tax) was recognized as a result of updating the value of operations and the value of Bezeq International's book value as of December 31, 2019 (see Note 9).

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

In addition, the Company performed an updated valuation as of December 31, 2018, following which an additional impairment loss of NIS 30 was recognized as a result of updating the value of operations and the value of Bezeq International's book value as of December 31, 2018 (see Note 9).

It should be noted that as of the date of the examination, no effect was found on the cash balance of Bezeq International and the Group.

In light of the findings of the examinations as stated above, the Company made an adjustment by way of restatement of its financial statements as of December 31, 2019 and for the year ended on the same date, in order to retrospectively reflect the effect of the above, in addition to comparative restated results as of December 31, 2018 and for the year then ended and as of January 1, 2018 and for the year ended December 31, 2017, in which there were adjustments as a result of the above.

The following is a breakdown of the effect of the restatement:

**Impact on the financial statements as of December 31, 2019 and for the year ended on that date**

| | **Effect on the statement on the financial position as of December 31, 2019** | | |
|---|---|---|---|
| | **As previously reported** | **Impact of restatement** | **As reported in these financial statements** |
| | **(audited)** | **(audited)** | **(audited)** |
| | **NIS** | **NIS** | **NIS** |
| Trade receivables, net | 1,689 | (12) | **1,677** |
| Other receivables | 313 | 29 | **342** |
| Inventory | 93 | 3 | **96** |
| Right of use assets | 1,182 | 35 | **1,217** |
| Property, plant and equipment | 6,032 | (68) | **5,964** |
| Intangible assets | 3,180 | (17) | **3,163** |
| Deferred expenses and non-current investments | 366 | (26) | **340** |
| Deferred tax assets | 59 | 22 | **81** |
| Trade and other payables | 1,425 | 191 | **1,616** |
| Deficit attributable to shareholders of the company | (187) | (54) | **(241)** |
| Deficit attributable to Non-Controlling interests | (15) | (182) | **(197)** |
| Total equity deficit | (202) | (236) | **(438)** |

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

| | Effect on the statement of income for the year ended December 31, 2019 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS | NIS | NIS |
| General and operating expenses | 3,276 | 45 | **3,321** |
| Impairment losses | 1,274 | 66 | **1,340** |
| Operating profit | 566 | (111) | **455** |
| Income tax expenses | 1,473 | (32) | **1,441** |
| Net loss for the year | (1,381) | (79) | **(1,460)** |
| Loss attributable to Non-controlling interest | (528) | (79) | **(607)** |
| Loss per share (in NIS) | (19.76) | 0.06 | **(19.70)** |

| | Effect on the comprehensive income for the year ended December 31, 2019 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS millions | NIS millions | NIS millions |
| Net loss for the year | (1,381) | (79) | **(1,460)** |
| Total comprehensive loss for the period | (1,413) | (79) | **(1,492)** |
| Loss attributable to Non-controlling interest | (551) | (79) | **(630)** |

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

## Impact on the financial statements as of December 31, 2018 and for the year ended on that date:

| | Effect on the statement on the financial position as of December 31, 2018 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS millions | NIS millions | NIS millions |
| Trade receivables, net | 1,773 | 2 | **1,775** |
| Other receivables | 269 | 17 | **286** |
| Intangible assets | 4,227 | (17) | **4,210** |
| Deferred expenses and non-current investments | 509 | 6 | **515** |
| Trade and other payables | 1,702 | 165 | **1,867** |
| Equity attributable to shareholders | 228 | (54) | **174** |
| Equity attributable to Non-Controlling interests | 536 | (103) | **433** |
| Total equity deficit | 764 | (157) | **607** |

| | Effect on the statement of income for the year ended December 31, 2018 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS millions | NIS millions | NIS millions |
| General and operating expenses | 3,394 | 34 | **3,428** |
| Impairment losses | 2,294 | 30 | **2,324** |
| Operating loss | (1,385) | (64) | **(1,449)** |
| Income tax expenses | (59) | (8) | **(67)** |
| Loss attributable to shareholders of the company | (1,029) | (37) | **(1,066)** |
| Loss attributable to Non-controlling interests | (830) | (20) | **(850)** |
| Net loss for the year | (1,859) | (57) | **(1,916)** |
| Loss per share (in NIS) | (35.46) | (1.04) | **(36.5)** |

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

| | Effect on the comprehensive income for the year ended December 31, 2018 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS millions | NIS millions | NIS millions |
| Net loss in the year | (1,859) | (57) | **(1,916)** |
| Total comprehensive loss for the period | (1,817) | (57) | **(1,874)** |
| Loss attributable to shareholders of the company | (1,018) | (37) | **(1,055)** |
| Loss attributable to Non-controlling interest | (799) | (20) | **(819)** |

**Impact on the financial statements as of January 1, 2018:**

| | Effect on the statement on the financial position as of January 1, 2018 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS | NIS | NIS |
| Trade receivables, net | 1,915 | 16 | **1,931** |
| Other receivables | 313 | 22 | **335** |
| Intangible assets | 5,840 | 13 | **5,853** |
| Deferred expenses and non-current investments | 558 | 12 | **570** |
| Trade and other payables | 1,719 | 148 | **1,867** |
| Equity attributable to shareholders of the company | 1,246 | (17) | **1,229** |
| Equity attributable to Non-Controlling interests | 1,840 | (83) | **1,757** |
| Total equity | 3,086 | (100) | **2,986** |

(All amounts are in millions except where otherwise stated)

## Note 2 - Basis of Preparation (cont'd)

**Impact on the financial statements as of January 1, 2018 and for the year ended on that date:**

| | Effect on the statement of income for the year ended December 31, 2017 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS millions | NIS millions | NIS millions |
| General and operating expenses | 3,905 | 12 | **3,917** |
| Operating profit | 1,611 | (12) | **1,599** |
| Profit attributable to shareholders | 78 | (3) | **75** |
| Profit attributable non-controlling interests | 664 | (9) | **655** |
| Net profit for the year | 742 | (12) | **730** |
| Earnings per share (in NIS) | 2.62 | (0.11) | **2.51** |

| | Effect on the comprehensive income for the year ended December 31, 2017 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS millions | NIS millions | NIS millions |
| Net profit for the year | 742 | (12) | **730** |
| Total comprehensive loss for the period | 734 | (12) | **722** |
| Loss attributable to shareholders of the company | 76 | (3) | **73** |
| Loss attributable to Non-controlling interest | 658 | (9) | **649** |

**Impact on statement of changes in equity:**

| | As of January 1, 2017 | | |
|---|---|---|---|
| | As previously reported | Impact of restatement | As reported in these financial statements |
| | (audited) | (audited) | (audited) |
| | NIS millions | NIS millions | NIS millions |
| Equity | 1,170 | (14) | **1,156** |
| Total equity | 2,131 | (75) | **2,056** |

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies

The accounting policies set out below have been applied consistently for all periods presented in these consolidated financial statements, and have been applied consistently by Group entities, except as explained in Note 2, Basis of Preparation, under section 2H, Initial Application of Accounting Standards and under sections 3.3, 3.7 and 3.14 below.

In this Note, where the Group has chosen accounting alternatives permitted in accounting standards and/or in accounting policy where there is no explicit provision in accounting standards, such disclosure is presented in bold. This does not attribute greater importance compared to other accounting policies that are not presented in bold.

### 3.1 Consolidation of the financial statements

3.1.1 Subsidiaries

Subsidiaries are entities controlled by the Company. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date of loss of control.

Control exists when the Group is exposed, or has rights, to variable returns from its involvement with the acquiree and it has the ability to affect those returns through its power over the acquiree. Substantive rights held by the Group and others are being taken into account when assessing control.

3.1.2 Transactions eliminated on consolidation

Intra-group balances and income and expenses arising from intra-group transactions, are eliminated in the consolidated statements.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

3.1.3 Contingent consideration for business combinations

Subsequent to the acquisition date, the Group recognizes changes in fair value of contingent consideration recognized under business combinations, classified as a financial liability in the statement of income under financing expenses.

### 3.2 Foreign currency transactions

Transactions in foreign currency are translated into the functional currency of the Group at the exchange rate on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies on the reporting date are retranslated to the functional currency at the exchange rate at that date.

### 3.3 Financial instruments

As from January 1, 2018, the Group applies IFRS 9, Financial Instruments ("IFRS 9"). Application of IFRS 9 did not have a material effect on the measurement of the Group's financial instruments in 2018, compared to the provisions in the previous standard, and the main effect of application of IFRS 9 in the Group is the use of the expected credit loss model.

Non-derivative financial assets

Non-derivative financial assets comprise mainly investments in deposits, trade and other receivables, and cash and cash equivalents.

The Group initially recognizes financial assets at the date at which the Group becomes a party to contractual provisions of the instrument, meaning the date that the Group undertakes to buy or sell the asset.

A financial asset is initially measured at fair value plus transaction costs that are directly attributable to the acquisition or issuance of the financial asset. A trade receivable without a significant financing component is initially measured at the transaction price.

Financial assets are derecognized when the contractual rights of the Group to the cash flows from the asset expire, or the Group transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred.

Classification of financial assets into categories and the accounting treatment in each category

Financial assets are classified at initial recognition to one of the following measurement categories: amortized cost; or fair value through profit or loss.

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated at fair value through profit or loss:

It is held within a business model whose objective is to hold assets so as to collect contractual cash flows.

The contractual terms of the financial asset give rise to cash flows representing solely payments of principal and interest on the principal amount outstanding on specified dates.

All financial assets of the Group that are not classified as measured at amortized cost are measured at fair value through profit or loss.

The Group classifies its financial assets as follows:

Cash and cash equivalents

Cash comprises cash balances available for immediate use and call deposits. Cash equivalents comprise short-term highly liquid investments (with original maturities of three months or less) that are readily convertible into known amounts of cash and are exposed to insignificant risks of change in value.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

Trade and other receivables and deposits

The Group has balances of trade and other receivables and deposits that are held within a business model whose objective is collecting contractual cash flows. The contractual cash flows of these financial assets represent solely payments of principal and interest that reflects consideration for the time value of money and the credit risk. Accordingly, these financial assets are measured at amortized cost.

Subsequent measurement and gains and losses

Financial assets at amortized cost are measured at amortized cost using the effective interest method. The amortized cost is reduced by impairment losses. Interest income, foreign exchange gains and losses and impairment are recognized in profit or loss. Any gain or loss on derecognition is recognized in profit or loss.

Financial assets at fair value through profit or loss are subsequently measured at fair value. Net gains and losses, including any interest income or dividend income, are recognized in profit or loss.

Non-derivative financial liabilities

Non-derivative financial liabilities include debentures issued by the Group, loans and borrowings from banks and other credit providers, and trade and other payables.

The Group initially recognizes debt instruments as they are incurred. Other financial liabilities are recognized at the time of the transaction. Financial liabilities are recognized initially at fair value less any attributable transactions costs. Subsequent to initial recognition, these financial liabilities are measured at amortized cost using the effective interest method.

Financial liabilities are derecognized when the obligation of the Group, as specified in the agreement, expires or when it is discharged or cancelled.

Modification in terms of debt instruments

An exchange of debt instruments having substantially different terms, between an existing borrower and lender is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability at fair value. **The difference between the amortized cost of the original financial liability and the fair value of the new financial liability is recognized in profit or loss as financing income or expense.**

The terms are substantially different if the discounted present value of the cash flows according to the new terms, including any commissions paid, less any commissions received and discounted using the original effective interest rate, is different by at least ten percent from the discounted present value of the remaining cash flows of the original financial liability.

In addition to the aforesaid quantitative criterion, the Group examines, among other things, whether there have also been changes in various economic parameters inherent in the exchanged debt instruments.

In a non-substantial modification in terms (or exchange) of a debt instruments at fixed interest, the new cash flows are discounted using the original effective interest rate, and the difference between the present value of the new financial liability and the present value of the original financial liability is recognized in profit or loss under **financing expenses (income).**

**According to the accounting policy applied by the Group, when the portfolio of the financial liabilities with similar characteristics is repaid/exchanged, the profit/loss from the derecognition/exchange is based on the FIFO method.**

CPI-linked assets and liabilities that are not measured at fair value

**The value of CPI-linked financial assets and liabilities, which are not measured at fair value, is revaluated in each period according to the actual increase in the CPI.**

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group currently has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

A. Hedge accounting

The Group holds derivative financial instruments to hedge cash flows for risks to future changes in the CPI in respect of the debentures issued by the Group.

At the inception of the hedging relationship, the Group documents its risk management objective and its hedging strategy. The Group also documents the economic relationship between the hedged item and the hedging instrument, including whether the changes in cash flows of the hedged item and the hedging instrument are expected to offset each other.

Derivatives are recognized initially at fair value. Attributable transaction costs are recognized in profit or loss as incurred. Subsequent to initial recognition, derivatives are measured at fair value, and the effective portion of changes in fair value of the hedging instrument is recognized in a hedge reserve under other comprehensive income. The effective portion of changes in fair value of a derivative, recognized in other comprehensive income, is limited to the cumulative change in fair value of the hedged item (based on present value), from inception of the hedge. The change in fair value in respect of the ineffective portion is recognized immediately in profit or loss.

B. Economic hedges

In addition, the Group holds derivative financial instruments to hedge cash flows for foreign currency risks. Hedge accounting is not applied for these instruments. The derivative instruments are recognized at fair value; changes in fair value are recognized in profit and loss as incurred, as a financing income or expense.

### 3.4 Broadcasting rights

Broadcasting rights are stated at cost, net of rights exercised and impairment losses.

The costs of broadcasting rights acquired for the broadcasting of content include the amounts paid to the rights provider, plus direct costs for adjusting the rights to the broadcast.

Broadcasting rights are assessed for impairment as part of the cash-generating unit to which the broadcasting rights are attributed (see Note 11).

The net adjustment of the broadcasting rights is presented as an adjustment of earnings as part of the ongoing operations in the statements of cash flows.

### 3.5 Fixed assets

Recognition and measurement

**The Group elected to measure items of fixed assets at cost less accumulated depreciation and accumulated impairment losses.**

Cost includes expenditures that are directly attributable to acquisition of the asset. The cost of self-constructed assets includes the cost of materials, direct labour and financing costs as well as any other cost directly attributable to bringing the asset to the condition for its use intended by the management, and the estimated costs of dismantling and removing the items and restoring the site on which they are located when the Group has an obligation to vacate and restore the site. The cost of purchased software that is integral to the functionality of the related equipment is recognized as part of the cost of the equipment.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

Spare parts, servicing equipment and stand-by equipment are classified as fixed assets when they meet the definition of fixed assets in IAS 16, and are otherwise to be classified as inventory.

When major parts of the fixed assets have different useful lives, they are accounted for as separate items (major components) of the fixed assets.

Gain or loss from the disposal of a fixed asset item is determined by comparing the proceeds from disposal of the asset with it carrying amount. **Gain or loss from the sale of fixed assets is recognized under other income or other expenses, as the case may be, in the statement of income.**

<u>Subsequent expenditure</u>

The cost of replacing part of a fixed asset item is recognized in the carrying amount of the item if it is probable that the future economic benefit embodied in the new item will flow to the Group and its cost can be measured reliably. The costs of day-to-day servicing are recognized in the statement of income as incurred.

<u>Depreciation</u>

Depreciation is recognized in the statement of income on a straight-line basis over the estimated useful life of each part of a fixed asset item, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Right of use assets under a finance lease are depreciated over the shorter of the lease term and their useful lives.

An asset is depreciated when it is ready for use, meaning when it reaches the location and condition necessary for it to be capable of operating in the manner intended by management.

Leasehold improvements are generally depreciated over the shorter of the lease term, including the extension option held by the Group and intended to be exercised and the useful life of the leasehold improvements.

The estimated useful lives for the current period are as follows:

| | **Years** |
|---|---|
| Fixed line and international network equipment (switches, transmission, power) | 4-12 |
| Network | 12-33 |
| Equipment and infrastructure for multichannel television | 3-15 |
| Subscriber equipment and installations | 4-8 |
| Vehicles | 6-7 |
| Office and general equipment | 5-10 |
| Electronic equipment, computers and internal communication systems | 3-7 |
| Cellular network | 4-10 |
| Passive radio equipment at cellular network sites | Up to December 31, 2037 |
| Buildings | 25 |
| Seabed cable | 4-25 (mainly 25) |

Depreciation methods, useful lives and residual values are reviewed at least in each reporting year and adjusted as required.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

### 3.6 Intangible assets

Goodwill

Goodwill that arises upon the acquisition of subsidiaries is included in intangible assets. Subsequent to initial recognition, goodwill is measured at cost less accumulated impairment losses. Goodwill is measured at least once a year to assess impairment. See also Note 9.

Software development costs

Software development costs are recognized as an intangible asset only if the development costs can be measured reliably; the software is technically and commercially applicable; and the Group has sufficient resources to complete the development and intends to use the software. The costs recognized as an intangible asset include the cost of the materials, direct labor and overhead expenses directly attributable to preparation of the asset for its intended use. Other development costs are recognized in the statement of income as incurred.

Capitalized development costs are measured at cost less amortization and accumulated impairment losses.

Software

Software that is an integral part of the hardware, which cannot function without the programs installed on it, is classified as fixed assets. However, licenses for stand-alone software which add functionality to the hardware, are classified as intangible assets.

Rights to frequencies

Rights to frequencies refer to frequencies assigned to Pelephone for cellular activities, after it won the dedicated tenders of the Ministry of Communications. Depreciation of the asset is recognized in the statement of income on the straight-line method over the term of the allocation of frequencies, which started from the use of the frequencies. The 4G frequencies (LTE) and 3G frequencies (UMTS/HSEA) are being amortized until August 22, 2028.

Other intangible assets

**Other intangible assets acquired by the Group, which have a definite useful life, are measured at cost less amortization and accumulated impairment losses.**

Subsequent expenditure

Subsequent expenditure is recognized as an intangible asset only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure relating to generated goodwill and brands, is recognized in the statement of income as incurred.

Amortization

Amortization of intangible assets is recognized in the statement of income on a straight-line basis (other than as set out below regarding amortization of customer relations), over the estimated useful life of the intangible assets, from the date on which the assets are available for use. Goodwill is not systematically amortized but is tested for impairment at least once a year.

Estimated useful lives for the current period are as follows:

| Type of asset | Amortization period |
|---|---|
| Frequency usage right | Over the license period up to 2028 |
| Computer programs and software licenses | 3-10 years depending on the term of the license period or the estimated time of use of the software |

Amortization methods and useful lives are reviewed at least at each reporting year and adjusted if appropriate.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

### 3.7 Leased assets

As from January 1, 2018, the Group applies IFRS 16, Leases.

Accounting policy applied in the periods prior to January 1.1, 2018

Leases, including leases of land from the Israel Land Administration, where the Group assumes substantially all the risks and rewards of ownership, were classified as finance leases. Upon initial recognition, the leased assets were measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the assets were measured at cost less accumulated amortization and impairment losses.

Other leases were classified as operating leases and the leased assets were not recognized in the Group’s statement of financial position. Payments made under operating leases were recognized in profit or loss on a straight-line basis over the term of the lease.

At inception or upon reassessment of an arrangement, the Group determined whether such an arrangement is or contains a lease. An arrangement was a lease or contained a lease if the following two criteria were met:

The fulfillment of the arrangement was dependent on the use of a specific asset or asset.

The arrangement contained rights to use the asset.

If, in accordance with these terms, the Group determines that the agreement does not contain a lease, the agreement is accounted for as a service agreement and payments for the service are recognized in profit or loss on a straight-line basis, over the service period.

Accounting policy applied as from January 1.1, 2018

Presented below are the principal accounting policies for leases in which the Group is the lessee, which were applied as from January 1, 2018 following the application of the Standard:

**Determining whether an arrangement contains a lease**

At the inception of the arrangement, the Group determines whether the arrangement is or contains a lease and examines whether the arrangement transfers the right to control the use of an identifiable asset for a period of time in return for payment. When assessing whether the arrangement transfers control over the use of an identifiable asset, the Group estimates, over the lease term, whether it has both rights set out below:

The right to essentially obtain all the economic rewards associated with the use of the identifiable asset.

The right to direct the use of the identifiable asset.

For lease contracts that include non-lease components, such as services or maintenance, which are related to a lease component, the Group elected to account for the contract as a single lease component without separating the components.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

### Leased assets and lease liability

Contracts that award the Group the right to control the use of an identifiable asset over a period of time for a consideration are accounted for as leases. At initial recognition, the Group recognizes a liability at the present value of the future minimum lease payments (these payments do not include variable lease payments that are not linked to the CPI, or to any change in the rate of interest, or any change in the exchange rate), and concurrently, the Group recognizes a right-of-use asset at the amount of the liability, adjusted for lease payments paid in advance or accrued, plus direct costs incurred in the lease.

Since the interest rate implicit in the lease is not readily determinable, the incremental borrowing rate of the Group is used (the borrowing rate that the Group would be required to pay to borrow the amounts required to obtain an asset at a similar value to the right-of-use asset in a similar economic environment, in a similar period and with similar collateral).

Subsequent to initial recognition, the asset is accounted for using the cost model and it is amortized over the lease term or the useful life of the asset (whichever is earlier).

### The lease term

The lease term is the non-cancellable period of the lease plus periods covered by an extension or termination option if it is reasonably certain that the Group will exercise or not exercise the option.

### Variable lease payments

Variable lease payments that are linked to the CPI are initially measured using the index or currency rate at the inception of the lease and are included in the measurement of the lease liability. When there is a change in the cash flows of the future lease payments arising from the change in the index, the liability is adjusted against the right-of-use asset.

### Depreciation of a right-of-use asset

After lease commencement, a right-of-use asset is measured on a cost basis less accumulated depreciation and accumulated impairment losses and is adjusted for re-measurements of the lease liability. Depreciation is calculated on a straight-line basis over the useful life or contractual lease period, whichever earlier, as follows:

| Type of asset | Weighted average of the agreement period as at January 1, 2019 (years) |
|---|---|
| Cellular communications sites | 6.6 |
| Buildings | 6 |
| Vehicles | 2 |

### Subleases

In leases in which the Company sublets the underlying asset, the Company assesses the classification of the sublease as a finance or operating lease, for the right-of-use received in the primary lease. The Company assessed the existing subleases on the initial application date, in accordance with the balance of their contractual terms as at that date.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

### 3.8 Investment property

Investment property is measured at cost. Cost includes expenditure that is directly attributable to the acquisition of the investment property.

### 3.9 Right of use of capacities

Transactions for acquiring an indefeasible right of use (IRU) of seabed cable capacities are accounted for as service transactions. The prepaid expense is amortized on a straight-line basis as stated in the agreement and no more than the expected estimated useful life of those capacities.

Identifiable capacities which serve the Group exclusively were recognized under fixed assets. The asset is depreciated on a straight-line basis as stated in the agreement and no more than the expected estimated useful life of those capacities.

### 3.10 Inventory

The cost of inventories includes the cost of purchase and cost incurred in bringing the inventories to their present location and condition.

Inventories are measured at the lower of cost or net realizable value. The Group elected to base the cost of inventories on the moving average principle.

The inventories include terminal equipment and accessories intended for sale and service, as well as spare parts used for repairs in the repair service provided to its customers.

Slow-moving inventory of terminal equipment, accessories and spare parts are stated net of the provision for impairment.

### 3.11 Impairment

<u>Non-derivative financial assets</u>

As from January 1, 2018, the Group applies IFRS 9, Financial Instruments (“IFRS 9”) and performs an assessment for any indications of impairment in accordance with IFRS 9. In practice, application of the New Standard did not have a material effect on the measurement of impairment of the Group’s financial assets in 2019 and 2018 compared with the previous standard.

**The Group has elected to measure the provision for expected credit losses in respect of trade receivables at an amount equal to the full lifetime credit losses of the instrument.**

Lifetime expected credit losses are expected credit losses that result from all possible default events over the expected life of the financial instrument.

Expected credit losses are a probability-weighted estimate of credit losses. Credit losses are measured as the present value of the difference between the cash flows due to the Group in accordance with the contract and the cash flows that the Group expects to receive and are discounted at the effective interest rate of the financial asset.

Expected credit losses for receivables in significant amounts are tested individually. Other financial assets are assessed for expected credit losses collectively in groups that share similar credit risk characteristics, taking into account past experience.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

The provision for expected credit losses is recognized net of the gross carrying amount of the receivables.

For bank deposits, for which the credit risk did not increase significantly from the date of initial recognition, the Group measures the provision for expected credit losses in an amount equal to the expected credit losses for an event of default in a 12-month period.

When determining whether the credit risk of a financial asset has increased significantly since initial recognition, and when estimating expected credit losses, the Group considers reasonable and supportable information that is relevant and available with no undue cost or effort. Such information includes quantitative and qualitative information, and an analysis, based on the Group’s past experience and informed credit assessment, and it includes forward looking information.

Non-financial assets

Timing of impairment testing

The carrying amounts of the Group’s non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the recoverable amount of the asset is estimated.

The Group assesses the recoverable amount of goodwill once a year, or more frequently if there are indications of impairment.

Measurement of recoverable amount

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or the cash generating unit (for which future cash flows were not adjusted).

Determining cash-generating units

For the purpose of impairment testing, the assets are grouped together into the smallest group of assets that generates cash from continuing use that are largely independent of other assets or groups of assets (cash-generating unit). See Note 9.

Allocation of goodwill to cash-generating units

For purposes of goodwill impairment testing, cash-generating units to which goodwill has been allocated are aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes, but in any event is not larger than an operating segment. Goodwill acquired in a business combination is allocated for the purpose of impairment testing to cash-generating units that are expected to generate benefits from the synergies of the combination.

Recognition of impairment loss

An impairment loss of cash generating units is recognized when the carrying amount of the cash generating unit, including goodwill, where relevant, exceeds its recoverable amount and is recognized in the statement of income. An impairment loss recognized in respect of a cash-generating unit is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to reduce the carrying amounts of the other assets in the cash-generating unit. To allocate an impairment loss, the assets are not impaired below the higher of their fair value less exercise costs and their value in use (if determinable) or zero.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

**The Company presents an analysis of expenses recognized in profit or loss based their nature. Impairment losses of non-current assets arising from one-time updates of financial forecasts are presented in our Statement of Income under Impairment losses. Impairment losses of non-current assets arising from continuous write-downs of asset to their fair value less costs of disposal costs (a result of forecasts for negative cash flows and negative enterprise value of the relevant companies), is reported in our Statement of Income under the operating expenses related to the ongoing consumption of economic benefits of such assets (i.e. depreciation, amortization and impairment or general and operating expenses). Such presentation better reflects the nature of these expenses and is more suitable for understanding of the Group's operations.**

**Accordingly, in the Statement of Income, the impairment of the broadcasting rights in DBS and Walla! is presented under "General and operating expenses", while the impairment of fixed assets and intangible assets is presented under "Depreciation, amortization and impairment". See also Note 9.**

### 3.12 Employee benefits

Post-employment benefits

The Group has a number of post-employment benefit plans. The plans are usually financed by deposits with insurance companies and they are classified as defined contribution plans and defined benefit plans.

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which the Group pays fixed contributions into a separate entity and has no legal or constructive obligation to pay further amounts.

The Group's obligations for contributions to defined contribution pension plans are recognized as an expense in the statement of income in the periods during which services are rendered by employees.

Defined benefit plans

The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is presented at its present value, and the fair value of any plan assets is deducted. The calculation is performed annually by a qualified actuary. The discount rate is the yield on high-quality corporate debentures at the reporting date, denominated in or linked to the currency of the paid benefit, with maturity dates approximating the terms of the Group's obligations.

Net interest costs on a defined benefit plan are calculated by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then-net defined benefit liability.

**The Group elected to recognize the interest costs that were recognized in profit or loss under financing expenses.**

Remeasurement of the net defined benefit liability comprises actuarial gains and losses and the return on plan assets (excluding interest). Remeasurements are recognized immediately directly in retained earnings through other comprehensive income.

When the benefits of a plan are improved or curtailed, the portion of the increased or curtailed benefit relating to past service by employees is recognized immediately in profit or loss when the plan improvement or curtailment occurs.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

Other long-term employee benefits

The Group's net obligation in respect of long-term employee benefits (such as an obligation for accumulated vacation days and sick leave) other than pension plans is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The amount of these benefits is stated at its present value. The discount rate is the yield at the reporting date on high-quality linked corporate debentures denominated in NIS, with maturity dates approximating the terms of the Group's obligations. Actuarial changes are recognized in the statement of income in the period in which they arise. Any actuarial changes arising from a change in the discount rate are recognized in the financing expenses item, while the other differences are recognized in salary expenses.

Early retirement and termination benefits

Termination benefits are recognized as an expense when the Group is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan to terminate employment before the normal retirement date. Termination benefits for voluntary redundancies are recognized as an expense if the Group has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

**Expenses for early retirement and termination recognized in the statement of income are presented under other operating expenses (income). The actuarial changes arising from a change in the discount rate, long-term benefits for early retirement and termination, are recognized under financing expenses, while the other actuarial changes are recognized under other operating expenses (income).**

Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

The employee benefits are classified, for measurement purposes, as short-term benefits or as other long-term benefits depending on the date when the benefits are expected to be to be wholly settled,

In the statement of financial position, the employee benefits are classified as current benefits or as non-current benefits according to the time the liability is due to be settled.

### 3.13 Provisions

A provision is recognized if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

Legal claims

Contingent liabilities are accounted for according to IAS 37 and its related provisions. Accordingly, the claims are classified by likelihood of realization of the exposure to risk, as follows:

More likely than not – more than 50% probability

Likely – probability higher than unlikely and less than 50%

Unlikely – probability of 10% or less

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

For claims which the Group has a legal or constructive obligation as a result of a past event, which are more likely than not to be realized, the financial statements include provisions which, in the opinion of the Group, based, among other things, on the opinions of its legal advisers retained in respect of those claims, are appropriate to the circumstances of each case, despite the claims being denied by the Group companies. There are also a small number of legal proceedings, most of which were received recently, for which the risks cannot be assessed at this stage, therefore no provisions have been made.

Note 19 describes the amount of additional exposure due to contingent liabilities that are likely to be realized.

Site dismantling and clearing costs

The provision in respect of an obligation to dismantle and clear sites is recognized for those rental agreements where Pelephone has an undertaking to restore the rental property to its original state at the end of the rental period, after dismantling and transferring the site, and restoring the site when required. The provision is measured by discounting the future cash flows by risk-free discounted interest reflecting the time until the expected termination of the contract for dismantling of the site by Pelephone. The carrying amount of the provision is adjusted in each period to reflect the time that has passed and is recognized as a financing expense.

Onerous contracts

A provision for onerous contracts is recognized when the unavoidable costs of a contract exceed the benefits expected to be received from the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the unavoidable costs (net of the revenues) of continuing with the contract. Unavoidable costs are costs that the Group cannot avoid as they are subject to a contract (such as incremental costs).

### 3.14 Revenues

The Group recognizes revenues when the customer gains control over the goods or services. The income is measured according to the amount of the consideration to which the Group expects to be entitled in exchange for the transfer of goods or services promised to the customer, other than amounts collected in favour of third parties.

The model for recognizing revenues from contracts with customers includes five steps for analysing transactions so as to determine when to recognize revenues and in what amount:

A. Identifying the contract with the customer.

B. Identifying separate performance obligations in the contract.

C. Determining the transaction price.

D. Allocating the transaction price to separate performance obligations.

E. Recognizing revenues when the performance obligations are satisfied.

Identifying the contract

The Group accounts for a contract with a customer only when the following conditions are met:

1. The parties to the contract have approved the contract (in writing, orally or according to other customary business practices) and they are committed to satisfying the obligations attributable to them.
2. The Group can identify the rights of each party in relation to the goods or services that will be transferred.
3. The Group can identify the payment terms for the goods or services that will be transferred.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

4. The contract has a commercial substance (i.e. the risk, timing and amount of the entity's future cash flows are expected to change as a result of the contract).
5. It is probable that the consideration, to which the Group is entitled to in exchange for the goods or services transferred to the customer, will be collected.

Identifying performance obligations

On the inception date of the contract, the Group assesses the goods or services promised in the contract with the customer and identifies as a performance obligation any promise to transfer to the customer one of the following:

(1) Goods or services (or a bundle of goods or services) that are distinct; or

(2) A series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer.

Determining the transaction price.

The transaction price is the amount of the consideration to which the Group expects to be entitled in exchange for the transfer of goods or services promised to the customer, other than amounts collected in favor of third parties. When determining the transaction price, the Group considers the effects of all the following: variable consideration, the existence of a significant financing component in the contract, non-cash consideration and consideration to be paid to the customer.

Existence of a significant financing component

In order to measure the transaction price, the Group adjusts the amount of the promised consideration in respect of the effects of the time value of money if the timing of the payments agreed between the parties provides to the customer or the Group a significant financing benefit. In these cases, the contract contains a significant financing component. When assessing whether a contract includes a significant financing component, the Group examines, among other things, the expected length of time between the date the Group transfers the promised goods or services to the customer and the date the customer pays for these goods or services, as well as the difference, if any, between the amount of the consideration promised and the cash selling price of the promised goods or services.

When the contract contains a significant financing component, the Group recognizes the amount of the consideration using the discount rate that would be reflected in a separate financing transaction between it and the customer on the inception date of the contract. The financing component is recognized as interest income or expenses over the period, which are calculated according to the effective interest method.

In cases where the difference between the time of receiving payment and the time of transferring the goods or services to the customer is one year or less, the Group applies the practical expedient included in the standard and does not separate a significant financing component.

Existence of performance obligations

Revenues are recognized when the Group satisfies a performance obligation by transferring to the customer control over promised goods or services.

Contract costs

Incremental costs of obtaining a contract with a customer such as sales fees to agents, are recognized as an asset when the Group is likely to recover these costs. Costs to obtain a contract that would have been incurred regardless of the contract are recognized as an expense as incurred, unless the customer can be billed for those costs.

Capitalized costs are amortized in the income statement on a systematic basis that is consistent with the expected average duration of subscribers and with their average projected churn rate based on the type of subscriber and the service received (mainly over a period of one to four years).

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

Every reporting period the Group examines whether the carrying amount of the asset recognized as aforesaid exceeds the consideration the entity expects to receive in exchange for the goods or services to which the asset relates, less the costs directly attributable to the provision of these goods or services that were not recognized as expenses, and if necessary an impairment loss is recognized in profit or loss.

Principal versus agent considerations

When another party is involved in providing goods or services to the customer, the Group examines whether the nature of its promise is a performance obligation to provide the defined goods or services itself, which means the Group is a principal and therefore recognizes revenues in the gross amount of the consideration, or to arrange that another party provide the goods or services which means the Group is an agent and therefore recognizes revenue in the amount of the net commission.

The Group is a principal when it controls the promised goods or services before their transfer to the customer. Indicators that the Group controls the goods or services before their transfer to the customer include the following: the Group is the primary obligor for fulfilling the promises in the contract; the Group has inventory risk before the goods or services are transferred to the customer; and the Group has discretion in setting the prices of the goods or services.

### 3.15 Financing income and expenses

Financing income comprises mainly interest income accrued using the effective interest method in respect of the sale of terminal equipment in installments, interest income on deposits, changes in the fair value of financial assets at fair value through profit or loss and gain from debt restructuring.

Financing expenses include mainly interest and linkage expenses on borrowings received and debentures issued, expenses for early repayment of the debt, and financing expenses for employee benefits.

In the statements of cash flows, interest received is presented as part of cash flows from investing activities. The Group elected to present interest and linkage differences paid for loans and debentures under cash flows used for financing activities.

### 3.16 Income tax expenses

Income tax expenses include current and deferred taxes and are recognized in the statement of income or in other comprehensive income to the extent that the expenses relate to items recognized in other comprehensive income.

Current taxes

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date. Current taxes also include taxes in respect of prior years.

Uncertain tax positions

A provision for uncertain tax positions, including additional tax and interest expenses, is recognized when it is more likely than not that the Group will have to use its economic resources to pay the obligation.

Deferred taxes

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The Group does not recognize deferred taxes for the following temporary differences:

1. Initial recognition of goodwill
2. Differences arising from investment in subsidiaries and associates, if it is probable that they will not reverse in the foreseeable future and if the Group controls the date of reversal.

(All amounts are in millions except where otherwise stated)

## Note 3 - Significant accounting policies (cont'd)

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognized for carryforward losses, tax benefits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized (see also Note 21).

Offsetting deferred tax assets and liabilities

The Group sets off deferred tax assets and liabilities if there is a legally enforceable right to offset deferred tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, and they intend to settle deferred tax liabilities and assets on a net basis or their deferred tax assets and liabilities will be realized simultaneously.

Presentation of tax expenses in the statement of cash flows

Cash flows arising from taxes on income are classified in the statement of cash flows as cash flows from operating activities, unless they can be specifically identified with investing and financing activities.

### 3.17 Dividends

An obligation relating to a dividend proposed or declared subsequent to the reporting date is recognized only in the period in which the declaration was made (approval of the general meeting). In the statements of cash flows, a dividend that has been paid is recognized under financing activities.

### 3.18 New standards not yet adopted

#### 3.18.1 Amendment to IAS 1, Presentation of Financial Statements: Classification of Liabilities as Current or Non-current

The amendment replaces certain classification requirements of liabilities as current or non-current. The amendment is effective for reporting periods beginning on January 1, 2023. Earlier application is permitted. The amendment is effective retrospectively, including reconciliation of comparative information. The Group has not yet commenced examining the effects of the application of the standard on the financial statements.

#### 3.18.2 Amendment to IAS 37, Provisions, contingent liabilities and Contingent assets

On May 14, 2020, an amendment was published to International Accounting Standard 37 - Provisions, Contingent Liabilities and Contingent Assets (IAS 37) in respect of onerous contracts (hereinafter: the "Amendment"). The Amendment stipulates that in examining the costs of maintaining an onerous contract, it is necessary to also consider indirect costs in addition to supplemental costs (see Note 3 to the Annual Financial Statements).

The date of initial application of the Amendment is set for January 1, 2022 and will be made by adjusting the surplus balance in respect of the cumulative effect as of that date. The Amendment may have effects on the identification and measurement of onerous contracts in the Group, which may even be reflected in the creation of material provisions, which the Group is unable to assess at this stage. The Group is studying the amendment and is preparing to implement it on the date scheduled.

(All amounts are in millions except where otherwise stated)

## Note 4 - Segment Reporting

The Group operates in four segments in the communications sector and every company in the Group operates in a separate business segment. The primary reporting format, by business segments, is based on the Group's management and internal reporting structure.

Each company provides services in the segment in which it operates, using the property, plant and equipment and the infrastructure it owns (see also Note 26). The infrastructure of each company is used only for providing its services. Each of the companies in the Group is exposed to different risks and yield expectations, mainly with respect to the technology and competition in the segment in which it operates. Accordingly, the separable components in the Group are each company in the Group.

Based on the above, the business segments of the Group are as follows:

- Bezeq - The Israel Telecommunication Corp., Limited.: fixed line domestic communications
- Pelephone Communications Ltd.: cellular communications
- Bezeq International Ltd.: international communications, internet services and network end point services
- D.B.S. Satellite Services (1998) Ltd.: multichannel television

The other companies in the Group are presented under the "Other" item. Other operations include call center services (Bezeq Online) and online shopping and classified ads (through Walla!). These operations are not reported as reporting segments as they do not fulfill the quantitative thresholds.

Inter-segment pricing is set at the price determined in a transaction in the ordinary course of business.

The results, assets and liabilities of a segment include items directly attributable to that segment, as well as those that can be allocated on a reasonable basis. The results of the segments are presented net of the impairment losses described in Note 9. This is in accordance with the manner in which the Group’s chief operating decision maker evaluates the performance of the segment and makes decisions regarding the allocation of resources to the segment.

Segment capital expenditure is the total cost incurred during the period for acquisition of property, plant and equipment and intangible assets.

**Notes to the Consolidated Financial Statements**

(All amounts are in millions except where otherwise stated)

## Note 4 - Segment Reporting (cont'd)

A. Operating Segments (cont'd)

| | Year ended December 31, 2017 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Domestic fixed–line communications | Cellular communications | International communications and Internet services | Multi-channel television | Others | Adjustments | Consolidated |
| | | | Restated | | | | Restated |
| | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| Revenue from external entities | 3,953 | 2,500 | 1,466 | 1,650 | 220 | - | 9,789 |
| Inter-segment revenues | 291 | 46 | 71 | - | 17 | (425) | - |
| Total revenue | 4,244 | 2,546 | 1,537 | 1,650 | 237 | (425) | 9,789 |
| **Depreciation and amortization** | 728 | 383 | 135 | 285 | 20 | 566 | 2,117 |
| Segment results - operating income | 1,971 | 72 | * 156 | 163 | (20) | (743) | *1,599 |
| Finance income | 36 | 54 | 4 | 10 | 5 | (40) | 69 |
| Finance expenses | (439) | (3) | (6) | (81) | - | (57) | (586) |
| Total financing income (expense), net | (403) | 51 | (2) | (71) | 5 | (97) | (517) |
| Segment profit (loss) after finance expenses, net | 1,568 | 123 | *154 | 92 | (15) | (840) | *1,082 |
| Share in profit (loss) of equity-accounted investee | - | - | - | - | (4) | (1) | (5) |
| Segment profit (loss) before income tax | 1,568 | 123 | *154 | 92 | (19) | (841) | *1,077 |
| Income tax | 396 | 28 | 39 | 336 | - | (452) | 347 |
| **Segment results - net profit (loss)** | 1,172 | 95 | *115 | (244) | (19) | (389) | *730 |

* Restated. See Note 2.I.

**Notes to the Consolidated Financial Statements**

(All amounts are in millions except where otherwise stated)

## Note 4 - Segment Reporting (cont'd)

A. Operating Segments (cont'd)

| | Year ended December 31, 2018 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Domestic fixed–line communications | Cellular communications | International communications and Internet services | Multi-channel *television | Others | Adjustments** | Consolidated |
| | | | Restated | | | | Restated |
| | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| Revenue from external entities | 3,883 | 2,401 | 1,338 | 1,473 | 226 | - | 9,321 |
| Inter-segment revenues | 313 | 42 | 53 | - | 15 | (423) | - |
| Total revenue | 4,196 | 2,443 | 1,391 | 1,473 | 241 | (423) | 9,321 |
| **Depreciation and amortization** | 850 | 655 | 194 | 323 | 21 | 345 | 2,388 |
| Segment results - operating income | 1,224 | (2) | *77 | (56) | (36) | (2,656) | *(1,449) |
| Finance income | 32 | 56 | 1 | 27 | - | (27) | 89 |
| Finance expenses | (502) | (22) | (11) | (16) | - | (69) | (620) |
| Total financing income (expense), net | (470) | 34 | (10) | 11 | - | (96) | (531) |
| Segment profit (loss) after finance expenses, net | 754 | 32 | *67 | (45) | (36) | (2,752) | *(1,980) |
| Share in profit (loss) of equity-accounted investee | - | - | 1 | - | (4) | - | (3) |
| Segment profit (loss) before income tax | 754 | 32 | *68 | (45) | (40) | (2,752) | *(1,983) |
| Income tax** | 187 | 8 | *17 | 3 | - | (282) | (67) |
| **Segment results - net profit (loss)** | 567 | 24 | *51 | (48) | (40) | (2,470) | *(1,916) |
| **Additional information:** | | | | | | | |
| Segment assets | 8,896 | 4,124 | * 1,358 | 1,606 | 157 | 972 | * 17,113 |
| Goodwill | - | - | 6 | - | - | 2,256 | 2,262 |
| Investment in equity-accounted investee | - | - | 6 | - | 2 | - | 8 |
| Segment liabilities | 14,284 | 1,425 | *733 | 687 | 84 | 1,563 | *18,776 |
| Investments in property, plant and equipment and intangible assets | 902 | 346 | 137 | 318 | 13 | - | 1,716 |

*Restated. See Note 2.I.

** Impairment losses of the multi-channel television segment, the cellular communications segment and the International communications and internet services segment are presented as part of the adjustments (please refer to Note 9). Adjustments also include depreciation, amortization and impairment of assets resulting from the Bezeq PPA.

(All amounts are in millions except where otherwise stated)

## Note 4 - Segment Reporting (cont'd)

A. Operating Segments (cont'd)

| | Year ended December 31, 2019 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Domestic fixed–line communications | Cellular communications** | International communications and Internet services** | Multi-channel television** | Others | Adjustments** | Consolidated |
| | | | Restated | | | | Restated |
| | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| Revenue from external entities | 3,757 | 2,316 | 1,283 | 1,344 | 229 | - | 8,929 |
| Inter-segment revenues | 316 | 46 | 56 | 1 | 9 | (428) | - |
| Total revenue | 4,073 | 2,362 | 1,339 | 1,345 | 238 | (428) | 8,929 |
| **Depreciation, amortization and impairment** | 861 | 633 | 190 | 219 | 14 | 147 | 2,064 |
| Segment results - operating income | 2,142 | (99) | *(196) | (135) | 1 | (1,258) | *455 |
| Finance income | 39 | 62 | 2 | 5 | - | 158 | 266 |
| Finance expenses | (608) | (23) | (8) | (17) | (1) | (81) | (738) |
| Total financing income (expense), net | (569) | 39 | (6) | (12) | (1) | 77 | (472) |
| Segment profit (loss) after finance expenses, net | 1,573 | (60) | *(202) | (147) | - | (1,181) | *(17) |
| Share in profit (loss) of equity-accounted investee | - | - | - | - | (2) | - | (2) |
| Segment profit (loss) before income tax | 1,573 | (60) | *(202) | (147) | (2) | (1,181) | *(19) |
| Income tax (benefit) | 381 | (13) | *(45) | 2 | - | 1,116 | 1,441 |
| **Segment results - net profit (loss)** | 1,192 | (47) | *(157) | (149) | (2) | (2,297) | (1,460) |
| **Additional information:** | | | | | | | |
| Segment assets | 8,091 | 4,088 | *1,080 | 1,491 | 149 | (911) | *13,988 |
| Goodwill | - | - | - | - | - | 1,559 | 1,559 |
| Investment in equity-accounted investee | - | - | 4 | - | 2 | - | 6 |
| Segment liabilities | 12,466 | 1,434 | *604 | 576 | 79 | 832 | *15,991 |
| Investments in property, plant and equipment and intangible assets | 914 | 335 | 110 | 222 | 9 | - | 1,590 |

*Restated. See Note 2.I.

** Impairment losses of the multi-channel television segment, the cellular communications segment and the International communications and internet services segment are presented as part of the adjustments (please refer to Note 9). Adjustments also include depreciation, amortization and impairment of assets resulting from the Bezeq PPA.

(All amounts are in millions except where otherwise stated)

## Note 4 - Segment Reporting (cont'd)

### B. Adjustments for segment reporting of revenue, profit or loss, assets and liabilities

| | Year ended December 31, | | |
|---|---|---|---|
| | **2017** | **2018** | **2019** |
| | **NIS** | **NIS** | **NIS** |
| **Revenue** | | | |
| Revenue from reporting segments | 9,977 | 9,503 | **9,119** |
| Revenue from other segments | 237 | 241 | **238** |
| Elimination of revenue from inter-segment sales | (425) | (423) | **(428)** |
| **Consolidated revenue** | 9,789 | 9,321 | **8,929** |

| | Year ended December 31, | | |
|---|---|---|---|
| | **2017** | **2018** | **2019** |
| | **Restated** | **Restated** | **Restated** |
| | **NIS** | **NIS** | **NIS** |
| **Profit or loss** | | | |
| Operating income for reporting segments | *2,362 | *1,243 | ***1,712** |
| Financing expenses, net | (517) | (531) | **(472)** |
| Adjustments for multi-channel television | - | - | **80** |
| Share in the losses of equity-accounted investees | (5) | (3) | **(2)** |
| Profit (loss) from operations classified in other categories | (20) | (36) | **1** |
| Depreciation and amortization of intangible assets resulting from the Bezeq PPA adjustments | (483) | *(988) | ***(152)** |
| Loss from impairment of assets (see Note 9) | - | (2,324) | ***(1,338)** |
| Other adjustments | (260) | 656 | ***152** |
| **Consolidated profit (loss) before income tax** | 1,077 | (1,983) | **(19)** |

* Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

## Note 4 - Segment Reporting (cont'd)

### B. Adjustments for segment reporting of revenue, profit or loss, assets and liabilities (cont'd)

| | December 31, | |
|---|---|---|
| | 2018 | 2019 |
| | Restated | Restated |
| | NIS | NIS |
| **Assets** | | |
| Assets from reporting segments | *15,996 | ***14,754** |
| Assets attributable to operations in other categories | 159 | **151** |
| Inter-segment assets | *- | **(124)** |
| Goodwill not attributable to segment assets | * 2,256 | ***1,559** |
| Loss from impairment of assets | *(1,638) | **(2,577)** |
| PPA not attributable to reporting segment | 1,166 | **-** |
| Assets resulting from the Bezeq PPA, net | 1,477 | **1,291** |
| Assets attributable to a non-reportable segment | (33) | ***499** |
| **Consolidated assets** | 19,383 | **15,553** |

| | December 31, | |
|---|---|---|
| | 2018 | 2019 |
| | Restated | Restated |
| | NIS | NIS |
| **Liabilities** | | |
| Liabilities from reporting segments | *17,129 | ***15,080** |
| Liabilities attributable to operations in other categories | 84 | **79** |
| Inter-segment liabilities | (1,159) | ***(1,236)** |
| Liabilities resulting from the Bezeq PPA, net | 246 | **194** |
| Liabilities attributable to a non-reportable segment | 2,476 | **1,874** |
| **Consolidated liabilities** | 18,776 | **15,991** |

* Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

## Note 5 - Cash and Cash Equivalents

As of December 31, 2018, and December 31, 2019, cash and cash equivalents include mainly bank deposits with a maturity of up to 90 days.

## Note 6 - Investments

| | December 31, 2018 | December 31, 2019 |
|---|---|---|
| | NIS | NIS |
| **Current investments** | | |
| Investments in marketable securities at fair value through profit and loss and others | 396 | **358** |
| Bank deposits | 1,384 | **883** |
| | 1,780 | **1,241** |

Bank deposits are repayable until December 2020. Investments in monetary funds and marketable securities of the Bezeq Group were disposed during 2020. A deposit used as collateral for hedging transactions is payable in December 2020.

## Note 7 - Trade and Other Receivables

### A. Composition of trade and other receivables

| | December 31, 2018 | December 31, 2019 |
|---|---|---|
| | Restated | Restated |
| | NIS | NIS |
| **Trade receivables, net*** | | |
| Outstanding debts | *711 | ***729** |
| Credit cards and checks receivable | 396 | **415** |
| Unbilled receivables | 237 | **146** |
| Current maturities of long-term receivables | 420 | **382** |
| Related parties | 11 | **5** |
| Total trade receivables | 1,775 | **1,677** |
| **Other receivables and current tax assets** | | |
| Prepaid expenses | *44 | ***39** |
| Current tax assets | *111 | ***56** |
| Other receivables (mainly from real estate sales) | 131 | **247** |
| Total other receivables | 286 | **342** |
| **Long-term trade and other receivables** | | |
| Trade receivables- open debts* (1) | 339 | **304** |
| Long term receivables (from real estate sales) | 131 | **173** |
| | 470 | **477** |
| | 2,531 | **2,496** |

* Restated. See Note 2.I.

** The amount of trade receivables is presented net of the provision for doubtful debts.

Discounted interest rates for long-term trade payables are based the estimated credit risk of trade payables. The discounted interest rates used by the Group in 2019 are 3.5%-5.6% (in 2018: 3.4%-4.6%).

(All amounts are in millions except where otherwise stated)

## Note 7 - Trade and Other Receivables (cont'd)

### B. Excepted payment dates for long-term trade and other receivables:

| | December 31, |
|---|---|
| | 2019 |
| | NIS |
| 2021 | **217** |
| 2022 | **83** |
| 2023 and thereafter | **177** |
| | **477** |

### C. Change in provision for doubtful debts during the year

| | December 31, | |
|---|---|---|
| | 2018 | 2019 |
| | NIS | NIS |
| Balance at January 1 | 92 | **87** |
| Expected credit loss recognized | 23 | **13** |
| Bad debts | (28) | **(20)** |
| Balance at December 31 | 87 | **80** |

### D. Aging of trade receivables

The aging of trade receivables at the reporting date was as follow:

| | December 31, 2018 | | December 31, 2019 | |
|---|---|---|---|---|
| | Gross | Impairment | Gross | Impairment |
| | NIS | NIS | NIS | NIS |
| Not past due | * 1,973 | (5) | ***1,800** | **(5)** |
| Past due up to one year | 151 | (34) | **185** | **(32)** |
| Past due one to two years | 38 | (16) | **34** | **(14)** |
| Past due more than two years | 39 | (32) | **42** | **(29)** |
| | * 2,201 | (87) | ***2,061** | **(80)** |

(All amounts are in millions except where otherwise stated)

## Note 8 - Property, Plant and Equipment

| | Land and buildings | Switching Transmission, power, Cellular, And satellite equipment | Network equipment | Multi-channel equipment and infrastructure | Subscriber equipment | Office equipment, computers and vehicles | Total |
|---|---|---|---|---|---|---|---|
| | Restated | | Restated | | | | |
| | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| **Cost** | | | | | | | |
| Balance as at January 1, 2018 | 1,004 | 5,865 | 5,968 | 1,200 | 1,738 | 1,076 | 16,851 |
| Additions | 22 | 396 | 213 | 247 | 311 | 86 | 1,275 |
| Disposals | (2) | - | - | (1) | (15) | (9) | (27) |
| Transfer to Investment property | (22) | - | - | - | - | - | (22) |
| Balance as at December 31, 2018 | 1,002 | 6,261 | 6,181 | 1,446 | 2,034 | 1,153 | 18,077 |
| Balance as at January 1, 2019 | **1,002** | **6,261** | **6,181** | **1,446** | **2,034** | **1,153** | **18,077** |
| Additions | **63** | **359** | **202** | **147** | **322** | **63** | **1,156** |
| Disposals | **(88)** | **(3)** | **-** | **(3)** | **(8)** | **(1)** | **(103)** |
| Transfer to assets held for sale | **(43)** | **-** | **-** | **-** | **-** | **-** | **(43)** |
| Balance as at December 31, 2019 | **934** | **6,617** | **6,383** | **1,590** | **2,348** | **1,215** | **19,087** |
| **Depreciation and impairment losses** | | | | | | | |
| Balance as at January 1, 2018 | 455 | 3,953 | 2,940 | 591 | 1,140 | 832 | 9,911 |
| Depreciation for the year | 73 | 481 | 210 | 214 | 215 | 84 | 1,277 |
| Loss from impairment of assets | 22 | - | - | 526 | - | 28 | 576 |
| Balance as at December 31, 2018 | 550 | 4,434 | 3,150 | 1,331 | 1,355 | 944 | 11,764 |
| Balance as at January 1, 2019 | **550** | **4,434** | **3,150** | **1,331** | **1,355** | **944** | **11,764** |
| Depreciation for the year | **57** | **433** | **201** | **26** | **249** | **65** | **1,031** |
| Loss from impairment of assets | ***36** | ***82** | ***63** | **106** | ***22** | ***19** | **328** |
| Balance as at December 31, 2019 | **643** | **4,949** | **3,414** | **1,463** | **1,626** | **1,028** | **13,123** |
| **Carrying amounts** | | | | | | | |
| As at January 1, 2018 | 549 | 1,912 | 3,028 | 609 | 598 | 244 | 6,940 |
| As at December 31, 2018 | 452 | 1,827 | 3,031 | 115 | 679 | 209 | 6,313 |
| As at December 31, 2019 | ***291** | ***1,668** | ***2,969** | **127** | ***722** | ***187** | **5,964** |

*Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

## Note 8 - Property, Plant and Equipment (cont'd)

**A.** The residual value of the Group's copper cables is assessed at the end of each quarter. The residual value is NIS 159 as at December 31, 2019 and NIS 168 as at December 31, 2018.

**B.** Fixed assets in the Group are derecognized at the end of each year upon reaching full depreciation, except for land, buildings, vehicles, copper cables and specific components for Pelephone's UMTS network, which are derecognized upon their sale. In 2019, the Group derecognized fully depreciated property at a cost of NIS 481 (in 2018, NIS 537).

**C.** The Group companies reviewed the useful life of the fixed assets through the depreciation committee, in order to determine the estimated useful life of their equipment. The change is not expected to have a material effect on the depreciation expenses of the Group. Following the findings of the depreciation committees, minor changes were made in the estimated useful life of certain assets.

**D.** Most of the real estate assets used by Bezeq are leased under a capitalized lease from the Israel Lands Administration as from 1993 for 49 years, with an option for an extension of another 49 years. Lease rights are amortized over the term of the lease period.

**E.** In 2013, Bezeq started to deploy a fiber optic network that will reach the subscriber's home, as a basis for future supply of advanced communications and broader bandwidths than those currently provided. In 2017, deployment of the fiber reached the state required for operation when a decision is made on the technology to be used, and Bezeq began to amortize the network. Commercial operation of the network is expected in the future.

**F.** In accordance with the Communications Order (Bezeq and Broadcasts) (Determination of Essential Service Provided by Bezeq - The Israel Telecommunication Corp., Limited), 1997, approval from the Prime Minister and Minister of Communications is required to confer rights in some of Bezeq's assets (including switches, cable network, transmission network, and information and databases).

**G.** For agreements for purchasing fixed assets please refer to Note 23.

**H.** For information about pledges see Note 24.

**I.** For information about pledges on loans and borrowings, see Note 15.

(All amounts are in millions except where otherwise stated)

# Note 9 - Intangible Assets

## A. Composition

| | Goodwill | Computer software and licenses | Right of use in cellular Frequencies** | Customer relationships and brand names | Others | Total |
|---|---|---|---|---|---|---|
| | Restated | Restated | Restated | | | Restated |
| | NIS | NIS | NIS | NIS | NIS | NIS |
| **Cost** | | | | | | |
| Balance as at January 1, 2018 | *3,079 | 2,006 | 480 | 7,479 | 221 | 13,265 |
| Acquisitions or additions from independent development | - | 220 | - | - | - | 220 |
| Disposals | - | (12) | - | - | - | (12) |
| Balance as at December 31, 2018 | 3,079 | 2,214 | 480 | 7,479 | 221 | 13,473 |
| Balance as at January 1, 2019 | ***3,079** | **2,214** | **480** | **7,479** | **221** | **13,473** |
| Acquisitions or additions from independent development | **-** | **234** | **-** | **-** | **-** | **234** |
| Disposals | **-** | **-** | **-** | **-** | **-** | **-** |
| Balance as at December 31, 2019 | **3,079** | **2,448** | **480** | **7,479** | **221** | **13,707** |
| **Amortization and impairment losses** | | | | | | |
| Balance as at January 1, 2018 | 129 | 1,456 | 271 | 5,356 | 200 | 7,412 |
| Amortization for the year | - | 226 | 20 | 290 | 6 | 542 |
| Impairment losses | *689 | 104 | - | 505 | 11 | 1,309 |
| Balance as at December 31, 2018 | 818 | 1,786 | 291 | 6,151 | 217 | 9,263 |
| Balance as at January 1, 2019 | ***818** | **1,786** | **291** | **6,151** | **217** | ***9,263** |
| Amortization for the year | **-** | **175** | **19** | **113** | **2** | **309** |
| Impairment losses | ***702** | ***111** | **20** | ***139** | **-** | **972** |
| Balance as at December 31, 2019 | **1,520** | **2,072** | **330** | **6,403** | **219** | **10,544** |
| **Carrying amounts** | | | | | | |
| As at January 1, 2018 | *2,950 | 550 | 209 | 2,123 | 21 | *5,853 |
| As at December 31, 2018 | *2,261 | 428 | 189 | 1,328 | 4 | *4,210 |
| As at December 31, 2019 | ***1,559** | ***376** | **150** | ***1,076** | **2** | ***3,163** |

## B. Total value of goodwill attributable to each cash-generating unit:

| | December 31 | |
|---|---|---|
| | 2018 | 2019 |
| | Restated | Restated |
| | NIS | NIS |
| Domestic fixed-line communications | *1,559 | ***1,559** |
| Cellular communications | 685 | **-** |
| International communications and internet services | *18 | **-** |
| Total | 2,262 | **1,559** |

* Restated. See Note 2.I.
** For Pelephone winning in frequencies tender after the date of the financial statements see Note 33.

(All amounts are in millions except where otherwise stated)

## Note 9 - Intangible Assets (cont'd)

### C. Goodwill impairment testing

For the purpose of impairment testing, goodwill is allocated to the Group's cash generating units ("CGU") which represent the lowest level within the Group at which the goodwill is monitored for internal management purposes. Several goodwill balances result from the requirement to recognize a deferred tax liability on business combination, calculated as the tax effect on the difference between the fair value of the acquired assets and liabilities, and their tax bases. For the purpose of testing this goodwill for impairment, any of the related deferred tax liabilities recognized on acquisition that remain at the balance sheet date are treated as part of the carrying amount of the relevant CGU. The annual impairment test date is December 31.

The recoverable amount of each CGU was calculated as the highest between its value in use and its fair value which was based on the Discounted Cash Flow method under the Income Approach.

**Domestic fixed-line communications (Bezeq Fixed Line)**

The value in use of the domestic fixed line cash-generating unit of the Bezeq Group was calculated by discounting future cash flows (DCF) based on a five-year cash flow forecast as at the end of the current period with the addition of the salvage value.

The cash flow forecast is based, among other things, on Bezeq's performance in recent years and assessments regarding the expected trends in the fixed-line market in the coming years (the level of competition, retail and wholesale price levels, regulation aspects, and technological developments).

Main assumptions underlying the forecast: the continued decrease in revenues from telephony (the decrease in the number of lines and erosion of average revenue per line), the erosion in short- and medium-term revenue from internet, and the return to a direction of long-term growth (supported by market growth and based on internet services over a fiber network), and increase in revenue from data communication and transmission, cloud and digital. Operating expenses, sales, marketing, and investments were adjusted to the scope of activity in the segment and in general, this includes discount forecasts regarding a gradual reduction in the Company's human resources and termination expenses and the resulting salary expenses and assumptions regarding the timing of the launch of the services based on the fiber network and regarding the deployment rate of the fiber infrastructure.

The nominal capital used in the valuation is 7.5% (after tax). In addition, a permanent growth rate of 0% was assumed.

The valuation was prepared by an external appraiser. Based on the valuation described above, the Group was not required to record an impairment loss for the domestic fixed-line communications cash-generating unit.

**Cellular communications (Pelephone)**

During the second quarter of 2019 the Company assessed the recoverable amount of the cellular communications CGU due to impairment indications. According to the valuation assessed during the second quarter 2019, the Company recognized impairment losses in the amount of NIS 1,345 which were attributed to goodwill, fixed and intangible assets. During the fourth quarter of 2019 and following changes that had a positive effect on the cellular segment, the recoverable amount of the cellular segment was reassessed and the impairment loss was partially reversed. The impairment loss and subsequent reversal in the amount of NIS 370 were recognized in impairment losses on the statement of income.

(All amounts are in millions except where otherwise stated)

## Note 9 - Intangible Assets (cont'd)

As of December 31, 2019, value in use of the cellular communications cash-generating unit of the Bezeq Group was calculated by discounting future cash flows (DCF) based on a five-year cash flow forecast as at the end of the current period with the addition of the terminal value. The cash flow forecast is based, among other things, on Pelephone's performance in recent years and assessments regarding the expected trends in the cellular market in the coming years (the level of competition, price level, regulation, and technological developments).

The main assumption underlying the forecast is that competition in the market will continue with high intensity in the short term and that stability and a certain increase will occur in the medium to long term. The revenues forecast is based on assumptions regarding the number of Pelephone subscribers, average revenue per user, and sales of terminal equipment. The forecast of expenses and investments is based, among other things, on assumptions regarding the number of Pelephone employees and the resulting salary expenses, while the other operating expenses and investments were adjusted to the projected volume of operations of Pelephone.

The circumstances that led to the recognition of an impairment loss were the lower revenues resulted from a lower ARPU forecast as a result of the price competition in the cellular market. The forecast also assumes a lower decrease in the expenses of the cellular telephone CGU, as a result of efficiency measures taken by management, however, it does not fully compensate for the expected decrease in the CGU's revenues.

In November 2019, Pelephone signed a streamlining and synergy agreement for the period from November 2019 until June 2022, and as a result, the valuation as at December 31, 2019 included recognition of streamlining measures that were not taken into account in the previous valuation as at June 30, 2019 (since they were restructured).

The nominal capital price used in the valuation is 10.3% (after tax). In addition, a permanent growth rate of 2.5% was assumed.

The valuation was prepared by an external appraiser. Based on the above valuation the recoverable amount of Pelephone is NIS 1,402. Consequently, net impairment losses of NIS 975 were recognized during 2019 from which NIS 685 were attributable to goodwill. Due to the net impairment losses of the CGU during 2019, the recoverable amount is the same as the carrying amount. The net impairment losses were first allocated to goodwill and then to the other unit assets proportionately, based on the carrying amount of each group of assets with similar characteristics, other than for assets for which the estimated fair value is higher than or the same as the carrying amount.

Allocation of the net impairment losses to assets of Pelephone as at December 31, 2019:

| | **NIS** |
|---|---|
| Fixed assets | **77** |
| Intangible assets | **122** |
| Rights of use for leased assets | **91** |
| Goodwill | **685** |
| **Net impairment recognized** | **975** |

(All amounts are in millions except where otherwise stated)

## Note 9 - Intangible Assets (cont'd)

**Multi-channel television (DBS)**

The results of the valuation of the multi-channel television cash-generating unit as at December 31, 2018 using the future discounted cash flow method (DCF) presented a value in use that is significantly lower than its carrying amount. Accordingly, the Group recognized an impairment loss of NIS 1,638 million in the multi-channel cash-generating unit, and in view of the negative value of the operations, the value of the non-current assets of DBS as at December 31, 2018 was determined as the higher of their fair value and zero.

The value in use of the multi-channel television cash-generating unit for Bezeq Group as at December 31, 2019 was calculated by discounting future cash flows (DCF) based on the seven-year cash flow forecast of DBS as at the end of the current period with the addition of the terminal value. The forecast period was chosen so that the representative year is the year following the estimated date for completion of the outline for the planned migration to internet-based broadcasting instead of satellite broadcasting, as set out below. The nominal capital price used in the valuation is 8.5% (after tax). In addition, a permanent growth rate of 0% was assumed.

The cash flow forecast was based, among other things, on the performance of DBS in recent years and assessments of the expected trends in the television market for the years ahead, including technology development, consumer preferences, competitors and the level of competition, price levels and regulatory obligations.

The main assumption underlying the forecast is that the relevant future technology will be interactive and two-way, and that a satellite product will be replaced by the IP product (television broadcasts over the internet) gradually, due to the growing gap in customer experience. As a result, the multi-year forecast reflects a plan for gradual migration (from satellite broadcasts to OTT internet streaming), and accordingly, assumptions include a gradual replacement of satellite converters with IP converters, upgrade of the broadcasting infrastructure, construction of a support system for customer service, and adaptation of content contracts for OTT broadcasts. As set out above, the forecast period reflects the period of migration from satellite broadcasts to OTT broadcasts, until complete discontinuation of satellite broadcasts. These circumstances, together with expectations for the continuation of intense competition throughout the forecast period and the relatively rigid expenditure structure, resulted in a forecast of significant operational losses and a significant negative cash flow in the coming years, and a low negative cash flow, close to a balance, is expected at the end of the forecast period in the technology and business model of DBS. It should be noted that the plan will be implemented together with an ongoing assessment of market conditions, competition, and the technological environment, and the adjustments that will be required as a result.

The valuation was prepared by an external appraiser. Based on the valuation as described above, the total value of the operations of DBS is negative, amounting to NIS 581 (as at December 31, 2018, a negative value of operations amounting to NIS 871). In view of the negative value of the operations, as at December 31, 2019, the value of the non-current assets of DBS was determined as the higher of their fair value and zero, the same as at the end of 2018.

Accordingly, the Group recognized an impairment loss of NIS 362 in 2019. The impairment loss was attributed to the assets of DBS, as set out below, and was included under depreciation, amortization and impairment, and under general and operating expenses under the statement of income, as set out in Note 3.11. above.

(All amounts are in millions except where otherwise stated)

## Note 9 - Intangible Assets (cont'd)

Allocation of impairment loss to Group assets recognized in the financial statements for 2019:

| | **NIS** |
|---|---|
| Broadcasting rights - less rights utilized (presented under operating and general expenses) | **202** |
| Fixed assets (presented under depreciation, amortization and impairment) | **117** |
| Intangible assets (presented under depreciation, amortization and impairment) | **44** |
| Rights of use in leased property (reduced expense presented under depreciation, amortization and impairment) | **(1)** |
| **Total impairment recognized** | **362** |

It should be noted that as a result of the negative value of operations as of December 31, 2019, DBS continued impairment its non-current assets also during 2020 to its net assets value. These impairment losses amounted to NIS 217 in the nine months ended September 30, 2020.

Allocation of impairment loss to Group assets recognized in the financial statements for 2018:

| | **NIS** |
|---|---|
| Broadcasting rights, net of rights exercised | 403 |
| Fixed assets | 559 |
| Intangible assets | 106 |
| Subscriber acquisition (assessed under IFRS 15) | 29 |
| Rights of use for leased assets | 3 |
| **Total impairment recognized in the statements of DBS** | **1,100** |
| Customer relations and branding | 505 |
| Goodwill | 33 |
| **Total impairment loss of assets** | **1,638** |
| Write-off of deferred tax attributed to customer relations and branding | (114) |
| **Total impairment loss of multi-channel television cash-generating unit after tax** | **1,524** |

Below is information about the Group's method for measuring the fair value of the assets of DBS, which were impaired as set out above:

Broadcasting rights: Measurement of the fair value of broadcasting rights took into account legal restrictions on their sale and based on the production stage, the probability of sale, and the expected rate of return on the investment in them.

Property, plants and equipment: The fair value of fixed asset items that are available for sale to a market participant (mainly converters) is based on their estimated selling value on the valuation date less selling costs.

Intangible assets: Material fair value was not attributed to the intangible assets of DBS, since most of the software and licenses of DBS were uniquely adapted to DBS, and therefore they have no material value in a transaction between a willing buyer and a willing seller.

Rights of use for leased assets: The fair value of right-of-use assets is affected by the ability to lease the asset underlying the lease to a third party, the lease fees of the property on the market, and the exit penalties in the lease contract.

## Note 9 - Intangible Assets (cont'd)

**International communications and Internet services (Bezeq International)**

As described on Note 2.I above and as a result of Bezeq International findings regarding differences in its assets and liabilities balances on its financial statements and the correction of its profitability for the years 2018 and 2019, the valuations of the CGU were updated for both December 2018 and 2019.

As described in note 2.I above, Bezeq International recalculated certain balances in its financial statements without relying on previous records and existing methodologies, in respect to balances with the aforementioned error. The recalculation was done with the assistance of an external consultant and other monitoring and internal audit reports that were examined during the process. The complexity and the methodology used under the tight timetable, did not allow for full investigation of the gaps and their impact on the forecasts used for the valuation works. Bezeq International estimates that the restatement's impact on the operating income will continue to influence all forecasted years including the terminal year.

As a result of the updated forecasts, the updated value in use of Bezeq International for December 31, 2018 was decreased to NIS 970 while its carrying amount was decreased to NIS 1,527. Therefore, the updated impairment loss for 2018 was increased to NIS 171, which was attributable to goodwill.

The value in use of the international communications, ISP and NEP services cash-generating unit for Bezeq Group was calculated by discounting future cash flows (DCF) based on a five-year cash flow forecast as at the end of the current period with the addition of the salvage value.

The cash flow forecast is based, among other things, on Bezeq International's performance in recent years and assessments regarding the expected trends in the markets in which it operates in the coming years (the level of competition, price level, regulation, and technological developments).

The updated revenue forecast for December 31, 2019 valuation is based on assumptions regarding the number of Bezeq International internet subscribers and the average revenue per subscriber, Bezeq International's operations in the international communications market, and its development in communications services for businesses. The updated expenses forecast is based, among other things, on assumptions regarding the extent of the decrease in the number of Bezeq International employees and the related salary expenses and the assumptions regarding the development of internet traffic costs (retail and wholesale prices and development of television broadcasts over the internet in general, and the expected migration of DBS from satellite television broadcasts to television broadcasts over the internet in particular). The other operating expenses and level of investments were adjusted to the updated forecasted scope of Bezeq International's operations.

The nominal capital price used in December 31, 2019 valuation is 9.7% (after tax). In addition, a permanent growth rate of 0.7% was assumed. These parameters were not changed from the original valuation.

The updated valuation was prepared by an external appraiser. Based on the updated valuation, Bezeq International CGU recoverable amount as of December 31, 2019 is NIS 374. Consequently, impairment losses of NIS 364 were recognized of which NIS 18 were attributable to goodwill. Due to the impairment of the CGU, the recoverable amount is the same as the carrying amount. The impairment loss was first attributed to goodwill and then to the other unit assets proportionately, based on the carrying amount of each group of assets with similar characteristics, other than for assets for which the estimated fair value is higher than or the same as the carrying amount.

(All amounts are in millions except where otherwise stated)

## Note 9 - Intangible Assets (cont'd)

The circumstances that led to the recognition of an impairment loss are the lower revenues resulted from the fierce competition in the Internet Service Provider market along with the wholesale market and lower revenues from the International Long-Distance market. The forecast also assumes a lower decrease in the expenses of the CGU, as a result of efficiency measures taken by management, however, it does not fully compensate for the expected decrease in the CGU's revenues.

Allocation of the impairment loss to assets of Bezeq International as at December 31, 2019:

| | NIS |
|---|---|
| Fixed assets | **131** |
| Intangible assets | **100** |
| Long-term prepaid expenses for capacity | **114** |
| Rights of use for leased assets | **1** |
| Goodwill | **18** |
| **Total impairment recognized** | **364** |

For additional developments regarding Bezeq International and additional impairment during 2020 please refer to Note 33.

## Note 10 - Deferred Expenses and Non-Current Investments

| | December 31 | |
|---|---|---|
| | 2018 | 2019 |
| | Restated | Restated |
| | NIS | NIS |
| Deferred expenses (A) | * 276 | ***130** |
| Subscriber acquisition asset, net (C) | 142 | **160** |
| Deposit used as collateral against hedging transactions | 41 | **-** |
| Bank deposit for loans to Company employees (B) | 48 | **44** |
| Investments in equity-accounted investee | 8 | **6** |
| | 515 | **340** |

* Restated. See Note 2.I.

A. For its operations, Bezeq International acquires indefeasible rights of use ("IRU") from Mediterranean Nautilus (Israel) Ltd. for the acquisition of seabed cable capacities, which are accounted for as service transactions.

Under the contract, Bezeq International has the right of use for capacities until 2022 with an option for an extension until 2027, which Bezeq International is expected to exercise. The value of the service is amortized on a straight line until 2027. The balance of the right of use of capacities is recognized net of impairment of assets in the amount of NIS 114 (see Note 9 for information about impairment of Bezeq International's assets). The balance of Bezeq International's liability for the agreement is US$ 8.4.

B. A bank deposit for loans to Company employees without a repayment date

(All amounts are in millions except where otherwise stated)

## Note 10 - Deferred Expenses and Non-Current Investments (cont'd)

### C. Subscriber acquisition assets:

| | Subscriber acquisition assets |
|---|---|
| | NIS |
| **Cost** | |
| Balance as at January 1, 2018 | 196 |
| Additions | 164 |
| Disposals | (27) |
| Balance as at December 31, 2018 | 333 |
| **Additions** | **130** |
| **Disposals** | **(25)** |
| **Balance as at December 31, 2019** | **438** |
| **Amortization and impairment losses** | |
| Balance as at January 1, 2018 | 81 |
| Depreciation | 108 |
| Disposals | (27) |
| Impairment loss | 29 |
| Balance as at December 31, 2018 | 191 |
| **Depreciation** | **112** |
| **Disposals** | **(25)** |
| **Balance as at December 31, 2019** | **278** |
| **Carrying amount** | |
| As at January 1, 2018 | 115 |
| As at January 1, 2019 | 142 |
| As at December 31, 2019 | **160** |

## Note 11 - Broadcasting Rights, Net of Rights Exercised

| | December 31 | |
|---|---|---|
| | 2018 | 2019 |
| | NIS | NIS |
| Cost | 1,010 | **1,242** |
| Less rights exercised | (547) | **(578)** |
| Impairment loss (see Note 9) | (403) | **(605)** |
| Total | 60 | **59** |

For further information about the Group's agreements for acquisition of broadcasting rights, see Note 23, Agreements.

**Notes to the Consolidated Financial Statements**

(All amounts are in millions except where otherwise stated)

# Note 12 - Investees

## A. Material subsidiaries held directly and indirectly by the Company

1. General

| | Principal location of the company's activity | Ownership interest |
|---|---|---|
| B Communications (SP1) Ltd. and B Communications (SP2) Ltd. (1) | Israel | 100% |
| Bezeq - The Israel Telecommunication Corp. Limited | Israel | 26.34% |
| Subsidiaries of Bezeq - The Israel Telecommunication Corp. Limited | | |
| Pelephone Communications Ltd. | Israel | 100% |
| Bezeq International Ltd. | Israel | 100% |
| DBS | Israel | 100% |
| Walla! Communications Ltd. | Israel | 100% |

(1) Held by B Communications (SP1) Ltd.

(2) Details of Group entities

a. **B Communications (SP1) Ltd. and B Communications (SP2) Ltd.**
B Communications (SP1) Ltd. ("SP1"), founded in 2010, is a wholly-owned subsidiary of the Company. SP1 is the sole shareholder of B Communications (SP2) Ltd. ("SP2") which directly holds the Bezeq controlling interest.

b. **Bezeq - The Israel Telecommunications Corporation Ltd.**
Bezeq is controlled by SP2 which holds 25.82% of Bezeq’s outstanding shares. An additional 0.52% of Bezeq outstanding shares are held by B Communications directly. Bezeq is the largest communications group in Israel.

c. **Pelephone Communications Ltd.**
Pelephone Communications Ltd. ("Pelephone") is a wholly-owned subsidiary of Bezeq. Pelephone provides cellular communication services and value-added services and terminal equipment.

d. **Bezeq International Ltd.**
Bezeq International Ltd. ("Bezeq International") is a wholly-owned subsidiary of Bezeq. Bezeq International provides internet access (ISP) services, international communications services and network end point (NEP) services.

e. **D.B.S. Satellite Services (1998) Ltd.**
D.B.S Satellite Services (1998) Ltd. ("DBS") is a wholly-owned subsidiary of Bezeq. DBS provides multi-channel television services.

f. **Walla! Communications Ltd.**
Walla! is wholly owned by Bezeq. Walla! provides internet, management and media services for a range of populations.

(All amounts are in millions except where otherwise stated)

# Note 12 - Investees (cont’d)

## A. Material subsidiaries held directly and indirectly by the Company (cont'd)

3. Bezeq did not pay dividend to non-controlling interests during 2019 (in 2018: NIS 505).

4. Bezeq’s Dividend Distribution Policy:

On August 4, 2009, the Board of Directors of Bezeq approved a dividend distribution policy in which Bezeq will distribute a dividend to its shareholders amounting to 100% of the semi-annual profit (after tax) (profit for the period attributable to the shareholders of Bezeq), in accordance with the consolidated financial statements of Bezeq.

On March 6, 2018, the Board of Directors of Bezeq resolved to revise the dividend distribution policy, such that Bezeq will distribute a dividend to its shareholders, on a semi-annual basis, of 70% of the semi-annual net profit in accordance with the consolidated financial statements of Bezeq, as from the next distribution following the resolution.

On March 27, 2019, Bezeq's Board of Directors resolved to cancel the Company's dividend distribution policy. The resolution was passed after a presenting a clear and transparent position with the shareholders and under the circumstances that arose due to the inability to distribute a dividend due to the expected failure to meet the profit test in the next two years. Accordingly, the Board of Directors resolved that it would not be appropriate to maintain a dividend policy when in practice it is not effective.

The cancellation of the policy will not prevent Bezeq's Board of Directors from assessing, from time to time, the distribution of dividends to its shareholders, taking into consideration, among other things, the provisions of the law, the state of its business and its capital structure, while maintaining a balance between ensuring its financial strength and stability, including its debt level and credit rating, and the continued attribution of value to its shareholders through ongoing distribution of a dividend, all subject to the approval of the general meeting of its shareholders regarding each specific distribution, as set out in Bezeq's articles of association.

As a result of the high losses of the Bezeq Group during the last two years, Bezeq will not be able distribute dividends to its shareholders during the next two years. The company has sufficient funds to serve its own debt until November 2024 even with no dividends from Bezeq.

On May 10, 2018, Bezeq distributed a cash dividend of NIS 368, representing 70% of its net profit for the second half of 2017. The Company received NIS 97 as its share of the dividend distribution.

On October 10, 2018, Bezeq distributed a cash dividend of NIS 318, representing 70% of its net profit for the first half of 2018. The Company received NIS 84 as its share of the dividend distribution.

(All amounts are in millions except where otherwise stated)

## Note 12 - Investees (cont'd)

### A. Material subsidiaries held directly and indirectly by the Company (cont'd)

Bezeq declared and paid the following dividends in cash:

| | 2017 | 2018 | 2019 |
|---|---|---|---|
| | NIS | NIS | NIS |
| **Distribution of a regular dividend** | | | |
| NIS 0.25 per share | - | 686 | - |
| NIS 0.47 per share | 1,286 | - | - |

5. On February 13, 2019, Bezeq's Board of Directors approved the request of each of the subsidiaries Pelephone, Bezeq International and DBS to apply to the Ministry of Communications for approval to change the corporate structures according to which the full operations and assets of each of the subsidiaries will be transferred to a separate limited partnership, wholly-owned by Bezeq (Bezeq as a limited partnership and a company (separate and different in each partnership), wholly owned by Bezeq as a general partner).

On January 28, 2020, Bezeq received a letter from the Ministry of Communications that it was not possible to approve the application at that time. This was for reasons that Bezeq believes are mistaken including, because there is no room to take interim decisions that might affect the issue of structural separation in the Group and change the existing range of incentives, while the obligation of structural separation applied to the Group is currently being examined by a special team at the Ministry of Communications. As part of its examination, a broad range of alternatives are being assessed - from cancellation of the obligation of separation to strengthening the separation. In addition, in the Ministry's opinion, this is a material change in the Group's operations and not a technical change of the corporate structure.

For agreement to sell Walla subsidiary after the date of the financial statements please refer to Note 33.

### B. DBS Satellite Services (1998) Ltd.

1. As at March 25, 2015, Bezeq held 49.78% of the share capital of DBS and it held options that confer the right to 8.6% in DBS shares, which Bezeq is unable to exercise. The balance of DBS shares was held by Eurocom DBS Ltd. (a company that was controlled (indirectly) by the controlling shareholder in Bezeq at that time). On March 25, 2015, Bezeq exercised the options that were allotted, for no consideration, and on June 24, 2016, Bezeq completed a transaction for the acquisition of the entire holdings of Eurocom DBS in DBS, and all of the owners loans provided by Eurocom to DBS ("the Acquisition Transaction").

On the completion date, Bezeq transferred the cash consideration of NIS 680 to Eurocom DBS for the Acquisition Transaction.

Under the terms of the Acquisition Transaction, in addition to the cash consideration of NIS 680, the consideration included two additional contingent considerations, as follows: one additional consideration of up to NIS 200, which will be paid in accordance with the tax synergy according to the terms defined in the acquisition agreement ("the First Contingent Consideration"); and another additional consideration of up to NIS 170, which will be paid in accordance with the business results of DBS in the 2015-2017 ("the Second Contingent Consideration").

(All amounts are in millions except where otherwise stated)

## Note 12 - Investees (cont'd)

On completion of the Acquisition Transaction, DBS became a wholly owned subsidiary (100%) of Bezeq. Bezeq consolidates the financial statements of DBS as from March 23, 2015.

Most of the First Contingent Consideration was paid after Bezeq signed an assessment agreement and the taxation decision of the Tax Authority regarding financing income, shareholder loans, the losses of DBS, and its merger.

Bezeq paid an advance of NIS 119 on account of the second contingent consideration. In accordance with the financial results of DBS for 2017, and since the final amount of the Second Contingent Consideration was lower than the amount of advances that Bezeq paid Eurocom DBS for the consideration, Eurocom DBS is required to return the difference to Bezeq. In this context, Bezeq joined the proceedings as creditor for liquidation of Eurocom Communications. In addition, following Bezeq's demand for Eurocom DBS to pay Bezeq the amount of the down payment on account of the Second Contingent Consideration plus interest as set out in the agreement, after the goals entitling Eurocom DBS to this consideration were not achieved, on April 22, 2018, the Tel Aviv District Court, at Bezeq's request, handed down a liquidation order for Eurocom DBS and Bezeq's legal counsel was appointed as the liquidator for Eurocom DBS. According to Bezeq's estimate as of December 31, 2019, taking into consideration the solvency of Eurocom DBS, no repayment of the advances is expected.

2. On March 13, 2019, Bezeq's Board of Directors approved a resolution of the Board of Directors of DBS to approve a plan for migration from satellite broadcasts to broadcasts over the internet (OTT) in a gradual, long-term process that is expected to spread over seven years. As from December 2019, alongside its satellite services, DBS offers the yes+ service, which includes linear TV channels, as well as VOD content and an advanced technological interface.
3. In 2018, Bezeq converted the balance of DBS debentures in the amount of NIS 422, which it held, to DBS capital, converted the shareholders' loan to DBS in the amount of NIS 97 to DBS capital, and invested an additional NIS 100 in DBS.
4. As at December 31, 2019, DBS has an equity deficit in the amount of NIS 105 and a working capital deficit in the amount of NIS 282. According to the forecasts of DBS, it expects to continue to accumulate operational losses in the coming years and therefore will be unable to meet its obligations and continue operating as a going concern without Bezeq's support.

   On February 13, 2019, Bezeq provided DBS with a letter of undertaking for a credit facility or capital investments in the amount of NIS 250, which DBS can withdraw for a period of 15 months from that date. Insofar as the support is provided by way of credit, the repayment date of the credit will not be earlier than the end of the term of the credit facility. The letter of undertaking was replaced by new letters of undertaking in a total amount of NIS 250 in May, August, and November 2019, with each letter of undertaking replacing the preceding one (and not in addition to). The last letter of undertaking is valid for 15 months as from October 1, 2019 and until December 31, 2020.

   In 2019, Bezeq invested NIS 145 in DBS, in accordance with the letters of undertaking as aforesaid.

(All amounts are in millions except where otherwise stated)

## Note 12 - Investees (cont'd)

During 2020, Bezeq's Board of Directors approved once a quarter, an irrevocable undertaking of Bezeq to DBS to provide a credit facility or a capital investment of NIS 250 for 15 months, while the last approval was given in August 2020 and was valid till September 30, 2021. During the nine months ended September 30, 2020, DBS did not use any of this credit facility.

In November 2020, Bezeq's board of directors approved an irrevocable undertaking of Bezeq to DBS to provide a credit facility or a capital investment of NIS 150 for 15 months, from October 1, 2020 till December 31, 2021, instead of the undertaking from August 2020.

5. The management of DBS believes that the financial resources at its disposal, which include the credit facility, and Bezeq's capital investments, as set out in section 12.B.4 above, will be adequate for the operations of DBS for the coming year.

### C. Non-controlling interests in subsidiaries

The table hereunder presents summary information of the Group's subsidiaries including fair value adjustments that were made on the date of acquisition, other than goodwill, in which there are non-controlling interests that are material to the Group.

| | December 31, | | | | | | |
|---|---|---|---|---|---|---|---|
| | Rate of ownership interests held by non-controlling interests | Current assets | Non-current assets | Current liabilities | Non-current liabilities | Total net assets | Carrying amount of non-controlling interests |
| | | Restated | | | | | |
| | % | NIS | | | | | |
| **2019** | | | | | | | |
| **Bezeq Group** | **73.66** | ***3,754** | ***10,003** | ***3,817** | **10,301** | ***(361)** | ***(197)** |
| 2018 | | | | | | | |
| Bezeq Group | 73.66 | *4,450 | *12,345 | *4,599 | 11,702 | *494 | *433 |
| 2017 | | | | | | | |
| Bezeq Group | 73.66 | *4,861 | *14,203 | *4,398 | 12,376 | *2,290 | *1,757 |

*Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

## Note 12 - Investees (cont'd)

| | Revenues | Profit (loss) | Other comprehensive Income (loss) | Total comprehensive Income (loss) | Profit (loss) attributable to non-controlling interests | Total comprehensive Income (loss) attributable to non-controlling interests | Cash flow from operating activities | Cash flow from investing activities | Cash flow from financing activities without dividend to non-controlling interests | Dividend paid to non-controlling interests | Total increase (decrease) in cash and cash equivalents |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Year ended December 31, | | | | | | | | | | |
| | NIS | | | | | | | | | | |
| | Restated | | | | | | | | | | |
| **2019** | | | | | | | | | | | |
| **Bezeq Group** | **8,929** | ***(822)** | **(32)** | ***(854)** | ***(605)** | ***(628)** | **2,924** | **(883)** | **(2,531)** | **-** | **(490)** |
| 2018 | | | | | | | | | | | |
| Bezeq Group | 9,321 | *(1,154) | 42 | *(1,112) | *(850) | *(819) | 3,512 | (2,552) | (1,746) | (505) | (1,291) |
| 2017 | | | | | | | | | | | |
| Bezeq Group | 9,789 | *888 | (8) | *880 | *655 | *649 | 3,525 | (1,148) | 104 | (948) | 1,533 |

* Restated. See Note 2.I.

**D. The Company's control over Bezeq**

The Company has control over Bezeq based on two facts: (i) the Company holds significantly more voting rights than any other shareholder and the holdings in Bezeq are widely dispersed, and (ii) the Israeli law and regulations require prior ministerial approval for any person to acquire holdings in Bezeq exceeding 5% or to take actions together with other shareholders to cause the appointment of a director in Bezeq and or to influence Bezeq's day-to-day operational decision-making policies. By these restrictions, the regulatory regime ensures that no individual or entity will interfere with the control of Bezeq by the holder of the Control Permit and that the Company is able to nominate the majority of the board of directors of Bezeq.

(All amounts are in millions except where otherwise stated)

## Note 13 - Disposal of Investment Property

On January 21, 2018, Bezeq signed an agreement for the sale of a real estate asset in the Sakia property and on May 5, 2019, the transaction was completed. The total consideration received by Bezeq for the asset (including linkage differences and interest under the provisions of the agreement) amounted to NIS 511 plus VAT.

On May 21, 2018, Bezeq received a demand from the Israel Lands Authority ("the ILA") for payment of a permit fee in the amount of NIS 148 plus VAT, for the asset betterment plan approved prior to signing the agreement ("the Demand"). Bezeq filed an objection on the legal argument of the Demand. On January 20, 2019, the ILA dismissed all of Bezeq's claims in the legal objection, however, the parties are currently negotiating within the mechanism to settle disputes set out in the settlement agreement (the agreement of 2003 between Bezeq and the ILA and the State regarding most of the real estate assets, including the real estate in the Sakia property, which was transferred to Bezeq under the asset transfer agreement signed before the initiation of Bezeq's business operations). If this mechanism does not bring the dispute to an end, Bezeq will file a monetary claim petitioning the court to order the ILA to refund the permit fees paid by Bezeq and to order the ILA to pay the demand for the betterment tax. At the same time, Bezeq filed an assessment objection on the Demand.

On August 5, 2018, Bezeq received a demand for payment from the local planning and building committee in Or Yehuda, for betterment tax in the amount of NIS 143.5 for disposal of the property by way of a sale ("the Demand for Betterment Tax"). On September 17, 2018, Bezeq filed an appeal on the Demand for Betterment Tax and sent the ILA a demand for full payment of the betterment tax according to the ILA's undertaking in the settlement agreement. On January 2019, the ILA dismissed Bezeq's Demand for Betterment Tax. On completion of the transaction as aforesaid and the receipt of the full consideration, Bezeq paid half of the betterment tax in the amount of NIS 75 and provided a bank guarantee for the other half of the tax, without this derogating from or impairing the steps taken by or to be taken by Bezeq to cancel or reduce this tax. It should be noted that the amount for the permit fee to be determined at the end of the proceedings may also affect the amount of the betterment tax Bezeq will be required to pay to the Planning Committee. Bezeq believes that the amount of the permit fee and the betterment tax that it will be required to pay is expected to be low and possibly even lower than the total amount of the demands.

Bezeq recognized a capital gain of NIS 403 in its financial statements for 2019. Recognition of the capital gain is based on Bezeq's estimates of the final amount to be paid to the authorities. It should be noted that if Bezeq's estimates do not materialize, the amounts of the final capital gain will be between NIS 250 and NIS 450.

(All amounts are in millions except where otherwise stated)

# Note 14 - Leases

As set out in Note 3.7, as from January 1, 2018, the Group early applies IFRS 16, Leases. Under the lease agreements, the Group leases mainly cellular communications sites, structures (including offices, warehouses, communication rooms, and points of sale), and vehicles.

## A. Right of use assets

| | Communications sites | Buildings | Vehicles | Total |
|---|---|---|---|---|
| | | Restated | | Restated |
| | NIS | NIS | NIS | NIS |
| **Cost** | | | | |
| Balance as at January 1, 2018 | 809 | 538 | 173 | 1,520 |
| Additions** | 159 | 15 | 146 | 320 |
| Derecognition for terminated agreements | (45) | (9) | (11) | (65) |
| Changes in agreements (mainly extension of the agreement periods) and revaluation | 43 | 81 | (22) | 102 |
| Balance as at December 31, 2018 | **966** | **625** | **286** | **1,877** |
| Additions** | **146** | **34** | **28** | **208** |
| Derecognition for terminated agreements | **(71)** | **(13)** | **(27)** | **(111)** |
| Balance as at December 31, 2019 | **1,041** | **646** | **287** | **1,974** |
| **Amortization and impairment losses** | | | | |
| Balance as at January 1, 2018 | - | - | - | - |
| Amortization for the year | 190 | 120 | 113 | 423 |
| Derecognition for terminated agreements | (18) | (4) | (9) | (31) |
| Changes in agreements and other | (3) | (1) | (18) | (22) |
| Impairment loss | - | - | 3 | 3 |
| Balance as at December 31, 2018 | **169** | **115** | **89** | **373** |
| Amortization for the year | **185** | **120** | **110** | **415** |
| Derecognition for terminated agreements | **(65)** | **(5)** | **(25)** | **(95)** |
| Changes in agreements and other | **(4)** | **(2)** | **(21)** | **(27)** |
| Impairment loss (see Note 9) | **82** | ***9** | **-** | **91** |
| Balance as at December 31, 2019 | **367** | **237** | **153** | **757** |
| **Carrying amount** | | | | |
| January 1, 2018 | 809 | 538 | 173 | 1,520 |
| December 31, 2018 | 797 | 510 | 197 | 1,504 |
| **December 31, 2019** | **674** | ***409** | **134** | **1,217** |

* Restated. See Note 2.I.
** Additions for new agreements and amendments to existing agreements

(All amounts are in millions except where otherwise stated)

## Note 14 - Leases (cont'd)

### B. Lease liabilities

| | Communications sites | Buildings | Vehicles | Total |
|---|---|---|---|---|
| | NIS | NIS | NIS | NIS |
| Balance as at January 1, 2018 | 809 | 538 | 188 | 1,535 |
| Additions * | 204 | 101 | 141 | 446 |
| Disposals | (27) | (5) | (2) | (34) |
| Financing expenses for lease liabilities | 14 | 9 | 3 | 26 |
| Payments for a lease | (190) | (124) | (108) | (422) |
| **Balance as at December 31, 2018** | **810** | **519** | **222** | **1,551** |
| Additions ***** | **150** | **32** | **53** | **235** |
| Disposals | **(6)** | **(8)** | **(2)** | **(16)** |
| Financing expenses for lease liabilities | **16** | **9** | **4** | **29** |
| Payments for a lease | **(180)** | **(124)** | **(110)** | **(414)** |
| **Balance as at December 31, 2019** | **790** | **428** | **167** | **1,385** |
| | | | | |
| **Carrying amount as at December 31,2018** | | | | |
| Current maturities of a lease liability | 203 | 124 | 118 | 445 |
| Long-term liabilities for a lease | 607 | 395 | 104 | 1,106 |
| **Total balance as at December 31, 2018** | 810 | 519 | 222 | 1,551 |
| | | | | |
| **Carrying amount as at December 31,2019** | | | | |
| Current maturities of a lease liability | **197** | **123** | **96** | **416** |
| Long-term liabilities for a lease | **593** | **305** | **71** | **969** |
| **Total balance as at December 31, 2019** | **790** | **428** | **167** | **1,385** |

* Additions for new agreements and amendments to existing agreements

1. **Analysis of repayment dates of liabilities for the Group's lease (including principal and interest to be paid)**

| **Expected payment dates** | **December 31, 2019** |
|---|---|
| | **NIS** |
| Up to one year | **419** |
| 1-5 years | **743** |
| More than five years | **320** |
| **Total** | **1,482** |

(All amounts are in millions except where otherwise stated)

## Note 14 - Leases (cont'd)

### 2. Options to terminate or extend a lease

In most of its leases, the Group assumed that it is reasonably certain that the extension option in the agreements will be exercised, therefore there are no material liabilities in respect of leases that were not presented in the financial statements.

Most of the lease agreements include an option to cancel the agreement with notice and/or payment of a penalty as set out in the agreements. The Group assumed that it is reasonably certain that the cancellation options will not be exercised.

### 3. Information about material lease agreements not yet included in measurement of the lease liability

In December 2018, Bezeq entered into an agreement to lease part of an office and commercial building. The agreement is for ten years and includes three option periods up to 24 years and 8 months, as from January 1, 2021. The annual rent amounts to NIS 20.

The right-of-use asset and liability for the lease was recognized in the financial statements at the date ownership of the asset is transferred, at the end of 2020.

## Note 15 - Bank Loans and Debentures

### A. Composition

| | December 31 | |
|---|---|---|
| | **2018** | **2019** |
| | **NIS** | **NIS** |
| **Current liabilities** | | |
| Current maturities of debentures | 3,376 | **590** |
| Current maturities of bank loans | 621 | **417** |
| | 3,997 | **1,007** |
| **Non-current liabilities** | | |
| Debentures | 5,537 | **7,443** |
| Bank loans | 4,100 | **2,969** |
| | 9,637 | **10,412** |
| | 13,634 | **11,419** |

(All amounts are in millions except where otherwise stated)

## Note 15 - Bank Loans and Debentures (cont'd)

### B. Debt terms and repayment schedule

| | December 31, 2018 | | December 31, 2019 | | | Nominal |
|---|---|---|---|---|---|---|
| | Par value | Carrying amount | Par value | Carrying amount | Currency | interest rate |
| | NIS | NIS | NIS | NIS | | % |
| **Loans from banks and others:** | | | | | | |
| Unlinked - Variable interest | 500 | 500 | **-** | **-** | **NIS** | P-0.33 to P+0.2 |
| Unlinked - Fixed interest | 4,208 | 4,221 | **3,376** | **3,386** | **NIS** | 3.2 to 6.85 |
| | 4,708 | 4,721 | **3,376** | **3,386** | | |
| **Debentures:** | | | | | | |
| Linked to the Israeli CPI - fixed interest | 3,290 | 3,464 | **3,181** | **3,263** | **NIS** | 2.1 to 3.7 |
| Unlinked - variable interest | 587 | 586 | **107** | **107** | **NIS** | zero-coupon bond for one year + 1.4 |
| Unlinked - fixed interest | 4,811 | 4,863 | **4,784** | **4,663** | **NIS** | 3.6 to 6.65 |
| | 8,688 | 8,913 | **8,072** | **8,033** | | |
| **Total interest-bearing liabilities** | 13,396 | 13,634 | **11,448** | **11,419** | | |

For developments regarding the Group's debt after the balance sheet date please refer to Note 33.

### C. Debt issued by the Company

1) On September 21, 2010, the Company issued NIS 400 of its Series B Debentures at par value to the public in Israel. In January 2012, August 2013 and April 2016, the Company completed private placements of additional Series B Debentures in the amount of NIS 126, NIS 180 and NIS 148 par value, respectively, to certain Israeli institutional investors.

   The Series B Debentures were denominated in NIS, bear interest at a fixed annual rate of 6.5% which was payable semi-annually. The principal of the Series B Debentures was paid in four annual equal installments from 2016 till 2019.

   The Company fully repaid its Series B Debentures (including accumulated interest) on December 2, 2019 as part of the Searchlight-Fuhrer transaction.

(All amounts are in millions except where otherwise stated)

## Note 15 - Bank Loans and Debentures (cont'd)

### C. Debt issued by the Company (cont'd)

2) On September 18, 2016, the Company issued, at par value, NIS 1.9 billion of Series C Debentures to the public in Israel. The principal of the Series C Debentures was payable in four equal instalments on November 30 of each of the years 2020 through 2023 and one instalment payable on November 30, 2024. Each of the first four instalments was equal to 7.5% of the principal amount of the aggregate amount of the Series C Debentures issued and the last instalment was equal to 70% of such principal amount. The annual coupon of the Series C Debentures was 3.6% and is denominated in NIS. The interest on the outstanding principal of the Series C Debentures was payable in semi-annual payments on May 31 and November 30 of each year.

On January 16, 2017, and January 23, 2018, the Company completed a private placements of NIS 118 par for consideration of NIS 118 and NIS 240 par value for NIS 249, respectively, of its Series C Debentures to Israeli institutional investors.

On December 2, 2019 as part of the Searchlight-Fuhrer Transaction, the company completed the following actions:

- Early repayment of NIS 614 par value of its Series C Debentures including payment of accrued interest as of this date;
- Private placement of NIS 310 par value of its Series C Debentures to Internet Gold;
- Exchange of NIS 58 par value of its Series C debentures to new Series D debentures;
- Increased the interest on Series C debentures to 3.85%;
- Replaced all covenants related to credit ratings, book equity, etc with LTV covenants as described below
- Provided Series C and D second lien on the Company's 26.34% stake in Bezeq
- Completed a public placement of NIS 100 par value of Series E Debentures

Series C, D and E Debentures are payable in one payment on November 30, 2024. The annual coupon of the three series is 3.85% and is denominated in NIS. The interest on the outstanding principal of the three Series is payable in semi-annual payments on May 31 and November 30 of each year from 2020 to 2024.

Under the terms of the Series C, D and E, the Company must deposit the next semi-annual intertest payment in accounts pledged as collateral to the trustee of the debentures for the benefit of the holders of the Debentures. As of December 31, 2019, the Company deposited NIS 39 in those pledged accounts, which are presented under restricted cash on the Company's statement of financial position.

As at December 31, 2019 the outstanding par value of Series C, D and E Debentures was NIS 2,036.

Below are the main undertakings and covenants with respect to the Company's Debentures:

**Loan to Value (LTV) ratio**

A. The LTV ratio shall not exceed the following during two consecutive quarters:
   (1) an 80% rate by November 30, 2023; and
   (2) a 75% rate from December 1, 2023 to the full and final maturity date of the debentures.

B. The LTV ratio will first become effective after a period of 24 months from the closing date (December 2, 2019).

(All amounts are in millions except where otherwise stated)

## Note 15 - Bank Loans and Debentures (cont'd)

### C. Debt issued by the Company (cont'd)

C. The LTV compliance test will be conducted at the time of inspection, with the first test being conducted at the test date in the calendar quarter during which a period of 24 months from the closing date will expire.

**Restrictions on dividend distributions**

The Company undertook not to distribute a dividend to its shareholders and/or perform a buyback of its shares and/or any other distribution as defined in the Israeli Companies Law unless all the conditions provided below are satisfied:

a. The Company is not in violation of any of the covenants;
b. No grounds for immediate repayment exist at the time a resolution to make a distribution is adopted, and no such grounds exist as a result of such distribution; and
c. LTV ratio post distribution must not exceed 65%.

**Lien on Bezeq Shares**

Series E Debentures have a first lien on the Company's 26.34% holdings in Bezeq while the Series C and D Debentures have a second lien on the same holdings. The Ministry of Communications approved the pledge and provided a pledge permit to the Debentures trustee.

**Control of Bezeq**

The Company undertook to hold (directly and/or indirectly) at least 25% of Bezeq's issued and paid-up capital, unless a regulatory permit/approval is received to reduce such shareholding percentage.

**Control of the Company**

Searchlight and the Fuhrer Group undertook to refrain from transferring control of the Company (directly or indirectly) to a party which has not been authorized in advance by the necessary regulatory entities, to the extent such approvals are required, at the relevant time.

**Gain from debt restructuring**

The Company concluded that the Searchlight-Fuhrer transaction detailed above gave rise to a substantial modification of the terms of the outstanding Series C debentures. As a result, the Company derecognized the original financial liability related to Series C debentures, and recognized a new financial liability measured at the quoted market price as of the closing date of Series C debentures as modified by the Searchlight-Fuhrer transaction and of Series D debentures. This resulted in a gain from debt restructuring of NIS 177 presented under finance income in the company's income statement for 2019.

## Note 15 - Bank Loans and Debentures (cont'd)

### D. Debt issued by Bezeq

Below are details of the terms that Bezeq undertook for the loans that it received and the debentures that were issued:

1. For Bezeq's overall debt, standard grounds were included for immediate repayment of the debentures and loans, including breach events, insolvency, dissolution procedures or receivership. In addition, a right was determined to call for immediate repayment if a third-party lender calls for immediate repayment of Bezeq's debts in an amount exceeding the amount determined.

   In addition, Bezeq has undertaken not to create additional liens on its assets unless liens are created at the same time in favor of the debenture holders and the lending banks (negative lien). The lien includes exceptions, including a lien on assets that will be purchased or expanded by Bezeq, if the undertakings underlying the lien are created for the purchase or expansion of those assets and for the matter of a token lien.

2. For Bezeq's public debentures, the debentures traded on the TACT-Institutional system in the amount of NIS 1.4 billion as at December 31, 2019, bank loans in the amount of NIS 1.8 billion as at December 31, 2019, and for loans from financial institutions in the amount of NIS 1.5 billion as at December 31, 2019, Bezeq has undertaken that if it Bezeq makes an undertaking towards any entity in respect of compliance with financial covenants, Bezeq will also provide the same undertaking to these lenders (subject to certain exceptions).

3. For Bezeq's public debentures, debentures traded on the TACT-Institutional system in the amount of NIS 1.4 billion, and for loans from financial institutions amounting to NIS 1.5 billion, grounds were included for immediate repayment, if telecommunication ceases to be the Group's core activity.

4. For Bezeq's public debentures, debentures traded on the TACT-Institutional system in the amount of NIS 1.4 billion, and for loans from financial institutions amounting to NIS 1.5 billion, Bezeq has undertaken to the lenders to take steps so that, to the extent under its control, the debentures will be rated by at least one rating agency, so long as there are debentures of the relevant series in circulation or a balance in loans, as the case may be.

5. For the Debentures (Series 9-10) traded on the TACT-Institutional system in the amount of NIS 1.4 billion, and for loans from financial institutions in the amount of NIS 1.5 billion, grounds for the immediate repayment of the loans in the event of a change in control were included, following which the controlling shareholders in Bezeq (as defined in the agreements) will cease to be controlling shareholders and control will be transferred to a third party ("the Transferee"), with the exception of: (1) transfer of control to a transferee that received approval for control in Bezeq in accordance with the provisions of the Telecommunications Law and/or the Telecommunications Order; or (2) transfer of control in which the Transferee holds control together with the controlling shareholders in Bezeq, provided that the holding rate of the controlling shareholders in Bezeq in the shares of Bezeq does not fall below 50.01% of the total shares of Bezeq held by the controlling shareholders together; or (3) a change in control to be approved by a meeting of the debenture holders/lenders.

(All amounts are in millions except where otherwise stated)

## Note 15 - Bank Loans and Debentures (cont'd)

### D. Debt issued by Bezeq (cont'd)

6. In addition, for the Debentures (Series 9 and 10) traded on the TACT-Institutional system in the amount of NIS 1.4 billion, and for loans from financial institutions in the amount of NIS 1.5 billion, grounds were included for immediate repayment of the debentures in the event of the recording of a going concern qualification in Bezeq's financial statements for two consecutive quarters, in the event of a material deterioration in Bezeq's business compared with the situation at the time of the issue, and there is real concern that Bezeq will not be able to repay the debentures/loans on time (as set out in section 35(I)1a1 of the Israel Securities Law).

7. **Changes in the debt composition of Bezeq during 2019:**

- **Debt issuance**

  In 2019, Bezeq raised debt in the amount of NIS 800 through private loans from an institutional entity and from a bank and completed a private placement of Debentures (Series 11 and 12) to institutional investors for a total consideration of NIS 1,068.

- **Early repayments and debt exchange**

  In 2019, Bezeq completed the early repayment of a number of loans from financial institutions and banks in the total principal amount of NIS 1.83 billion. In addition, in September 2019, Bezeq completed a tender offer for NIS 444 par value Debentures (Series 7) at a price of 101.50 agorot per NIS 1 par value debenture.

  In December 2019, Bezeq completed a private exchange of NIS 300 par value its Debentures (Series 6) for an allocation of NIS 337.5 par value Debentures (Series 12) by way of expanding Debentures (Series 12), reflecting an exchange ratio of NIS 1.125 par value for each NIS 1 par value Debentures (Series 6). The Debentures (Series 12) are traded on the TACT Institutional.

  As a result of the early repayments, Bezeq recognized financing costs in the amount of NIS 93 and also recognized financing income in the amount of NIS 14 for the exchange of Debentures (Series 6) for Debentures (Series 12).

  As at December 31, 2019 and the approval date of the financial statements, Bezeq was in compliance with all its debt undertakings and covenants, there were no grounds to call for immediate repayment, and financial covenants were not set out as described above.

(All amounts are in millions except where otherwise stated)

# Note 15 - Bank Loans and Debentures (cont'd)

## E. Movement in liabilities arising from financing activities

| | Debentures (including accrued interest) | Loans (including accrued interest) | Total |
|---|---|---|---|
| | NIS | NIS | NIS |
| **Balance as at January 1, 2018** | **9,235** | **5,114** | **14,349** |
| **Changes due to cash flows used in financing activities** | | | |
| Consideration from the issue of debentures and receipt of loans, less transaction costs | 819 | 320 | 1,139 |
| Repayment of debentures and loans | (1,107) | (686) | (1,793) |
| Interest paid | (325) | (198) | (523) |
| **Net cash used in finance activities** | **(613)** | **(564)** | **(1,177)** |
| Financing expenses recognized in the statement of income | 320 | 188 | 508 |
| **Balance as at December 31, 2018** | **8,942** | **4,738** | **13,680** |
| **Changes due to cash flows used in financing activities** | | | |
| Consideration from the issue of debentures and receipt of loans, less transaction costs | **1,475** | **800** | **2,275** |
| Repayment of debentures and loans | **(2,156)** | **(2,131)** | **(4,287)** |
| Interest paid | **(323)** | **(172)** | **(495)** |
| **Net cash used in finance activities** | **(1,004)** | **(1,503)** | **(2,507)** |
| Financing expenses recognized in the statement of income | **116** | **166** | **282** |
| **Balance as at December 31, 2019** | **8,229** | **3,401** | **11,455** |

(All amounts are in millions except where otherwise stated)

## Note 16 - Trade and Other Payables

| | December 31, 2018 Restated NIS | December 31, 2019 Restated NIS |
|---|---|---|
| Open accounts** | *996 | ***925** |
| Checks payable | 21 | **2** |
| **Trade payables** | 1,017 | **927** |
| **Other payables including derivatives:** | | |
| Liabilities to employees and other liabilities for salaries | *343 | ***356** |
| Advance payment for Sakia property (see Note 13) | 155 | **-** |
| Institutions | *90 | ***71** |
| Accrued interest | *47 | ***37** |
| Deferred income | *135 | ***136** |
| Derivatives | 43 | **55** |
| Other payables | 37 | **37** |
| Total other payables including derivatives | 850 | **692** |
| Total Trade and Other Payables | 1,867 | **1,619** |

* Restated. See Note 2.I.

** Of which, the carrying amount of trade payables that are payable to related parties as at December 31, 2019 amounts to NIS 2 (as at December 31, 2018 – NIS 2).

## Note 17 - Provisions

| | Customer claims NIS | Additional legal claims NIS | Dismantling and clearing of cellular and other sites NIS | Total NIS |
|---|---|---|---|---|
| **Balance as at January 1, 2019** | 134 | 35 | 44 | 213 |
| Provisions created | **22** | **7** | **11** | **40** |
| Provisions used | **(31)** | **(26)** | **-** | **(57)** |
| Provisions cancelled | **(14)** | **(7)** | **(1)** | **(22)** |
| **Balance as at December 31, 2019** | **111** | **9** | **54** | **174** |
| Current | **111** | **9** | **5** | **125** |
| Non-current | **-** | **-** | **49** | **49** |
| | **111** | **9** | **54** | **174** |

**Claims**
For details of legal claims, see Note 22.

(All amounts are in millions except where otherwise stated)

# Note 18 - Financial Risk Management

## A. General

The Group is exposed to the following risks, arising from the use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk (which includes currency, interest, inflation and other price risks)

This note provides information about the Group's exposure to each of the above risks, an explanation as to how the risks are managed, and the measurement processes.

## B. Framework for risk management

The Company’s Board of Directors has overall responsibility for the Company’s risk management. Bezeq's Board of Directors has responsibility for the Bezeq Group’s risk management. The purpose of risk management in the Group is to define and monitor those risks constantly, and to minimize their possible effects arising from the exposure on the basis of assessments and expectations for parameters that affect the risks. The Company's policy is to hedge, in part and where required according to policies determined by the board, exposure from fluctuations in foreign currencies rates and the Israeli CPI rates. Bezeq’s policy is to hedge, in part and where required according to policies determined by the board, exposure to fluctuations in foreign currencies and the Israeli CPI.

## C. Credit risk

The Company's management monitors the Company’s exposure to credit risks on a regular basis. Bezeq’s management monitors the Bezeq Group's exposure to credit risks on a regular basis. Cash and investments in deposits and securities are deposited in highly-rated banks.

### Trade and other receivables

Bezeq's management regularly monitors customer debts, and the financial statements include provisions for doubtful debts which properly reflect, in the management's estimation, the loss inherent in doubtful debts. In addition, the balances of trade receivables are widely spread.

### Investments in financial assets

The Company's investment policy, which was approved by its Audit Committee and established by the Company's Board of Directors, seeks to preserve principal and maintain adequate liquidity while maximizing the income received from investments without significantly increasing the risk of loss. In accordance with the Company's investment policy, since March 2019 the Company has invested all its funds in investment-grade securities.

(All amounts are in millions except where otherwise stated)

## Note 18 - Financial Risk Management (cont'd)

### C. Credit risk (cont'd)

**Investments in financial assets (cont'd)**

Any investments made by Bezeq in securities are made in securities which are liquid, marketable and have low risk. Transactions involving derivatives are made with entities that have high credit ratings.

As of the reporting date there is no significant concentration of credit risk.

### D. Liquidity risk

The Group's liquidity management policy is to ensure, to the extent possible, adequate liquidity to meet its existing and expected liabilities when they due, in a normal business scenario and under stress conditions, without causing undesirable losses or impairment of goodwill. The cash balances held by the Group, which are not required to finance current operations, are in liquid investment channels and are available for use as required. The Group assesses the existing and expected cash requirements for the foreseeable future, also in the scenario of an unexpected deterioration in its business. These forecasts take into account, among other things, raising and refinancing of debt from banking and non-banking sources. For information about the terms of the debentures issued by Group companies and the loans received, see Note 15 above.

### E. Market risks

The purpose of market risk management is to manage and oversee the exposure to market risks within accepted parameters to prevent significant exposures to market risks that will influence the Group's results, liabilities and cash flows.

During the normal course of its business, the Group enters into full or partial hedging actions. The Group takes into account the effects of the exposure in its considerations for determining the type of loans it incurs and in the management of its investment portfolio.

<u>Israeli CPI risk</u>

Changes in the rate of Israeli inflation affect the Group's profitability and its future cash flows, mainly due to its Israeli CPI-linked liabilities. In applying a policy of minimizing the exposure the Company has invested in bonds that are linked to the Israeli CPI in order to partially hedge the exposure to changes in the Israeli CPI. In addition, the Group enters into forward transactions against the Israeli CPI. The duration of the forward transactions is the same as, or shorter than, the duration of the hedged exposures. Bezeq applies hedge accounting with regards to its forward CPI hedge transactions.

A considerable portion of Bezeq's cash balances are invested in deposits, monetary funds or ETFs which are exposed to changes in their real value as a result of changes in the Israeli CPI.

<u>Interest rate risk</u>

In an attempt to meet targets for allocation of debt to interest exposure components, the Group will enter into interest rate swap transactions as required.

(All amounts are in millions except where otherwise stated)

## Note 18 - Financial Risk Management (cont'd)

Foreign currency risk

The Group is exposed to foreign currency risks mainly due to payments for purchases of terminal equipment and fixed assets, some of which are denominated in or linked to the US$ or EUR. In addition, the Group provides services for customers and receives services from suppliers worldwide for which it is paid and it pays in foreign currency, mainly the US$. The Group's policy is to reduce, to the extent possible, foreign currency acquisition agreements, and to partially hedge US$ exposure through forward transactions against the US$ and management of US$ deposits.

## Note 19 - Financial Instruments

### A. Liquidity risk

Below are the contractual repayment dates of financial liabilities, including estimated interest payments:

The Company:

| | December 31, 2019 | | | | | |
|---|---|---|---|---|---|---|
| | Carrying amount | Contractual cash flow | First half 2020 | Second half 2020 | 2021 | 2022-2024 |
| | NIS | NIS | NIS | NIS | NIS | NIS |
| **Non-derivative financial liabilities** | | | | | | |
| Other payables | **14** | **14** | **14** | **-** | **-** | **-** |
| Debentures | **1,861** | **2,419** | **32** | **39** | **78** | **2,270** |
| **Total** | **1,875** | **2,433** | **46** | **39** | **78** | **2,270** |

Consolidated:

| | December 31, 2019 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Carrying amount | Contractual cash flow | First half 2020 | Second half 2020 | 2021 | 2022-2024 | 2025 and later |
| | Restated | Restated | Restated | | | | |
| | NIS | NIS | NIS | NIS | NIS | NIS | NIS |
| **Non-derivative financial liabilities** | | | | | | | |
| Trade and other payables | ***1,628** | ***1,471** | ***1,410** | **61** | **-** | **-** | **-** |
| Bank loans | **3,386** | **3,942** | **316** | **204** | **448** | **1,341** | **1,633** |
| Debentures | **8,033** | **9,426** | **114** | **694** | **811** | **5,331** | **2,476** |
| **Total** | ***13,047** | ***14,839** | ***1,840** | **959** | **1,259** | **6,672** | **4,109** |
| **Financial liabilities for derivative instruments** | **122** | **122** | **4** | **53** | **29** | **34** | **2** |
| Forward contracts on the Israeli CPI | ***13,169** | ***14,961** | ***1,844** | **1,012** | **1,288** | **6,706** | **4,111** |

* Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

# Note 19 - Financial Instruments (cont'd)

## A. Linkage and foreign currency risks

| | December 31, 2018 | | |
|---|---|---|---|
| | Unlinked | Israeli CPI-linked | Foreign currency linked (mainly US$) |
| | Restated | Restated | |
| | NIS | NIS | NIS |
| **Current assets** | | | |
| Cash and cash equivalents | 1,058 | - | 46 |
| Trade receivables | *1,734 | 22 | 19 |
| Other receivables | 92 | *144 | - |
| Investments including derivatives | 1,613 | 56 | 110 |
| **Total current assets** | *4,497 | *222 | 175 |
| **Non-current assets** | | | |
| Trade and other receivables | 365 | 105 | - |
| Investments including derivatives | 49 | - | 41 |
| Total non-current assets | 414 | 105 | 41 |
| **Total assets** | *4,911 | *327 | 216 |
| **Current liabilities** | | | |
| Debentures, loans and borrowings | 3,365 | 632 | - |
| Trade and other payables | *1,547 | 53 | 166 |
| **Total current liabilities** | *4,912 | 685 | 166 |
| **Non-current liabilities** | | | |
| Debentures and bank loans | 6,879 | 2,758 | - |
| Other liabilities including derivatives | - | 95 | 5 |
| **Total non-current liabilities** | 6,879 | 2,853 | 5 |
| **Total liabilities** | 11,791 | 3,538 | 171 |
| **Total exposure in the statement of financial position** | *(6,880) | *(3,211) | 45 |
| **Forward transactions** | (1,520) | 1,350 | 170 |

* Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

# Note 19 - Financial Instruments (cont'd)

## A. Linkage and foreign currency risks (cont'd)

| | December 31, 2019 | | |
|---|---|---|---|
| | Unlinked | Israeli CPI-linked | Foreign currency linked (mainly US$) |
| | Restated | Restated | |
| | NIS | NIS | NIS |
| **Current assets** | | | |
| Cash and cash equivalents | 788 | - | 26 |
| Restricted cash | 39 | - | - |
| Trade receivables | *1,637 | 20 | 21 |
| Other receivables | 44 | *251 | - |
| Assets held for sale | - | - | - |
| Investments including derivatives | 1,200 | - | 41 |
| **Total current assets** | 3,708 | *271 | 88 |
| **Non-current assets** | | | |
| Trade and other receivables | 304 | 173 | - |
| Investments including derivatives | 45 | - | - |
| Total non-current assets | 349 | 173 | - |
| **Total assets** | *4,057 | *444 | 88 |
| **Current liabilities** | | | |
| Debentures, loans and borrowings | 486 | 521 | - |
| Current maturities of liabilities for leases | 21 | 395 | - |
| Trade and other payables | *1,303 | 65 | 159 |
| Employee benefits | 651 | - | 3 |
| Provisions | 33 | 92 | - |
| **Total current liabilities** | 2,494 | 1,073 | 162 |
| **Non-current liabilities** | | | |
| Debentures and bank loans | 7,681 | 2,731 | - |
| Liability for leases | 6 | 962 | 1 |
| Employee benefits | 307 | - | 49 |
| Other liabilities including derivatives | - | 66 | - |
| Deferred tax liabilities | - | - | - |
| Provisions | 49 | - | - |
| **Total non-current liabilities** | 8,043 | 3,759 | 50 |
| **Total liabilities** | 10,537 | 4,832 | 212 |
| **Total exposure in the statement of financial position** | *(6,480) | *(4,388) | (124) |
| **Forward transactions** | (1,745) | 1,555 | 190 |

* Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

# Note 19 - Financial Instruments (cont'd)

## B. Linkage and foreign currency risks (cont'd)

Information regarding the Israeli CPI and significant exchange rates:

| | Year ended December 31 | | | December 31 | | |
|---|---|---|---|---|---|---|
| | 2017 | 2018 | 2019 | 2017 | 2018 | 2019 |
| | Rate of change | | | Reporting date spot rate | | |
| | % | % | % | NIS | NIS | NIS |
| 1 US dollar | (9.8) | 8.1 | **(7.79)** | 3.467 | 3.748 | **3.456** |
| 1 euro | 2.7 | 3.32 | **(9.62)** | 4. 153 | 4.291 | **3.878** |
| Israeli CPI in Points | 0.4 | 0.9 | **0.7** | 140.00 | 141.26 | **142.10** |

A change of 1% of the CPI as at December 31, 2019 would have no effect on total equity and net income. This analysis assumes that all other variables, in particular interest rates, remain constant. In addition, A change of 10% in the US$ exchange rate as at December 31, 2019 would have immaterial effect on total equity and net income.

## C. Interest rate risk

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

| | December 31 | |
|---|---|---|
| | 2018 | 2019 |
| | NIS | NIS |
| **Fixed rate instruments** | | |
| Financial assets | 2,739 | **2,284** |
| Financial liabilities | (12,547) | **(11,312)** |
| | (9,808) | **(9,028)** |
| **Variable rate instruments** | | |
| Financial assets | 59 | **-** |
| Financial liabilities | (1,086) | **(107)** |
| | (1,027) | **(107)** |

(All amounts are in millions except where otherwise stated)

# Note 19 - Financial Instruments (cont'd)

## C. Interest rate risk (cont’d)

### 2. Fair value sensitivity analysis for fixed rate financial liabilities and derivatives

The Group’s assets and liabilities at fixed interest are not measured at fair value through profit or loss. Accordingly, a change in interest rates at the reporting date will not affect profit or loss.

### 3. Sensitivity analysis of cash flow for instruments at variable interest

An increase/decrease of 1% in the interest rates at the reporting date would not have a material effect on profit and on capital.

## D. Cash flow hedge accounting

### Cash flow hedges for CPI-linked liabilities

The Bezeq Group entered into several forward contracts, as described in the table below, to reduce exposure to changes in the CPI for CPI-linked debentures. These transactions hedge specific cash flows of some of the debentures and are recognized as cash flow hedge accounting. The expiry date of these transactions complies with the repayment schedule of the relevant debentures. The fair value of the forward contracts is based on available market information (tier 2 in the fair value hierarchy)

| Hedge item | Repayment date | Number of Transactions | Nominal Value | Fair value | Capital reserve |
|---|---|---|---|---|---|
| | | | NIS | NIS | NIS |
| **December 31, 2018:** | | | | | |
| Debentures (Series 6) | December 2019 - December 2022 | **6** | 1,350 | (138) | (12) |
| | | | 1,350 | (138) | (12) |
| **December 31, 2019:** | | | | | |
| Debentures (Series 6) | December 2020 - December 2022 | 4 | **1,005** | **(112)** | **(10)** |
| Debentures (Series 10) | December 2022 - December 2025 | 4 | **300** | **(5)** | **(2)** |
| Debentures (Series 12) | June 2026 - June 2030 | 5 | **250** | **(1)** | **(1)** |
| | | 13 | **1,555** | **(118)** | **(13)** |

DBS has forward transactions to reduce exposure to changes in the US$ exchange rate. As at December 31, 2019, the net fair value of these transactions is a liability of NIS 4 (as at December 31, 2018, an asset of NIS 3).

(All amounts are in millions except where otherwise stated)

## Note 19 - Financial Instruments (cont'd)

### E. Fair value

### (1) Financial instruments measured at fair value for disclosure purposes only

The table below shows the difference between the carrying amount and the fair value of groups of financial instruments. The carrying amount of other financial assets and liabilities does not differ significantly from their fair value. The fair value of debentures issued to the public is based on their quoted closing price at the reporting date (Level 1).

The fair value of loans and non-marketable debentures is based on the present value of future principal and interest cash flows, discounted at the market rate of interest suitable for similar liabilities plus the required adjustments for risk premium and non-marketability at the reporting date (Level 2).

| | December 31, 2018 | | December 31, 2019 | | |
|---|---|---|---|---|---|
| | Carrying amount | Fair value | Carrying amount | Fair value | Fair value weighted average discount rate |
| | NIS | NIS | NIS | NIS | % |
| **Secured loans from banks and others** | | | | | |
| Unlinked | 4,235 | 4,324 | **3,401** | **3,561** | **2.39** |
| **Debentures** | | | | | |
| Issued to the public (CPI linked) | 3,464 | 3,602 | **2,508** | **2,647** | **0.05** |
| Issued to the public (Unlinked) | 4,681 | 4,405 | **4,071** | **4,160** | **1.00** |
| Issued to institutional investors (CPI linked) | 8 | 8 | **762** | **855** | **1.24** |
| Issued to institutional investors (unlinked) | 202 | 211 | **607** | **646** | **2.69** |
| | 12,590 | 12,550 | **11,349** | **11,869** | |

### (2) Financial instruments measured at fair value

The table below analyses financial instruments carried at fair value, by valuation method.

| | December 31, 2018 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| | NIS | NIS | NIS | NIS |
| **Financial assets held for trading** | | | | |
| Monetary funds and ETFs | 18 | - | - | 18 |
| Marketable securities | 376 | - | - | 376 |
| Forward contracts | - | (135) | - | (135) |
| | 394 | (135) | - | 259 |

(All amounts are in millions except where otherwise stated)

# Note 19 - Financial Instruments (cont'd)

## E. Fair value (cont'd)

| | December 31, 2019 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| | **NIS** | **NIS** | **NIS** | **NIS** |
| **Financial assets held for trading** | | | | |
| Monetary funds and ETFs | **312** | **-** | **-** | **312** |
| Marketable securities | **46** | **-** | **-** | **46** |
| Forward contracts | **-** | **(122)** | **-** | **(122)** |
| | **358** | **(122)** | **-** | **236** |

a. The fair value of investments in financial funds, ETFs and marketable securities is determined by reference to their average quoted selling price at the reporting date (Level 1).

b. The fair value of forward contracts on the CPI or foreign currency is based on discounting the difference between the price in the forward contact and the price of the present forward contact for the balance of the contract term until redemption, at an appropriate interest rate (Level 2). The estimate is made under the assumption that a market participant takes into account the credit risks of the parties when pricing such contracts.

## F. Offset of financial assets and liabilities

The Group has agreements with various communication companies to supply and receive communication services. In accordance with the agreements, each party has the right to offset the amounts due by each party. The table below presents the carrying amount of the offset balances as stated in the statement of financial position:

| | December 31, | |
|---|---|---|
| | **2018** | **2019** |
| | **NIS** | **NIS** |
| Trade and other receivables, gross | 94 | **90** |
| Offset amounts | (83) | **(81)** |
| Trade and other receivables presented in the statement of financial position | 11 | **9** |
| Trade payables, gross | 121 | **100** |
| Offset amounts | (83) | **(81)** |
| Trade and other payables presented in the statement of financial position | 38 | **19** |

(All amounts are in millions except where otherwise stated)

# Note 20 - Employee Benefits

Employee benefits include post-employment benefits, other long-term benefits, termination benefits, short-term benefits.

## A. Liabilities for employee benefits

| | December 31, | |
|---|---|---|
| | 2018 | 2019 |
| | NIS | NIS |
| **Current liabilities for:** | | |
| Holiday | 112 | **120** |
| Sick leave | 133 | **152** |
| Early retirement | 329 | **375** |
| Current maturities of pensioner benefits | 7 | **7** |
| Total current liability for employee benefits | 581 | **654** |
| **Non-current liabilities for:** | | |
| Voluntary redundancy for employees transferred from civil service | 241 | **94** |
| Liability for pensioner benefits | 115 | **137** |
| Severance compensation (net) (see composition below) | 54 | **65** |
| Early notice and pension | 35 | **29** |
| Provision for the streamlining plan | - | **31** |
| Total non-current liabilities for employee Benefits | 445 | **356** |
| Total liabilities for employee benefits | 1,026 | **1,010** |
| **Composition of liabilities for severance pay:** | | |
| Liabilities for severance pay | 218 | **230** |
| Fair value of plan assets | (164) | **(165)** |
| | 54 | **65** |

## B. Defined contribution plans

Liabilities for employee benefits at retirement age in respect of the period of their service with Bezeq and its subsidiaries, and for employees to which Section 14 of the Severance Pay Law – 1963 applies, are covered in full by regular payments made by Bezeq and its subsidiaries to pension funds and insurance companies.

| | Year ended December 31, | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | NIS | NIS | NIS |
| Amount recognized as an expense for a defined contribution plan | 228 | 232 | **223** |

The pension rights of the Bezeq Group employees for the period of their employment in the civil service through January 31, 1985, are covered by a pension fund ("the Makefet Fund"), which assumed the State's obligation following an agreement between the Government of Israel, the Company, the Histadrut Federation of Labor and the Makefet Fund.

(All amounts are in millions except where otherwise stated)

## Note 20 - Employee Benefits (cont'd)

The severance obligation to employees who leave their employment on terms entitling them to compensation is covered, for the period from February 1, 1985, by regular contributions to such pension funds and insurance companies (in accordance with Section 14 of the Severance Pay Law).

Severance pay for the period of employment in the civil service through January 31, 1985, is paid by the Bezeq Group, and the monies accumulated in the Makefet Fund for that period are kept in a fund that will be used for the employees' rights.

For certain employees, the Bezeq Group has an obligation to pay severance in excess of the amount accumulated in the compensation fund which is in the employees' names. See section below.

### C. Defined benefit plans

Obligations for defined benefit plans in the Bezeq Group include the following:

1. The severance pay obligation for the balance of the obligation not covered by contributions and/or insurance policies in accordance with the existing labor agreements and the Severance Pay Law. For this part of the obligation, there are deposits in the name of Group companies in pension funds and insurance companies. The deposits in pension funds and insurance companies include accrued linkage differences and interest. Withdrawal of the reserve monies is contingent upon fulfilment of the provisions in the Severance Pay Law.
2. An obligation in accordance with the employment agreements of some of the senior employees in the Group for payment of a benefit for notice upon severance. The Company also has an obligation to a number of senior employees who are entitled to early retirement terms (pension and retirement grants) which are not dependent on the existing retirement agreements for all employees
3. Company retirees receive, in addition to pension payments, benefits which consist mainly of a holiday gift (linked to the dollar exchange rate), financing for the upkeep of retiree clubs and social activities The Company's liability for these costs accumulates in the employment period. The Company's financial statements include the liabilities for expected costs in the severance period.

### D. Sick leave provision

The financial statements include a provision in respect of redemption and utilization of sick leave. The right to accumulate sick leave was taken into account for all employees in the Bezeq Group. Only employees eligible under the terms of the employment agreement may redeem sick leave. The provision was computed on the basis of an actuarial calculation, including the assumption of positive accumulation of days by most of the employees and utilization of days in accordance with the last in first out (LIFO) method.

(All amounts are in millions except where otherwise stated)

## Note 20 - Employee Benefits (cont'd)

### E. Benefits for early retirement and termination

1. According to the collective agreement of December 2006, between Bezeq and the employees union and the Histadrut Federation of Labor, and according to the amendment to the agreement of August 2015, Bezeq may, at its discretion, terminate the employment of 163 long-standing permanent employees in each of the years 2015-2021 (Bezeq's right is accumulated over the years).

   Bezeq recognizes expenses for early retirement when Bezeq is committed demonstrably, without realistic possibility of withdrawal, to a defined plan to terminate employment before the defined date, according to a defined plan. The collective agreement allows Bezeq to dismiss employees but does not create a demonstrable commitment without realistic possibility of withdrawal. Accordingly, the expenses for early retirement are recognized in Bezeq's financial statements at the approval date of the plan.

   On November 6, 2019, as part of its streamlining plan, Bezeq's Board of Directors approved the retirement of 140 permanent employees and the termination of employment of another 60 employees with flexible employment status. In view of the above, in its financial statements for the fourth quarter of 2019, Bezeq recognized an expense for severance pay in early retirement in the amount of NIS 137. Total expenses for early retirement in Bezeq in 2019 amounted to NIS 109 and included a decrease in the provision for retirement for previous plans.

2. On December 16, 2018, an early retirement plan was decided on, by the end of the collective agreement period (the end of 2021), for all employees of Bezeq who were transferred to Bezeq from the Ministry of Communications (94 employees). The balance of the unpaid provision for the retirement liability as at December 31, 2019 is NIS 264.

3. Pelephone, Bezeq International, and DBS have collective agreements with the Histadrut Federation of Labor and the employees' committees as follows:

   On March 14, 2019, DBS signed a collective arrangement with the Histadrut Federation of Labor and the employees' representatives regarding retrenchment and synergy procedures, commencing on June 1, 2019 until December 31, 2021 ("the Arrangement"). According to the Arrangement, DBS will be entitled to terminate the employment of up to 325 employees during the Arrangement years, and employees who are not included in the retirement plan will receive a one-time grant. In addition, according to the Arrangement, DBS may also retrench by not recruiting employees to replace employees whose employment has terminated. Following the Arrangement and the submission of the efficiency plan outline to the employees' representatives, DBS recognized expenses of NIS 45 million, mainly due to termination benefits.

   On November 17, 2019, DBS signed an extension to its collective agreement with the Histadrut New General Federation of Labor and the employees' committee, with certain revisions, until December 31, 2021.

   On July 11, 2019, Bezeq International signed a collective agreement with the Histadrut New General Federation of Labor and the employees' committee at Bezeq International. The agreement includes efficiency and synergy processes for the period from July 11, 2019 to December 31, 2021. Under to the agreement, Bezeq International may retrench up to 325 employees (of which 150 are permanent employees, some as part of voluntary early retirement), in addition to the option of not hiring employees to replace those employees that terminate their employment. The agreement also includes a one-time bonus for employees who are not included in the retirement plan.

(All amounts are in millions except where otherwise stated)

## Note 20 - Employee Benefits (cont’d)

### E. Benefits for early retirement and termination (cont'd)

Following the agreement and the submission of the efficiency plan outline to the employees' representatives, Bezeq International recognized expenses of NIS 45, mainly termination benefits and other employee benefits.

On November 13, 2019, Pelephone signed a renewal of the existing collective agreement with the Histadrut General Federation of Labor - Cellular, Internet, and High-Tech Workers Union ("the Histadrut") and the employees’ representatives, which includes streamlining and synergy processes for the period from November 12, 2019 until June 30, 2022. Under the agreement, Pelephone will be able, among other things, to terminate the employment of 210 permanent employees during the agreement period, some as part of a voluntary retirement plan. In addition, according to its plan, Pelephone will terminate the employment of another 190 non-permanent employees, and employees will not be hired to replace those persons whose employment is terminated. The agreement also includes a one-time bonus for employees who are not included in the retirement plan. Following the agreement and the submission of the efficiency plan outline to the employees’ representatives, Pelephone recognized expenses of NIS 77, mainly termination benefits and other employee benefits.

For Bezeq's board approval of early retirement plan for 2021 and update of special collective agreement of Bezeq, please refer to Note 33.

### F. Actuarial assumptions

The main actuarial assumptions for defined benefit plans at the reporting date are as follows:

Mortality rates are based on the rates published in Pension Circular 2017-3-6 of the Capital Market Authority. Future declines in mortality rates are based on rates published in Circular 2019-1-10.

Churn rates were determined on the basis of the past experience of the Company and the subsidiaries, distinguishing between different employee populations and taking into account the number of years of employment. The churn rates include a distinction between severance with entitlement to full termination compensation and severance without entitlement to full termination compensation.

The discount rate (nominal) is based on the yield on linked high-quality corporate debentures with maturity dates approximating those of the gross obligation.

The main discount rates are as follows:

| | December 31, 2018 | December 31, 2019 |
|---|---|---|
| | Average capitalization rate | Average capitalization rate |
| | % | % |
| Severance compensation | 3.73 | **2.4** |
| Retirement benefits | 4.1 | **2.9** |

Assumptions regarding salary increments for calculation of the liabilities were made on the basis of the management’s assessments, distinguishing between the groups of employees. The main assumptions (in nominal terms) regarding salary increases of the main employee groups are as follows:

(All amounts are in millions except where otherwise stated)

## Note 20 – Employee Benefits (cont'd)

### F. Actuarial assumptions (cont'd)

| | **Salary increase assumptions** |
|---|---|
| Permanent and long-standing employees in the Company | The calculation was based on individual assumptions regarding an expected salary increase for 2020 through to 2026, arising from the collective agreement signed in August 2015. |
| Permanent employees in the Company | Average adjustment of 3.2% for young employees, decreasing gradually to 1.4% at the age of 66. |
| Company's employees that are not permanent | 6.4% for young employees decreasing gradually to 0.1%, 2% (in real terms) for senior employees |
| Pelephone employees | Salary increases were based on the collective agreements signed by Pelephone. The annual salary increase for Pelephone employees is 3% in 2020 and 2% thereafter. |
| Bezeq International employees | Assumptions about salary increases were based on the collective agreement signed in 2019. The average salary increase for Bezeq International employees is 2.95% in 2020 and 2% thereafter. |
| DBS employees | Rate of increase of 3.5%. |

(5) **Sensitivity analysis for actuarial assumptions**

The following is an analysis of the possible effect of the changes in the principal actuarial assumptions on liabilities to employee benefits. The calculation is made for each assumption separately, assuming that the remaining assumptions remain unchanged.

| | **Year ended December 31,** | |
|---|---|---|
| | **2018** | **2019** |
| | **Years** | **Years** |
| Discount rate - addition of 0.5% | (37) | **(42)** |
| Rate of future salary increases - addition of 0.5% | 27 | **35** |
| Rate of employees leaving - addition of 5.0% | (12) | **(25)** |
| Mortality rate assumption, addition of 5.0% | (2) | **(4)** |

(6) Average weighted useful life of liabilities for the main severance benefits:

| | **Year ended December 31,** | |
|---|---|---|
| | **2018** | **2019** |
| | **Years** | **Years** |
| Severance compensation | 9.9 | **10.8** |
| Retirement benefits | 13.6 | **16.6** |

(All amounts are in millions except where otherwise stated)

## Note 21 - Income Tax

### A. Corporate tax rate

The corporate tax rate for 2017, 2018 and 2019 was 24%, 23% and 23%, respectively.

Deferred tax balances as at December 31, 2019 were calculated according to the new tax rates expected to apply on the date of reversal. The current taxes for the reported periods are calculated according to the actual tax rates as set out above.

### B. Composition of income tax expenses

| | Year ended December 31, | | |
|---|---|---|---|
| | **2017** | **2018** | **2019** |
| | **Restated** | **Restated** | **Restated** |
| | **NIS** | **NIS** | **NIS** |
| **Current tax expenses** | | | |
| Expenses for the current year | 438 | *303 | ***391** |
| Adjustments for prior years | 54 | (24) | **(11)** |
| **Total current tax expenses** | 492 | *279 | ***380** |
| **Deferred tax expenses (income)** | | | |
| Adjustments for prior years according to an assessment agreement | (54) | - | - |
| Derecognition of previously recognized deductible temporary differences | - | *(93) | **1,259** |
| Derecognition of deferred tax liability | | *(114) | - |
| Reversal of temporary differences according to an assessment agreement | 21 | - | - |
| Creation and reversal of temporary differences | (112) | *(139) | ***(198)** |
| **Total deferred tax expenses** | (145) | (346) | **1,061** |
| **Income tax expense** | 347 | *(67) | ***1,441** |

* Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

## Note 21 - Income Tax (cont'd)

### C. Reconciliation between the theoretical tax on the pre-tax income and the tax expense

| | Year ended December 31, | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | Restated | Restated | Restated |
| | NIS | NIS | NIS |
| Income (loss) before income tax | *1,077 | *(1,983) | ***(19)** |
| Statutory tax rate | 24% | 23% | **23%** |
| Income tax at the statutory tax rate | *257 | *(456) | **(4)** |
| Expenses not recognized for tax purposes | 51 | 54 | **42** |
| Gain from debt restructuring not recognized for tax purposes | - | - | **(41)** |
| Current year tax losses and benefits for which deferred taxes were not created | 29 | 26 | **27** |
| Utilization of tax losses and benefits from prior years for which deferred taxes were not created | - | 160 | **-** |
| Creation of deferred taxes for losses and benefits from prior years for which deferred taxes were not recorded in the past | - | - | **(3)** |
| Impairment of assets for which deferred taxes were not recognized | 10 | *149 | **161** |
| Derecognition of previously recognized deductible temporary differences | - | - | **1,259** |
| Income tax expenses (benefit) | 347 | (67) | **1,441** |

* Restated. See Note 2.I.

(All amounts are in millions except where otherwise stated)

# Note 21 - Income Tax (cont'd)

## D. Recognized deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following items:

| | Property, plant equipment, and intangible assets | Employee benefits plan | Carry-forward losses for DBS | Brand Names and Customers relationship | Others | Total |
|---|---|---|---|---|---|---|
| | NIS | NIS | NIS | NIS | NIS | NIS |
| **Balance of deferred tax asset (liability) as at December 31, 2017** | (323) | 165 | 1,166 | (488) | 40 | 560 |
| Recognized in profit or loss | (13) | 101 | 93 | 184 | (18) | 347 |
| Recognized in equity | - | 2 | - | - | (6) | (4) |
| **Balance of deferred tax assets (liability)as at December 31, 2018** | (336) | 268 | 1,259 | (304) | 16 | 903 |
| **Balance of deferred tax asset (liability) as at December 31, 2018** | **(336)** | **268** | **1,259** | **(304)** | **16** | **903** |
| Recognized in profit or loss | ***76** | **28** | **-** | ***68** | ***26** | **198** |
| Disposal of deferred tax asset | **-** | **-** | **(1,259)** | **-** | **-** | **(1,259)** |
| Recognized in equity | **-** | **2** | **-** | **-** | **-** | **2** |
| **Balance of deferred tax assets (liability)as at December 31, 2019** | **(260)** | **298** | **-** | **(236)** | **42** | **(156)** |

* Restated. See Note 2.I.

## E. Unrecognized deferred tax assets or liabilities and carry-forward tax loss

As at December 31, 2019, the Group has tax losses carry forwards in the amount of NIS 5 billion (December 31, 2018: NIS 5 billion) and capital loss carry forwards in the amount of NIS 86 (December 31, 2018: NIS 51). The Group did not create deferred tax assets with respect to current losses and capital losses since their utilization is not probable. In addition, deferred taxes of NIS 216 related to impairment losses in DBS were not taken into account, since their utilization is not expected. The deductible temporary differences and tax losses do not expire under current tax legislation in Israel.

Following the acquisition of control in DBS by the Group, the Group recognized a deferred tax asset for carryforward losses for tax purposes in DBS, amounting to NIS 1,259. The approval from the Tax Authority for the utilization of the carryforward tax losses is subject to approval from the Ministry of Communications for cancellation of the structural separation between the two companies and requires the extension from the Tax Authority for an additional year as from 2020 for every year until the actual merger takes place.

The Group wrote off the tax assets by way of revising the estimate and recognized tax expenses in the amount of NIS 1,259 in the income statement of 2019, since the Group's assessment of the probability of using the tax asset was no longer more likely than not. For the purpose of assessing the probability of utilization of the tax asset, the Group considered, among other things, the absence of developments in its discussions with authorities and government agencies, various developments in recent months, and the effect of the passage of time.

(All amounts are in millions except where otherwise stated)

## Note 21 - Income Tax (cont'd)

### E. Unrecognized deferred tax assets or liabilities and carry-forward tax loss (cont'd)

Accordingly, as at December 31, 2019, deferred taxes for carryforward losses for tax purposes of DBS in the amount of NIS 5 billion were not recognized. In addition, deferred taxes of NIS 216 for an impairment loss in DBS are not taken into account, since their utilization is not expected.

In addition, the calculation of deferred taxes does not take into account the taxes that would be applicable in the case of disposal of investments in subsidiaries and associates, since the Group intends and is able to retain these investments. Deferred taxes in respect of a distribution of profit in subsidiaries and associates were also not taken into account since the dividends are not taxable.

### F. Final tax assessments

(1) The Company has final tax assessments up to and including 2014.

(2) Bezeq has final tax assessments up to and including 2014.

On September 15, 2016, parallel to signing the assessment agreement ending the disputes between Bezeq and the tax assessor that ended the dispute regarding the financing income for the shareholder loans to DBS, the Tax Authority granted approval for tax purposes of the merger of DBS with and into Bezeq in accordance with section 103(B) of the Income Tax Ordinance. According to the approval, the losses of DBS as at the merger date may be offset against the profits of the absorbing company, provided that in each tax year, it will not be permitted to offset an amount exceeding 12.5% (spread over eight years) of the total losses of the transferring company and the absorbing company, or 50% of the taxable income of the absorbing company in that tax year prior to offsetting the loss from previous years, whichever is lower.

The approval was granted in accordance with the applicable tax laws in effect at the time. Without derogating from the amount of the losses set out in the assessment agreement, if there is any change in the applicable tax laws, the Tax Authority will reconsider the taxation decision in accordance with the tax laws applicable at the merger date. However, it is clarified that the approval is effective until December 31, 2019. The Income Tax Authority will extend the date of the approval each year by an additional year, subject to the declaration of Bezeq and DBS that there has been no material change in their business affairs and subject to the terms of the taxation decision, and subject to the interpretation given to the tax laws, provided that such interpretation is published in writing. Any change in the tax laws that does not require a change in the approval will not result in any such change.

On October 2, 2019, Bezeq received a letter from the Tax Authority ("the Approval") extending, at Bezeq 's request, the validity of the tax decision for one year (until December 31, 2020). In the Approval, the Tax Authority clarified, among other things, that the Tax Authority has full authority to revoke the Approval if it emerges that as from the signing date of the Approval until December 31, 2019, there has been a material change in the business of Bezeq and DBS, that the extension of the validity of the tax decision refers to the tax decision of September 15, 2016 in the outline set out in the tax decision only, that it does not derogate from the Tax Authority's authority not to extend the validity of the Approval beyond December 31, 2020, and that it does not contain any confirmation that the two companies are in compliance with the terms of the Approval. On November 8, 2020, Bezeq received a letter from the Tax Authority extending, the validity of the tax decision by additional year (until December 31, 2021).

The tax losses of DBS as at December 31, 2019 amount to NIS 5 billion.

(All amounts are in millions except where otherwise stated)

## Note 21 - Income Tax (cont'd)

2. Pelephone has received final tax assessments up to and including 2014.
3. Bezeq International has received final tax assessments up to and including 2015.
4. DBS has received final tax assessments up to and including 2014.
5. Walla! has received final tax assessments up to and including 2014.

## Note 22 - Contingent Liabilities

### A. Legal proceedings against the Company

(1) On June 29, 2017, plaintiff Lynne P. Maleeff commenced litigation on behalf of a purported class of persons and entities who purchased or otherwise acquired our shares between March 18, 2015 and September 6, 2017. The original defendants were the Company, Doron Turgeman (our former CEO), Itzik Tadmor (our CFO) and Ehud Yahalom (our former CFO). On December 8, 2017, lead plaintiffs filed an amended complaint adding ten additional defendants: Shaul Elovitch, Or Elovitch, Ron Eilon, Stella Handler, David Mizrahi, Micky Neiman, Allon Raveh, Linor Yochelman, DBS and Eurocom Communications.

The amended complaint alleges a single cause of action against the Company for violation of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder. The complaint alleges that the Company made false and misleading statements and omissions in its SEC filings.

On February 20, 2018, the Company moved to dismiss the litigation for failure to state a claim or, alternatively, to stay the litigation pending the outcome of criminal investigations in Israel. Our motion to dismiss asserted that plaintiffs failed to allege that the Company had the required knowledge or scienter about the purported wrongdoing by other defendants and that we did not make any materially false statements. Plaintiffs filed their opposition to the motion.

The court issued a decision dated September 27, 2018 granting in part and denying in part our motion to dismiss. The court dismissed all claims against our company relating to our code of ethics, internal controls, and compliance with laws generally and all claims relating to the Bezeq subcommittee review of the Bezeq-DBS transaction, except for certain allegations relating to statements in one particular filing and to allegations regarding our statements about our or Bezeq's free cash flow. The court denied our motion to stay without prejudice to our ability to seek a stay in the future if circumstances change. On July 12, 2018, motions to dismiss were filed by (1) defendants Doron Turgeman, Itzik Tadmor, and Ehud Yahalom, all former officers of our company, (2) Ron Eilon, Micky Neiman and DBS; and (3) Stella Handler, Allon Raveh, Linor Yochelman, and David Mizrahi, officers of Bezeq.

On March 28, 2019, the court concluded that the complaint failed to allege claims against our executive officers for either primary violations of the U.S. securities laws or "control person" liability for the alleged violations by others of the U.S. securities laws. The court therefore dismissed the complaint against Doron Turgeman, Itzik Tadmor and Ehud Yahalom. The court also concluded that the complaint failed to adequately allege personal jurisdiction against certain executive officers of Bezeq and DBS. The court therefore dismissed the complaint against the DBS and Bezeq defendants for lack of personal jurisdiction.

## Note 22 - Contingent Liabilities (cont'd)

On December 5, 2019, the court held a teleconference to address plaintiffs' request that the Company be compelled to produce documents held by Bezeq or DBS. The court denied plaintiffs' request, and the plaintiffs indicated that they anticipate filing a formal motion to compel the Company to produce these documents. The court directed the parties to meet and confer about what discovery would be needed in advance of plaintiffs' anticipated motion.

The Company's counsel and counsel for the plaintiffs executed a stipulation of settlement dated March 3, 2020. The stipulation of settlement provides in relevant part that the Company (through its insurance) will pay a total of US$1.2, the litigation will be dismissed with prejudice, and all class members who do not opt out of the settlement will be deemed to fully and finally release all claims against the defendants which were or could have been asserted in the litigation relating to the purchase, holding or sale of the Company's shares during the class period. The settlement will not take final effect unless and until it is approved by the court. The plaintiffs filed a motion for approval of the settlement on March 3, 2020. For final settlement of this litigation during 2020, please refer to Note 33N.

Similar class action lawsuit was filed in Israel and is described in section B below.

(2) The company, Internet Gold and five members of the Company's Board of Directors were named as respondents in a motion to certify a claim as a derivative claim instituted in the Tel Aviv District Court (Economic Affairs Division) on July 28, 2016. The plaintiff has alleged that NIS 113 out of the dividends distributed by us in May 2016 was distributed unlawfully as such amount was not included in our profit and loss report, and therefore does not qualify as a "surplus" that may be lawfully distributed as dividends under the Israeli Companies Law. A pretrial hearing was held in March 2017, in which the court allowed us to file an additional brief response and a supplementary expert opinion, in order to respond to the arguments. The Company filed the additional responses in June 2017. The court further held that the parties should consider the possibility of a constructive arbitration regarding the issues in dispute and instructed the parties to inform the court about the results of this dialogue, and whether they want to set a date for an evidentiary hearing or additional preliminary motions. The dialogue process failed, and accordingly, the court set dates for the evidentiary hearing (as part of the motion to certify) for January 6, 2019. On January 6, 2019, evidentiary hearings were held. The court decided that our summaries must be submitted by May 28, 2019, and the reply on behalf of the plaintiff must be submitted by June 10, 2019.

In July 2019, the District court approved the derivative claim with respect to Internet Gold and dismissed the claim with respect to the Company's directors. Shortly thereafter, in October 2019, the plaintiff filed statement of appeal to the Supreme Court against the dismissal of the claim in respect to the directors. In addition, The Company and Internet Gold, also filed, separately, a motion to regarding the initial Court's decision approving the derivative claim.

(All amounts are in millions except where otherwise stated)

## Note 22 - Contingent Liabilities (cont'd)

On March 30, 2020, the Company announced that it has entered into a settlement agreement under which the Company will receive a total of NIS 22 (principal plus accrued interest) of the Company’s Series C Debentures currently held by Internet Gold, in return for a waiver of the derivative action against Internet Gold. The derivative plaintiff will be awarded a total amount of NIS 4.23 for expenses, lawyers' fees and reward (which amount will come out of the NIS 22 amount being paid by Internet Gold). The settlement agreement is subject to court approval (by both the District Court and the Insolvency Court dealing with Internet Gold’s insolvency proceedings). For final settlement of this litigation during 2020, please refer to Note 33N.

For additional updates regarding legal proceedings against the company please refer to Note 33.

**B. Legal proceedings against the Group**

During the normal course of business, legal claims were filed against Bezeq Group companies or there are pending claims against the Bezeq Group (“in this section: “Legal Claims”).

In the opinion of the managements of the Bezeq Group companies, based, among other things, on legal opinions as to the likelihood of success of the claims, the financial statements include adequate provisions (as described in Note 17), where provisions are required to cover the exposure resulting from such claims.

In the opinion of the managements of the Bezeq Group companies, the additional exposure (beyond these provisions) as at December 31, 2019 for claims filed against Bezeq Group companies on various matters and which are unlikely to be realized, amounted to NIS 5.1 billion. There is also additional exposure of NIS 3.3 billion for claims, the chances of which cannot yet be assessed.

In addition, motions for certification of class actions have been filed against the Company and Bezeq Group companies, for which the Company and the Bezeq Group has additional exposure beyond the aforesaid, since the exact amount of the claim is not stated in the claim.

The amounts of the additional exposure in this Note are linked to the CPI and are stated net of interest.

(All amounts are in millions except where otherwise stated)

## Note 22 - Contingent Liabilities (cont'd)

Following is a detailed description of the Bezeq Group's contingent liabilities classified into groups with similar characteristics.

| Claims group | Nature of the claims | Balance of provisions as of December 31, 2019 NIS | Amount of additional exposure (restated) NIS | Amount of exposure for claims for which the amount of exposure cannot be assessed (restated) NIS |
|---|---|---|---|---|
| Customer claims | Mainly motions for certification of class actions concerning contentions of unlawful collection of payment and impairment of the service provided by the Group companies. | 111 | 8,117[(1)] | 2,147[(2)] |
| Claims by enterprises and companies | Claims alleging liability of the Group companies in respect of their activities and/or the investments made in various projects. | - | 687[(3)] | 1,873[(4)] |
| Claims of employees and former employees of Bezeq Group companies | Mainly individual lawsuits filed by employees and former employees of the Group, regarding various payments. | - | 1 | - |
| Claims by the State and authorities | Various claims by the State of Israel, government institutions and authorities (“the Authorities”). These are mainly procedures related to regulations relevant to the Group companies and financial disputes concerning monies paid by the Group companies to the Authorities (including property taxes). | 9 | 4 | - |
| Supplier and communication provider claims | Legal claims for compensation for alleged damage as a result of the supply of the service and/or the product. | - | 4 | 14 |
| Claims for punitive damages, real estate and infrastructure | Claims for alleged physical damage or damage to property caused by Group companies and in relation to real estate and infrastructure. The additional amount of exposure for punitive damages does not include claims for which the insurance coverage is not disputed. | - | 12 | - |
| **Total legal claims against the Bezeq Group companies** | | **120** | **8,825** | **4,034** |

(All amounts are in millions except where otherwise stated)

## Note 22 - Contingent Liabilities (cont'd)

(1) Including exposure in respect of a claim filed in July 2020 alongside a motion for approval as class action against Walla, alleging the misleading of the users of Walla's website regarding the number and / or scope of commercial advertisements to which surfers are required to be exposed, as a condition of consuming the requested content and / or in respect of the waiting time before viewing the requested content. The motion states that the amount of the class action cannot be accurately estimated at this stage and only an initial estimate is made, which totals in more than NIS 5 billion. If and to the extent that the Walla sale is completed, as described in Note 33, the claim will be deducted from the Bezeq Group's additional exposure. As of the date of approval of these financial statements all the regulatory approvals for the sale were granted. The Walla sale was not complete.

(2) Including exposure in the amount of NIS 0.9 billion in respect of a motion for approval of a class action lawsuit filed against the Bezeq in May 2020 and concerns Internet advertising packages via the B144 website (the amount of exposure was specified in handwriting and no explanation or calculation was included).

(3) Exposure in respect of a class action by a shareholder against the Bezeq and officers in Bezeq in which it was alleged that Bezeq failed to report on the matter of the wholesale market reform.

(4) The total includes two motions for approval of class actions in the total amount of NIS 1.8 billion, filed in June 2017 against Bezeq, officers in the Bezeq Group, the Company and companies that then controlled the Company in the matter of the acquisition of DBS shares by the Company from Eurocom DBS Ltd. In accordance with a court decision, the filing of a consolidated motion is expected to replace these two motions. The procedure was delayed in light of the investigation (as described in Note 1.3) and at the request of the Attorney General until the second half of September 2020. At the request of the State, an extension was granted to submit update notices regarding the continued delay in these cases until January 15, 2021.

(All amounts are in millions except where otherwise stated)

## Note 23 - Agreements

1. DBS has agreements for the acquisition of space segments, content, and copyrights, up to the end of 2025. The amounts of future agreements for these contracts as at December 31, 2019 are as follows:

| Year ended December 31 | Space segments (see section 2 below) NIS | Content and copyright NIS | Total NIS |
|---|---|---|---|
| 2020 | **78** | **471** | **549** |
| 2021 | **78** | **280** | **358** |
| 2022 | **75** | **236** | **311** |
| 2023 | **75** | **79** | **154** |
| 2024 | **75** | **8** | **83** |
| 2025 | **75** | **-** | **75** |
| 2026 | **12** | **-** | **12** |
| | **468** | **1,074** | **1,542** |

2. In accordance with the agreement with Space Communications Ltd. ("Spacecom") entered into in 2013, as amended, DBS leases space segments in the Amos satellites ("the Spacecom Agreement"). In accordance with the Spacecom Agreement, DBS leases space segments on the Amos 3 satellite (which is expected to end its service at the beginning of 2026), as well as on the Amos 7 satellite, in which Spacecom has the right to lease space segments under an agreement with the holder of rights in this satellite, which was leased to DBS until February 2021. In February 2020, Spacecom exercised the option granted to it by the holder of the satellite rights to extend the lease of Amos 7 for an additional year, and it extended the lease period of DBS accordingly until February 2022.

   Under the Spacecom Agreement, Spacecom has undertaken to make the most reasonable efforts to install the new satellite, Amos 8, by February 2021, and in this case, DBS will lease space segments from that date in Amos 3 and in Amos 8, and from the end of life of Amos 3, in Amos 8 only. If Amos 8 is not deployed by February 2022, DBS will lease space segments in Amos 3 until the end of its life, and will have the right, if it so chooses, to lease space segments in Amos 8, to the extent it is deployed at a later stage. DBS believes, taking into consideration, among other things, that Spacecom did not announce the agreement to construct Amos 8 and according Spacecom reports, the agreement for construction of Amos 8 was cancelled by Spacecom in 2018). Based on such reports, Amos 8 is not expected to be in place before February 2022, if at all. Therefore, in accordance with the Spacecom Agreement and although the term of the original agreement is until 2028, the agreement will terminate prematurely at the end life of the Amos 3 satellite, which, to the best of DBS' knowledge, is expected to be at the beginning of 2026, without compensation and under the terms set out in the agreement (subject to additional premature termination options).

   Leased space segments: Under the Spacecom Agreement, in the agreement period (and subject to unavailability events), DBS will lease 12 space segments from Spacecom, according to the distribution among the relevant satellites set out in the agreement for the different periods, and as from the end of the lease of the Amos 7 satellite, DBS is expected to lease ten space segments in Amos 3. The agreement also establishes the positioning of the leased backup space segments in the agreement period, under the terms and within the limitations in the agreement.

(All amounts are in millions except where otherwise stated)

## Note 23 – Agreements (cont'd)

Early termination of the agreement: The Spacecom Agreement stipulates the right to early termination without cause, subject to advance notice of 12 months and payment of the consideration in accordance with the prescribed mechanism. The Spacecom Agreement also stipulates the right of DBS to terminate the agreement in February 2021 due to a delay in the effective date of the Amos 8 construction agreement. DBS informed Spacecom that it would not exercise this right.

3. The cellular infrastructure equipment in Pelephone's UMTS/HSPA and LTE networks is manufactured by LM Ericsson Israel Ltd. ("Ericsson"), which serves as a supplier of Pelephone for the deployment of a fourth-generation radio network (LTE). Ericsson is also a material supplier of Pelephone for microwave transmission. Pelephone has multi-year agreements for maintenance, support and upgrade of software for the UMTS/HSPA network and an agreement for acquisition of 4G network (LTE) equipment with Ericsson, and Pelephone believes that it could be dependent on Ericsson for network support and its expansion. As at December 31, 2019, Pelephone has agreements with Ericsson for the acquisition of terminal equipment and the receipt of services, in a total amount of NIS 6.

   As at December 31, 2019, the Group companies have agreements for the acquisition of terminal equipment, fixed assets, intangible assets, and other assets amounting to NIS 309 and other agreements for the receipt of various services in the future amounting to NIS 93.

   For information about transactions with related parties, see Note 32D.

(All amounts are in millions except where otherwise stated)

## Note 24 - Securities, Pledges and Guarantees

The Bezeq Group's policy is to supply tender, performance and legal guarantees. In addition, Bezeq provides bank guarantees, where necessary, for banking obligations of subsidiaries.

A. The Bezeq Group companies have provided guarantees of NIS 165 in favor of the Ministry of Communications to secure the terms of their licenses (of which an amount of NIS 41 is linked to the CPI and NIS 35 to the US$ exchange rate).

B. The Bezeq Group companies provided bank guarantees totaling NIS 176 in favor of third parties.

C. In accordance with its cellular license, Pelephone is not permitted to sell, lease or pledge any of its assets used for the implementation of the license, without the consent of the Minister of Communications, except for:

1) A pledge on one of the license assets in favor of a bank operating lawfully in Israel, to receive bank credit, provided that it submitted notice to the Ministry of Communications regarding the pledge it intends to register, noting that the pledge agreement includes a clause ensuring that in any event, exercise of the rights by the bank will not impair, in any way, the services provided under the license.
2) Sale of items of equipment when implementing an upgrade, including sale of equipment by the trade-in method.

D. For information about the conditions for loans and debentures, see Note 15.

## Note 25 - Capital

Share capital of ordinary shares of NIS 0.1 par value each

| | Number of ordinary shares | | |
|---|---|---|---|
| | **2017** | **2018** | **2019** |
| Registered and paid up share capital as at January 1 | 29,889,045 | 29,889,045 | **29,889,045** |
| Issued for cash during the period (1)(2) | - | - | **86,427,518** |
| Registered and paid up share capital as at December 31 | 29,889,045 | 29,889,045 | **116,316,563** |
| Authorized share capital | 50,000,000 | 50,000,000 | **150,000,000** |

1) On January 20, 2019, the Company conducted a private placement of 7,385,600 of its Ordinary Shares, NIS 0.1 par value, to certain institutional, “qualified” and private investors in Israel. The Company received gross proceeds from the offering of approximately NIS 118, based on a price of NIS 16 per share.

2) On December 2, 2019 as part of the Searchlight-Fuhrer Transaction, the Company issued 79,041,918 of its Ordinary Shares, NIS 0.1 par value to Searchlight, the Fuhrer Group, Internet Gold and the public for a total consideration of NIS 330, based on a price of NIS 4.175 per share.

**Notes to the Consolidated Financial Statements**

(All amounts are in millions except where otherwise stated)

## Note 26 - Revenues

| | Year ended December 31, | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | NIS | NIS | NIS |
| **Domestic fixed line communications – Bezeq fixed-line** | | | |
| Fixed line telephony | 1,255 | 1,130 | **1,017** |
| Internet – infrastructure | 1,488 | 1,525 | **1,497** |
| Transmission and data communication | 775 | 769 | **745** |
| Cloud and digital services | 230 | 260 | **273** |
| Other services | 205 | 199 | **225** |
| | 3,953 | 3,883 | **3,757** |
| **Cellular communications - Pelephone** | | | |
| Cellular services and terminal equipment | 1,743 | 1,713 | **1,674** |
| Sale of terminal equipment | 757 | 688 | **642** |
| | 2,500 | 2,401 | **2,316** |
| **International communications, internet services and NEP – Bezeq International** | 1,467 | 1,338 | **1,283** |
| **Multi-channel television - DBS** | 1,650 | 1,473 | **1,344** |
| **Others** | 219 | 226 | **229** |
| | 9,789 | 9,321 | **8,929** |

## Note 27 - Salaries

| | Year ended December 31, | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | NIS | NIS | NIS |
| Total salaries and incidentals | 2, 578 | 2,574 | **2,476** |
| Less - salaries recognized in investments in property, plant and equipment and in intangible assets | 571 | 579 | **539** |
| | 2 , 007 | 1,995 | **1,937** |

(All amounts are in millions except where otherwise stated)

## Note 28 - General and Operating Expenses

| | Year ended December 31, | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | Restated | Restated | Restated |
| | NIS | NIS | NIS |
| Terminal equipment and materials | *866 | *771 | ***806** |
| Interconnectivity and payments to domestic and international operators | 805 | 789 | **757** |
| Maintenance of buildings and sites | 584 | 286 | **271** |
| Marketing and general expenses | 610 | 570 | **502** |
| Services and maintenance by sub-contractors | 260 | 277 | **270** |
| Vehicle maintenance expenses** | 156 | 82 | **71** |
| Content services expenses | 636 | 653 | **644** |
| | *3,917 | *3,428 | ***3,321** |

* Restated. See Note 2.I.

** General and operating are presented net of NIS 43 capitalized in 2019 to the cost of fixed and intangible assets (in 2018, NIS 46 and in 2017, NIS 65).

## Note 29 - Other Operating Expenses, net

| | Year ended December 31, | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | NIS | NIS | NIS |
| Provision for severance pay in early retirement, see Note 20E | 23 | 559 | **276** |
| Provision for claims | 19 | 91 | **10** |
| Capital gain from sale of property plant and equipment | (27) | 1 | **(475)** |
| Profit from sale of an associate | - | (15) | **-** |
| Others | 5 | (1) | **1** |
| | 20 | 635 | **(188)** |

**Notes to the Consolidated Financial Statements**

(All amounts are in millions except where otherwise stated)

## Note 30 - Financing Expenses, Net

| | Year ended December 31 | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | NIS | NIS | NIS |
| Income on bank deposits, investments and others | (2) | (1) | **-** |
| Gain from debt restructuring (see Note 15) | - | - | **(191)** |
| Change in fair value of financial assets measured at fair value through profit or loss | (7) | (27) | **-** |
| Income in respect of credit in sales, net of discount | (35) | (30) | **(29)** |
| Linkage and exchange rate differences, net | - | - | **-** |
| Other finance income | (25) | (31) | **(46)** |
| **Total financing income** | (69) | (89) | **(266)** |
| Interest expenses on financial liabilities | 445 | 472 | **458** |
| Linkage and exchange rate differences, net | 48 | 64 | **46** |
| Costs of early repayment of loans and debentures | - | - | **93** |
| Change in contingent consideration in a business combination | (14) | 43 | **-** |
| Change in fair value of financial assets measured at fair value through profit or loss | 39 | - | **9** |
| Financing expenses on employee benefits, net | 35 | 9 | **89** |
| Financing expenses on lease liabilities | - | 26 | **29** |
| Other financing expenses | 33 | 6 | **14** |
| **Total financing expenses** | 586 | 620 | **738** |
| **Financing expense, net** | 517 | 531 | **472** |

(All amounts are in millions except where otherwise stated)

## Note 31 - Earnings (loss) per Share

The calculation of basic and diluted earnings per share was based on income (loss) attributable to ordinary shareholders, and on a weighted average number of ordinary shares outstanding, calculated as follows:

| | Year ended December 31 | | |
|---|---|---|---|
| | **2017** | **2018** | **2019** |
| | **Restated** | **Restated** | **Restated** |
| | **NIS** | **NIS** | **NIS** |
| **Earnings (loss) attributable to ordinary Shareholders** | | | |
| Basic earnings (loss) for the year | * 75 | *(1,066) | ***(853)** |
| Effect of diluted per share loss in a subsidiary | - | - | **-** |
| Diluted earnings (loss) for the year | * 75 | *(1,066) | ***(853)** |

| | Year ended December 31 | | |
|---|---|---|---|
| | **2017** | **2018** | **2019** |
| | **Thousands of shares of NIS 0.1 par value** | **Thousands of shares of NIS 0.1 par value** | **Thousands of Shares of NIS 0.1 par value** |
| Balance as at January 1 | 29,889 | 29,889 | **29,889** |
| Effect of shares issued during the year | - | - | **13,297** |
| Weighted average number of ordinary shares (basic and diluted) as at December 31 | 29,889 | 29,889 | **43,186** |

* Restated. See Note 2.I.

## Note 32 - Transactions with Related Parties

### A. Identity of related parties

The Company’s interested and related parties as defined in the Securities Law and in IAS 24 – Related Party Disclosures include mainly: Searchlight and the Fuhrer Group from December 2, 2019, Internet Gold, Eurocom and its subsidiaries until December 2 2019, Bezeq and its subsidiaries, as well as, associates, directors and key management personnel in the Company and a person who is close to a family member of any of the above parties.

It should be noted that the transactions described below with interested and related parties do not include reference to Note 1 regarding the investigations of the Israel Securities Authority and the Israel Police or its possible implications.

(All amounts are in millions except where otherwise stated)

# Note 32 - Transactions with Related Parties (cont'd)

## B. Balances with related parties

| | December 31, | |
|---|---|---|
| | 2018 | 2019 |
| | NIS | NIS |
| Receivables - associates | 7 | **5** |
| Liabilities to related parties, net | 6 | **(1)** |
| Advanced payment to Eurocom DBS (not including interest) for contingent consideration (see Note 12.B.1) | *99 | ***99** |

* As of December 31, 2018 and 2019, the advance payment to Eurocom DBS was provided for in full.

## C. Transactions with related parties

| | Year ended December 31, | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | NIS | NIS | NIS |
| **Revenues** | | | |
| From associates | 8 | 6 | **1** |
| From related parties | 23 | 31 | **13** |
| **Expenses** | | | |
| To related parties | 122 | *54 | **20** |
| To associates | 5 | 5 | **-** |
| **Investments** | | | |
| Related parties | 28 | 1 | **-** |
| Acquisition of DBS (see Note 12.B.1) | **(70) | - | **-** |
| Revised fair value of the excess advance payments for acquisition of DBS (see Note 12.B.1) | **56 | **43 | - |

* Related-party expenses include amounts paid by DBS to Spacecom up to May 3, 2018. It should be noted subsequent to this date, Bezeq believes, based on information it received, that Spacecom ceased to be a related party. In 2018, DBS paid a total of NIS 74 to Spacecom.

** Adjustment of the liability for contingent consideration for a business combination with DBS and adjustment of the fair value estimate of the amount expected to be returned to Bezeq from the excess of the advance payments that it paid, recognized as financing income, net.

(All amounts are in millions except where otherwise stated)

## Note 32 - Transactions with Related Parties (cont’d)

### D. Transactions listed in section 270(4) of the Companies Law

| Approval date of the general meeting (after approval of Bezeq's audit committee and Board of Directors) | Nature of the transaction | Amount of the transaction |
|---|---|---|
| April 3, 2017 | Approval of Bezeqs's vote at the general meeting of DBS in favor of the agreement between DBS and Space Communications Ltd. ("Spacecom" and "the Parties" respectively) with an amendment/addendum to the existing agreement between the parties dated November 4, 2013, for the lease of satellite segments in Spacecom’s satellites ("the Agreement"), including in favor of implementation of the Agreement. | A total nominal cost of up to US$ 263 for the entire term of the Agreement (until December 31, 2028), reflecting an average annual cost of US$ 21.9. For further information about the Spacecom agreement, see Note 23.1 and 23.2. |

Bezeq had a personal interest in the transaction as at the date of its approval, since, as at the date of the transaction, Spacecom was controlled by Eurocom Communications, which as the controlling shareholder (linked) in B Communications at that time. To the best of Bezeq's knowledge and in accordance with information provided to Bezeq by Eurocom Communications, as from May 3, 2018, the connection between Eurocom Communications and Spacecom was severed and Bezeq ceased to regard Spacecom as a related party.

## Note 32 - Transactions with Related Parties (cont'd)

### D. Transactions listed in section 270(4) of the Companies Law (cont'd)

On March 7, 2011, Bezeq's Board of Directors resolved to adopt guidelines and regulations to classify a transaction of Bezeq or its subsidiary with an interested party as a negligible transaction, which is not an extraordinary transaction, as set out in Article 41(A3) of the Securities Regulations (Financial Statements Regulations), 2010 ("the Financial Statements Regulations"). These guidelines and regulations, as revised from time to time, are also used to assess the scope of disclosure in the periodic report and prospectus (including shelf offering reports) regarding a transaction of Bezeq, a company under its control and a subsidiary or associate with a controlling shareholder or in which the controlling shareholder has a personal interest as set out in Article 22 of the Securities Law (Periodic and Immediate Reports), 1970 ("the Periodic Reports Regulations") and Article 54 of the Securities Regulations (Prospectus Details and Draft Prospectus – Structure and Form), 1969. The types of transactions set out in the Financial Statements Regulations, the Periodic Report Regulations, and Prospectus Details Regulations will be referred to hereunder as "Interested Party Transactions". Bezeq will also use these guidelines to assess whether an Interested Party Transaction is a "non-negligible transaction" within the meaning of section 117(2A) of the Companies Law, 1999.

In the reporting year and/or in comparative periods, Bezeq and its subsidiaries entered into negligible transactions, which are not extraordinary transactions, with interested parties in Bezeq (or in which the controlling shareholder has a personal interest), of the types and nature set out below:

1. Sales of communications services and products by Group companies, including: basic communication services (telephony, transmission and PRI) and hosting at server farms; cellular services, value added services and sales and upgrading of cellular end equipment; web browsing services, international telephony services, hosting services and data communication services; television services.

2. Purchase of devices from Eurocom Group companies (companies owned by the former controlling shareholder of Bezeq or companies controlled by the former controlling shareholder at the approval date of the agreement), including acquisition of electronic equipment, terminal equipment, communication equipment, and pit covers.

3. Acquisition of maintenance and development services from companies in the Eurocom Group, including maintenance, development and upgrading services for systems used in the Group companies, maintenance and spare parts for exchanges, content development services and communication applications.

4. Sales of maintenance, upgrading and development services by Group companies, including maintenance of equipment, content development services and communication applications

5. Sale of user rights in communication infrastructure, call transfer, including sale of user rights in international communication infrastructure and supply of a local segment in Israel, hosting services at server farms, and reciprocal call transfer and completion agreements with Eurocom Group companies.

6. Placement and outsourcing services

(All amounts are in millions except where otherwise stated)

## Note 32 - Transactions with Related Parties (cont'd)

### D. Transactions listed in section 270(4) of the Companies Law (cont'd)

7. Rental, management and real estate acquisition agreements, including rental of areas used for communication facilities and warehouses; and rental of areas to Eurocom Group companies in properties owned by Bezeq

8. Acquisition of advertising and content services, including agreements to acquire media slots from media companies in the Eurocom Group; agreement for to use content on Pelephone's cellular portal; acquisition of portals from Eurocom Group companies; media content management services by Eurocom Group companies.

9. Transactions relating to joint marketing, advertising, discounts and sponsorship with Eurocom Group companies or related to products of Eurocom Group companies, including distribution agreements (dealer) for marketing Company services, joint marketing campaigns, consignment agreements for the sale of Eurocom Digital Communications equipment, and technological sponsorship at exhibitions organized by Bezeq.

10. Contribution to the community together with Eurocom Group companies and contribution to organizations/projects in which the controlling shareholder of Bezeq or his relative volunteers as an officer. These contributions are part of Bezeq 's contribution policy.

In the absence of special qualitative considerations all the circumstances, a transaction that is in Bezeq 's regular course of business, is carried out in market conditions and has no material effect on Bezeq, shall be deemed negligible if all the following parameters exist:

- The amount of the transaction does not exceed NIS 10.
- Bezeq is not required to issue an immediate report for the transaction under Article 36 of the periodic report's regulations or any other law.

The transaction does not include the terms of the office and employment (as defined in the Companies Law, 1999, ("the Companies Law") of an interested party or his relative, and does not constitute a transaction as set out in section 270(4) of the Companies Law (transaction of a public company with a holder of control therein, directly or indirectly, including through a company he controls, in respect of receiving services from it by Bezeq and if such person is also an officer - as to the conditions of his office and employment, and if he is an employee of Bezeq but not an officer, as to his employment by Bezeq).

According to the provisions of the Companies Law, as amended from time to time, once a year, before publication of the annual financial statements, the audit committee will review the parameters set out above, and whether they require updating. In general, each transaction will be tested separately for negligibility. Notwithstanding the aforesaid, separate transactions that are part of the same continuing transaction or very similar transactions that are carried out routinely and repeatedly, will be tested as one transaction on an annual basis for negligibility, provided the scope of the transaction does not exceed NIS 10, as set out above.

## Note 32 - Transactions with Related Parties (cont'd)

### D. Transactions listed in section 270(4) of the Companies Law (cont'd)

The Board of Directors may, from time to time and at its discretion, amend the parameters for a negligible transaction. This amendment will be duly reported. On February 27, 2020, Bezeq's audit committee revised the list of types of transactions set out above in accordance with the relevant types of transactions, since the Eurocom Group is no longer the controlling shareholder of Bezeq.

### E. Company's key management personnel (including directors) compensation:

| | Year ended December 31 | | |
|---|---|---|---|
| | 2017 | 2018 | 2019 |
| | NIS | NIS | NIS |
| Compensation | 2 | 2 | **4** |

## Note 33 - Subsequent Events

A. At the beginning of 2020, the novel coronavirus (COVID 19) broke out globally, which is an event with many implications, including macroeconomic implications ("the Event"). Due to the Event, many countries, including Israel, are taking significant steps in an attempt to contain the virus, such as restrictions on civilian movements, gatherings, restrictions on transportation of passengers and goods, and closing of borders. As a result, the Event and the actions set out above have significant implications for many economies as well as global capital markets.

As of the date of approval of these financial statements, there was an impairment mainly in revenues from roaming services in Pelephone and a certain impairment in revenues from the business segment in all Bezeq Group companies, when the total impact of the pandemic on the financial position and business position of the Bezeq Group companies was mixed, while the increase in Bezeq's activity, along with actions taken by the Bezeq Group companies in view of the consequences of the event, offset most of the damage to roaming revenues.

In addition, Bezeq's observations show that at this stage, the COVID-19 crisis did not have a material effect on Bezeq's ability to meet liabilities, measurement of assets and liabilities, impairment of assets and recognition of expected credit losses (in this context, see also Note 5 regarding the examination of indicators of impairment in Pelephone). In addition, there was no material impact on critical estimates and considerations.

As of the date of the report, Bezeq Group's working assumption regarding the further spread of the COVID-19 pandemic is that measures to limit the spread of the virus will continue with varying intensity also during 2021, alongside a gradual recovery in the aviation and international tourism industries. Accordingly, and subject to the above assumptions, Bezeq anticipates that the effects of the COVID-19 pandemic on its activities will be mainly reflected in the decline in Pelephone's revenues from roaming services, as a result of the effects of the spread of the pandemic on the aviation and international tourism segments. In addition, a certain decrease in the Bezeq Group companies' revenues from the business segment is expected.

The prolongation of the crisis or its exacerbation beyond the Group's assumptions as detailed above, insofar as such occur, may have a material adverse effect on Bezeq Group's results. These effects may be reflected, inter alia, in the impairment, beyond the estimates as stated above, of revenues from roaming services and from equipment for businesses, as well as in revenues from the business segment. The prolongation or exacerbation of the crisis may also affect revenues from the sale of cellular end equipment, employee availability, customer service and technician activity systems, supply chain, and the amounts and collection dates in respect of the Group's customers.

Bezeq's estimates as stated above may vary depending on various developments regarding the COVID-19 pandemic and its effects, in particular the duration and extent of the event, the nature and extent of the economic and other restrictions that accompany it, as well as the intensity and duration of the economic recession that will develop as a result

(All amounts are in millions except where otherwise stated)

## Note 33 - Subsequent Events (cont'd)

B. On January 9, 2020, the Company announced the appointment of Tomer Raved as Chief Executive Officer and member of the Board of Directors. Tomer succeeded Ami Barlev, who was the Chief Executive Officer of the Company since January 2019.

C. On February 13, 2020, the Company held an extraordinary general meeting of the shareholders and approved the following resolutions: (1) An amendment to the articles of association of the Company, in order to comply with the terms of the control permit applicable to the holdings of the Company in Bezeq; and (2) the compensation terms of the new Chief Executive Officer of the Company, Mr. Tomer Raved. Mr. Raved is entitled to a monthly base salary of NIS 94.33 thousand and a one-time grant of options to purchase up to 2,677,362 of our ordinary shares, representing as of the date of his employment agreement, 2.25% of the issued and outstanding share capital of the Company.

D. On April 7, 2020 Bezeq published a listing and derestriction prospectus, and Bezeq's shelf prospectus dated April 8, 2020. Following the publication of the prospectus, on April 26, 2020, Series 11 and 12 debentures were delisted from trading in the "tact institutional" list and began trading on the Stock Exchange's main list at that time. The interest rate to be paid in respect of the balance of the debenture principal as of the date of their listing for trading on the Stock Exchange's main list has been reduced by 0.4%, in accordance with the terms of the debentures.

E. In May 2020, Bezeq completed an issue according to a shelf offer report dated May 26, 2020, which was published according to the prospectus (as stated above), of Bezeq's debentures (Series 11 and 12) by expanding the series listed on the Stock Exchange's main list. The total (gross) proceeds received in respect of the issue amounted to NIS 724.4.

F. In June 2020, Bezeq made an early repayment of a private loan from an institutional entity in the amount of NIS 500. Bezeq recognized financing expenses in respect of the payment of the early repayment fee in the amount of NIS 51.

G. In August, 2020, Pelephone won a cluster of frequencies following its participation in the tender for advanced bandwidth cellular services. Pelephone's win in the frequency allocation has a total cost of NIS 88.2 million, with the payment date set for September 2022.

   In accordance with the terms of the tender, in order to promote and accelerate the development of cellular networks, *inter alia* in order to advance the deployment of the 5G technology, the winning companies would be eligible for a grant if they meet the engineering conditions of deployment and operation of 250 intracellular 5G radio stations, and the operation of a minimum bandwidth as specified in the terms of the tender, the amount of which, for all its winners, can reach a total amount of NIS 200.

   The grants will be divided among the eligible winners according to the following distribution:

(All amounts are in millions except where otherwise stated)

## Note 33 - Subsequent Events (cont'd)

The first eligible winner will be entitled to 41% of the grant (NIS 82), the second eligible winner will be entitled to 33% of the grant (NIS 66), and the third eligible winner will be entitled to 26% of the grant (NIS 52). If there are two first eligible winners, the grant will be divided between these winners as an average between the amounts (approximately NIS 74 million). If there are three first eligible winners, the grant will be divided equally between them.

As of the date of these financial statements, Pelephone estimates that it meets the conditions for eligibility for the grant and expects that it will be entitled to a grant of approximately NIS 74 million, which was recognized in the statement of financial position within the Trade Receivable and Other Receivables item, under non-current assets.

On September 29, 2020, upon receipt of the frequencies, Pelephone began operating the 5G frequencies at the broadcast sites it upgraded.

H. On August 26, 2020, the Company announced its intention to delist its shares from trading on the Nasdaq Stock Exchange and terminate its reporting liability to the US Securities and Exchange Commission (SEC). The documents required for the delisting were filed on September 9, 2020 and the Company's stock stopped trading on NASDAQ on the same day. The termination of the Company's reporting obligation on the Nasdaq Stock Exchange began on September 21, 2020, following the submission of a required document to the US Securities and Exchange Commission (SEC) on the same day.

I. On September 15, 2020, Bezeq entered into an agreement with Jerusalem Post Ltd. (the "Buyer") for the sale of all of Bezeq's holdings in Walla, in exchange for a total of NIS 65, of which NIS 55 in cash, and the balance of NIS 10 in the Bezeq's eligibility to receive advertising space from the Buyer and Walla (and related entities) for a period of up to 7 years from the date of completion of the transaction.

The sale agreement included the Bezeq's undertaking to indemnify the Buyer in certain circumstances. Completion of the agreement is subject to the approval of the Competition Commissioner and the approval of the Ministers, as well as other conditions included in the sale agreement. On December 20, 2020, the Ministers approval for the sale of Bezeq's holding in Walla to the Buyer was granted according to the Communication Order (after the Competition Commissioner approval of the sale was granted on October 21, 2020) and by that all the regulatory approvals for the sale were completed.

Following the signing of the sale agreement, Walla recognized a gain from the cancellation of the previously recognized impairment of NIS 14 in its statement of income for the three months ended September 30, 2020. Bezeq is expected to record, after the transaction is completed, an equity gain in the amount of approximately NIS 24, before additional tax. This amount may vary depending on the results of Walla's business until the transaction is completed. In addition, Bezeq recognized a deferred tax asset of approximately NIS 28 in respect of an expected loss for tax purposes from the sale of Walla.

(All amounts are in millions except where otherwise stated)

## Note 33 - Subsequent Events (cont'd)

J. On September 17, 2020, the meetings of the holders of the debentures (Series C and E) of the Company approved the amendment of the trust deeds of the said series, in a manner that will enable the Company to raise additional debt that will be secured by a lien on Bezeq shares pledged in favor of Series C, pari passu with Series C, under the following restrictions:

a. The additional debt borrowed by the Company (less the issuance expenses) will first repay the debentures (Series D) and the debentures (Series E) in full, so that after its borrowing and after the completion of the conditions required for release for the issuance of the additional series and correction of existing liens in favor of Series C, a first-degree lien will be registered on Bezeq shares pledged (as defined in the trust deed) for the benefit of the holders of the debentures (Series C), in lieu of a second-degree lien registered in their favor (as long as the debentures (Series E) are in circulation).

b. After the full repayment of the debentures in respect of the debentures (Series D) and the debentures (Series E), the balance of the proceeds from the net issue of the additional debt will be used for the purpose of repayment of the debentures (Series C), by early redemption (full or partial) in accordance with the terms of the existing trust deed.

c. The duration of the new series issued by the Company will be longer than that of the debentures (Series C), and the first principal payment in respect of the debentures from the new series as aforesaid will be only after full repayment of the debentures (Series C).

In addition, the early repayment amount to be paid to the bondholders in the event of early repayment of the bonds by the Company was also amended as follows:

With respect to the debentures (Series C) - in the case of a partial early repayment of the debentures (Series C), the price of the partial early repayment will be the highest of the par value of the debentures (Series C) or their market value according to the price of the debentures on the stock exchange in the 30 trading days preceding the early repayment.

In relation to bondholders (Series E) - the full early repayment price will be the highest of: (1) The market value of the debentures according to the price of the debentures on the stock exchange in the 30 trading days preceding the early repayment, in the early repayment price, but not more than 103.5%, Or (2) the par value of the debentures (Series E).

K. On September 10, 2020, the Ministry of Communications contacted Bezeq International (and other telecom operators) in a letter in which it raised concerns that some subscribers to Internet services or other services, such as an e-mail box, do not use them and are not even aware of this. In its address, the Ministry recommends that action be taken to notify and stop charging subscribers who do not use these services, and also requests periodic reports on the matter within the next 6 months. On November 8, 2020, another letter was received from the Ministry of Communications, according to which the Ministry expects that in the next reporting point (set for December 17, 2020), the data reported to the Ministry by the telecom operators will demonstrate a significant reduction of the phenomenon, and that reference should be made at this time to the question of how the licensee acts to prevent the recurrence of the phenomenon. It was also written that the Ministry will consider in the future whether to set binding provisions in the matter, in case proactive actions will not lead to a significant reduction in this matter.

(All amounts are in millions except where otherwise stated)

## Note 33 - Subsequent Events (cont'd)

L. On October 4, 2020, the Ministry of Communications issued a "hearing to examine the separation between broadband infrastructure service and Internet access service (ISP)" according to which the Ministry of Communications intends to take, inter alia, the following policy measures:

1. Cancellation of the "Internet Services Licensing" policy document dated December 17, 2000.

2. Correction of the licenses of the infrastructure owners - Bezeq and "Hot Telecom", so that from January 1, 2022 they will be allowed to provide customers with a unified Internet service (infrastructure and ISP service), and that they will not be allowed to offer infrastructure service to new retail customers. This section relates to Internet services that cater to the private sector.

3. Prohibition on infrastructure owners to contact certain customers with various marketing proposals before and after January 1, 2022 (the "Effective Date") as specified in the said document of the Ministry of Communications.

4. Postponement of the Effective Date in the event of a significant increase in the percentage of customers of the infrastructure owner who consume service in a unified non-wholesale configuration, in the period up to a certain date to be determined before the Effective Date, and in cases of anti-competitive practices.

5. Determination of arrangements regarding the transition between operators and preventing the formation of the phenomenon of double charges.

Bezeq International is evaluating the possible implications of the hearing its business. The approval of the hearing in its current form may lead to significant damage to Bezeq International's business and to impairment of its assets.

M. As of the financial statements for the third quarter of 2020, Bezeq International identified indicators of a possible impairment in view of the lack of a gap between the value of its operations and the book value of its net operating assets as measured on December 31, 2019 (after restatement, as described in Note 2.I above), and following its preparation, also following the recommendation of the Ministry of Communications in its addresses dated September 10, 2020 and November 8, 2020 to market operators (as described in section K above), to act in the outline of informing and treating customers who pay Bezeq International by virtue of an agreement and do not use ISP services for an extended period. Due to the aforesaid, the Group estimated the recoverable amount of the Internet Services, International Communications and network endpoint cash-generating unit as of September 30, 2020. The value in use is calculated using the method of discounting future cash flows (DCF) based on the forecast of cash flows from operations for a period of four years starting from the end of the year 2020.

## Note 33 - Subsequent Events (cont'd)

Based on the valuation, Bezeq International's recoverable amount as of September 30, 2020 amounted to approximately NIS 123, compared with carrying amount of NIS 392. Therefore, in the context of the statement of income for the period of three months which ended on September 30, 2020, the Group recognized a loss from impairment attributable to the Internet Services, International Communications and Networks segment in the amount of approximately NIS 269. Since Bezeq International does not expect future profits, no tax asset has been recognized. In addition, the Group derecognized the deferred tax balance that existed in its books in the amount of NIS 37 million.

It should be noted that the cash flow forecast used for the valuation does not include the possible effects of the Ministry of Communications' hearing dated October 4, 2020 to examine the existing separation between broadband infrastructure services and Internet access services (ISP) described in section L above, since, in the opinion of Bezeq International and the Company, this event does not indicate circumstances that existed as of September 30, 2020.

N. Update on legal proceeding against the Company after the balance sheet date:

1. Following the settlement regarding the Horev Claim, the Company reached on March 30, 2020, the Company received a total amount of NIS 22 (principal plus accrued interest) of the Company's Series C debentures which were held by Internet Gold, in exchange for waiving the derivative claim against Internet Gold. Moreover, the derivative plaintiff received an amount of NIS 4.23 for legal expenses and monetary compensation (which was paid out of the NIS 22 that Internet Gold is required to pay).
2. On June 2, 2020, the Company and former directors of the Company signed a settlement agreement as part of the Horev Claim, according to which the directors will pay NIS 2.5 million (hereinafter "the Directors' Settlement Amount") to the Company. During July 2020, the District Court approved the settlement agreement, and the directors' insurance paid the Company the full Directors' Settlement Amount. As part of the settlement, the Company paid the derivative plaintiff and their attorney a total of NIS 720 thousand.
3. On August 10, 2020, the final approval was obtained from the Court for the settlement of the Mallif case. The Company paid a sum of USD 1.2 during August 2020, which was fully covered by the insurance of the directors and officers of the Company, who released the Company from all claims related to the class action by both the plaintiffs and the members of the settlement, without any admission of guilt.

(All amounts are in millions except where otherwise stated)

## Note 33 - Subsequent Events (cont’d)

O. Retirement plan in the Bezeq Fixed Line

On December 10, 2020, as part of the implementation of a restructuring plan in Bezeq, Bezeq's Board of Directors approved the retirement of approximately 50 veteran permanent employees in the early retirement track with a total cost of approximately NIS 68. In light of the aforesaid, Bezeq is expected to record an expense in the amount of approximately NIS 65 in its financial statements for the fourth quarter of 2020.

P. Amendment of the collective bargaining agreement in Bezeq

On December 10, 2020, the Bezeq's Board of Directors approved an amendment (No. 6) to the special collective bargaining agreement dated December 5, 2006 between Bezeq and its employees’ organization and the new Histadrut (the "Collective Agreement"). Approved principles of the agreement are as follows:

1. Amendment and extension of the collective agreement until December 31, 2025 and the retirement arrangement in the collective agreement until December 31, 2026.
2. As part of the retirement arrangements, Bezeq may at its discretion terminate the employment of up to 80 permanent employees (including new permanent) each year (in addition to the retirement quota of approximately 300 permanent employees remaining from the previous agreement, which Bezeq may terminate at the end of the agreement).
3. The estimated cost of the agreement, not including the retirement of employees at Bezeq's discretion (but including the additional retirement cost of employees transferred to Bezeq from the Ministry of Communications) is approximately NIS 65 throughout the period of the agreement.
4. The agreement is currently at signing process.

(All amounts are in millions except where otherwise stated)

## Note 33 - Subsequent Events (cont'd)

Q. Remuneration Plan

On December 10, 2020, Bezeq's Board of Directors approved a capital remuneration plan ("the Plan") under which options exercisable into up to 84,000,000 ordinary shares of Bezeq can be allotted, constituting approximately 2.94% of Bezeq's issued and paid-up capital fully diluted after exercise. As part of the approval, an allotment of up to 58,735,000 options was approved for up to 117 officers, executives and senior employees of Bezeq and the subsidiaries, including the chairman of Bezeq's board of directors and Bezeq's CEO, in respect of which Bezeq published an outline and a material private offer report.

In addition, on December 12, 2020, a special general meeting of Bezeq's shareholders was convened by Bezeq, on the agenda of which:

1. Approval to increase the registered share capital of Bezeq by 24,485,753 ordinary shares of NIS 1 par value each in order to enable future allocation of capital remuneration up to the maximum available for allocation under the Plan.
2. Approval of the terms of office and the employment of Mr. Gil Sharon as Chairman of the Bezeq's Board of Directors, which will apply retroactively starting from August 27, 2020, the effective date of his entry into office (including allocation of 12,000,000 options according to the plan).
3. Approval of allocation of 9,000,000 options to Mr. Dudu Mizrahi, CEO of Bezeq, in accordance with the Plan.
4. Approval to make amendments and updates to Bezeq's Remuneration Policy.

R. Additional investment in Bezeq

On December 10, 2020, the Company purchased 10,580,000 ordinary shares of its subsidiary, Bezeq. The Company purchased the shares in exchange for the payment of a total amount of approximately NIS 40 and at an average price per share of NIS 3.78. Following this purchase, the Company now holds 26.72% of the issued and outstanding shares and voting rights in Bezeq. The shares were purchased free and clear from any pledge, mortgage, lien, foreclosure or any other right of any third party, including any other obligation to banks, financial institutions and others.

S. Hearing on setting maximum rates for Bezeq's retail telephony services

On December 15, 2020, a hearing was published by the Ministry of Communications regarding the determination of maximum rates for Bezeq's retail telephony services ("the Hearing").

1. According to the hearing documents, in view of the time that has elapsed since the establishment of the existing retail telephony rates ("the rates") and the changes in the communications industry, the control mechanism and the level of the rates must be adjusted to these changes.

(All amounts are in millions except where otherwise stated)

## Note 33 - Subsequent Events (cont'd)

Also, following a previous hearing published by the Ministry in 2017 regarding the rate control mechanism in which two alternatives were proposed (beyond maximum Rates and removal of the control from the rates of the major telephony services), the Ministry believes that at present the alternative of removing tariff control is irrelevant and will not necessarily reduce rates. Bezeq's rate level should be examined and updated according to the passage of time, the current cost structure and the state of competition.

2. Accordingly, and based on an economic opinion attached to the hearing documents, it is proposed at the hearing to adopt a uniform usage fee rate and that the usage fee rates and call minutes be set as maximum rates. According to the hearing, the basis for determining the proposed rates is the wholesale costs plus a proposed retail margin component of 25%.
3. Accordingly, it is proposed that the maximum rates for a line and calling (in NIS) be as follows:

| Service | Current rate | | Rate proposed at hearing (maximum) | |
|---|---|---|---|---|
| | Excluding VAT | Including VAT | Excluding VAT | Including VAT |
| Monthly usage fee for telephone line | 49.5 | 57.92 | 20.82 | 24.36 |
| Rates for call minutes to landline networks | Low – 0.035<br>High – 0.0857 | Low – 0.041<br>High – 0.010 | 0.012 | 0.014 |
| Rate for one minute of call to mobile networks | 0.1098 | 0.128 | 0.072 | 0.084 |

4. In addition, it is proposed to set a maximum rate for a package of line services and a quota of minutes that Bezeq will be obligated to market to its subscriber, which will include 500 minutes of calls to landline and mobile destinations at a maximum rate of NIS 28 plus VAT plus the fixed rate for each minute. At the same time, it is proposed to cancel all existing exchange payment packages while allowing Bezeq to market new service packages at reasonable rates in relation to the maximum rates that are proposed to be determined at the hearing and which are not higher than them.
5. The Ministry of Communications estimates that the proposed change in rates is expected to reduce the expenses of subscribers to the individual lines segment in a way that will reduce the expenses of Bezeq's landline telephony consumers by NIS 331 per year (approximately 390 including VAT).
6. It should be noted that the hearing offers additional changes to Bezeq's service rates, including adjustments to the new rates proposed at the hearing, setting existing rates for ancillary telephone line services as maximum rates and allowing Bezeq to set lower prices relative to them, and discontinuing call rates initiated by business customers using PRI axes.
7. Also, according to the hearing, insofar as there is a change in the interconnect rates, this will result in a change in the corresponding call minute rates that include this component.
8. Bezeq is studying the hearing documents and is preparing to submit its reference. On December 17, 2020, Bezeq sent the Ministry of Communication a request for delay in the submission date of for the hearing response due the complexity of the matter (until March 15, 2021 instead of January 4, 2020). Bezeq's request also stated its initial substantial reservations from the MOC's position in the hearing. In Bezeq's assessment, insofar as the changes proposed at the hearing are made, a material adverse effect on Bezeq's financial results is expected.

# B-Communications Ltd.

***Goodwill Impairment Test of Bezeq International***

**December 31, 2019 - following the November 2020 Restatement**

***November 2020***

14 Kremenetski St., Tel Aviv, 6789912 | Phone: **| 03-5617801 Fax: 03-5617765**

# Foreword and Limitation of Liability

- We were retained by Tomer Raved, CEO of B Communications Ltd. ("**BCOM**" or the "**Client**") to prepare a valuation of the activity of Bezeq International Ltd. (“**Bezeq International**" or the "**Company**") as at December 31, 2019 ,according to IAS36 standard requirements (“**The report**”).
- The Report intended solely for the internal use of the Client. This Report may not be reproduced, in whole or in part, and the findings of this Report may not be used by a third party for any purpose, without our expressed written consent. Notwithstanding any of the above, this Report may be included in the Client’s financial statements of as of Dec. 31, 2019.
- For the purpose of preparing this Report, we relied upon financial and other information including prospective financial information obtained from the Company and/or the Client and/or anyone on their behalf (the “**Information**”). We assumed that the Information is credible and therefore did not perform an independent audit of the information. In addition, nothing suggesting that the Information may be unreasonable has come to our attention. The Information has not been examined in an independent manner, and therefore this Report does not constitute a verification of the Information’s correctness, completeness and accuracy. If the case that the Information is not complete nor accurate or credible, the results of this valuation might change. We reserve the right to update this Report in light of new information which might have not been known to us. We shall not be liable for the manner of the Client’s and/or the Company's presentation of any financial data quoted in the Report in terms of its accuracy, completeness, accounting compliance and implications of its accounting presentation, as far as any such implications exist.
- This Report includes prospective information, as defined in the Securities Law, 5728-1968, obtained, among others from the Company/Client. The realization of this information is not certain. The information is based in part on data that was known by the Company prior to preparing this Report, as well as on various assumptions and forecasts as well as many external factors; including the state of the relevant markets, potential competitors and the general state of the economy. There is no certainty that such assumptions or forecasts will be realized, in whole or in part.
- Economic evaluations reflect in a reasonable and fair manner a given state of being at a given time, based on known information, while considering the basic assumptions and estimated forecasts. To remove all doubt, this Report is valid only for its preparation date.
- This Report does not constitute a due diligence review and is not meant to replace such a review. In addition, this Report is not intended to determine value for a specific investor, and there is nothing in this Report to constitute a legal advice or opinion.
- This Report does not include any accounting audit regarding the compliance with accounting rules. We are not liable for the manner in which the Client’s and/or the Company's financial statements are prepared and audited in connection with the accuracy and completeness of the data presented in these statements and the implications of their accounting presentation, as far as such exist.
- This Report includes a description of the methodology and main assumptions and analyses used by us. The description does not purport to provide a full and detailed breakdown of all the procedures that we applied in formulating the Report.
- We hereby confirm that we are an independent expert, with no personal interest in the Company and/or the Client, and/or their controlling stakeholders, and/or the outcome of this Report. Our fee for preparing this Report is not contingent on the outcome of our work.
- We hereby confirm that we have no personal stake in the Company and/or the Client and/or their controlling stakeholders.
- Calculations and figures presented herein have generally been rounded. As the underlying calculations were performed on the exact figures, adding or multiplying table values may result in minor differences compared to the presented figures.

# Foreword and Limitation of Liability

- Prometheus Financial Advisory Ltd. and any company controlled by it directly and / or indirectly as well as any controlling shareholder, officer and employee in any of such, are not liable for any damage, loss of profit or expense of any kind and nature, including direct and / or indirect, which might incur to anyone relying on the mentioned in this Report, in whole or in part.
- Nothing in this Report constitutes an offer or recommendation or opinion regarding making or avoiding making any transaction
- The Client shall not be entitled to receive from us, whether due to contract or damages, in accordance with the law or otherwise, any sum due to loss of profits, data or reputation, or due to any consequential damage, random or indirect, or as special or punitive damages regarding any lawsuits resulting from services provided within this report or which are related in any other way with the services provided by us within this report. All, whether the likeliness of such loss or damage has been expected or not, in the case where we have not acted with malice.
- In addition, and without detracting from the generality of the aforementioned, as far as we shall be obligated to pay any sum to any third party regarding the execution of the services detailed in this report, in any legal or other obligating procedures, the Client undertakes to indemnify us for any sum as aforesaid paid by us, immediately upon our first request.
- Notwithstanding any of the above, we shall cover if the total indemnification amount shall be less than three times our fees under this engagement letter, we shall not be entitled to any indemnification.
- The provided final and executed version of our work (the "**Report**"). Shall be the only binding document. No other document shall be considered binding.

# Previous financial studies

## Previous financial studies:

The Firm performed an impairment test of Bezeq International's Operations as of December 31, 2019. Below is a comparison of the segment's impairment test and it's key metrics (this report) and the previous impairment, prior to restatement:

| Impairment Test | EV (NIS millions) | ISP subscribers in the terminal year (retail and wholesale) | Terminal year ARPU (retail and wholesale) | Discount rate (post-tax) | Terminal growth rate |
|---|---|---|---|---|---|
| Impairment test of Bezeq International's operations as of Dec. 31, 2019 | 652 | 830 | 48.4 | 9.7% | 0.7% |
| Impairment test of Bezeq International's operations as of Dec. 31, 2019 (Restated) * | 374 | 830 | 48.4 | 9.7% | 0.7% |

* The primary reduction in the enterprise value was caused by the restatement.

# Profile of the Appraising Firm and the Appraisers

## Prometheus Financial Advisory Ltd.

Prometheus Financial Advisory specializes in providing clients with financial and economic advisory services as well as expert opinions. The Firm is led by Yuval Zilberstein (APC), Eyal Szewach (B.Sc, MBA), Eli Makla (CPA), Ben Orion (CPA) and Gideon Peltz (CPA).

The Firm is committed to personal service, while providing clients with in-depth, value added, advisory services. The Firm's executives were involved in many of the major transactions in Israel in recent years and have decades of experience in providing expert opinions for boards of directors, tax and securities authorities, and courts.

Gideon Peltz, CPA, Partner and the head of the expert opinion and valuations. Mr. Peltz has vast expertise in providing business consulting, valuations, transaction services consultation as well as preparing expert opinions.

Sincerely,

**Prometheus Financial Advisory Ltd.**

November 30, 2020

# Sources of Information

**Key sources of information used to prepare the Report:**

- Unaudited restated financial statements for Bezeq International and its operating segments for 2017-2019,.
- BCOM's audited financial statements for 2018, and its draft financial statements as of December 31, 2019
- Long-term forecast prepared by management
- Adjustments to the long-term forecast, prepared by management to reflect the restated statements
- Other financial data and various verbal clarifications received on demand
- Background data and market data, from public sources on the internet, news print, or other public sources
- Israel Central Bureau of Statistics and Bank of Israel data
- The Capital IQ system
- Discussions and meetings with executives from Bezeq and its subsidiaries
- UK fixed-line market report entitled Telecom Data Update Q3 2019, OFCOM

# Table of Contents

# Executive Summary

# Executive Summary

## BCOM - overview

### General

B Communications Ltd. ("BCOM") is a public company listed on the TASE. It functions as a holding company whose sole asset is 26.3% of the outstanding capital of Bezeq The Israel Telecommunication Corporation Ltd. ("Bezeq" and/or the "Group").

Bezeq is a public company listed on the TASE. Bezeq Group is a key provider of telecommunications services, including domestic fixed-line communications services, mobile radio-telephone (cellular) services, international communications services, multichannel satellite television services, internet access and infrastructure services, maintenance and development of communication infrastructures, communication services to other communications providers, and other services related to its areas of operation. The Group holds a substantial market share in all its operational segments and has been declared a monopoly in the fixed-line communications segment.

Bezeq wholly owns Pelephone Communications Ltd. ("Pelephone"), D. B. S. Satellite Services (1998) Ltd. ("DBS" and/or "YES"), Bezeq International Ltd. ("Bezeq International“, or “the Company”), Walla Communications Ltd. ("Walla") and Bezeq Online Ltd. ("Online").

Bezeq's operations are divided into four segments:

Domestic Fixed-Line Communications - This segment consists primarily of Bezeq’s operations as a Domestic Carrier, including telephony services, Internet infrastructure and access services, transmission and data communications services. Bezeq also provides wholesale services, granting access to its physical infrastructure.

Pelephone - Cellular Communications - Mobile phone services (cellular communications), marketing of handsets, installation, operation and maintenance of cellular communication equipment and systems.

Bezeq International - International long distance ("ILD“) communications, internet service provider ("ISP") services, NEP services, and integration services for businesses.

DBS Multi-Channel Television (yes) - Digital multi-channel television broadcasting services to subscribers via satellite and IP.

# Executive Summary

## Valuation method and key assumptions

### Valuation methods

Our valuation of Bezeq International's operations was prepared using the discounted cash flow (DCF) model.

Forecasts for the Company's cash flows were based, among other things, on its operating results for 2016-2018, its draft financial statements 2019, and Management's forecast for 2020-2024.

Prometheus, to the best of its ability, assessed the likelihood of the various scenarios based on the information that it was presented with, and by conducting independent analysis.

Said analysis was limited in scope to broad evaluations of economic soundness which did not amount to an investigative accounting effort. We were informed by the company that the services of an accounting firm were retained in order to perform an investigation. If and when any findings are reported during the investigation, we retain the right to update our valuation.

# Executive Summary

## Valuation method and key assumptions

### Restated Items

We were informed by Management that, as part of preparation of the third quarter 2020 report, and as a result of internal controls put in place, the Company identified material disparities between the book value of it's assets and liabilities and the assets and liabilities as measured in actuality, in part caused by the partial recognition of booked expenses for advances to suppliers that were not transferred to the profit and loss statements, and as a result of erroneous recognition of receivables.

The accounting systems contained numerous manually entered transactions which have been insufficiently documented, and as such have severely hampered the attempts to trace and scrutinize said transactions and evaluate their full impact on the financial reports. The Company elected to recompile the balances in which mistakes were discovered, with out relying on said manual transactions, and with the aid of an external impartial expert. In the process the Company performed additional reasonability checks and utilized additional reports, developed through out the process. Bezeq International is still examining the source of the disparities, in conjunction to the ongoing investigation performed by the impartial expert, may yet discover additional discrepancies. The Company expects that such discrepancies will not bear a material impact on the Bezeq Group's financial statements.

# Executive Summary

## Valuation method and key assumptions

### Valuation methods

In the process of issuing the restatement of the Dec. 31, 2019 statements, a number of issues were identified whose impact resulted in a reduction of NIS 186 million (net of tax, as of June 30, 2020). Presented below:

1. A reduction in the surpluses as of June 30, 2020 in the amount of NIS 114 million, as a result of past balances from 2002-2017. The majority of the sum, some NIS 80 million, was identified as being recorded in 2002-2003.
2. A reduction in stated profits of an aggregate amount of NIS 72 million as a result of balances recorded between Jan. 1, 2018 and Jun. 30, 2020.
3. In light of the issues stated above, the Company drafted new forecasts for the following years, and performed an updated valuation as of Dec 31. 2019. As a result, the Company updated the impairment of the asset.

The recompilation process and the fact that not all records have been fully scrutinized have resulted in the Company's impaired ability to fully qualify the impact of the restated items on the forecasts that have been utilized in valuations prepared for the company.

The company assumes that the effects the restated items on the operating profit, for the nine months ending Sep 30, 2020, and it's extrapolation for the entirety of the year, will carry forward to the forecast years, including the terminal year.

| Period | Restatement effect on the operating profit (difference vs. original, millions) |
|---|---|
| 2018 FY | (34) |
| 2019 FY | (45) |
| 2020 FY, est. | (33) |

**We've adopted the Company's most recent estimates, which have been updated to address said differences.**

# Executive Summary

## Valuation method and key assumptions

### Principal assumptions

- **Internet services:** We adopted the Company's forecast whereby ISP segment revenues would stabilize around NIS 620 million, annually. Negative net subscriber growth would be reduced over the forecast period, as growth of the wholesale subscriber base will offset the decrease in retail subscribers. A key assumption of the forecast is Bezeq launching its fiber-based internet services in early 2021, and the right-of-use pricing model for wholesale usage of the copper and fiber infrastructures, as layed out in the Ministry of Communications (hereby “**MoC**”) regulations (published February 23, 2020).

The forecast is further based on transmission costs, according to projected traffic volumes across Bezeq's network (including traffic due to yes's migration).

- **ILD services:** We assumed ILD revenues will decline over the forecast period, similar to the trend in recent years and projections that the market will continue to shrink due to IP-based alternative services.
- **Enterprise services:** We assumed that Company revenues from enterprise communication services will gradually grow over the forecast period, mainly due to the Company's strategy of focusing on these services (cloud services, data centers, etc.). It is noted that these services are seeing accelerated growth in Israel and abroad.
- **Discounting rate:** This Valuation uses a discount rate of 9.7% (equal to 11.2% pre-tax), calculated using the CAPM model (for details, see Appendix A).
- **Terminal growth rate:** We assumed an 0.7% terminal growth rate, considering the growth rate for direct profits from ISP and ILD operations, and procurement and equipment, and enterprise service operations.

# Executive Summary

## Company overview

### Results of valuation

Bezeq International's EV, as of December 31, 2019, was valued at NIS 374 million. Based on information provided by BCOM, this segment's book value was NIS 767 million. It is thus necessary to write-off NIS 393 million (pre-tax) in the segment's value.

Sensitivity to the discount rate and terminal growth rate

Analysis of Bezeq International's EV's sensitivity to changes in the discount and terminal growth rates:

| | | Discount rate | | | | |
|---|---|---|---|---|---|---|
| | | 7.7% | 8.7% | 9.7% | 10.7% | 11.7% |
| Terminal growth rate | (0.3%) | 410 | 367 | 332 | 304 | 280 |
| | 0.2% | 440 | 391 | 352 | 320 | 294 |
| | 0.7% | 475 | 418 | **374** | 338 | 308 |
| | 1.2% | 515 | 448 | 397 | 357 | 324 |
| | 1.7% | 562 | 483 | 425 | 379 | 342 |

Summary

A 1% increase (decrease) in the discount rate causes a NIS 36 million to NIS 57 million decrease (increase) in Bezeq International's EV. An 0.5% increase (decrease) in the terminal growth rate causes a NIS 22 million to NIS 27 million increase (decrease) in Bezeq International's EV.

Sensitivity to the effects of the restatement

As previously stated, we've adopted Managements's assumptions regarding the impact of the restatement, resulting in an increase of NIS 33 million in the operating costs for 2020 FY, and the following forecast years. As Management's unable to fully explain the differences between the original and the restated statements, we have performed a sensitivity analysis of the forecasted impact on the EBITDA in 2024 on the enterprise value of the company:

| NIS, millions | - | (5) | (10) | (15) | (20) | (25) | (30) | (33) | (35) | (40) | (45) |
|---|---|---|---|---|---|---|---|---|---|---|---|
| 2024 FY EBITDA | 189 | 184 | 179 | 173 | 168 | 163 | 158 | **156** | 153 | 148 | 143 |
| Enterprise value | 653 | 610 | 567 | 524 | 481 | 438 | 395 | **374** | 351 | 310 | 268 |

An increase (decrease) of NIS 5 million in the operating expenses results in a decrease (increase) of NIS 43 million in the enterprise value.

For a summary of the main differences this valuation and the valuation for Dec. 31, 2019 prior to the restatement, see Appendix D.

# Executive Summary

## Summary

### :Summary of Results

| Valuation Results | NIS, Millions |
|---|---|
| Value accrued from the model years | 138 |
| Value accrued from the terminal year | 236 |
| **Enterprise Value** | **374** |

The enterprise value of Bezeq International, as of Dec. 31, 2019, on the basis of the assumptions stated above and the data received from the Company, is NIS 374 million. BCOM's book value stands at NIS 767 million, and as such a write-off of 393 is required.

### Sensitivity Analysis

**Sensitivity of the Result - Terminal Growth and Discount Rate.**

Displayed below is an analysis of Bezeq International's EV's sensitivity to changes in the discount and terminal growth rates:

| | | Discount rate | | | | |
|---|---|---|---|---|---|---|
| | | **7.7%** | **8.7%** | **9.7%** | **10.7%** | **11.7%** |
| Terminal growth rate | **(0.3%)** | 410 | 367 | 332 | 304 | 280 |
| | **0.2%** | 440 | 391 | 352 | 320 | 294 |
| | **0.7%** | 475 | 418 | **374** | 338 | 308 |
| | **1.2%** | 515 | 448 | 397 | 357 | 324 |
| | **1.7%** | 562 | 483 | 425 | 379 | 342 |

Summary

A 1% increase (decrease) in the discount rate causes a NIS 36 million to NIS 57 million decrease (increase) in Bezeq International's EV. An 0.5% increase (decrease) in the terminal growth rate causes a NIS 22 million to NIS 27 million increase (decrease) in Bezeq International's EV.

# Chapter 1 - Bezeq International's Operating Segments

## ISP Services

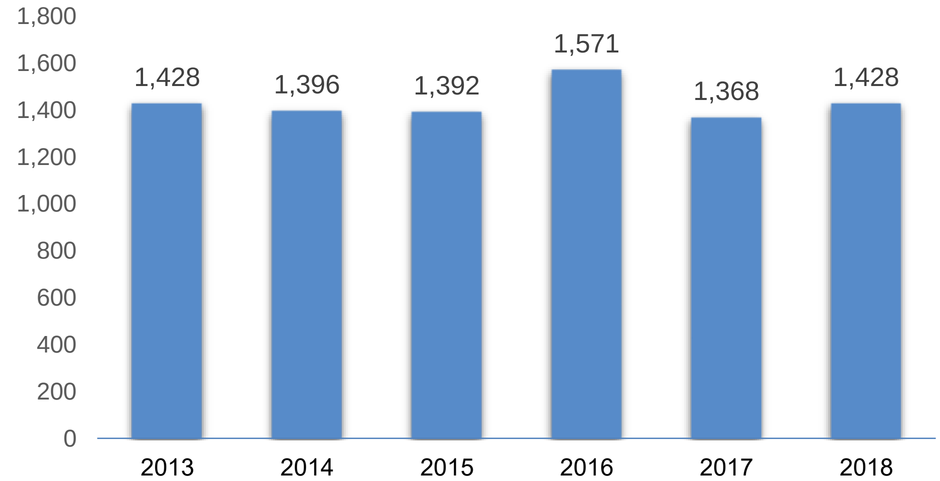
### General

The internet services segment is comprised of ISP services to households and businesses (including the wholesale market). This segment also includes additional services mainly offered to businesses, such as:

- **Hosting services:** website and server hosting services in specialized facilities.
- **Information security services:** Internet connection and LAN security services.
- **Data services:** Including international data communications solutions for enterprise clients, with a global presence.
- **Wi-Fi services:** For private and public areas.

In 2018, Bezeq International began offering bundles coupling yes's TV services with internet and household fixed-line services. Bezeq international provides its internet services through its wholly and exclusively-owned marine cable connecting Israel and Italy, and through rights-of-use to third-party cables. Domestic traffic is primarily transmitted over Bezeq's infrastructure.

**Exhibit 1: ISP revenues in Israel, NIS millions[1]**




**Data indicate that the market has reached equilibrium. Market revenues have remained relatively stable since 2013. Fixed-line internet penetration in Israel is among the highest in the OECD, and is not expected to show any material growth.**

The Ministry of Communications indicates that the fluctuations around 2016 were due to changes in methods for classifying revenues across business lines when selling service bundles.

1. *Source: Ministry of Communications, "Summary of Telecom Market Revenues for 2018", June 2019.*

# Chapter stnemgeS gnitarepO s'lanoitanretnI qezeB -1

## *ISP Services*

### Competition

The ISP market is saturated. The major competitors are Cellcom, Partner, and Hot Net. Bezeq International estimates its market share in 2019 at 30%.[2]

According to the Company's financial statements, bundle prices have been going down since 2017, while sales have increased for service plans. This trend has been fueled by expansion of the wholesale offering model (ISP + infrastructure) and growth in triple-bundle sales by competitors. Market players are trying to cope with eroding prices, including by selling value added services such as household security solutions.

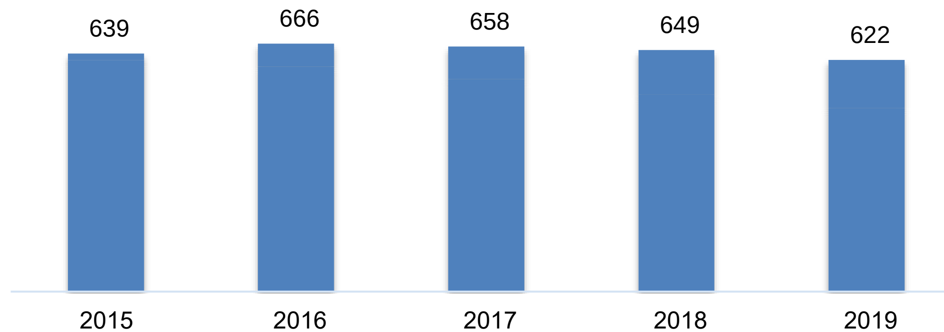
### Changes in the wholesale market model

In February 2020, the Ministry of Communications updated the right-of-use fee charged by Bezeq under the wholesale market model - Communications Regulations (Bezeq and Broadcasts) (Use of Public Bezeq Network by Domestic Carriers) (Amendment and Temporary Provision), 2020.

2. *Source: Company data.*

### Bezeq International's revenues

**Exhibit : Company revenues from ISP services[3]**




Since neeb evah secivres PSI morf seunever ynapmoC ,2015 elaselohw morf seunever ,sraey eht revO .elbats ylevitaler srebircsbus liater morf seunever elihw ,nworg evah srebircsbus .knurhs evah

3. *Source: Company data.*

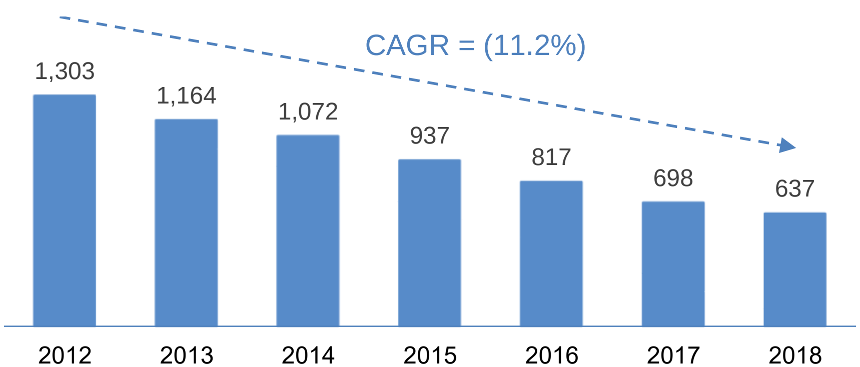
# Chapter 1 - Bezeq International's Operating Segments

## ILD operations

### General

Bezeq International's ILD services include outgoing ILD calls, incoming ILD calls, and transferring ILD calls between foreign carriers (hubbing). Services are provided using Bezeq and Hot's domestic networks, as well as cellular networks, to connect subscribers to the ILD exchange.

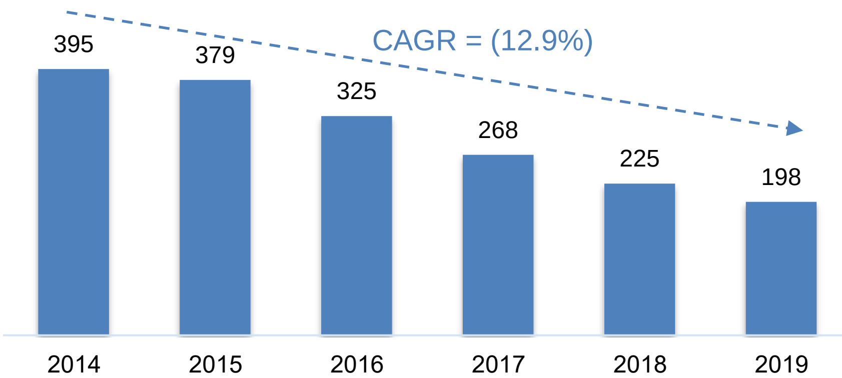
**Exhibit 3: ILD market revenues in Israel, NIS millions[4]**




Data indicates that ILD market revenues consistently decreased in recent years.

4. *Source: Ministry of Communications, "Summary of Telecom Market Revenues for 2018", June 2019.*
5. *Source: Bezeq financial statements for 2016-2019 (voice service revenues)*
6. *For example, in 2007-2018, ILD call minutes in England decreased 10.6% a year on average, while revenues decreased 13.6% a year on average (Telecom Data Update Q3 2019, OFCOM).*

**Exhibit 4: Bezeq International's ILD revenues (NIS millions)[5]**




Bezeq International's ILD revenues have decreased consistently in recent years, following the general trend for the ILD market. In 2019, Company revenues totaled only NIS 198 million, about a half of the revenue recorded for 2014, and down 12% from 2018's revenues of NIS 225 million.

This erosion is due to a decrease in both incoming and outgoing call minutes, mainly driven by service plans including international call minutes offered by cellular operators, and use of free VoIP apps such as Skype and WhatsApp.

Similar to the domestic call market, the downward trend in the ILD market is a world-wide phenomenon.[6]

## ILD operations

### Competition

At the end of 2018, there were more than ten companies operating in the ILD market (including Bezeq International, Cellcom, Partner, Golan Telecom, and HOT Mobile). The Company estimates its market share in 2019 at 27% for outgoing ILD calls, and 30% for incoming ILD calls.[7]

As call minutes are a commodity product, ILD prices and call volumes are expected to continue to decline.

7. *Source:* Company data (market share is based on Ministry of Communications surveys of overall call minutes in the market).

## Enterprise telecom services

### General

Bezeq International provides enterprises with two main telecom services:

1. **International data services:** International data communication solutions for business customers including customized global deployment.

2. **ICT services:** ICT services are diverse, and Bezeq International offers the following:
   - Server and website hosting
   - Maintenance and tech support
   - System and networking services
   - Cyber risk management and security
   - IP-based managed services
   - Cloud computing
   - Telecom equipment and licenses for telecom services
   - PBX services

### Competition and global trends

Locally, the Company competes with Binat, Teldor, IBM's local operations, and others. In January 2020, Microsoft announced that it plans to supply its cloud services from Israel. Microsoft provides cloud services (including services such as 365, Azure, etc.) through servers operating from designated server farms. As part of its enterprise telecom offering, Bezeq International also provides hosting services on the Company's server farms. These include server security, back-up, and other services. Bezeq International also offers cloud-based enterprise services, but at a relatively small scope. The bulk of its operations in this segment is not exposed to competition from Microsoft.

Microsoft's entry into the Israeli market could lay the groundwork for major Israeli companies to migrate to cloud-based services. This is expected to stimulate the Israeli cloud-service market.

Additional competitors in the enterprise telecom services market include Partner, Altice, and Cellcom, who are trying to penetrate this market.

The enterprise telecom market is expected to see significant growth in the coming years. IDC, for example, predicts an annual growth rate of 13.3% in 2019-2022 for cloud integration services in existing IT systems.[8]

8. *Source:* https://www.idc.com/getdoc.jsp?containerId=prUS44670519

# Chapter 2 - Financial Statement Analysis

## Balance Sheet - Bezeq International's Operations

Bezeq International's balance sheets for 2017-2019 (Draft, Restated):

| NIS millions | Dec. 31, 2017 Draft | Dec. 31, 2018 Draft | Dec. 31, 2019 Draft |
|---|---|---|---|
| **Assets** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | 66 | 124 | 69 |
| Current trade and other receivables | 423 | 354 | 346 |
| Inventory | 37 | 28 | 21 |
| Current tax assets | 2 | 8 | 26 |
| **Total current assets** | **528** | **513** | **462** |
| **Non-current assets** | | | |
| Long-term trade receivables | 28 | 22 | 17 |
| PP&E | 303 | 397 | 373 |
| Intangible assets | 109 | 114 | 116 |
| Right-of-use leased assets | - | 141 | 112 |
| Deferred and other expenses | 284 | 269 | 261 |
| Investment in associates | 5 | 6 | 4 |
| Deferred tax assets | 2 | 2 | - |
| **Total non-current assets** | **720** | **830** | **759** |
| **Total assets** | **1,210** | **1,344** | **1,221** |

### Assets - Key Items

**Current assets**

Total current assets: 2019 saw a decrease of NIS 50 million, mainly due to a decrease in cash balances. This decrease in cash was mainly due to loan repayments to principal shareholders.

**Non-current assets**

Property, plant and equipment: The Company's PP&E is composed mainly of switching and internet equipment, computers, office equipment, and its marine cable. The decrease in 2019 was due to amortization of the Company's marine cable and lower investment in telecom equipment.

Right-of-use in leased assets: This item mainly comprises buildings and vehicles used by the Company. Rights were first recognized in 2018, upon the first implementation of IFRS 16

Deferred and other expenses: This item mainly comprises right-of-use in capacity (network traffic), amortized subscriber acquisition costs, and advances on Company expenses. The decrease in these assets was mainly due to a write-off in the network capacity usage rights.

## Balance Sheet - Bezeq International's Operations

| NIS millions | Dec. 31, 2016 Audited | Dec. 31, 2017 Audited | Dec. 31, 2018 Audited | Dec. 31, 2019 Un-audited |
|---|---|---|---|---|
| **Liabilities + equity** | | | | |
| **Current liabilities** | | | | |
| Principal shareholder loans | 81 | 72 | 104 | 17 |
| Trade and other payables | 348 | 369 | 351 | 371 |
| Short-term lease liabilities | - | - | 30 | 24 |
| Short-term provisions | 1 | - | 8 | 18 |
| Employee benefits | 15 | 17 | 17 | 31 |
| Current tax liabilities | 2 | - | - | - |
| **Total current liabilities** | **447** | **458** | **510** | **462** |
| **Non-current liabilities** | | | | |
| Principal shareholder loan | 83 | 95 | 90 | 32 |
| Long-term lease liabilities | - | - | 113 | 90 |
| Employee benefits | 14 | 16 | 15 | 21 |
| Provisions | - | 1 | 0 | 0 |
| Deferred tax liabilities | 2 | 3 | 4 | 11 |
| Other liabilities | 1 | 1 | - | - |
| **Total non-current liabilities** | **100** | **115** | **222** | **155** |
| **Total liabilities** | **546** | **573** | **733** | **616** |
| Equity | 706 | 686 | 637 | 632 |
| **Total liabilities + equity** | **1,252** | **1,259** | **1,370** | **1,248** |

### Liabilities and Equity - Key Items

Principal shareholder loan (Bezeq): In 2019, the loan balance decreased by NIS 145 million (repayment of NIS 149 million, including interest). The payment was financed through the Company's cash flows and cash balances (as indicated in the previous slide).

Trade and other payables: Trade payables were down in 2019 mainly due to a decrease in the balance to equipment suppliers (with a corresponding asset-side decrease in trade receivables, to a similar amount).

Lease liabilities: The increase in 2018 was due to the first-time application of IFRS 16.

Short-term provisions: The increase in 2018 and 2019 was due to provisions for legal actions.

Employee benefits: The increase in 2019 was due to a provision for the cost of a collective labor agreement for 2019-2021.

## Profit and Loss - Bezeq International

Bezeq International's operating income statements for 2017-2019 (unaudited):

| NIS millions | 2017 Unaudited | 2018 Unaudited | 2019 Unaudited |
|---|---|---|---|
| ISP revenues | 670 | 659 | 632 |
| YoY change | (1%) | (2%) | (4%) |
| ILD revenues | 268 | 225 | 198 |
| YoY change | (18%) | (16%) | (12%) |
| Enterprise telecom revenues* | 600 | 507 | 508 |
| YoY change | 10% | (16%) | 0% |
| **Total revenues** | **1,537** | **1,391** | **1,339** |
| **YoY change** | **(1%)** | **(10%)** | **(4%)** |
| General and operating expenses (including leases)[9] | 917 | 856 | 920 |
| % of revenues | 60% | 62% | 69% |
| Salary expenses[9] | 327 | 300 | 261 |
| % of revenues | 21% | 22% | 20% |
| Depreciation and amortization | 136 | 160 | 161 |
| % of revenues | 9% | 12% | 12% |
| **Total operating expenses** | **1,380** | **1,316** | **1,341** |
| **% of revenues** | **89.80%** | **94.70%** | **100.20%** |
| **Adjusted operating profit** | **157** | **74** | **(3)** |
| **% of revenues** | **10%** | **5%** | **(0%)** |
| **Adjusted EBITDA** | **293** | **234** | **158** |
| **% of revenues** | **19%** | **17%** | **12%** |
| CAPEX | 138 | 126 | 129 |
| % of revenues | 9% | 9% | 10% |
| **EBITDA net of CAPEX** | **154** | **108** | **30** |
| **% of revenues** | **10%** | **8%** | **2%** |

*Including equipment and license sales to businesses.

9. *Including retrospective classification of credit fee expenses from finance expenses to operating expenses, and classification of meal costs from operating expenses to salary costs.*

### Analysis of key items

**Revenues**

Revenues from ISP operations: Revenues totaled NIS 632 million (down 4% from NIS 659 million in 2018). Revenues from ISP operations continued to decline due to subscriber attrition, driven by market competition and a slight decrease in service prices.

Revenues from ILD operations: Revenues from ILD operations totaled NIS 198 million (down 12% from 2018's NIS 225 million), mainly due to the continued downward trend in call minutes and the loss of a major enterprise client.

Revenues from enterprise telecom services*: Revenues from enterprise telecom services totaled NIS 508 million (similar to the figure for 2018). Revenues from data and terminal equipment for integration grew, compensating for a decrease in PBX revenues. It is noted that segment revenues in 2017 were exceptional, following the one-time sale of terminal equipment and licenses.

In summary, Bezeq International's operating revenues in 2019 totaled NIS 1,339 million, down 3.7% from 2018's NIS 1,391 million.

## Profit and Loss - Bezeq International

Bezeq International's operating income statements for 2017-2019 (unaudited):

| NIS millions | 2017 Unaudited | 2018 Unaudited | 2019 Unaudited |
|---|---|---|---|
| ISP revenues | 670 | 659 | 632 |
| YoY change | (1%) | (2%) | (4%) |
| ILD revenues | 268 | 225 | 198 |
| YoY change | (18%) | (16%) | (12%) |
| Enterprise telecom revenues* | 600 | 507 | 508 |
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*Including equipment and license sales to businesses.

*10. Including retrospective classification of credit fee expenses from finance expenses to operating expenses, and classification of meal costs from operating expenses to salary costs.*

### Analysis of key items

**Expenses**

General and operating expenses: General and operating expenses grew relative to 2018, mainly due to a provision for a collective labor agreement for 2019-2021, legal provisions, and higher bandwidth consumption in both retail and wholesale sectors. This increase was partially offset by lower ILD expenses (corresponding with the decrease in revenue).

Salary expenses: Salary expenses decreased in 2019 mainly due to the sale of outsourcing operations, and a decrease in the workforce following reorganization efforts.

Overall, Bezeq International's operating expenses grew NIS 25 million from 2018, accounting for a higher percentage of revenues – 100.2%.

## Profit and Loss - Bezeq International

Bezeq International's operating income statements for 2017-2019 (unaudited):

| NIS millions | 2017 Unaudited | 2018 Unaudited | 2019 Unaudited |
|---|---|---|---|
| ISP revenues | 670 | 659 | 632 |
| YoY change | (1%) | (2%) | (4%) |
| ILD revenues | 268 | 225 | 198 |
| YoY change | (18%) | (16%) | (12%) |
| Enterprise telecom revenues* | 600 | 507 | 508 |
| YoY change | 10% | (16%) | 0% |
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| **YoY change** | **(1%)** | **(10%)** | **(4%)** |
| General and operating expenses (including leases)[9] | 917 | 856 | 920 |
| % of revenues | 60% | 62% | 69% |
| Salary expenses[9] | 327 | 300 | 261 |
| % of revenues | 21% | 22% | 20% |
| Depreciation and amortization | 136 | 160 | 161 |
| % of revenues | 9% | 12% | 12% |
| **Total operating expenses** | **1,380** | **1,316** | **1,341** |
| **% of revenues** | **89.80%** | **94.70%** | **100.20%** |
| **Adjusted operating profit** | **157** | **74** | **(3)** |
| **% of revenues** | **10%** | **5%** | **(0%)** |
| **Adjusted EBITDA** | **293** | **234** | **158** |
| **% of revenues** | **19%** | **17%** | **12%** |
| CAPEX | 138 | 126 | 129 |
| % of revenues | 9% | 9% | 10% |
| **EBITDA net of CAPEX** | **154** | **108** | **30** |
| **% of revenues** | **10%** | **8%** | **2%** |

*Including equipment and license sales to businesses.

*11. Including retrospective classification of credit fee expenses from finance expenses to operating expenses, and classification of meal costs from operating expenses to salary costs.*

### Analysis of key items

**CAPEX, EBITDA, and operating cash flows**

**Adjusted operating profit (loss):** Loss totaled NIS 3 million a decline of NIS 77 million from 2018. Adjusted for a provision for the collective labor agreement, operating profit totaled NIS 42 million (3.2% of revenues). Adjusted **EBITDA** totaled NIS 158 million (down 32% from 2018).

CAPEX: The Company's expenses did not grow significantly, and **EBITDA net of CAPEX** (operating cash flows before changes in operating work capital and tax expenses) was down from NIS 108 million in 2018 to NIS 30 million in 2019.

## 2019 budget vs. actual

| NIS millions | Forecast (budget)* | Actual | Difference |
|---|---|---|---|
| ISP revenues | 645 | 632 | (13) |
| ILD revenues | 212 | 198 | (14) |
| Enterprise telecom revenues** | 523 | 508 | (15) |
| **Total revenue** | **1,380** | **1,339** | **(41)** |
| Total operating expenses | **(1,319)** | **(1,341)** | **(22)** |
| *% of revenues* | *(96%)* | *(100%)* | |
| **Adjusted operating profit** | **61** | **(3)** | **(64)** |
| *% of revenues* | *4%* | *(0%)* | |
| Total depreciation and amortization | 151 | 161 | 10 |
| **Adjusted EBITDA** | **212** | **158** | **(54)** |
| *% of revenues* | *15%* | *12%* | |
| CAPEX | (144) | (129) | 16 |
| *% of revenues* | *(11%)* | *(10%)* | |
| **EBITDA-CAPEX** | **68** | **30** | **(38)** |
| *% of revenues* | *5%* | *2%* | |

* Based on the Company's forecast used in the December 31, 2018 valuation.

** Including equipment and license sales to businesses.

The above is the Company's budget for 2019, prepared in late 2018, compared with actual 2019 results (based on data available at the end of the period, and the draft financial statements for that year).

Revenues: Operating revenues were NIS 41 million below the Company's planned budget for 2019 -

- In ISP operations, subscriber attrition exceeded projections, mainly due to clients migrating to competitors' fiber networks.
- In ILD operations, the Company lost a major enterprise client (with a large number of call minutes).
- Revenues from enterprise telecom services were down as equipment and licensing sales under-performed.

Expenses and adjusted operating profit Operating **expenses** were NIS 22 million above the Company's planned budget, and their share of the Company's revenues grew. This was mainly due to the impact of the restatement, provisions made as part of the Company's streamlining efforts and an increase in asset depreciation costs. As a result, **adjusted operating profit** was down by NIS 64 million.

Adjusted EBITDA and operating cash flows: **Adjusted EBITDA** was down NIS 54 million, while the profit margin remained materially unchanged. Actual **investments** were NIS 16 million below the planned budget, after postponement of planned IT investments. As a result, operating cash flows (as reflected in **EBITDA net of CAPEX** before changes in operating working capital and tax expenses) declined by NIS 38 million compared to the Company's planned budget.

# Chapter 3 - Valuation

## Bezeq International - Key Assumptions

### Value in Use

As part of this Valuation, we reviewed the asset's primary market. We also sought to identify a potential investor. Based on our analysis, we could not identify a potential market partner. Furthermore, since Bezeq International is part of a comprehensive telecom group (Bezeq), its value reflects certain benefits such as joint management for Bezeq's subsidiaries, headquarters services, lower debt terms based on Bezeq's rating, etc. Moreover, Bezeq International's ISP operations, and a substantial part of its commercial operations, rely on Bezeq infrastructure. Its operation as a separate entity is due to regulatory reasons applicable to some of its operations. As such, we believe that Bezeq International's fair value cannot exceed its value in use. Thus, this Valuation applies the value in use approach.

Our valuation of Bezeq International's operations was prepared using the discounted cash flow (DCF) model.

Forecasts for the Company's cash flows were based, among other things, on its restated results for 2017-2019, and Management's forecast for 2020-2024.

Prometheus, to the best of its ability, assessed the likelihood of various scenarios based on available information presented to Prometheus, and independent analysis.

### Restatement

Management expects that the differences in cash flow as a result of the restatement will impact the forecast years and the permanent year as well. As of the date of this report, we have adopted the most recent estimates made available to us by Management.

## Bezeq International - Key Assumptions

### Revenues

**ISP**

We adopted the Company's forecast whereby ISP segment revenues would stabilize around NIS 620 million, annually. Negative net subscriber growth would be reduced over the forecast period, as growth in wholesale subscribers will offset the decrease in retail subscribers. The forecast relies on Bezeq launching its fiber-based internet services in early 2021, and wholesale pricing for copper and fiber infrastructure as set by current Ministry of Communications regulations.[12] The forecast is further based on transmission costs, according to projected traffic volumes across Bezeq's network, including traffic due to yes's migration.

ISP

- *Subscribers:* Based on the trend from recent years, we assumed that the subscriber base would shrink from 886 thousand at the end of 2019 to 830 thousand at the end of 2024 (a cumulative decrease of 6%).
- *ARPU:* Moderate growth was assumed, from NIS 46.0 in 2019 to NIS 48.4 in 2024, due to changes in subscriber composition.

12. *Source: Ministry of Communications, "Communications Regulations (Bezeq and Broadcasting)(Use of Public Bezeq Network by Domestic Carriers)(Amendment and Temporary Provision), 2020, February 2020; "Recommendation for Setting a Maximum Rate for Ultra-Broadband Managed Access Services over Bezeq's Fiber Network", July 2019.*

Summary of revenue forecast for ISP operations:

| | A2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|---|
| ISP subscribers (thousands) | 886 | 859 | 844 | 835 | 830 | 830 |
| *Change from previous period* | *(3.4%)* | *(3.0%)* | *(1.7%)* | *(1.1%)* | *(0.6%)* | *-* |
| | | | | | | |
| Weighted ARPU (NIS millions) | 46.0 | 46.4 | 47.3 | 47.8 | 48.2 | 48.4 |
| *Change from previous period* | | *0.8%* | *1.9%* | *1.1%* | *0.8%* | *0.4%* |
| | | | | | | |
| **Total ISP revenues (NIS millions)[13]** | **632** | **619** | **619** | **618** | **620** | **623** |
| *Change from previous period* | *(4.0%)* | *(2.2%)* | *-* | *(0.1%)* | *0.2%* | *0.5%* |

**ILD**

We adopted the Company's forecast whereby ILD revenues would decline over the forecast period (similar to the trend seen in recent years), and the call market would continue to shrink (due to IP-based alternative products). Thus, ILD revenues would decrease from NIS 198 million in 2019, to NIS 157 million in 2024 (21% cumulative decrease).

13. *Total ISP revenues include revenues from major connections, SHAAM and domestic carriers, who are not counted as subscribers, to the amount of NIS 120-125 million in the forecast period.*

## Bezeq International - Key Assumptions

### Enterprise telecom services

We adopted the Company's forecast, whereby enterprise telecom revenues would grow from NIS 508 million in 2019 to NIS 620 million in 2024 (cumulative growth of 22%). Growth in these services is driven by the Company's strategy to focus on these operations (cloud, data center, and other services). In recent years, these services have grown at an accelerated rate in Israel and abroad.

## Bezeq International - Key Assumptions

### Operating, depreciation and amortization expenses

Operating, depreciation and amortization expenses for Bezeq International in 2019, and forecast expenses for 2020-2024:

| NIS millions | 2019A | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|---|
| General and operating expenses (including leases)* | (920) | (901) | (931) | (962) | (995) | (1,012) |
| *% of revenues* | *68.7%* | *66.9%* | *68.9%* | *70.5%* | *71.9%* | *72.3%* |
| | | | | | | |
| Salary expenses | (261) | (258) | (236) | (227) | (230) | (233) |
| % of revenues | *19.5%* | *19.2%* | *17.5%* | *16.6%* | *16.6%* | *16.6%* |
| | | | | | | |
| Depreciation and amortization | (161) | (163) | (163) | (161) | (159) | (157) |
| *% of revenues* | *12.0%* | *12.1%* | *12.1%* | *11.8%* | *11.5%* | *11.2%* |
| | | | | | | |
| **Total operating, depreciation and amortization expenses** | **(1,341)** | **(1,322)** | **(1,330)** | **(1,350)** | **(1,384)** | **(1,402)** |
| % of revenues | 100.2% | 98.2% | 98.5% | 98.9% | 100.0% | 100.2% |

*Including payments for leases and an annual expense of NIS 4.6 million (starting 2022) for the universal access fund (based on Company estimates). Including other expenses of NIS 60 million in 2019 (NIS 45 million for retirement agreements and NIS 15 million for updates to the provision for legal actions).5.

The decrease in salary expenses is mainly due to streamlining efforts, as per the collective agreement signed with the Histadrut Clalit. We assumed that, at this time there is uncertainty concerning the second phase of the streamlining efforts, and so the effect of the second phase was not taken into account for 2022-2024. The increase in other operating expenses (except ILD expenses) is due to opex growth in enterprise telecom services, equipment and licensing (matching the growth in revenues). The change was also driven by increased domestic capacity costs due to growing consumption and usage, and rate adjustments by the Ministry of Communications.[14] The decrease in ILD expenses was due to a decrease in direct expenses from ILD operations, matching the decrease in revenues.

14. *Bandwidth pricing in Company forecasts are based on the Ministry of Communications updated regulations as of February 23, 2020 - "Communications Regulations (Bezeq and Broadcasting)(Use of Public Bezeq Infrastructure by Domestic Carriers)(Amendment and Temporary Provision), 2020".*

## Bezeq International - Key Assumptions

### Adjusted EBITDA

Applying the above assumptions to operating income and expenses, we assumed that EBITDA would total NIS 187 million in 2020, and NIS 155 million in 2024:

| NIS millions | 2019A | 2020E | 2021E | 2022E | 2023E | 2024E |
|---|---|---|---|---|---|---|
| **EBITDA** | **204** | **187** | **184** | **176** | **159** | **155** |
| *% of revenues* | *15.20%* | *13.90%* | *13.60%* | *12.90%* | *11.50%* | *11.00%* |

### Tax expenses

We assumed a 23% corporate tax rate, according to the current statutory rate in Israel.

### CAPEX

Forecast capital expenses are based on Bezeq International's forecasts. In 2020-2024, investments are expected while migrating to upgraded IT systems. Furthermore, completion of the marine cable back-up project is expected to lower expenses in the forecast period, compared to previous years. In the terminal year, we estimated investment at 8% of turnover, similar to the figure for 2024.

### Operating working capital

Operating working capital was estimated based on the average working capital as a percentage of revenues in the last three years, adjusted for one-time streamlining costs which were not taken into account in 2022-2024.

## Bezeq International - Key Assumptions

### Discount rate

This Valuation uses a discount rate of 9.7% (equal to 12.1% pre-tax), calculated using the CAPM model (for details, see Appendix A).

### Terminal growth rate

We assumed an 0.7% terminal growth rate, considering the combined growth rate for direct profits from ISP and ILD operations, and procurement and equipment, and enterprise service operations*.

* We assumed that ISP, ILD, and equipment and licensing operations (accounting for 65% of the direct contribution[15]) would see zero growth, while enterprise service operations would grow 2%, according to the population growth rate.

15. *Profit directly attributable to the Company's operating segments, based on Company data.*

## Bezeq International - Projected Cash Flows

| NIS millions | 2019A | 2020E | 2021E | 2022E | 2023E | 2024E | TY |
|---|---|---|---|---|---|---|---|
| ISP revenues | 632 | 619 | 619 | 618 | 620 | 623 | |
| ILD revenues | 198 | 191 | 182 | 173 | 165 | 157 | |
| Enterprise telecom and other revenues | 508 | 536 | 550 | 573 | 600 | 620 | |
| **Total revenue** | **1,339** | **1,346** | **1,351** | **1,365** | **1,384** | **1,400** | **1,410** |
| *% change from previous period* | *(3.7%)* | 0.5% | 0.4% | 1.0% | 1.4% | 1.1% | 0.7% |
| Salary expenses | (261) | (258) | (236) | (227) | (230) | (233) | |
| *% of revenues* | *19.5%* | *19.2%* | *17.5%* | *16.6%* | *16.6%* | *16.6%* | |
| General and operating expenses | (888) | (869) | (898) | (930) | (963) | (980) | |
| *% of revenues* | *66.3%* | *64.6%* | *66.4%* | *68.2%* | *69.6%* | *70.0%* | |
| Payments for leases | (32) | (32) | (33) | (32) | (32) | (32) | |
| *% of revenues* | *2.40%* | *2.30%* | *2.50%* | *2.30%* | *2.30%* | *2.30%* | |
| **Total operating expenses (less depreciation and amortization)** | **(1,180)** | **(1,159)** | **(1,167)** | **(1,189)** | **(1,225)** | **(1,245)** | |
| *% of revenues* | *88.2%* | *86.1%* | *86.4%* | *87.1%* | *88.5%* | *89.0%* | |
| **Adjusted EBITDA** | **158** | **187** | **184** | **176** | **159** | **155** | **156** |
| *% of revenues* | *11.8%* | *13.9%* | *13.6%* | *12.9%* | *11.5%* | *11.0%* | *11.0%* |
| Total depreciation and amortization | (161) | (163) | (163) | (161) | (159) | (157) | (116) |
| **Adjusted operating profit** | **(3)** | **24** | **21** | **15** | **-** | **(2)** | **40** |
| *% of revenues* | (0.2%) | 1.8% | 1.5% | 1.1% | - | (0.2%) | 2.8% |
| Tax income (expenses) | (9) | (5) | (5) | (3) | - | - | (9) |
| *Tax rate* | - | *23.0%* | *23.0%* | *23.0%* | - | - | *23.0%* |
| CAPEX | (129) | (134) | (131) | (125) | (116) | (115) | (116) |
| *% of revenues* | *63200.0%* | *10.0%* | *9.7%* | *9.2%* | *8.4%* | *8.2%* | *8.2%* |
| Positive (negative) cash flow from working capital changes | | (48) | (8) | 6 | 4 | 2 | 1 |
| **Cash flow** | | **(1)** | **41** | **53** | **46** | **41** | **32** |
| Discounting period | | 0.5 | 1.5 | 2.5 | 3.5 | 4.5 | 4.5 |
| **Discounted cash flow** | | **(1)** | **36** | **42** | **34** | **27** | **236** |

## Bezeq International - Valuation Results and Sensitivity Analysis

### :Summary of Results

| Valuation Results | NIS, Millions |
|---|---|
| Value accrued from the model years | 138 |
| Value accrued from the terminal year | 236 |
| **Enterprise Value** | **374** |

The enterprise value of Bezeq International, as of Dec. 31, 2019, on the basis of the assumptions stated above and the data received from the Company, is NIS 374 million. BCOM's book value stands at NIS 767 million, and as such a write-off of 393 is required.

### Sensitivity Analysis

**Sensitivity of the Result - Terminal Growth and Discount Rate.**

Displayed below is an analysis of Bezeq International's EV's sensitivity to changes in the discount and terminal growth rates:

| | | Discount rate | | | | |
|---|---|---|---|---|---|---|
| | | **7.7%** | **8.7%** | **9.7%** | **10.7%** | **11.7%** |
| **Terminal growth rate** | **(0.3%)** | 410 | 367 | 332 | 304 | 280 |
| | **0.2%** | 440 | 391 | 352 | 320 | 294 |
| | **0.7%** | 475 | 418 | **374** | 338 | 308 |
| | **1.2%** | 515 | 448 | 397 | 357 | 324 |
| | **1.7%** | 562 | 483 | 425 | 379 | 342 |

<u>Summary</u>

A 1% increase (decrease) in the discount rate causes a NIS 36 million to NIS 57 million decrease (increase) in Bezeq International's EV. An 0.5% increase (decrease) in the terminal growth rate causes a NIS 22 million to NIS 27 million increase (decrease) in Bezeq International's EV.

## Bezeq International - Valuation Results and Sensitivity Analysis

### Sensitivity analysis (contd.)

**Sensitivity to bandwidth prices (expenses)**

Bandwidth prices under the valuation model as of December 31, 2019 were based on Company forecasts, whereby retail and wholesale gigabits prices are NIS 8,000 and NIS 10,200, respectively, in 2020, and go down gradually through 2024. [16]

Analysis of Bezeq International's appraised EV to changes in retail and wholesale gigabits prices (compared to the Company's forecast prices for each year):

| | | Change in retail gigabit prices (NIS)[17] | | | | |
|---|---|---|---|---|---|---|
| | | **(1,000)** | **(500)** | **-** | **500** | **1,000** |
| **Change in whole-sale gigabit prices (NIS)** | **(1,000)** | 515 | 470 | 425 | 380 | 335 |
| | **(500)** | 489 | 444 | 399 | 354 | 309 |
| | **-** | 463 | 418 | **374** | 328 | 284 |
| | **500** | 437 | 392 | 348 | 303 | 258 |
| | **1,000** | 411 | 367 | 322 | 277 | 232 |

<u>Summary</u>

A NIS 500 increase (decrease) in retail gigabits prices causes a NIS 45 million decrease (increase) in Bezeq International's EV. A NIS 500 increase (decrease) in wholesale gigabits prices causes a NIS 26 million decrease (increase) in Bezeq International's EV.

16. *Gigabits prices in Company forecasts are based on the Ministry of Communications updated regulations as of February dna qezeB) snoitalugeR snoitacinummoC" -2020 ,23 202 ,(noisivorP yraropmeT dna tnemdnemA)(sreirraC citsemoD yb erutcurtsarfnI qezeB cilbuP fo esU)(gnitsacdaorB0”.*
17. *Based on Company assumptions, we assumed that changes in gigabits prices are only relevant for payments to Bezeq, while payments to HOT will remain unchanged.*

## Bezeq International - Valuation Results and Sensitivity Analysis

### Sensitivity analysis (contd.)

**Sensitivity to the impact of the restatement**

As previously stated, we've adopted Managements's assumptions regarding the impact of the restatement, resulting in an increase of NIS 33 million in the operating costs for 2020 FY, and the following forecast years. As Management's unable to fully explain the differences between the original and the restated statements, we have performed a sensitivity analysis of the forecasted impact on the EBITDA in 2024 on the enterprise value of the company:

| NIS, millions | No measured impact | (5) | (10) | (15) | (20) | (25) | (33) |
|---|---|---|---|---|---|---|---|
| 2024 FY EBITDA | 189 | 184 | 179 | 173 | 168 | 163 | **156** |
| Enterprise value | 653 | 610 | 567 | 524 | 481 | 438 | **374** |

As demonstrated above, an increase of NIS 33 million in the operating costs results in a decrease of NIS 33 million NIS and a resulting decrease of NIS 280 million in the enterprise value.

# Appendices

# Appendix A

## WACC - Bezeq International

### Calculating the discount rate for Bezeq International's operations

| Symbol | Parameter | Value | Comments |
|---|---|---|---|
| D/V | Debt to asset value ratio | 25.6% | *Based on the median of comparative companies (see table)* |
| E/V | Equity to asset value ratio | 74.4% | **(D/V) = 1 - (E/V)** |
| D/E | Debt to equity ratio | 34.5% | **(D/E) = (D/V) / (E/V)** |
| βUL | **Unleveraged beta for comparative companies** | **0.61** | *In order to estimate the beta for these operations, we reviewed a group of similar companies. There were no publicly traded companies whose operations are identical to the operations under assessment, and so we chose companies that are partially similar to said operations yet differ from each other, or order to create a mix which would optimally reflect the Company's profile. Beta is calculated on a weekly basis over a .doirep raey-5* |
| Tax | Long term tax rate for the operations | 23.0% | Long term tax rate for the operations under assessment. |
| βL | **Leveraged beta for the operations** | **0.77** | **βL= βUL*{1+(1-Tax)*(D/E)}** |
| Rf | Risk-free interest rate | 1.4% | *Nominal yield to long-term maturity on NIS-based government bonds, for a .2019 ,31 rebmeceD fo sa ,doirep raey-15* |
| MRP | Market risk premium | 6.9% | *The risk premium in the Israeli market, based on Damodaran data as of 2019.* |
| SRP | Specific risk premium | 3.4% | *Premium according to Duff and Phelps data for -dim rof ,2019 .sesirpretne dezis* |
| Re | **Cost of equity** | 10.1% | **RE = Rf + βL * MRP + SRP** |
| Rd | **Cost of Company debt** | 3.1% | Long-term cost of debt for the operations, based on the yield to maturity as of the valuation date of AA- rated bonds. |
| **WACC** | **Weighted average cost of capital** | **8.1%** | **WACC = Re *(E/V) + Rd*(D/V)*(1-TAX)** |

The above table presents the calculations behind the 8.1% discounting rate, as of December 31, 2019.

As we believe the market risk inherent in Bezeq International's operations has not decreased from 2018, we used a 9.7% discounting rate, similar to the discounting rate used in Bezeq International's previous valuation, as of December 31, 2018 (equal to 12.1% pre-tax).

### Additional information on comparative companies:

| Company | Unleveraged beta | D/V |
|---|---|---|
| Chorus Limited | 0.58 | 50.9% |
| United Internet AG | 0.64 | 32.9% |
| WideOpenWest, Inc. | 0.38 | 78.8% |
| Bahnhof AB (publ) | 0.68 | 0.0% |
| TPG Telecom Limited | 0.70 | 18.4% |
| Bredband2 i Skandinavien AB (publ) | 0.53 | 0.0% |
| **Median** | **0.61** | **25.6%** |

## WACC - Bezeq International

### Discount rate

The WACC is significantly lower than the discount rate that we adopted.

The calculated discount rate of the WACC decreased significantly compared to last year, mainly due to a decrease in risk-free yield rate of Israeli government bonds.

A review of various professional public announcements and discussions with professionals in the macroeconomics segment shows that the decline in yield rate on government bonds is due to macroeconomic reasons, including (summary):

- A decrease in interest rates in the USA
- The pending introduction of the World Government Bond Index (WBGI) into Israel, which is expected to increase demand for bonds and decrease the yield.
- Additional factors, such as the low inflation level in Israel, or interest rate decreases by central banks worldwide as a measure to combat uncertainty in the markets.

On other words, in this specific case, this decline in the yield rate of government bonds and decrease in the WACC rate of the segment does not necessarily reflect a decrease in the economic risk inherent in the market.

As a result, we believe that in the specific case of the Israeli telecommunications market, the decrease in WACC does not express a decrease in the sectoral risk and the appropriate return from an investor's point of view.

Accordingly, we adopted the discount rate used in the valuation for 2018.

# Appendix B

## Book value - Bezeq International

### Book value - Bezeq International

Details on Bezeq International's book value, as of December 31, 2019, as provided by BCOM:

| Item | Value (NIS millions) |
|---|---|
| Assets | 1,269 |
| Liabilities | (544) |
| Goodwill attributed to Bezeq International in BCOM's books | 42 |
| **Bezeq International's total book value in BCOM's books** | **767** |

# Appendix C

## Differences Compared to the Previous Valuation

### Differences compared to the previous valuation

In accordance with the Israeli Securities Authority - Regulations (Periodic and Immediate Statements),1970, in case of difference of over 40% between the valuation of Dec. 31 2018 and Dec. 31 2019, a summary of the Dec. 31 2018 valuation should be presented.

The valuation of Dec. 31 2018 was not prepared by us, and will be presented via other client’s publication.

# Appendix D

## Summary of differences between the Dec 31st, 2019 valuations, pre- and post- restatement

### Differences compared to the previous valuation

The primary difference between the original valuation dated Dec. 31, 2019, and the valuation date Dec. 31, 2019 post restatement lies with the increase of roughly NIS 33 million in operating expenses, due to the restated financial statement for the same date. The Company estimated the effect of the restated financial statements based on the nine months ending Sep. 30, 2020, and extrapolating that to the full year 2020. The Company expects the effects to carry on into the forecast years, including the terminal year.

| NIS, millions | Enterprise value |
|---|---|
| **Enterprise value, Dec 31 2019, original** | **652** |
| Restated – operating costs increase of NIS 33 mil. | (285) |
| Working capital methodology impact | 5 |
| Permanent growth impact | 2 |
| **Enterprise value, Dec 31 2019, restated** | **374** |